

OCEANEERING INTERNATIONAL INC

Form 10-Q

November 01, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2018

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 1-10945

---

OCEANEERING INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

Delaware 95-2628227

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

11911 FM 529 77041

Houston, Texas (Address of principal executive offices) (Zip Code)

(713) 329-4500 (Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed from 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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).  Yes  No

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Number of shares of Common Stock outstanding as of October 26, 2018: 98,532,769

---

Oceaneering International, Inc.  
Form 10-Q  
Table of Contents

Part I Financial Information

- Item 1. Financial Statements.  
Consolidated Balance Sheets  
Consolidated Statements of Operations  
Consolidated Statements of Comprehensive Income  
Consolidated Statements of Cash Flows  
Notes to Consolidated Financial Statements
- Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.
- Item 3. Quantitative and Qualitative Disclosures About Market Risk.
- Item 4. Controls and Procedures.

Part II Other Information

- Item 1. Legal Proceedings.
- Item 6. Exhibits.

Signatures

Table of Contents

## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements.

OCEANEERING INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)	Sep 30, 2018 (unaudited)	Dec 31, 2017
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$367,150	\$430,316
Accounts receivable, net of allowances for doubtful accounts of \$6,430 and \$6,217	579,205	476,903
Inventory, net	189,119	215,282
Other current assets	54,362	64,901
Total Current Assets	1,189,836	1,187,402
Property and Equipment, at cost	2,831,728	2,815,579
Less accumulated depreciation	1,838,214	1,751,375
Net Property and Equipment	993,514	1,064,204
Other Assets:		
Goodwill	500,164	455,599
Other non-current assets	240,185	316,745
Total Other Assets	740,349	772,344
Total Assets	\$2,923,699	\$3,023,950
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities:		
Accounts payable	\$111,756	\$85,539
Accrued liabilities	364,558	350,258
Total Current Liabilities	476,314	435,797
Long-term Debt	782,190	792,312
Other Long-term Liabilities	163,722	131,323
Commitments and Contingencies		
Equity:		
Common Stock, par value \$0.25 per share; 360,000,000 shares authorized; 110,834,088 shares issued	27,709	27,709
Additional paid-in capital	217,613	225,125
Treasury stock; 12,301,319 and 12,554,714 shares, at cost	(704,436 )	(718,946 )
Retained earnings	2,268,687	2,417,412
Accumulated other comprehensive loss	(313,454 )	(292,136 )
Oceaneering Shareholders' Equity	1,496,119	1,659,164
Noncontrolling interest	5,354	5,354
Total Equity	1,501,473	1,664,518
Total Liabilities and Equity	\$2,923,699	\$3,023,950

The accompanying Notes are an integral part of these Consolidated Financial Statements.

Table of Contents

OCEANEERING INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(unaudited)

(in thousands, except per share data)	Three Months Ended		Nine Months Ended Sep	
	2018	2017	2018	2017
Revenue	\$519,300	\$476,120	\$1,414,387	\$1,437,332
Cost of services and products	471,665	421,235	1,318,196	1,284,021
Gross Margin	47,635	54,885	96,191	153,311
Selling, general and administrative expense	49,187	44,354	144,529	133,540
Income (Loss) from Operations	(1,552 )	10,531	(48,338 )	19,771
Interest income	2,645	1,997	8,187	5,379
Interest expense, net of amounts capitalized	(9,885 )	(8,650 )	(28,058 )	(22,517 )
Equity in income (losses) of unconsolidated affiliates	(1,684 )	(424 )	(3,264 )	(1,798 )
Other income (expense), net	5,632	(1,287 )	(6,398 )	(3,901 )
Income (Loss) Before Income Taxes	(4,844 )	2,167	(77,871 )	(3,066 )
Provision (benefit) for income taxes	61,135	3,935	70,317	4,104
Net Income (Loss)	\$(65,979 )	(1,768 )	\$(148,188 )	\$(7,170 )
Weighted average shares outstanding				
Basic	98,533	98,270	98,483	98,224
Diluted	98,533	98,270	98,483	98,224
Earnings (loss) per share				
Basic	\$(0.67 )	\$(0.02 )	\$(1.50 )	\$(0.07 )
Diluted	\$(0.67 )	\$(0.02 )	\$(1.50 )	\$(0.07 )
Cash dividends declared per share	\$—	\$0.15	\$—	\$0.45

The accompanying Notes are an integral part of these Consolidated Financial Statements.

Table of Contents

OCEANEERING INTERNATIONAL, INC. AND SUBSIDIARIES  
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)  
 (unaudited)

(in thousands)	Three Months		Nine Months Ended	
	Ended Sep 30,		Sep 30,	
	2018	2017	2018	2017
Net Income (Loss)	\$(65,979)	\$(1,768)	\$(148,188)	\$(7,170)
Other comprehensive income (loss):				
Foreign Currency Translation Adjustments	(5,688 )	16,547	(21,318 )	20,269
Total other comprehensive income (loss)	(5,688 )	16,547	(21,318 )	20,269
Comprehensive Income (Loss)	(71,667 )	14,779	\$(169,506)	\$13,099

The accompanying Notes are an integral part of these Consolidated Financial Statements.

Table of Contents

OCEANEERING INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(unaudited)

(in thousands)	Nine Months Ended	
	Sep 30, 2018	2017
Cash Flows from Operating Activities:		
Net income (loss)	\$(148,188)	\$(7,170 )
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	164,674	160,480
Deferred income tax provision (benefit)	27,021	(25,065 )
Net loss (gain) on sales of property and equipment and cost method investment	(8,513 )	429
Noncash compensation	8,562	10,854
Excluding the effects of acquisitions, increase (decrease) in cash from:		
Accounts receivable	(85,278 )	25,501
Inventory	(7,094 )	35,000
Other operating assets	6,377	(20,162 )
Currency translation effect on working capital, excluding cash	2,495	253
Current liabilities	60,998	(56,148 )
Other operating liabilities	14,602	20,042
Total adjustments to net income	183,844	151,184
Net Cash Provided by Operating Activities	35,656	144,014
Cash Flows from Investing Activities:		
Purchases of property and equipment	(83,919 )	(59,900 )
Business acquisitions, net of cash acquired	(68,398 )	(11,278 )
Proceeds from redemption of investments in Angola bonds	62,021	—
Purchase of Angola bonds	(10,417 )	(10,777 )
Distributions of capital from unconsolidated affiliates	2,372	2,556
Proceeds from sale of property and equipment and cost method investment	15,897	635
Net Cash Used in Investing Activities	(82,444 )	(78,764 )
Cash Flows from Financing Activities:		
Net proceeds from issuance of 6.000% Senior Notes, net of issuance costs	295,816	—
Repayment of term loan facility	(300,000 )	—
Cash dividends	—	(44,220 )
Other financing activities	(1,565 )	(1,772 )
Net Cash Used in Financing Activities	(5,749 )	(45,992 )
Effect of exchange rates on cash	(10,629 )	2,930
Net Increase (Decrease) in Cash and Cash Equivalents	(63,166 )	22,188
Cash and Cash Equivalents—Beginning of Period	430,316	450,193
Cash and Cash Equivalents—End of Period	\$367,150	\$472,381

The accompanying Notes are an integral part of these Consolidated Financial Statements.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF MAJOR ACCOUNTING POLICIES

**Basis of Presentation.** Oceaneering International, Inc. ("Oceaneering," "we" or "us") has prepared these unaudited consolidated financial statements pursuant to instructions for quarterly reports on Form 10-Q, which we are required to file with the U.S. Securities and Exchange Commission (the "SEC"). These financial statements do not include all information and footnotes normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"). These financial statements reflect all adjustments that we believe are necessary to present fairly our financial position as of September 30, 2018 and our results of operations and cash flows for the periods presented. Except as otherwise disclosed herein, all such adjustments are of a normal and recurring nature. These financial statements should be read in conjunction with the consolidated financial statements and related notes included in our annual report on Form 10-K for the year ended December 31, 2017. The results for interim periods are not necessarily indicative of annual results.

**Principles of Consolidation.** The consolidated financial statements include the accounts of Oceaneering and our 50% or more owned and controlled subsidiaries. We also consolidate entities that are determined to be variable interest entities if we determine that we are the primary beneficiary; otherwise, we account for those entities using the equity method of accounting. We use the equity method to account for our investments in unconsolidated affiliated companies of which we own an equity interest of between 20% and 50% and as to which we have significant influence, but not control, over operations. We use the cost method for all other long-term investments. Investments in entities that we do not consolidate are reflected on our balance sheet in Other non-current assets. All significant intercompany accounts and transactions have been eliminated.

**Use of Estimates.** The preparation of financial statements in conformity with U.S. GAAP requires that our management make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenue and expense during the reporting period. Actual results could differ from those estimates.

**Cash and Cash Equivalents.** Cash and cash equivalents include demand deposits and highly liquid investments with original maturities of three months or less from the date of investment.

**Accounts Receivable – Allowances for Doubtful Accounts.** We determine the need for allowances for doubtful accounts using the specific identification method. We generally do not require collateral from our customers.

**Inventory.** Inventory is valued at the lower of cost or net realizable value. We determine cost using the weighted-average method.

**Property and Equipment and Long-Lived Intangible Assets.** We provide for depreciation of property and equipment on the straight-line method over their estimated useful lives. We charge the costs of repair and maintenance of property and equipment to operations as incurred, while we capitalize the costs of improvements that extend asset lives or functionality. Upon the disposition of property and equipment, the related cost and accumulated depreciation accounts are relieved and any resulting gain or loss is included as an adjustment to cost of services and products.

Intangible assets, primarily acquired in connection with business combinations, include trade names, intellectual property and customer relationships and are being amortized over their estimated useful lives.

We capitalize interest on assets where the construction period is anticipated to be more than three months. We capitalized \$1.9 million and \$1.1 million of interest in the three-month periods ended September 30, 2018 and 2017, respectively, and \$5.3 million and \$3.3 million of interest in the nine-month periods ended September 30, 2018 and 2017, respectively. We do not allocate general administrative costs to capital projects.

Our management periodically, and upon the occurrence of a triggering event, reviews the realizability of our property and equipment and long-lived intangible assets to determine whether any events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable. For long-lived assets to be held and used, we base our evaluation on impairment indicators, such as the nature of the assets, the future economic benefits of the assets, any historical or future profitability measurements and other external market conditions or factors that may be present. If such impairment indicators are present or other factors exist that indicate that the carrying amount of an asset may not



be recoverable, we determine whether an impairment has occurred through the use of an undiscounted cash flows analysis of the asset at the lowest level for which

6

---

## Table of Contents

identifiable cash flows exist. If an impairment has occurred, we recognize a loss for the difference between the carrying amount and the fair value of the asset. For assets held for sale or disposal, the fair value of the asset is measured using fair market value less estimated costs to sell. Assets are classified as held-for-sale when we have a plan for disposal of certain assets and those assets meet the held for sale criteria.

**Business Acquisitions.** We account for business combinations using the acquisition method of accounting, and, in each case, we allocate the acquisition price to the assets acquired and liabilities assumed based on their fair market values as of the date of acquisition.

