
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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 001-35003

RigNet, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

15115 Park Row Blvd, Suite 300
Houston, Texas
(Address of principal executive offices)

76-0677208
(I.R.S. Employer
Identification No.)

77084-4947
(Zip Code)

(281) 674-0100
Registrant's telephone number, including area code

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit 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
Non-accelerated filer

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

At October 31, 2018, there were outstanding 19,411,467 shares of the registrant's Common Stock.

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PART I – FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

**RIGNET, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)**

	September 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 20,726	\$ 34,598
Restricted cash	42	43
Accounts receivable, net	68,161	49,021
Costs and estimated earnings in excess of billings on uncompleted contracts	4,395	2,393
Prepaid expenses and other current assets	6,388	5,591
Total current assets	99,712	91,646
Property, plant and equipment, net	60,835	60,344
Restricted cash	1,546	1,500
Goodwill	46,275	37,088
Intangibles, net	34,485	30,405
Deferred tax and other assets	8,385	9,111
TOTAL ASSETS	\$ 251,238	\$ 230,094
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	\$ 17,579	\$ 12,234
Accrued expenses	17,021	16,089
Current maturities of long-term debt	4,943	4,941
Income taxes payable	—	1,601
Deferred revenue and other current liabilities	4,419	8,511
Total current liabilities	43,962	43,376
Long-term debt	66,214	53,173
Deferred revenue	369	546
Deferred tax liability	3,281	189
Other liabilities	32,101	25,533
Total liabilities	145,927	122,817
Commitments and contingencies (Note 11)		
Equity:		
Stockholders' equity		
Preferred stock—\$0.001 par value; 10,000,000 shares authorized; no shares issued or outstanding at September 30, 2018 or December 31, 2017	—	—
Common stock—\$0.001 par value; 191,000,000 shares authorized; 19,411,467 and 18,232,872 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively	19	18
Treasury stock—89,880 and 5,516 shares at September 30, 2018 and December 31, 2017, respectively, at cost	(1,246)	(116)
Additional paid-in capital	172,599	155,829
Accumulated deficit	(46,796)	(33,726)
Accumulated other comprehensive loss	(19,295)	(14,806)
Total stockholders' equity	105,281	107,199
Non-redeemable, non-controlling interest	30	78
Total equity	105,311	107,277
TOTAL LIABILITIES AND EQUITY	\$ 251,238	\$ 230,094

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

RIGNET, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Unaudited)

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>
	(in thousands, except per share amounts)			
Revenue	\$ 64,770	\$ 50,844	\$ 178,610	\$ 148,078
Expenses:				
Cost of revenue (excluding depreciation and amortization)	40,734	32,385	110,661	95,298
Depreciation and amortization	8,413	7,999	24,756	22,867
Selling and marketing	2,728	2,400	9,866	5,968
General and administrative	13,916	11,011	43,148	31,401
Total expenses	65,791	53,795	188,431	155,534
Operating loss	(1,021)	(2,951)	(9,821)	(7,456)
Other income (expense):				
Interest expense	(807)	(689)	(2,773)	(1,921)
Other income (expense), net	(658)	209	(40)	62
Loss before income taxes	(2,486)	(3,431)	(12,634)	(9,315)
Income tax benefit (expense)	(312)	(762)	11	(1,075)
Net loss	(2,798)	(4,193)	(12,623)	(10,390)
Less: Net income attributable to non-redeemable, non-controlling interest	49	39	109	117
Net loss attributable to RigNet, Inc. stockholders	\$ (2,847)	\$ (4,232)	\$ (12,732)	\$ (10,507)
COMPREHENSIVE LOSS				
Net loss	\$ (2,798)	\$ (4,193)	\$ (12,623)	\$ (10,390)
Foreign currency translation	(3,897)	1,737	(4,489)	3,503
Comprehensive loss	(6,695)	(2,456)	(17,112)	(6,887)
Less: Comprehensive income attributable to non-controlling interest	49	39	109	117
Comprehensive loss attributable to RigNet, Inc. stockholders	\$ (6,744)	\$ (2,495)	\$ (17,221)	\$ (7,004)
LOSS PER SHARE—BASIC AND DILUTED				
Net loss attributable to RigNet, Inc. common stockholders	\$ (2,847)	\$ (4,232)	\$ (12,732)	\$ (10,507)
Net loss per share attributable to RigNet, Inc. common stockholders, basic	\$ (0.15)	\$ (0.23)	\$ (0.69)	\$ (0.58)
Net loss per share attributable to RigNet, Inc. common stockholders, diluted	\$ (0.15)	\$ (0.23)	\$ (0.69)	\$ (0.58)
Weighted average shares outstanding, basic	18,905	18,086	18,566	17,982
Weighted average shares outstanding, diluted	18,905	18,086	18,566	17,982