In March 2018, we acquired Ecosse Subsea Limited (“Ecosse”) for \$68 million in cash. Headquartered in Aberdeen, Scotland, Ecosse builds and operates tools for seabed preparation, route clearance and trenching for the installation of submarine cables and pipelines. These services are offered on an integrated basis that includes vessels, ROVs and survey services. We have accounted for this acquisition by allocating the purchase price to the assets acquired and liabilities assumed based on their estimated fair values as of the date of acquisition. This purchase price allocation is preliminary and is subject to change upon completion of our valuation procedures. We have included Ecosse’s operations in our consolidated financial statements starting from the date of closing and its operating results are reflected in our Subsea Projects segment.

**Dispositions.** In September 2018, we consummated the sale of our cost method investment in ASV Global, LLC for \$15.1 million. The total consideration is subject to final working capital adjustments and customary holdbacks. The sale resulted in a pre-tax gain of \$9.3 million, which is reflected in Other income (expense), net in our Consolidated Statement of Operations for the three- and nine-month periods ended September 30, 2018

**Goodwill.** Annually, we are required to evaluate our goodwill by performing a qualitative or quantitative impairment test. Under the qualitative approach and after assessing the totality of events or circumstances, we determine that it is more likely than not the fair value of a reporting unit is less than its carrying amount, we are required to perform the quantitative analysis to determine the fair value. We tested the goodwill attributable to each of our reporting units for impairment as of December 31, 2017 and concluded that there was no impairment.

In addition to our annual evaluation of goodwill for impairment, upon the occurrence of a triggering event, we review our goodwill to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount.

**Foreign Currency Translation.** The functional currency for several of our foreign subsidiaries is the applicable local currency. Results of operations for foreign subsidiaries with functional currencies other than the U.S. dollar are translated into U.S. dollars using average exchange rates during the period. Assets and liabilities of these foreign subsidiaries are translated into U.S. dollars using the exchange rates in effect as of the balance sheet date, and the resulting translation adjustments are recognized, in accumulated other comprehensive income as a component of shareholders' equity. All foreign currency transaction gains and losses are recognized currently in the Consolidated Statements of Operations.

**Revenue Recognition.** On January 1, 2018, we adopted Accounting Standard Update (“ASU”) 2014-09, “Revenue from Contracts with Customers,” which implemented Accounting Standards Codification Topic 606 (“ASC 606”). We have used the modified retrospective method applied to those contracts which were not completed as of January 1, 2018, and have utilized the practical expedient to reflect the effect on contract modifications in the aggregate. The cumulative effect of applying ASC 606 has been recognized as an adjustment to retained earnings as of January 1, 2018. The comparative information with respect to prior periods has not been retrospectively restated and continues to be reported under the accounting standards in effect for those periods.



Table of Contents

The cumulative effect of the changes made to our Consolidated Balance Sheet as of January 1, 2018 for the adoption of ASC 606 was as follows:

(in thousands)	Dec 31, 2017	Adjustments Due to ASC 606	Jan 1, 2018 Under ASC 606
<b>Assets</b>			
Accounts receivable	\$476,903	\$(163,963 )	\$312,940
Contract assets	—	171,956	171,956
Total accounts receivable	476,903	7,993	484,896
Inventory	215,282	(34,187 )	181,095
<b>Liabilities</b>			
Accrued liabilities	350,258	(63,045 )	287,213
Contract liabilities	—	37,590	37,590
Total accrued liabilities	350,258	(25,455 )	324,803
Other long-term liabilities	131,323	(202 )	131,121
<b>Equity</b>			
Retained earnings	2,417,412	(537 )	2,416,875

In accordance with the ASC 606 requirements, the impact of adoption on carryover contracts on our Consolidated Statement of Operations and Consolidated Balance Sheet was as follows:

## Consolidated Statement of Operations

Nine Months Ended Sep 30, 2018

(in thousands)	As Reported Under ASC 606	Effect of Change	Balances Without Adoption of ASC 606
Revenue	\$1,414,387	\$12,552	\$1,426,939
Cost of services and products	1,318,196	14,042	1,332,238
Provision (benefit) for income taxes	70,317	(212 )	70,105
Net income (loss)	(148,188 )	(1,278 )	(149,466 )

## Consolidated Balance Sheet

(in thousands)	Sep 30, 2018 As Reported Under	Effect of Change	Balances Without Adoption
----------------	---	---------------------	---------------------------------

Edgar Filing: OCEANEERING INTERNATIONAL INC - Form 10-Q

	ASC 606		of ASC 606
<b>Assets</b>			
Accounts receivable	\$345,803	\$ —	\$345,803
Unbilled accounts receivable	—	221,657	221,657
Contract assets	233,402	(233,402)	—
Total accounts receivable	579,205	(11,745)	567,460
Inventory	189,119	19,359	208,478
<b>Liabilities</b>			
Accrued liabilities	338,272	(321 )	337,951
Contract liabilities	26,286	8,683	34,969
Total accrued liabilities	364,558	8,362	372,920
Other long-term liabilities	163,722	(10 )	163,712
<b>Equity</b>			
Retained earnings	2,268,687	(741 )	2,267,946

8

---

Table of Contents

All of our revenue is realized through contracts with customers. We recognize our revenue according to the contract type. On a daily basis, we recognize service revenue over time for contracts that provide for specific time, material and equipment charges, which we bill periodically, ranging from weekly to monthly. We use the input method to faithfully depict revenue recognition, because each day of service provided represents value to the customer. The performance obligations in these contracts are satisfied, and revenue is recognized, as the work is performed. We have used the expedient available to recognize revenue when the billing corresponds to the value realized by the customer where appropriate.

We account for significant fixed-price contracts, mainly relating to our Subsea Products segment, and to a lesser extent in our Subsea Projects and Advanced Technologies segments, by recognizing revenue over time using an input, cost-to-cost measurement percentage-of-completion method. We use the input cost-to-cost method to faithfully depict revenue recognition. This commonly used method allows appropriate calculation of progress on our contracts. A performance obligation is satisfied as we create a product on behalf of the customer over the life of the contract. The remainder of our revenue is recognized at the point in time when control transfers to the customer, thus satisfying the performance obligation.

We have elected to recognize the cost for freight and shipping as an expense when incurred. Taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction, that are collected by us from a customer, are excluded from revenue.

In our service-based business lines, which principally charge on a day rate basis for services provided, there is no significant impact in the pattern of revenue and profit recognition as a result of implementation of ASC 606. In our product-based business lines, we expect impacts on the pattern of our revenue and profit recognition in our contracts using the percentage-of-completion method, as a result of the requirement to exclude uninstalled materials and significant inefficiencies from the measure of progress. This is most likely to occur in our Subsea Products segment.

We apply judgment in the determination and allocation of transaction price to performance obligations, and the subsequent recognition of revenue, based on the facts and circumstances of each contract. We routinely review estimates related to our contracts and, where required, reflect revisions to profitability in earnings immediately. If an element of variable consideration has the potential for a significant future reversal of revenue, we will constrain that variable consideration to a level intended to remove the potential future reversal. If a current estimate of total contract cost indicates an ultimate loss on a contract, we recognize the projected loss in full when we determine it. In prior years, we have recorded adjustments to earnings as a result of revisions to contract estimates. We always strive to estimate our contract costs and profitability accurately. However, there could be significant adjustments to overall contract costs in the future, due to changes in facts and circumstances.

In general, our payment terms consist of those services billed regularly as provided and those products delivered at a point in time, which are invoiced after the performance obligation is satisfied. Our product and service contracts with milestone payments due at agreed progress points during the contract are invoiced when those milestones are reached, which may differ from the timing of revenue recognition. Our payment terms generally do not provide financing of contracts to customers, nor do we receive financing from customers as a result of these terms.

Please see Note 2 — "Revenue" — for more information on our revenue from contracts with customers.

New Accounting Standards. In January 2016, the Financial Accounting Standards Board ("FASB") issued ASU No. 2016-01, "Financial Instruments — Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities." This update:

requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value, with changes in fair value recognized in net income; and provides an expedient for the valuation and impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify value and impairment — when a qualitative assessment indicates that an impairment exists, an entity is required to measure the investment at fair value.

Table of Contents

ASU No. 2016-01 was effective for us beginning on January 1, 2018, and we have utilized the expedient for valuing equity investments without readily determinable fair values. This update has not had a material impact on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases," which requires reporting entities to separate the lease components from the non-lease components in a contract unless certain practical expedients are elected. This update also requires reporting entities to recognize lease assets and lease liabilities on the balance sheet for substantially all lease arrangements.

In July 2018, the FASB issued ASU No. 2018-011, an amendment to ASU 2016-02 (collectively, the "New Leases Standard"), which provides entities with an additional and optional transition method to adopt the new standard. The amendments in this ASU also provide lessors with a practical expedient to not separate nonlease components from associated lease component and to account for those components as a single component if the required conditions are met. We have evaluated the impact of this amendment on the financial statements. The New Leases Standard will become effective for us beginning January 1, 2019.

We intend to use the optional transition method that allows us to apply the New Leases Standard at the effective date prospectively without restating the prior periods presented. A cumulative-effect adjustment will be recognized to the opening balance of retained earnings in the period of adoption. We plan to elect the package of practical expedients that permit us to retain the identification and classification of leases under the previous accounting guidance, to keep the leases with an initial term of twelve months or less off the balance sheet, and to not separate nonlease components from associated lease components for both lessee and lessor leases.

We have identified that there will be a material increase in both assets and liabilities resulting from the adoption of the New Leases Standard, predominantly from real estate operating leases, which were not required to be recognized on the balance sheet under the previous lease standard. We will complete all of the required work to assess our position, create the necessary policy, procedures and controls and calculate the effect of applying the New Leases Standard at the date of initial application in line with the timeline and requirements of the standard.

In October 2016, the FASB issued ASU 2016-16, "Income Taxes (Topic 740) – Intra-Entity Transfers of Assets Other than Inventory." Previously, U.S. GAAP generally prohibited the recognition of current and deferred income taxes for an intra-entity asset transfer until the asset was sold to an outside party. The amendments in this update eliminate the exception for an intra-entity transfer of an asset other than inventory. Two common examples of assets included within the scope of this update are intellectual property and property, plant and equipment. The exception for an intra-entity transfer of inventory will remain in place. The amendments in this update were effective for us beginning January 1, 2018. This ASU has not had a material effect on our consolidated financial statements.

In February 2018, the FASB issued ASU 2018-02, "Income Statement – Reporting Comprehensive Income (Topic 220) Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." The amendments in this update allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the December 2017 enactment of U.S. tax reform legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). However, because the amendments only relate to the reclassification of the income tax effects of the Tax Act, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The amendments in this update also require certain disclosures about stranded tax effects. The amendments in this update will become effective for us beginning January 1, 2019, and early adoption is permitted. We do not anticipate that this ASU will have a material effect on our consolidated financial statements.



In June 2018, the FASB issued ASU 2018-07, "Compensation – Stock Compensation (Topic 718) Improvements to Nonemployee Share-Based Payment Accounting." This ASU expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. The amendments in this ASU will become effective for us beginning January 1, 2019, and early adoption is permitted. We do not anticipate that this ASU will have a material effect on our consolidated financial statements.

Table of Contents

## 2. Revenue

## Revenue By Category

The following table presents Revenue disaggregated by business segment, geographical region, and timing of transfer of goods or services.

(in thousands)	Three Months Ended			Nine Months Ended	
	Sep 30, 2018	Sep 30, 2017	Jun 30, 2018	Sep 30, 2018	Sep 30, 2017
<b>Business Segment:</b>					
Energy Services and Products					
Remotely Operated Vehicles	\$105,045	\$104,617	\$107,426	\$298,065	\$302,071
Subsea Products	137,099	143,583	121,704	385,491	469,115
Subsea Projects	104,972	80,116	78,036	239,868	218,617
Asset Integrity	62,346	61,098	67,422	191,056	171,948
Total Energy Services and Products	409,462	389,414	374,588	1,114,480	1,161,751
Advanced Technologies	109,838	86,706	104,086	299,907	275,581
Total	\$519,300	\$476,120	\$478,674	\$1,414,387	\$1,437,332
<b>Geographic</b>					
<b>Operating Areas:</b>					
Foreign:					
Africa	\$51,669	\$57,901	\$61,966	\$168,722	\$213,172
United Kingdom	56,769	48,074	50,999	153,087	189,534
Norway	51,952	54,412	51,827	142,820	128,965
Asia and Australia	39,764	50,407	43,448	122,158	147,555
Brazil	14,554	7,862	13,461	46,844	25,807
Other	45,898	23,192	14,811	80,348	54,540
Total Foreign	260,606	241,848	236,512	713,979	759,573
United States	258,694	234,272	242,162	700,408	677,759
Total	\$519,300	\$476,120	\$478,674	\$1,414,387	\$1,437,332

Sep 30,  
2018

Timing of Transfer of Goods or Services:	
Revenue recognized over time	\$1,297,095
Revenue recognized at a point in time	117,292
Total	\$1,414,387

## Contract Balances

Our contracts with milestone payments have, in the aggregate, a significant impact on the Contract asset and the Contract liability balances. Milestones are contractually agreed with customers and relate to significant events across the contract lives. Some milestones are achieved before revenue is recognized, resulting in a Contract liability, other milestones are achieved after revenue is recognized resulting in a Contract asset.

The following table provides information about Contract assets, and Contract liabilities from contracts with customers.

	Sep 30, 2018	Jan 1, 2018
Contract assets	\$ 233,402	\$ 171,956
Contract liabilities	26,286	37,590

## Table of Contents

Our payment terms consist of those services billed regularly as provided and those products delivered at a point in time, which are invoiced after the performance obligation is satisfied. Our product and service contracts with milestone payments due at agreed progress points during the contract are invoiced when those milestones are reached, which may differ from the timing of revenue recognition.

During the nine months ended September 30, 2018, Contract assets increased by \$61.4 million from its opening balance due to the revenue recognition of \$1.4 billion exceeding amounts billed of \$1.3 billion. Contract liabilities decreased \$11.3 million from its opening balance, due to revenue recognition of \$27.7 million less deferrals of milestone payments that totaled \$16.4 million. There were no cancellations, impairments or other significant impacts in the period that relate to other categories of explanation.

### Performance Obligations

As of September 30, 2018, the aggregate amount of the transaction price allocated to remaining performance obligations was \$276 million. We expect to recognize revenue for the remaining performance obligations of \$223 million over the next twelve months.

The aggregate amount of transaction price allocated to remaining performance obligations that were unsatisfied (or partially unsatisfied) as of September 30, 2018 are noted above. In arriving at this value, we have used two expedients available to us and are not disclosing amounts in relation to performance obligations: (1) that are part of contracts with an original expected duration of one year or less; or (2) on contracts where we recognize revenue in line with the billing.

Due to the nature of our service contracts in our Remotely Operated Vehicle, Subsea Projects, Asset Integrity and Advanced Technologies segments, the majority of our contracts either have initial contract terms of one year or less or have customer option cancellation clauses that lead us to consider the original expected duration of one year or less.

In our Subsea Products and Advanced Technologies segments, we have long-term contracts that extend beyond one year, and these make up the majority of the balance reported. We also have shorter-term product contracts with an expected original duration of one year or less that have been excluded.

Where appropriate, we have made estimates within the transaction price of elements of variable consideration within the contracts and constrained those amounts to a level where we consider that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. The amount of revenue recognized in the nine months ended September 30, 2018, which was associated with performance obligations completed or partially completed in prior periods was not significant.

As of September 30, 2018, there was no outstanding liability balance for refunds or returns due to the nature of our contracts and the services and products we provide. Our warranties are limited to assurance warranties that are of a standard length and are not considered to be a material right. The majority of our contracts consist of a single performance obligation. When there are multiple obligations, we look for observable evidence of stand-alone selling prices on which to base the allocation. This involves judgment as to the appropriateness of the observable evidence relating to the facts and circumstances of the contract. If we do not have observable evidence, we estimate stand-alone selling prices by taking a cost plus margin approach, using typical margins from the type of service or product, customer and regional geography involved.

### Costs to Obtain or Fulfill a Contract

In line with the available expedient, we capitalize costs to obtain a contract when those amounts are significant and the contract is expected at inception to exceed one year in duration; otherwise, the costs are expensed in the period when incurred. Costs to obtain a contract primarily consist of bid and proposal costs, which are incremental to our fixed costs. There was no balance or amortization of Costs to obtain a contract in the current reporting period.

Costs to fulfill a contract primarily consist of certain mobilization costs incurred to provide services or products to our customers. These costs are deferred and amortized over the period of contract performance. The closing balance of Costs to fulfill a contract as of September 30, 2018 was \$12.7 million, with \$2.6 million and \$5.1 million

Table of Contents

of amortization for the three- and nine-month periods ended September 30, 2018, respectively. No impairment costs were recognized.

## 3. INVENTORY

The following is information regarding our inventory:

(in thousands)	Sep 30, 2018	Dec 31, 2017
Inventory, net:		
Remotely operated vehicle parts and components	\$105,956	\$97,313
Other inventory, primarily raw materials	83,163	117,969
Total	\$189,119	\$215,282

## 4. DEBT

Long-term Debt consisted of the following:

(in thousands)	Sep 30, 2018	Dec 31, 2017
4.650% Senior		
Notes due 2024	\$500,000	\$500,000
6.000% Senior		
Notes due 2028	300,000	—
Term Loan Facility	—	300,000
Fair value of interest rate swaps on \$200 million of principal	(9,717 )	(2,990 )
Unamortized debt issuance costs	(8,093 )	(4,698 )
Revolving Credit Facility	—	—
Long-term Debt	\$782,190	\$792,312

In November 2014, we completed the public offering of \$500 million aggregate principal amount of 4.650% Senior Notes due 2024 (the "2024 Senior Notes"). We pay interest on the 2024 Senior Notes on May 15 and November 15 of each year. The 2024 Senior Notes are scheduled to mature on November 15, 2024.

In February 2018, we completed the public offering of \$300 million aggregate principal amount of 6.000% Senior Notes due 2028 (the "2028 Senior Notes"). We will pay interest on the 2028 Senior Notes on February 1 and August 1 of each year, beginning on August 1, 2018. The 2028 Senior Notes are scheduled to mature on February 1, 2028.

We may redeem some or all of the 2024 Senior Notes and the 2028 Senior Notes (collectively, the "Senior Notes") at specified redemption prices. We used the net proceeds from the 2028 Senior Notes to repay our term loan indebtedness described further below.

In October 2014, we entered into a credit agreement (as amended, the "Credit Agreement") with a group of banks. The Credit Agreement provided for a \$500 million five-year revolving credit facility (the "Revolving Credit Facility"). Subject to certain conditions, the aggregate commitments under the Revolving Credit Facility may be increased by up to \$300 million at any time upon agreement between us and existing or additional lenders. Borrowings under the Revolving Credit Facility may be used for general corporate purposes. The Credit Agreement also provided for a \$300 million term loan (the "Term Loan Facility"), which we repaid in full in February 2018, using net proceeds from the issuance of our 2028 Senior Notes referred to above, and cash on hand.

In February 2018, we entered into Agreement and Amendment No. 4 to the Credit Agreement ("Amendment No. 4"). Amendment No. 4 amended the Credit Agreement to, among other things, extend the maturity of the Revolving Credit Facility to January 25, 2023 with the extending Lenders, which represent 90% of the existing commitments of the Lenders, such that the total commitments for the Revolving Credit Facility will be \$500 million until October 25, 2021, and thereafter \$450 million until January 25, 2023.

## Table of Contents

Borrowings under the Revolving Credit Facility bear interest at an Adjusted Base Rate or the Eurodollar Rate (both as defined in the Credit Agreement), at our option, plus an applicable margin based on our Leverage Ratio (as defined in the Credit Agreement) and, at our election, based on the ratings of our senior unsecured debt by designated ratings services, thereafter to be based on such debt ratings. The applicable margin varies: (1) in the case of advances bearing interest at the Adjusted Base Rate, from 0.125% to 0.750% for borrowings under the Revolving Credit Facility; and (2) in the case of advances bearing interest at the Eurodollar Rate, from 1.125% to 1.750%. The Adjusted Base Rate is the highest of (1) the per annum rate established by the administrative agent as its prime rate, (2) the federal funds rate plus 0.50% and (3) the daily one-month LIBOR plus 1%. We pay a commitment fee ranging from 0.125% to 0.300% on the unused portion of the Revolving Credit Facility, depending on our Leverage Ratio. The commitment fees are included as interest expense in our consolidated financial statements.

The Credit Agreement contains various covenants that we believe are customary for agreements of this nature, including, but not limited to, restrictions on our ability and the ability of each of our subsidiaries to incur debt, grant liens, make certain investments, make distributions, merge or consolidate, sell assets and enter into certain restrictive agreements. We are also subject to a maximum adjusted total Capitalization Ratio (as defined in the Credit Agreement) of 55%. The Credit Agreement includes customary events of default and associated remedies. As of September 30, 2018, we were in compliance with all the covenants set forth in the Credit Agreement.

We have two interest rate swaps in place on a total of \$200 million of the 2024 Senior Notes for the period to November 2024. Please refer to Note 5 — "Commitments and Contingencies" — for more information on our interest rate swaps.

We incurred \$6.9 million and \$4.2 million of issuance costs related to the 2024 Senior Notes and the 2028 Senior Notes, respectively, and \$2.6 million of loan costs, including costs of the amendments prior to Amendment No. 4, related to the Credit Agreement. The costs, net of accumulated amortization, are included as a reduction of Long-term Debt in our Consolidated Balance Sheet, as it pertains to the Senior Notes, and in Other non-current assets, as it pertains to the Credit Agreement. We are amortizing these costs to Interest expense through the maturity date for the Senior Notes and to January 2023 for the Credit Agreement.

## 5. COMMITMENTS AND CONTINGENCIES

**Litigation.** In the ordinary course of business, we are subject to actions for damages alleging personal injury under the general maritime laws of the United States, including the Jones Act, for alleged negligence. We report actions for personal injury to our insurance carriers and believe that the settlement or disposition of those claims will not have a material adverse effect on our consolidated financial position, results of operations or cash flows.

Various other actions and claims are pending against us, most of which are covered by insurance. Although we cannot predict the ultimate outcome of these matters, we believe that our ultimate liability, if any, that may result from these other actions and claims will not materially affect our results of operations, cash flows or financial position.