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

RIGNET, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30,	
	2018	2017
(in thousands)		
Cash flows from operating activities:		
Net loss	\$ (12,623)	\$ (10,390)
Adjustments to reconcile net loss to net cash provided by operations:		
Depreciation and amortization	24,756	22,867
Stock-based compensation	4,368	2,949
Amortization of deferred financing costs	141	192
Deferred taxes	(117)	(271)
Change in fair value of earn-out/contingent consideration	2,050	(846)
Accretion of discount of contingent consideration payable for acquisitions	368	417
Loss on sales of property, plant and equipment, net of retirements	34	55
Changes in operating assets and liabilities, net of effect of acquisition:		
Accounts receivable, net	(15,428)	(122)
Costs and estimated earnings in excess of billings on uncompleted contracts	(1,095)	716
Prepaid expenses and other assets	(1,634)	3,714
Accounts payable	3,986	1,697
Accrued expenses	(1,584)	1,733
Deferred revenue	1,512	6,212
Other liabilities	(1,807)	(8,035)
Payout of TECNOR contingent consideration—inception to date change in fair value portion	(1,575)	—
Net cash provided by operating activities	1,352	20,888
Cash flows from investing activities:		
Acquisitions (net of cash acquired)	(5,405)	(32,205)
Capital expenditures	(18,791)	(13,186)
Proceeds from sales of property, plant and equipment	685	274
Net cash used in investing activities	(23,511)	(45,117)
Cash flows from financing activities:		
Proceeds from issuance of common stock net of stock withheld to cover employee taxes on stock-based compensation	967	800
Stock withheld to cover employee taxes on stock-based compensation	(1,130)	(116)
Subsidiary distributions to non-controlling interest	(157)	(76)
Payout of TECNOR contingent consideration—fair value on acquisition date portion	(6,425)	—
Proceeds from borrowings	16,750	15,000
Repayments of long-term debt	(3,848)	(16,660)
Net cash provided by (used) in financing activities	6,157	(1,052)
Net change in cash and cash equivalents	(16,002)	(25,281)
Cash and cash equivalents including restricted cash:		
Balance, January 1,	36,141	58,805
Changes in foreign currency translation	2,175	919
Balance, September 30,	\$ 22,314	\$ 34,443
Supplemental disclosures:		
Income taxes paid	\$ 2,989	\$ 1,515
Interest paid	\$ 2,284	\$ 1,362
Non-cash investing—capital expenditures accrued	\$ 2,612	\$ 2,785
Non-cash investing—tenant improvement allowance	\$ —	\$ 1,728
Non-cash investing—contingent consideration for acquisitions	\$ 7,600	\$ 3,798
Non-cash investing and financing - stock for acquisitions	\$ 11,436	\$ 3,304
Liabilities assumed in acquisitions	\$ 5,513	\$ 674
	September 30,	September 30,
	2018	2017
Cash and cash equivalents	\$ 20,726	\$ 32,900
Restricted cash—current portion	42	43
Restricted cash—long-term portion	1,546	1,500
Cash and cash equivalents including restricted cash	\$ 22,314	\$ 34,443