**Financial Instruments and Risk Concentration.** In the normal course of business, we manage risks associated with foreign exchange rates and interest rates through a variety of strategies, including the use of hedging transactions. As a matter of policy, we do not use derivative instruments unless we have an underlying exposure. Other financial instruments that potentially subject us to concentrations of credit risk are principally cash and cash equivalents and accounts receivable.

The carrying values of cash and cash equivalents approximate their fair values due to the short-term maturity of the underlying instruments. Accounts receivable are generated from a broad group of customers, primarily from within



the energy industry, which is our major source of revenue. Due to their short-term nature, carrying values of our accounts receivable and accounts payable approximate fair market values.

We estimated the aggregate fair market value of the Senior Notes to be \$790 million as of September 30, 2018, based on quoted prices. Since the market for the Senior Notes is not an active market, the fair value of the Senior Notes is classified within Level 2 in the fair value hierarchy under U.S. GAAP (inputs other than quoted prices in active markets for similar assets and liabilities that are observable or can be corroborated by observable market data for substantially the full terms for the assets or liabilities).

Table of Contents

We have two interest rate swaps in place on a total of \$200 million of the 2024 Senior Notes for the period to November 2024. The agreements swap the fixed interest rate of 4.650% on \$100 million of the 2024 Senior Notes to the floating rate of one month LIBOR plus 2.426% and on another \$100 million to one month LIBOR plus 2.823%. We estimate the combined fair value of the interest rate swaps to be a net liability of \$9.7 million as of September 30, 2018, which is included on our balance sheet in our Other Long-term Liabilities. These values were arrived at based on a discounted cash flow model using Level 2 inputs.

Since the second quarter of 2015, the exchange rate for the Angolan kwanza relative to the U.S. dollar generally has been declining, although the exchange rate was relatively stable during 2017. As our functional currency in Angola is the U.S. dollar, we recorded foreign currency transaction losses related to the kwanza of \$4.5 million and \$16.9 million in the three- and nine-month periods ended September 30, 2018, respectively, as a component of Other income (expense), net in our Consolidated Statements of Operations for those respective periods. Our foreign currency transaction gains or losses are related primarily to the remeasurement of our Angolan kwanza cash balances to U.S. dollars. Any conversion of cash balances from kwanza is controlled by the central bank in Angola, and the central bank slowed this process from mid-2015 to 2017, causing our kwanza cash balances to increase during that period of time. However, beginning in 2018, the Angolan central bank has allowed us to repatriate cash from Angola. Through September 30, 2018, we were able to repatriate \$57 million of cash from Angola. As of September 30, 2018 and December 31, 2017, we had the equivalent of approximately \$14 million and \$27 million of kwanza cash balances, respectively, in Angola reflected on our balance sheet. The decrease in kwanza cash balances in 2018 was mainly attributable to the repatriation of cash from Angola and cash used in our Angolan operations. Since December 31, 2017, Angola has devalued its currency by almost 75%. We will incur further foreign currency exchange losses in Angola if further currency devaluations occur.

To mitigate our currency exposure risk in Angola, we have used kwanza to purchase equivalent Angolan central bank (Banco Nacional de Angola) bonds. The bonds are denominated as U.S. dollar equivalents, so that, upon payment of semi-annual interest and principal upon maturity, payment is made in kwanza, equivalent to the respective U.S. dollars at the then-current exchange rate. Our intention was to hold the bonds to maturity, and to reinvest funds from maturing bonds in similar long-term assets. We previously believed the chance of selling the bonds before maturity and repatriating cash out of Angola was remote. In the second quarter of 2018, \$10 million of bonds matured, and the proceeds were reinvested by us in similar long-term assets. Additionally, we sold \$52 million of bonds prior to their maturity date through September 30, 2018. Because we intend to sell the bonds if we are able to repatriate the proceeds, we changed our accounting for these bonds from held-to-maturity securities to available-for-sale securities. As of September 30, 2018, we classified \$3 million of bonds due to mature in the next twelve months as Other current assets and \$15 million of bonds due to mature after twelve months as Other non-current assets on our Consolidated Balance Sheet, with \$5 million maturing in 2020 and \$10 million maturing in 2023.

We estimated the fair market value of the Angolan bonds to be approximately \$18 million as of September 30, 2018 using quoted prices. Since the market for the Angolan bonds is not an active market, the fair value of the Angolan bonds is classified within Level 2 in the fair value hierarchy under U.S. GAAP. As of September 30, 2018, we have not recorded the difference between the fair market value and carrying amount of the outstanding bonds through the Consolidated Statement of Comprehensive Income (Loss) due to the insignificance of the difference between the fair market value and the carrying amount of the bonds.

**6. EARNINGS (LOSS) PER SHARE, SHARE-BASED COMPENSATION AND SHARE REPURCHASE PLAN**  
Earnings per Share. For each period presented, the only difference between our calculated weighted average basic and diluted number of shares outstanding is the effect of outstanding restricted stock units. In periods where we have a net loss, the effect of our outstanding restricted stock units is anti-dilutive, and therefore does not increase our diluted shares outstanding.

Edgar Filing: OCEANEERING INTERNATIONAL INC - Form 10-Q

For each period presented, our net income (loss) allocable to both common shareholders and diluted common shareholders is the same as our net income (loss) in our consolidated statements of operations.

Dividends. From the second quarter of 2014 through the third quarter of 2016, we paid a quarterly dividend to our common shareholders of \$0.27 per share. Starting in the fourth quarter of 2016 through the third quarter of 2017,

15

---

## Table of Contents

we paid a dividend of \$0.15 per share. Our last quarterly dividend was \$0.15 per share and was declared in July 2017 and was paid in September 2017.

**Share-Based Compensation.** We have no outstanding stock options and, therefore, no share-based compensation to be recognized pursuant to stock option grants.

During 2016, 2017 and through June 30, 2018, we granted restricted units of our common stock to certain of our key executives and employees. During 2016 through 2018, our Board of Directors granted restricted common stock to our nonemployee directors. The restricted units granted to our key executives and key employees generally vest in full on the third anniversary of the award date, conditional on continued employment. The restricted stock unit grants can vest pro rata over three years, provided the individual meets certain age and years-of-service requirements. The shares of restricted common stock we grant to our non-employee directors vest in full on the first anniversary of the award date, conditional upon continued service as a director. Each grantee of shares of restricted stock is deemed to be the record owner of those shares during the restriction period, with the right to vote and receive any dividends on those shares. The restricted stock units outstanding have no voting or dividend rights.

For each of the restricted stock units granted in 2016 through September 30, 2018, at the earlier of three years after grant or at termination of employment or service, the grantee will be issued one share of our common stock for each unit vested. As of September 30, 2018 and December 31, 2017, respective totals of 1,474,642 and 1,181,805 shares of restricted stock or restricted stock units were outstanding.

We estimate that share-based compensation cost not yet recognized related to shares of restricted stock or restricted stock units, based on their grant-date fair values, was \$13 million as of September 30, 2018. This expense is being recognized on a staged-vesting basis over three years for awards attributable to individuals meeting certain age and years-of-service requirements, and on a straight-line basis over the applicable vesting period of one or three years for the other awards.

**Share Repurchase Plan.** In December 2014, our Board of Directors approved a plan to repurchase up to 10 million shares of our common stock. Under this plan, in 2015, we had repurchased 2.0 million shares of our common stock for \$100 million. We did not repurchase any shares during 2016 through through September 30, 2018. We account for the shares we hold in treasury under the cost method, at average cost.

## 7. INCOME TAXES

In December 2017, the United States enacted the the Tax Act, which included a number of changes to existing U.S. tax laws that have an impact on our income tax provision, most notably a reduction of the U.S. corporate income tax rate from 35 percent to 21 percent for tax years beginning after December 31, 2017, and the creation of a territorial tax system with a one-time mandatory tax on applicable previously deferred earnings of foreign subsidiaries. We recognized the income tax effects of the Tax Act in our financial statements for the year ended December 31, 2017 in accordance with Staff Accounting Bulletin No. 118 (“SAB 118”), which provided SEC staff guidance for the application of accounting standards for income taxes in the reporting period in which the Tax Act was enacted. As such, our financial results reflected provisional amounts for those specific income tax effects of the Tax Act for which the accounting was incomplete but a reasonable estimate could be determined. The final determination is expected to be completed and reflected in our financial statements issued for subsequent reporting periods that fall within the measurement period contemplated by SAB 118.

During the second quarter of 2018, the United States Internal Revenue Service issued Notice 2018-26, announcing its intent to issue regulations related to the application of the Section 965 one-time mandatory tax on applicable previously deferred earnings of foreign subsidiaries and potential anti-avoidance measures. Subsequently, on August 1, 2018, the United States Internal Revenue Service issued Proposed Regulations providing guidance regarding Section 965 of the Internal Revenue Code as amended by the Tax Act. We have included the provisional impact of the proposed regulations in our third quarter 2018 tax expense.

During interim periods, we provide for income taxes based on our current estimated annual effective tax rate using assumptions as to (1) earnings and other factors that would affect the tax provision for the remainder of the year and (2) the operations of foreign branches and subsidiaries that are subject to local income and withholding taxes. In the

three-month period ended September 30, 2018, we recognized additional tax expense of \$56.5 million for discrete items, primarily related to \$39.1 million of valuation allowances on certain deferred tax assets recognized in prior years that may not be realizable in certain foreign jurisdictions, \$7.9 million of provisional tax related to the Tax

Table of Contents

Act, \$3.6 million related to uncertain tax positions and \$5.9 million associated with various other issues. In the nine-month period ended September 30, 2018, we recognized additional tax expense of \$60.1 million for discrete items, primarily related to \$39.1 million of valuation allowances on certain deferred tax assets recognized in prior years that may not be realizable in certain foreign jurisdictions, \$7.9 million of provisional tax related to the Tax Act, \$4.8 million related to uncertain tax positions and \$8.3 million associated with various other issues.

The effective tax rate for the nine months ended September 30, 2018 was different from the federal statutory rate of 21.0%, primarily due to the geographic mix of operating revenue and results that generated taxes in certain jurisdictions that exceeded the tax benefit from losses and credits in other jurisdictions, and the discrete items discussed above. We will continue to evaluate the realizability of our recorded deferred tax assets. It is our intention to continue to indefinitely reinvest in certain of our international operations; therefore, we do not provide withholding taxes on the possible distribution of these earnings. We do not believe the effective tax rate before discrete items is meaningful, as current conditions do not allow for relevant guidance in this regard.

The effective tax rate for the nine months ended September 30, 2017 was lower than the federal statutory rate of 35.0%, primarily due to our intention to indefinitely reinvest in certain of our international operations, partially offset by a discrete tax item associated with share-based compensation. In 2017, we did not provide for U.S. taxes on the portion of our foreign earnings that we deemed indefinitely reinvested.

We conduct our international operations in a number of locations that have varying laws and regulations with regard to income and other taxes, some of which are subject to interpretation. We recognize the benefit for a tax position if the benefit is more likely than not to be sustainable upon audit by the applicable taxing authority. If this threshold is met, the tax benefit is then measured and recognized at the largest amount that we believe is greater than 50% likely of being realized upon ultimate settlement. We do not believe that the total of unrecognized tax benefits will increase or decrease significantly in the next twelve months.