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

RIGNET, INC.
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(Unaudited)

	Common Stock		Treasury Stock		Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity	Non-Redeemable, Non-Controlling Interest	Total Equity
	Shares	Amount	Shares	Amount						
Balance, January 1, 2017	17,933	\$ 18	—	\$ —	\$147,906	\$ (17,550)	\$ (17,971)	\$ 112,403	\$ 175	\$ 112,578
Issuance of common stock upon the exercise of stock options	58	—	—	—	800	—	—	800	—	800
Issuance of common stock upon the vesting of Restricted Stock Units, net of share cancellations	48	—	—	—	—	—	—	—	—	—
Issuance of common stock upon the acquisition of Cyphre	192	—	—	—	3,304	—	—	3,304	—	3,304
Stock withheld to cover employee taxes on stock-based compensation	(6)	—	6	(116)	—	—	—	(116)	—	(116)
Stock-based compensation	—	—	—	—	2,949	—	—	2,949	—	2,949
Foreign currency translation	—	—	—	—	—	—	3,503	3,503	—	3,503
Non-controlling owner distributions	—	—	—	—	—	—	—	—	(76)	(76)
Net income (loss)	—	—	—	—	—	(10,507)	—	(10,507)	117	(10,390)
Balance, September 30, 2017	18,225	\$ 18	6	\$ (116)	\$154,959	\$ (28,057)	\$ (14,468)	\$ 112,336	\$ 216	\$ 112,552
Balance, January 1, 2018	18,233	\$ 18	6	\$ (116)	\$155,829	\$ (33,726)	\$ (14,806)	\$ 107,199	\$ 78	\$ 107,277
Issuance of common stock upon the exercise of stock options	59	—	—	—	967	—	—	967	—	967
Issuance of common stock upon the vesting of Restricted Stock Units, net of share cancellations	330	—	—	—	—	—	—	—	—	—
Issuance of common stock for acquisitions	789	1	—	—	11,435	—	—	11,436	—	11,436
Stock withheld to cover employee taxes on stock-based compensation	—	—	84	(1,130)	—	—	—	(1,130)	—	(1,130)
Stock-based compensation	—	—	—	—	4,368	—	—	4,368	—	4,368
Cumulative effect adjustment from implementation of ASU 2016-16	—	—	—	—	—	(338)	—	(338)	—	(338)
Foreign currency translation	—	—	—	—	—	—	(4,489)	(4,489)	—	(4,489)
Non-controlling owner distributions	—	—	—	—	—	—	—	—	(157)	(157)
Net income (loss)	—	—	—	—	—	(12,732)	—	(12,732)	109	(12,623)
Balance, September 30, 2018	19,411	\$ 19	90	\$ (1,246)	\$172,599	\$ (46,796)	\$ (19,295)	\$ 105,281	\$ 30	\$ 105,311

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

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 – Basis of Presentation

The interim unaudited condensed consolidated financial statements of RigNet, Inc. (the Company or RigNet) include all adjustments which, in the opinion of management, are necessary for a fair presentation of the Company's financial position and results of operations. All such adjustments are of a normal recurring nature. These financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and Rule 10-01 of Regulation S-X. The preparation of these financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying footnotes. Estimates and assumptions about future events and their effects cannot be perceived with certainty. Estimates may change as new events occur, as more experience is acquired, as additional information becomes available and as the Company's operating environment changes. Actual results could differ from estimates. These interim financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2017 included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 6, 2018.

Significant Accounting Policies

Please refer to RigNet's Annual Report on Form 10-K for fiscal year 2017 for information regarding the Company's accounting policies.

Revenue Recognition—Revenue from Contracts with Customers

Revenue is recognized to depict the transfer of promised goods or services in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those goods or services.

Revenue Recognition—Managed Services and Applications and Internet-of-Things

Managed Services and Applications and Internet-of-Things customers are primarily served under fixed-price contracts, either on a monthly or day rate basis or for equipment sales and consulting services. Our contracts are generally in the form of Master Service Agreements, or MSAs, with specific services being provided under individual service orders that have a term of up to three years with renewal options for offshore locations that are generally longer-term contracts with few cancellation provisions, while land-based locations are generally shorter term or terminable on short notice without a penalty. Service orders are executed under the MSA for individual remote sites or groups of sites, and generally permit early termination on short notice without penalty in the event of force majeure, breach of the MSA or cold stacking of a drilling rig (when a rig is taken out of service and is expected to be idle for a protracted period of time).

Performance Obligations Satisfied Over Time—The delivery of service represents the single performance obligation under Managed Services and Applications and Internet-of-Things contracts. Revenue for contracts is generally recognized over time as service is transferred to the customer and the Company expects to be entitled to the agreed monthly or day rate in exchange for those services.

Performance Obligations Satisfied at a Point in Time—The delivery of equipment represents the single performance obligation under equipment sale contracts. Revenue for equipment sales is generally recognized upon delivery of equipment to customers.

Revenue Recognition – Systems Integration

Revenues related to long-term, fixed-price Systems Integration contracts for customized network solutions are recognized based on the percentage of completion for the contract. At any point, RigNet has numerous contracts in progress, all of which are at various stages of completion. Accounting for revenues and profits on long-term contracts requires estimates of total estimated contract costs and estimates of progress toward completion to determine the extent of revenue and profit recognition.

Performance Obligations Satisfied Over Time — The delivery of a Systems Integration solution represents the single performance obligation under Systems Integration contracts. Progress towards completion on fixed-price contracts is measured based on the ratio of costs incurred to total estimated contract costs (the cost-to-cost method). These estimates may be revised as additional information becomes available or as specific project circumstances change.

The Company reviews all material contracts on a monthly basis and revises the estimates as appropriate for developments such as providing services, purchasing third-party materials and equipment at costs differing from those previously estimated, and incurring or expecting to incur schedule issues. Changes in estimated final contract revenues and costs can either increase or decrease the final estimated contract profit or loss. Profits are recorded in the period in which a change in estimate is recognized, based on progress achieved through the period of change. Anticipated losses on contracts are recorded in full in the period in which they become evident. Revenue recognized in excess of amounts billed is classified as a current asset under Costs and estimated earnings in excess of billings on uncompleted contracts.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Systems Integration contracts are billed in accordance with the terms of the contract which are typically either based on milestones or specified time intervals. As of September 30, 2018 and December 31, 2017, the amount of Costs and estimated earnings in excess of billings on uncompleted contracts related to Systems Integration projects was \$4.4 million and \$2.4 million, respectively. Under long-term contracts, amounts recorded in Costs and estimated earnings in excess of billings on uncompleted contracts may not be realized or paid, respectively, within a one-year period. As of September 30, 2018 and December 31, 2017, \$1.3 million and \$0.4 million, respectively, of amounts billed to customers in excess of revenue recognized to date are classified as a current liability, under deferred revenue. All of the billings in excess of costs as of December 31, 2017 were recognized as revenue during the nine months ended September 30, 2018.

Variable Consideration – Systems Integration — The Company records revenue on contracts relating to certain probable claims and unapproved change orders by including in revenue an amount less than or equal to the amount of costs incurred to date relating to these probable claims and unapproved change orders, thus recognizing no profit until such time as claims are finalized or change orders are approved. The amount of unapproved change orders and claim revenues is included in the Company's Condensed Consolidated Balance Sheets as part of Costs and estimated earnings in excess of billings on uncompleted contracts. No material unapproved change orders or claims revenue was included in Costs and estimated earnings in excess of billings on uncompleted contracts as of September 30, 2018 and December 31, 2017. As new facts become known, an adjustment to the estimated recovery is made and reflected in the current period.