We account for any applicable interest and penalties on uncertain tax positions as a component of our provision for income taxes on our financial statements. Through September 30, 2018, we have \$10.4 million accrued in Other Long-term Liabilities for uncertain tax positions. Any additions or reductions to those liabilities would affect our effective income tax rate in the periods of change.

Our tax returns are subject to audit by taxing authorities in multiple jurisdictions. These audits often take years to complete and settle. The following lists the earliest tax years open to examination by tax authorities where we have significant operations:

Jurisdiction	Periods
United States	2014
United Kingdom	2015
Norway	2015
Angola	2013
Brazil	2013
Australia	2013

## 8. BUSINESS SEGMENT INFORMATION

We are a global provider of engineered services and products, primarily to the offshore energy industry. Through the use of our applied technology expertise, we also serve the defense, aerospace and commercial theme park industries. Our Energy Services and Products business consists of Remotely Operated Vehicles ("ROVs"), Subsea Products, Subsea Projects and Asset Integrity. Our ROV segment provides submersible vehicles operated from the surface to support offshore energy exploration, development and production activities. Our Subsea Products segment supplies a variety of specialty subsea hardware and related services. Our Subsea Projects segment provides multiservice subsea

support vessels and offshore diving and support vessel operations, primarily for inspection, maintenance and repair and installation activities. We have also provided survey, autonomous underwater vehicle and satellite-positioning services. Our Asset Integrity segment provides asset integrity management and assessment services, nondestructive testing and inspection. Our Advanced Technologies business provides project management, engineering services and equipment for applications in non-energy

Table of Contents

industries. Unallocated Expenses are those not associated with a specific business segment. These consist of expenses related to our incentive and deferred compensation plans, including restricted stock and bonuses, as well as other general expenses, including corporate administrative expenses.

There are no differences in the basis of segmentation or in the basis of measurement of segment profit or loss from those used in our consolidated financial statements for the year ended December 31, 2017.



Table of Contents

The table that follows presents Revenue, Income (Loss) from Operations and Depreciation and Amortization by business segment for each of the periods indicated.

(in thousands)	Three Months Ended			Nine Months Ended	
	Sep 30, 2018	Sep 30, 2017	Jun 30, 2018	Sep 30, 2018	Sep 30, 2017
<b>Revenue</b>					
<b>Energy Services and Products</b>					
Remotely Operated Vehicles	\$ 105,045	\$ 104,617	\$ 107,426	\$ 298,065	\$ 302,071
Subsea Products	137,099	143,583	121,704	385,491	469,115
Subsea Projects	104,972	80,116	78,036	239,868	218,617
Asset Integrity	62,346	61,098	67,422	191,056	171,948
Total Energy Services and Products	409,462	389,414	374,588	1,114,480	1,161,751
Advanced Technologies	109,838	86,706	104,086	299,907	275,581
Total	\$ 519,300	\$ 476,120	\$ 478,674	\$ 1,414,387	\$ 1,437,332
<b>Income (Loss) from Operations</b>					
<b>Energy Services and Products</b>					
Remotely Operated Vehicles	\$ 772	\$ 5,009	\$ 4,542	\$ 2,916	\$ 21,310
Subsea Products	5,367	12,383	2,295	9,417	34,418
Subsea Projects	6,088	6,512	(10,358 )	(6,629 )	9,699
Asset Integrity	2,275	3,050	3,357	7,311	9,072
Total Energy Services and Products	14,502	26,954	(164 )	13,015	74,499
Advanced Technologies	8,960	6,602	7,886	18,514	19,260
Unallocated Expenses	(25,014 )	(23,025 )	(27,359 )	(79,867 )	(73,988 )
Total	\$(1,552 )	\$ 10,531	\$(19,637 )	\$(48,338 )	\$ 19,771
<b>Depreciation and Amortization</b>					
<b>Energy Services and Products</b>					
Remotely Operated Vehicles	\$ 27,428	\$ 28,269	\$ 28,269	\$ 83,339	\$ 86,534
Subsea Products	12,349	13,340	14,914	41,288	39,124
Subsea Projects	7,464	7,881	13,053	28,830	23,742
Asset Integrity	1,635	2,139	1,836	5,319	5,379
Total Energy Services and Products	48,876	51,629	58,072	158,776	154,779
Advanced Technologies	792	796	737	2,295	2,377
Unallocated Expenses	1,035	1,088	1,034	3,603	3,324
Total	\$ 50,703	\$ 53,513	\$ 59,843	\$ 164,674	\$ 160,480

We determine Income (Loss) from Operations for each business segment before interest income or expense, Other income (expense) and Provision for income taxes. We do not consider an allocation of these items to be practical. Our Equity in earnings (losses) of unconsolidated affiliates is part of our Subsea Projects segment.

Table of Contents

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

Certain statements we make in this quarterly report on Form 10-Q are forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements include, without limitation, statements regarding our expectations about:

fourth quarter and the full year of 2018 operating results and the contributions from our segments to those results (including the expected benefits from the acquisition of Ecosse Subsea Limited, anticipated revenue, operating income or loss, and utilization information), as well as the items below the operating income (loss) line;

- our cash flows and earnings before interest, taxes and depreciation and amortization (EBITDA) in 2018;
- future demand, business activity levels, industry conditions and contract awards during the remainder of 2018;
- long-term industry fundamentals and recovery, and the higher level of activity being required before prices for our services and products can be increased enough to generate satisfactory returns;
- 2019 outlook and increased activity levels in each of our segments;
- our plans for future operations (including planned additions to and retirements from our remotely operated vehicle ("ROV") fleet, our intent regarding the new multiservice subsea support vessel scheduled for delivery at the end of 2018 and expected to be placed into service during the first quarter of 2019 and other capital expenditures);
- our future dividends;
- the adequacy of our liquidity, cash flows and capital resources;
- our ability and intent to redeem Angolan bonds and repatriate cash;
- shares to be repurchased under our share repurchase plan;
- our estimated effective tax rate and the cash tax implications of our tax provision for discrete items in the foreseeable future;
- the implementation of new accounting standards and related policies, procedures and controls; and
- seasonality.

These forward-looking statements are subject to various risks, uncertainties and assumptions, including those we have referred to under the headings "Risk Factors" and "Cautionary Statement Concerning Forward-Looking Statements" in Part I of our annual report on Form 10-K for the year ended December 31, 2017. Although we believe that the expectations reflected in such forward-looking statements are reasonable, because of the inherent limitations in the forecasting process, as well as the relatively volatile nature of the industries in which we operate, we can give no assurance that those expectations will prove to have been correct. Accordingly, evaluation of our future prospects must be made with caution when relying on forward-looking information.

The following discussion should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in our annual report on Form 10-K for the year ended December 31, 2017.

Executive Overview

Our diluted loss per share for the three- and nine-month periods ended September 30, 2018 were \$(0.67) and \$(1.50), respectively, compared to \$(0.02) and \$(0.07) for the corresponding periods of the prior year. 2018 results included the impact of certain tax adjustments and the after-tax effects of a gain realized on the sale of a cost method investment, both predominantly in the third quarter of 2018, as well as foreign currency exchange losses. Our operating results for nine-month period ended September 30, 2018 also included the write-offs of certain equipment and intangible assets associated with exiting the land survey business and equipment obsolescence that occurred in the second quarter of 2018.

Our third quarter 2018 operating results improved significantly compared to the second quarter of 2018. Each of our operating segments was profitable, led by favorable profit contributions from Subsea Projects and Subsea Products, partially offset by lower profitability in our ROV segment. Additionally, we had lower Unallocated Expenses and the absence of the write-offs of certain equipment and intangible assets which occurred in the second quarter of 2018,

For the fourth quarter of 2018, compared to the third quarter, we believe our operating results will be lower due to the onset of seasonality leading to reduced levels of offshore energy activity. Sequentially, we expect lower

## Table of Contents

operating income from each of our energy segments, with most of the decline expected to be in our Subsea Products and Subsea Projects segments. Additionally, in our Subsea Products segment, we are expecting an unfavorable impact at our manufacturing facility in Panama City, Florida, due to damage caused by Hurricane Michael in mid-October of 2018. For our non-energy segment, Advanced Technologies, we are projecting a quarterly improvement in operating income. Unallocated Expenses are expected to be in the upper-\$20 million range.

For the full year of 2018, we continue to expect each of our operating segments will contribute positive EBITDA.

Below the operating income (loss) line, we expect:

- increased interest expense from higher overall interest rates, which affect our floating rate debt and our swaps to floating rates on \$200 million of fixed-rate debt; and
- a loss on our equity investment in Medusa Spar LLC, as volume continues to be low in current producing zones.

We are encouraged that the long-term fundamentals for the offshore energy industry have stabilized and we believe that we are now in the early stages of a recovery in activity in general, and in our businesses. We expect that a recovery will take time, and only after a sustained higher level of activity can the prices for our services and products be increased enough to generate satisfactory returns.

Accordingly, looking into 2019, we are projecting increased activity levels in each of our segments, likely led by revenue gains in our Subsea Products manufacturing business unit. However, the pace of recovery is still difficult to determine, and at this time we are not prepared to offer more detailed guidance on 2019.

## Critical Accounting Policies and Estimates

For information about our Critical Accounting Policies and Estimates, please refer to the discussion in our annual report on Form 10-K for the year ended December 31, 2017 under the heading "Critical Accounting Policies and Estimates" in Item 7 – "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Effective January 1, 2018, we adopted Accounting Standards Codification Topic 606, "Revenue from Contracts with Customers." See Notes 1 and 2 of Notes to Consolidated Financial Statements included in this report for further details, including our accounting policy for Revenue Recognition under this newly adopted accounting standard.

## Liquidity and Capital Resources

As of September 30, 2018, we had working capital of \$714 million, including \$367 million of cash and cash equivalents. Additionally, Amendment No. 4 to the Credit Agreement (as defined below) provides for a \$500 million revolving credit facility until October 25, 2021 and thereafter \$450 million until January 25, 2023 with a group of banks. We consider our liquidity, cash flows and capital resources to be adequate to support our existing operations and capital commitments.

Our capital expenditures were \$152 million during the first nine months of 2018, including the \$68 million purchase price for the acquisition of Ecosse Subsea Limited ("Ecosse"), as compared to \$71 million in the first nine months of 2017, including \$11 million for a business acquisition. We acquired Ecosse in March 2018, reflecting our commitment to expand our service line capabilities, grow our market position within the offshore renewable energy market, and provide our customers with proven tools to optimize installation projects. Ecosse builds and operates tools for seabed preparation, route clearance and trenching for the installation of submarine cables and pipelines. These services are offered on an integrated basis that includes vessels, ROVs and survey services. The operating results are reflected in our Subsea Projects segment.

We currently estimate our capital expenditures for 2018, excluding business acquisitions, will be in the range of \$100 million to \$140 million, which includes approximately \$40 million to \$50 million of maintenance capital expenditures and \$60 million to \$90 million of growth capital expenditures. We expect to spend \$20 million in our Subsea Projects segment to complete the new-build multiservice subsea support vessel Ocean Evolution, scheduled for delivery at the end of 2018 and expected to be placed into service during the first quarter of 2019.