Backlog—As of September 30, 2018, we have backlog for our percentage of completion projects of \$41.4 million, which will be recognized over the remaining contract term for each contract. Percentage of completion contract terms are typically one to three years.

Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2014-09 (ASU 2014-09), Revenue from Contracts with Customers (Topic 606). The core principle of this amendment is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued Accounting Standards Update No. 2015-14 (ASU 2015-14), Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date. In March 2016, the FASB issued Accounting Standards Update No. 2016-08 (ASU 2016-08), Revenue from Contracts with Customers: Principal versus Agent Considerations. The amendments are intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. In April and May of 2016, the FASB issued Accounting Standards Update No. 2016-10 (ASU 2016-10) and Accounting Standards Update No. 2016-12 (ASU 2016-12), Revenue from Contracts with Customers (Topic 606), respectively, that provide scope amendments, performance obligations clarification and practical expedients. These ASUs allow for the use of either the full or modified retrospective transition method and are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period, with early adoption permitted for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The Company adopted this ASU on January 1, 2018. The Company's evaluation of this ASU included a detailed review of representative contracts from each segment and comparing historical accounting policies and practices to the new standard. The adoption of this ASU did not have any material impact on the Company's condensed consolidated financial statements.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02 (ASU 2016-02), Leases. This ASU is effective for annual reporting periods beginning after December 15, 2018. This ASU introduces a new lessee model that generally brings leases on to the balance sheet. Based on the Company's current leases, the Company anticipates the new guidance will require additional assets and liabilities on the condensed consolidated balance sheet; however, the Company has not yet completed an estimation of such amount and we are still evaluating the overall impact of the new guidance on our condensed consolidated financial statements, related disclosures and internal controls.

In August 2016, the FASB issued Accounting Standards Update No. 2016-15 (ASU 2016-15), Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. The new ASU reduces diversity of practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows under Topic 230, Statement of Cash Flows, and other Topics, including the treatment of contingent consideration payments made after a business combination. The ASU is effective for annual and interim reporting periods beginning after December 15, 2017. The Company adopted this ASU on January 1, 2018. The adoption of this ASU did not have any material impact on the Company's condensed consolidated financial statements.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In October 2016, the FASB issued Accounting Standards Update No. 2016-16 (ASU 2016-16), Income Taxes: Intra-Entity Transfer of Assets Other Than Inventory. The new ASU requires an entity to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs, rather than the previous requirement to defer recognition of current and deferred income taxes for an intra-entity asset transfer until the asset had been sold to an outside party. The ASU is effective for annual and interim reporting periods beginning after December 15, 2017. The Company adopted this ASU on January 1, 2018 using the modified retrospective method through a \$0.3 million cumulative effect that directly lowered accumulated deficit. The adoption of this ASU did not have any material impact on the Company's condensed consolidated financial statements.

In November 2016, the FASB issued Accounting Standards Update No. 2016-18 (ASU 2016-18), which includes restricted cash in the cash and cash equivalents balance in the statement of cash flows. The ASU is effective for annual and interim reporting periods beginning after December 15, 2017. The Company adopted this ASU on January 1, 2018. The adoption of this ASU did not have any material impact on the Company's condensed consolidated financial statements.

In June 2018, the FASB issued Accounting Standards Update No. 2018-07 (ASU 2018-07), which expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. The ASU is effective for annual and interim reporting periods beginning after December 15, 2018. The Company is currently in the process of evaluating the impact the adoption of this ASU will have on the Company's condensed consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-13 (ASU 2018-13), which eliminates disclosures, modifies existing disclosures and adds new Fair Value disclosure requirements to Topic 820 for the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements. The ASU is effective for annual and interim reporting periods beginning after December 15, 2019. The Company is currently in the process of evaluating the impact the adoption of this ASU will have on the Company's condensed consolidated financial statements.