Table of Contents

The Ocean Evolution is intended to be U.S.-flagged and documented with a coastwise endorsement by the U.S. Coast Guard. It is expected to have an overall length of 353 feet, a Class 2 dynamic positioning system, accommodations for 110 personnel, a helideck, a 250-ton active heave-compensated crane, and a working moonpool. We expect to outfit the vessel with two of our high specification 4,000 meter work-class ROVs. The vessel will also be equipped with a satellite communications system capable of transmitting streaming video for real-time work observation by shore-based personnel. We anticipate the vessel will be used to augment our ability to provide subsea intervention services in the U.S. Gulf of Mexico. These services are required to perform inspection, maintenance and repair projects and hardware installations.

We previously had several deepwater vessels under long-term charter. The last of our long-term deepwater vessel charters expired in March 2018. With the current market conditions, we attempt to charter vessels for specific projects on a back-to-back basis with the vessel owners. We also charter vessels on a short-term basis as necessary to augment our fleet.

In Angola, the Ocean Intervention III ended its work scope for our customer on July 31, 2018, under the field support vessel services contract. At the conclusion of the vessel work, the vessel was returned to the owner. Pursuant to our contract for field support services, we continue to supply project management and engineering services to the customer through January 2019.

As of September 30, 2018, we had long-term debt in the principal amount of \$800 million outstanding and \$500 million available under our revolving credit facility provided for under the Credit Agreement. None of our outstanding debt is scheduled to mature before November 2024.

In October 2014, we entered into a credit agreement (as amended, the "Credit Agreement") with a group of banks. The Credit Agreement provided for a \$500 million five-year revolving credit facility (the "Revolving Credit Facility"). Subject to certain conditions, the aggregate commitments under the Revolving Credit Facility may be increased by up to \$300 million at any time upon agreement between us and existing or additional lenders. Borrowings under the Revolving Credit Facility may be used for general corporate purposes. The Credit Agreement also provided for a \$300 million term loan, which we repaid in full in February 2018, using net proceeds from the issuance of our 6.000% Senior Notes due 2028 (the "2028 Senior Notes") described further below, and cash on hand.

In February 2018, we entered into Agreement and Amendment No. 4 to the Credit Agreement ("Amendment No. 4"). Amendment No. 4 amended the Credit Agreement to, among other things, extend the maturity of the Revolving Credit Facility to January 25, 2023 with the extending Lenders, which represent 90% of the existing commitments of the Lenders, such that the total commitments for the Revolving Credit Facility will be \$500 million until October 25, 2021, and thereafter \$450 million until January 25, 2023.

Borrowings under the Credit Agreement bear interest at an Adjusted Base Rate or the Eurodollar Rate (both as defined in the Credit Agreement), at our option, plus an applicable margin based on our Leverage Ratio (as defined in the Credit Agreement) and, at our election, based on the ratings of our senior unsecured debt by designated ratings services, thereafter to be based on such debt ratings. The applicable margin varies: (1) in the case of advances bearing interest at the Adjusted Base Rate, from 0.125% to 0.750%; and (2) in the case of advances bearing interest at the Eurodollar Rate, from 1.125% to 1.750%. The Adjusted Base Rate is the highest of (1) the per annum rate established by the administrative agent as its prime rate, (2) the federal funds rate plus 0.50% and (3) the daily one-month LIBOR plus 1%. We pay a commitment fee ranging from 0.125% to 0.300% on the unused portion of the Revolving Credit Facility, depending on our Leverage Ratio. The commitment fees are included as interest expense in our consolidated financial statements.

The Credit Agreement contains various covenants that we believe are customary for agreements of this nature, including, but not limited to, restrictions on our ability and the ability of each of our subsidiaries to incur debt, grant liens, make certain investments, make distributions, merge or consolidate, sell assets and enter into certain restrictive agreements. We are also subject to a maximum adjusted total Capitalization Ratio (as defined in the Credit Agreement) of 55%. The Credit Agreement includes customary events of default and associated remedies. As of September 30, 2018, we were in compliance with all the covenants set forth in the Credit Agreement.

In November 2014, we completed the public offering of \$500 million aggregate principal amount of 4.650% due 2024 (the "2024 Senior Notes"). We pay interest on the 2024 Senior Notes on May 15 and November 15 of each year. The 2024 Senior Notes are scheduled to mature on November 15, 2024.

Table of Contents

In February 2018, we completed the public offering of the 2028 Senior Notes. We pay interest on the 2028 Senior Notes on February 1 and August 1 of each year, beginning on August 1, 2018. The 2028 Senior Notes are scheduled to mature on February 1, 2028. We may redeem some or all of the 2024 Senior Notes and 2028 Senior Notes at specified redemption prices.

Our principal source of cash from operating activities is our net income (loss), adjusted for the non-cash effects of, among other things, depreciation and amortization, deferred income taxes and noncash compensation under our share-based compensation plans. Our \$36 million and \$144 million of cash provided from operating activities in the nine-month periods ended September 30, 2018 and 2017, respectively, were principally affected by operating results and cash increases (decreases) of:

\$(85) million and \$26 million, respectively, from changes in accounts receivable;  
\$(7) million and \$35 million, respectively, from changes in inventory; and  
\$61 million and \$(56) million, respectively, from changes in current liabilities.

The decrease in cash related to accounts receivable in the nine months ended September 30, 2018, reflected higher business levels in September 2018 as compared to December of 2017 along with timing of customer payments. Conversely, we had an increase in cash related to accounts receivable in the nine months ended September 30, 2017, as we had lower revenue in the quarter ended September 30, 2017 as compared to the fourth quarter of 2016. As a result, combined with our cash collections, our overall accounts receivable balances decreased. The decrease in inventory levels in 2017 reflected usage on a large umbilical project and our lower Subsea Products backlog in 2017. The increase in cash related to changes in current liabilities in 2018 reflected timing of customer payments. The 2017 decrease in cash related to changes in current liabilities reflected generally lower business levels.

In the nine months ended September 30, 2018, we used \$82 million of cash in investing activities, mainly related to purchases of property and equipment of \$84 million and the Ecosse acquisition of \$68 million. Additionally, we purchased \$10 million of Angola bonds. These investing cash outflows were partially offset by the proceeds of \$62 million received from a maturity and redemptions of Angola bonds and proceeds from the sale of a cost method investment of \$15.1 million. In the nine months ended September 30, 2017, we used \$79 million of cash in investing activities, primarily related to capital expenditures of \$71 million.

In the nine months ended September 30, 2018, we also used \$6 million in financing activities, mainly as a result of the repayment of the Term Loan Facility of \$300 million, substantially offset by \$296 million net proceeds from the issuance of the 2028 Senior Notes, net of issuance costs. In the nine months ended September 30, 2017, we also used \$46 million in financing activities, primarily for the payment of cash dividends of \$44 million.

We have not guaranteed any debt not reflected on our consolidated balance sheet as of September 30, 2018, and we do not have any off-balance sheet arrangements, as defined by SEC rules.

In December 2014, our Board of Directors approved a plan to repurchase up to 10 million shares of our common stock. In 2015, we repurchased 2.0 million shares of our common stock for \$100 million under this plan. We did not repurchase any shares during 2016 through September 30, 2018. We account for the shares we hold in treasury under the cost method, at average cost. The timing and amount of any future repurchases will be determined by our management. We expect that any additional shares repurchased under the plan will be held as treasury stock for possible future use. The plan does not obligate us to repurchase any particular number of shares.

From the second quarter of 2014 through the third quarter of 2016, we paid a quarterly dividend to our common shareholders of \$0.27 per share. Starting in the fourth quarter of 2016 through the third quarter of 2017, we paid a dividend of \$0.15 per share. Our last quarterly dividend was declared in July 2017 at \$0.15 per share and paid in September 2017. Subsequently, the Board suspended the payment of a quarterly dividend. Although we will continue



to review our dividend position periodically, we do not anticipate our Board to consider reinstating a quarterly cash dividend until we see a significant improvement in our market outlook and projected free cash flow.

#### Results of Operations

We operate in five business segments. The segments are contained within two businesses — services and products provided primarily to the offshore energy industry ("Energy Services and Products") and services and

Table of Contents

products provided to non-energy industries ("Advanced Technologies"). Our Unallocated Expenses are those not associated with a specific business segment.

Consolidated revenue and profitability information is as follows:

	Three Months Ended		Nine Months Ended		
(dollars in thousands)	Sep 30, 2018	Sep 30, 2017	Jun 30, 2018	Sep 30, 2018	Sep 30, 2017
Revenue	\$519,300	\$476,120	\$478,674	\$1,414,387	\$1,437,332
Gross Margin	47,635	54,885	29,728	96,191	153,311
Gross Margin %	% 12	% 6	% 7	% 11	%
Operating Income (Loss)	(1,552)	10,531	(19,637)	(48,338)	19,771
Operating Income %	% 2	% (4)	%) (3	)% 1	%

## Seasonality

In our Subsea Projects segment, we generate a material amount of our consolidated revenue from contracts for services in the U.S. Gulf of Mexico, which has historically been more active from April through October, as compared to the rest of the year. The European operations of our Asset Integrity segment have historically been more active in the second and third quarters. However, the reduced customer spending levels in the current commodity price environment have substantially obscured this seasonality since mid-2014. Revenue in our ROV segment is generally subject to seasonal variations in demand, with our first quarter typically being the lower quarter of the year. The level of our ROV seasonality primarily depends on the number of ROVs we have engaged in vessel-based subsea infrastructure inspection, maintenance and repair and installation, which is more seasonal than drilling support. Periods since mid-2014 reflect an exception, as there has been a general decline in offshore activity, which caused a decrease in our ROV days on hire and utilization. Revenue in our Subsea Products and Advanced Technologies segments generally has not been seasonal.

## Energy Services and Products

The primary focus of our Energy Services and Products business over the last several years has been toward increasing our asset base and capabilities for providing services and products for offshore energy operations and subsea completions. In recent years, we have focused on increasing our service and product offerings toward our energy customers' operating expenditures and the offshore renewable energy market.

The following table sets forth the Revenue, Gross Margin and Operating Income (Loss) for our Energy Services and Products business segments for the periods indicated. In the ROV section of the table that follows, "Days available" includes all days from the first day that an ROV is placed into service until the ROV is retired. All days during this period are considered available days, including periods when an ROV is undergoing maintenance or repairs. Our ROVs do not have scheduled maintenance or repair that requires significant time when the ROVs are not available for utilization.



Table of Contents

(dollars in thousands)	Three Months Ended			Nine Months Ended		
	Sep 30, 2018	Sep 30, 2017	Jun 30, 2018	Sep 30, 2018	Sep 30, 2017	
<b>Remotely Operated Vehicles</b>						
Revenue	\$105,045	\$104,617	\$107,426	\$298,065	\$302,071	
Gross Margin	8,757	12,102	12,176	25,888	41,783	
Operating Income	772	5,009	4,542	2,916	21,310	
Operating Income %	1	% 5	% 4	% 1	% 7	%
Days available	25,668	25,695	25,386	76,192	76,214	
Days utilized	14,249	12,742	13,654	38,937	36,497	
Utilization	56	% 50	% 54	% 51	% 48	%
<b>Subsea Products</b>						
Revenue	137,099	143,583	121,704	385,491	469,115	
Gross Margin	18,748	24,949	16,075	49,828	72,702	
Operating Income	5,367	12,383	2,295	9,417	34,418	
Operating Income %	4	% 9	% 2	% 2	% 7	%
Backlog at end of period	333,000	284,000	245,000	333,000	284,000	
<b>Subsea Projects</b>						
Revenue	104,972	80,116	78,036	239,868	218,617	
Gross Margin	10,829	10,187	(5,145 )	6,801	20,673	
Operating Income (Loss)	6,088	6,512	(10,358 )	(6,629 )	9,699	
Operating Income (Loss) %	6	% 8	% (13 )	% (3 )	% 4	%
<b>Asset Integrity</b>						
Revenue	62,346	61,098	67,422	191,056	171,948	
Gross Margin	9,430	9,754	9,461	26,909	28,139	
Operating Income	2,275	3,050	3,357	7,311	9,072	
Operating Income %	4	% 5	% 5	% 4	% 5	%
<b>Total Energy Services and Products</b>						
Revenue	\$409,462	\$389,414	\$374,588	\$1,114,480	\$1,161,751	
Gross Margin	47,764	56,992	32,567	109,426	163,297	
Operating Income (Loss)	14,502	26,954	(164 )	13,015	74,499	
Operating Income (Loss) %	4	% 7	% —	% 1	% 6	%

In general, our energy related businesses focus on supplying services and products to the offshore energy market. During the downturn in oil prices since mid-2014, we have experienced lower activity levels and reduced pricing. In 2018, with oil prices stabilizing and activity in some areas improving, we believe that we are in the early stages of a recovery in activity in general, and in our businesses. We expect that a recovery will take time, and only after a sustained higher level of activity can the prices for our services and products be increased enough to generate satisfactory returns.

We believe we are the world's largest provider of ROV services, and this business segment historically, but not currently, has been the largest contributor to our Energy Services and Products business operating income. Our ROV segment revenue reflects the utilization percentages, fleet sizes and average pricing of the respective periods. Our ROV operating margins have declined as depreciation has become a higher percentage of revenue as we have experienced lower utilization and pricing in recent years. In the full years of 2015, 2016 and 2017, ROV

Table of Contents

depreciation and amortization was 18%, 27% and 29% of ROV revenue, respectively; and in the nine-month period ended September 30, 2018, it was 28% of ROV revenue.

During the third quarter of 2018, ROV days on hire increased 4%, largely on increased demand to provide vessel-based services, as our fleet utilization improved to 56% from 54% in the second quarter. Average revenue per day on hire declined 6% sequentially, as we experienced a geographic shift in activity to lower day rate operating areas, notably Europe and Brazil. Our operating income decreased compared to the immediately preceding quarter, due to operational inefficiencies associated with the reactivation of equipment and crews. We added four new ROVs to our fleet and retired four during the nine months ended September 30, 2018, leaving our fleet size unchanged at 279 ROVs as of September 30, 2018.

Our ROV operating income decreased in the three- and nine-month periods ended September 30, 2018 compared to the corresponding periods of the prior year, mainly due to lower average revenue per day on hire in 2018, as a result of a geographic shift in activity to lower day rate operating areas and market condition, partially offset by an increase in utilization. We expect an operating loss for ROV in the fourth quarter of 2018 due to fewer days utilization, largely on decreased seasonal demand to provide vessel-based services, and lower average revenue per day on hire. We believe our overall ROV fleet utilization for the fourth quarter to be in the lower 50% range.

Our Subsea Products segment consists of two business units: (1) manufactured products; and (2) service and rental. Manufactured products includes production control umbilicals and specialty subsea hardware, while service and rental includes tooling, subsea work systems and installation and workover control systems. The following table presents revenue from manufactured products and service and rental, as their respective percentages of total Subsea Products revenue:

	Three Months Ended		Nine Months Ended	
	Sep 30, 2018	Sep 30, 2017	Sep 30, 2018	Sep 30, 2017
Manufactured products	54%	59%	50%	67%
Service and rental	46%	41%	50%	33%

Subsea Products operating income in the third quarter of 2018 improved on a 13% increase in quarterly revenues compared to that of the immediately preceding quarter, due to increased throughput in our manufactured products businesses and the absence of certain equipment write-offs that occurred in the second quarter of 2018. Our Subsea Products operating income decreased in the three- and nine-month periods ended September 30, 2018 compared to the corresponding periods of the prior year, mainly due to lower demand in manufactured products as a result of reduced umbilical-related backlog from the beginning of the year and the quarter, partially offset by an improvement in execution. Lower operating income in the nine-month period ended September 30, 2018 was also attributable to the write-offs of certain equipment in the second quarter 2018.

Our Subsea Products backlog was \$333 million as of September 30, 2018, compared to \$276 million as of December 31, 2017. The backlog improvement was largely attributable to an increase in order intake for our service and rental business offerings. Subsea Products book-to-bill ratio year-to-date was 1.2 and the past twelve months has been 1.1. We expect Subsea Products to incur an operating loss on relatively flat revenue in the fourth quarter of 2018 compared to the third quarter, primarily due to substantially lower levels of production at our manufacturing facility in

Panama City, Florida as a result of damage caused by Hurricane Michael in mid-October 2018. We expect an increase in contract awards during the remainder of 2018, which should keep our book-to-bill ratio above 1.0 for the full year.

In the three-month period ended September 30, 2018, our Subsea Projects operating results achieved a return to profitability, on a 35% increase in quarterly revenues compared to the immediately preceding quarter, and generated \$6.1 million of operating income. These results were mainly driven by higher levels of seasonal utilization and pricing in the U.S. Gulf of Mexico deepwater vessel and diving services, an increase in survey services, and the absence of the second quarter 2018 write-offs of certain equipment and intangible assets associated with exiting the land survey business and equipment obsolescence. Our Ecosse results were lower than projected due to equipment modifications and field trials that delayed execution.

Table of Contents

Our Subsea Projects operating results in the three- and nine-month periods ended September 30, 2018 decreased compared to the corresponding periods of the prior year, due to lower pricing, lower vessel demand principally as a result of the completion of the Island Pride vessel working offshore India in the fourth quarter of 2017, reduced diving work in Angola, and the second quarter 2018 write-offs of equipment and intangible assets. These results were partially offset by stronger demand for global survey services and increased diving activity in Mexico. In the fourth quarter of 2018, we expect Subsea Projects operating results to be lower on reduced revenue compared to the third quarter, due to the seasonal decrease in the U.S. Gulf of Mexico deepwater vessel and diving work, as well as decreased survey services, offset slightly by increased contributions from the Ecosse operations.

Asset Integrity's operating income in the three-month period ended September 30, 2018 compared to the immediately preceding quarter was down due to delays in anticipated project awards by customers. For the three- and nine-month periods ended September 30, 2018, compared to the corresponding periods of the prior year, Asset Integrity's operating income did not change significantly. For the fourth quarter of 2018, we expect Asset Integrity's operating income to be lower compared to the third quarter due to seasonal decreases, and expect margins to be in the low single digit range.

## Advanced Technologies

Revenue, Gross Margin and Operating Income information was as follows:

	Three Months Ended			Nine Months Ended	
(dollars in thousands)	Sep 30, 2018	Sep 30, 2017	Jun 30, 2018	Sep 30, 2018	Sep 30, 2017
Revenue	\$100,838	\$86,706	\$104,086	299,907	275,581
Gross Margin	\$14,824	\$11,833	\$13,999	\$36,645	\$36,038
Operating Income	8,960	6,602	7,886	18,514	19,260
Operating Income %	% 8	% 8	% 6	% 7	%

Advanced Technologies operating income in the third quarter of 2018 was slightly higher than that of the immediately preceding quarter, due to increased project throughput in our commercial theme park unit. Operating income for the three-month period ended September 30, 2018 was higher compared to the corresponding period of the prior year, due to an increase in the commercial theme park unit and government work. The operating income for the nine-month period ended September 30, 2018 was slightly lower than that of the corresponding period of the prior year, due to execution issues in our Automated Guided Vehicles ("AGV") project, and delay in awards of AGV projects and government work, partially offset by increased activity in the theme park business. We expect our Advanced Technologies operating income in the fourth quarter of 2018 to improve compared to the third quarter, driven from backlog in our commercial theme park unit and improved results within our AGV business.

## Unallocated Expenses

Our Unallocated Expenses, (i.e., those not associated with a specific business segment), within gross margin consist of expenses related to our incentive and deferred compensation plans, including restricted stock units, performance units and bonuses, as well as other general expenses. Our Unallocated Expenses within operating income consist of those expenses within gross margin plus general and administrative expenses related to corporate functions.



Edgar Filing: OCEANEERING INTERNATIONAL INC - Form 10-Q

The following table sets forth our Unallocated Expenses for the periods indicated.

Three Months Ended			Nine Months Ended	
(dollars, in 2018 thousands)	Sep 30, 2017	Jun 30, 2018	Sep 30, 2018	Sep 30, 2017
Gross Margin	\$ 14,953	\$ 16,838	49,880	46,024
Operating Income	23,025	27,359	79,867	73,988
Operating Income of Revenue	% 5	% 6	% 6	% 5

Our Unallocated Expenses for the third quarter were lower than the immediately preceding quarter as performance-based compensation expenses were reduced based on our expected level of results relative to the respective plan targets. Our Unallocated Expenses for the three- and nine-month periods ended September 30, 2018 were higher

Table of Contents

compared to the corresponding period of the prior year, primarily due to higher Information Technology-related expenses. For the fourth quarter of 2018, we expect our quarterly Unallocated Expenses to be in the upper-\$20 million range.

## Other

The following table sets forth our significant financial statement items below the Income (Loss) from Operations line.

	Three Months Ended			Nine Months Ended	
	(in thousands)	Sep 30, 2017	Jun 30, 2018	Sep 30, 2018	Sep 30, 2017
Interest income	\$2,645	\$1,997	\$2,950	8,187	5,379
Interest expense, net of amounts capitalized	(9,885)	(8,650)	(8,802)	(28,058)	(22,517)
Equity in income (loss) of unconsolidated affiliates	(1,668)	(424)	(737)	(3,264)	(1,798)
Other income (expense), net	5,632	(1,287)	(3,556)	(6,398)	(3,901)
Provision (benefit) for income taxes	1,135	3,935	3,294	70,317	4,104

In addition to interest on borrowings, interest expense includes amortization of loan costs, fees for lender commitments under our revolving credit agreement and fees for standby letters of credit and bank guarantees that banks issue on our behalf for performance bonds, bid bonds and self-insurance requirements.

Foreign currency transaction gains and losses are the principal component of Other income (expense), net. In the three- and nine-month periods ended September 30, 2018, we incurred foreign currency transaction losses of \$3.8 million and \$15.5 million, respectively. The currency losses primarily related to the Angolan kwanza and its declining exchange rate relative to the U.S. dollar, as we are required to remeasure our Angola kwanza cash balance to U.S. dollar. Any conversion of cash balances from Angolan kwanza is controlled by the central bank in Angola, and the central bank slowed this process from mid-2015 to 2017, causing our cash balances in kwanza to increase during this period of time. However, during the nine months ended September 30, 2018, we were able to repatriate \$57 million of cash out of Angola.

For the three- and nine-month periods ended September 30, 2018, Other income (expense), net also included a pre-tax gain of \$9.3 million resulting from the sale of our cost method investment in ASV Global, LLC in September 2018. The total consideration from the sale was \$15.1 million, which is subject to final working capital adjustments and customary holdbacks.

The provisions for income taxes are related to our current estimated annual effective tax rate using assumptions as to (1) earnings and other factors that would affect the tax provision for the remainder of the year and (2) the operations of foreign branches and subsidiaries that are subject to local income and withholding taxes. Factors that could affect our estimated tax rate include our profitability levels in general and the geographic mix in the sources of our results. The effective tax rate for the nine months ended September 30, 2018 was different from the federal statutory rate of 21.0%, primarily due to the geographic mix of operating revenue and results that generated taxes in certain jurisdictions that exceeded the tax benefit from losses and credits in other jurisdictions and the discrete items discussed below. We will continue to evaluate the realizability of our recorded deferred tax assets. It is our intention to continue to indefinitely reinvest in certain of our international operations; therefore, we do not provide withholding taxes on the possible distribution of these earnings. We do not believe the effective tax rate before discrete items is meaningful, as current conditions do not allow for relevant guidance in this regard.

In the three-month period ended September 30, 2018, we recognized additional tax expense of \$56.5 million for discrete items, primarily related to \$39.1 million of valuation allowances on certain deferred tax assets recognized in prior years that may not be realizable in certain foreign jurisdictions, \$7.9 million of provisional tax related to the Tax Cuts and Jobs Act enacted in December 2017 (the "Tax Act"), \$3.6 million related to uncertain tax position and \$5.9 million associated with various other issues. In the nine-month period ended September 30, 2018, we recognized additional tax expense of \$60.1 million for discrete items, primarily related to \$39.1 million of valuation allowances on certain deferred tax assets recognized in prior years that may not be realizable in certain foreign jurisdictions, \$7.9 million of provisional tax related to the Tax Act, \$4.8 million related to uncertain tax position and \$8.3 million associated with various other issues. We expect the above tax provision for discrete items will have

Table of Contents

minimal cash tax implications for the foreseeable future. During the nine months ended September 30, 2018, our cash taxes paid totaled \$25.8 million as compared to the \$30 million paid during the corresponding period of 2017. The effective tax rate for the nine months ended September 30, 2017 was lower than the federal statutory rate of 35.0%, primarily due to our intention to indefinitely reinvest in certain of our international operations, partially offset by a discrete tax item associated with share-based compensation. In 2017, we did not provide for U.S. taxes on the portion of our foreign earnings that we deemed indefinitely reinvested.

Table of Contents

## Item 3. Quantitative and Qualitative Disclosures About Market Risk.

We are currently exposed to certain market risks arising from transactions we have entered into in the normal course of business. These risks relate to interest rate changes and fluctuations in foreign exchange rates. Except for our exposure in Angola, we do not believe these risks are material. We have not entered into any market risk sensitive instruments for speculative or trading purposes. When we have a significant amount of borrowings, we typically manage our exposure to interest rate changes through the use of a combination of fixed- and floating-rate debt. See Note 4 of Notes to Consolidated Financial Statements included in this report for a description of our revolving credit facility and interest rates on our borrowings. We have two interest rate swaps in place on a total of \$200 million of the 2024 Senior Notes. The agreements swap the fixed interest rate of 4.650% on \$100 million of the 2024 Senior Notes to the floating rate of one month LIBOR plus 2.426% and on another \$100 million to one month LIBOR plus 2.823%. We believe significant interest rate changes would not have a material near-term impact on our future earnings or cash flows.

Because we operate in various oil and gas exploration and production regions in the world, we conduct a portion of our business in currencies other than the U.S. dollar. The functional currency for several of our international operations is the applicable local currency. A stronger U.S. dollar against the U.K. pound sterling, the Norwegian kroner and the Brazilian real may result in lower operating income. We manage our exposure to changes in foreign exchange rates principally through arranging compensation in U.S. dollars or freely convertible currency and, to the extent possible, by limiting compensation received in other currencies to amounts necessary to meet obligations denominated in those currencies. We use the exchange rates in effect as of the balance sheet date to translate assets and liabilities as to which the functional currency is the local currency, resulting in translation adjustments that we reflect as accumulated other comprehensive income or loss in the equity section of our Consolidated Balance Sheets. We recorded net adjustments to our equity accounts of \$(21.3) million and \$20.3 million in the nine-month periods ended September 30, 2018 and 2017, respectively. Negative adjustments reflect the net impact of the strengthening of the U.S. dollar against various foreign currencies for locations where the functional currency is not the U.S. dollar. Conversely, positive adjustments reflect the effect of a weakening U.S. dollar.

We recorded foreign currency transaction losses of \$3.8 million and \$15.5 million in the three- and nine-month periods ended September 30, 2018, respectively. Those losses are included in Other income (expense), net in our Consolidated Statements of Operations in those respective periods. Since the second quarter of 2015, the exchange rate for the Angolan kwanza relative to the U.S. dollar generally has been declining, although the exchange rate was relatively stable during 2017. As our functional currency in Angola is the U.S. dollar, we recorded foreign currency transaction losses related to the kwanza of \$4.5 million and \$16.9 million in the three- and nine-month periods ended September 30, 2018, as a component of Other income (expense), net in our Consolidated Statements of Operations for those respective periods. Our foreign currency transaction losses are related primarily to the remeasurement of our Angolan kwanza cash balances to U.S. dollars. Any conversion of cash balances from kwanza is controlled by the central bank in Angola, and the central bank slowed this process from mid-2015 to 2017, causing our kwanza cash balances to increase during that period of time. However, beginning in 2018, the Angolan central bank has allowed us to repatriate cash from Angola. Through September 30, 2018, we were able to repatriate \$57 million of cash from Angola. As of September 30, 2018 and December 31, 2017, we had the equivalent of approximately \$14 million and \$27 million of kwanza cash balances in Angola, respectively, reflected on our balance sheet. The decrease in kwanza cash balances in 2018 was mainly attributable to the repatriation of cash from Angola and cash used in our Angolan operations. Since December 31, 2017, Angola has devalued its currency by almost 75%. We will incur further foreign currency exchange losses in Angola if further currency devaluations occur.

To mitigate our currency exposure risk in Angola, we have used kwanza to purchase equivalent Angolan central bank (Banco Nacional de Angola) bonds. The bonds are denominated as U.S. dollar equivalents, so that, upon payment of semi-annual interest and principal upon maturity, payment is made in kwanza, equivalent to the respective U.S. dollars at the then-current exchange rate. Our intention was to hold the bonds to maturity, and to reinvest funds from

maturing bonds in similar Angola bonds. We previously believed the chance of selling the bonds before maturity and repatriating cash out of Angola was remote. In the second quarter of 2018, \$10 million of bonds matured, and the proceeds were reinvested by us in similar long-term assets. Additionally, we sold \$52 million of bonds prior to their maturity date through September 30, 2018. Because we intend to sell the bonds if we are able to repatriate the proceeds, we changed our accounting for these bonds from held-to-maturity securities to available-for-sale securities. As of September 30, 2018, we classified \$3 million of bonds due to mature in the next twelve months as Other current assets and \$15 million of bonds due to mature after twelve months as Other non-

Table of Contents

current assets on our Consolidated Balance Sheet, with \$5 million maturing in 2020 and \$10 million maturing in 2023.

We estimated the fair market value of the Angolan bonds to be approximately \$18 million as of September 30, 2018 using quoted prices. Since the market for the Angolan bonds is not an active market, the fair value of the Angolan bonds is classified within Level 2 in the fair value hierarchy under U.S. GAAP. As of September 30, 2018, we have not recorded the difference between the fair market value and carrying amount of the outstanding bonds through the Consolidated Statement of Comprehensive Income (Loss) due to the insignificance of the difference between the fair market value and the carrying amount of the bonds.

Item 4. Controls and Procedures.

In accordance with Rules 13a-15 and 15d-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), we carried out an evaluation, under the supervision and with the participation of management, including our principal executive officer and principal financial officer, of the effectiveness of our disclosure controls and procedures (as that term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on that evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective as of September 30, 2018 to provide reasonable assurance that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

There has been no change in our internal control over financial reporting that occurred during the three months ended September 30, 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

In the ordinary course of business, we are subject to actions for damages alleging personal injury under the general maritime laws of the United States, including the Jones Act, for alleged negligence. We report actions for personal injury to our insurance carriers and believe that the settlement or disposition of those claims will not have a material adverse effect on our consolidated financial position, results of operations or cash flows.

Various other actions and claims are pending against us, most of which are covered by insurance. Although we cannot predict the ultimate outcome of these matters, we believe that our ultimate liability, if any, that may result from these other actions and claims will not materially affect our results of operations, cash flows or financial position.



Table of Contents

Item 6. Exhibits.

## Index to Exhibits

		Registration or	Form of	Report	Exhibit
		File Number	Report	Date	Number
*3.1	<u>Restated Certificate of Incorporation</u>	1-10945	10-K	Dec. 2000	3.1
*3.2	<u>Certificate of Amendment to Restated Certificate of Incorporation</u>	1-10945	8-K	May 2008	3.1
*3.3	<u>Certificate of Amendment to Restated Certificate of Incorporation</u>	1-10945	8-K	May 2014	3.1
*3.4	<u>Amended and Restated Bylaws</u>	1-10945	8-K	Aug. 2015	3.1
*4.1	<u>Agreement and Amendment No. 4 Credit Agreement, dated as of February 16, 2018, by and among Oceaneering International, Inc. ("Oceaneering"), Wells Fargo Bank, National association, as administrative agent and swing the lender, and the lenders party thereto</u>	1-10945	8-K	Feb. 2018	4.1
*4.2	<u>Second Supplemental Indenture, dated February 6, 2018, between Oceaneering and Wells Fargo Bank, National Association, as Trustee, providing for the issuance of Oceaneering's 6.000% Senior Notes due 2028 (including Form of Notes)</u>	1-10945	8-K	Feb. 2018	4.2
4.3	<u>Specimen of Common Stock Certificate</u>				
12.1	<u>Computation of Ratio of Earnings to Fixed Charges</u>				
31.1	<u>Rule 13a – 14(a)/15d – 14(a) certification of principal executive officer</u>				
31.2	<u>Rule 13a – 14(a)/15d – 14(a) certification of principal financial officer</u>				
32.1	<u>Section 1350 certification of principal executive officer</u>				
32.2	<u>Section 1350 certification of principal financial officer</u>				
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				
+	Management contract or compensatory plan or arrangement.				
*	Exhibit previously filed with the Securities and Exchange Commission, as indicated, and incorporated herein by reference.				

Table of Contents

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.

October 31, 2018 /S/ RODERICK A. LARSON  
Date Roderick A. Larson  
President and Chief Executive Officer  
(Principal Executive Officer)

October 31, 2018 /S/ ALAN R. CURTIS  
Date Alan R. Curtis  
Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

October 31, 2018 /S/ W. CARDON GERNER  
Date W. Cardon Gerner  
Senior Vice President and Chief Accounting Officer  
(Principal Accounting Officer)