Note 2 – Business Combinations

Auto-Comm and SAFCON

On April 18, 2018, RigNet completed the separate acquisitions of Automation Communications Engineering Corp. (Auto-Comm) and Safety Controls, Inc. (SAFCON) for an aggregate purchase price of \$6.7 million. Of this aggregate purchase price RigNet paid \$2.2 million in cash and \$4.1 million in stock in April 2018. In September 2018, the Company paid \$0.3 million in cash for a working capital adjustment.

Auto-Comm provides a broad range of communications services, for both onshore and offshore remote locations, to the oil and gas industry. Auto-Comm brings over 30 years of systems integration experience in engineering and design, installation, testing, and maintenance. SAFCON offers a diverse set of safety, security, and maintenance services to the oil and gas industry. Auto-Comm and SAFCON have developed strong relationships with major energy companies that complement the relationships that RigNet has established over the years. Auto-Comm and SAFCON are based in Louisiana.

The assets and liabilities of Auto-Comm and SAFCON have been recorded at their estimated fair values at the date of acquisition. The excess of the purchase price over the estimated fair values of the underlying net tangible and identifiable intangible assets and liabilities has been recorded as goodwill. The Company's allocation of the purchase price is preliminary as the amounts related to the identifiable intangible assets and effects of income taxes resulting from the transaction, are still being finalized.

The goodwill of \$1.0 million arising from the acquisitions consists largely of growth prospects, synergies and other benefits that the Company believes will result from combining the operations of the Company and Auto-Comm and SAFCON, as well as other intangible assets that do not qualify for separate recognition, such as assembled workforce in place at the date of acquisition. The goodwill recognized is expected to be nondeductible for income tax purposes. The acquisitions of Auto-Comm and SAFCON, including goodwill, are included in the Company's condensed consolidated financial statements as of the acquisition date and are primarily reflected in the Systems Integration segment.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	<u>Weighted Average Estimated Useful Life (Years)</u>	<u>Fair Market Values</u> (in thousands)
Current assets		\$ 4,882
Property and equipment		484
Trade name	7	\$ 540
Customer relationships	7	980
Total identifiable intangible assets		1,520
Goodwill		1,003
Current liabilities		(909)
Deferred tax liability		(319)
Total purchase price		<u>\$ 6,661</u>

Intelie

On March 23, 2018, RigNet completed its acquisition of Intelie™ Soluções Em Informática S.A (Intelie), for an estimated aggregate purchase price of \$18.1 million. Of this aggregate purchase price, RigNet paid R\$10.6 million (BRL) (or approximately \$3.2 million) in cash, \$7.3 million in stock and expects to pay \$7.6 million worth of RigNet stock as contingent consideration earn-out, estimated as of the date of acquisition. The initial estimate of the earn-out payable was preliminary and remains subject to change based on the achievement of certain post-closing performance targets under the acquisition agreement. The maximum earn-out is \$17.0 million payable in stock. Intelie is a real-time, predictive analytics company that combines an operational understanding with a machine learning approach. Intelie facilitates innovation via Intelie Pipes™, a distributed query language with a complex event processor to aggregate and normalize real-time data from a myriad of data sources. This technology enables the Intelie LIVE™ platform to solve data integration, data quality, data governance and monitoring problems. Intelie LIVE is an operational intelligence platform that empowers clients to make timely, data-driven decisions in mission-critical real-time operations, including drilling, and longer-term, data-intensive projects, such as well planning. While primarily applicable to oil and gas, Intelie Live has broad applicability across many industry verticals. Intelie is based in Brazil.

The assets and liabilities of Intelie have been recorded at their estimated fair values at the date of acquisition. The excess of the purchase price over the estimated fair values of the underlying net tangible and identifiable intangible assets and liabilities has been recorded as goodwill. The Company's allocation of the purchase price is preliminary as the amounts related to contingent consideration, identifiable intangible assets, and the effects of income taxes resulting from the transaction, are still being finalized.

The earn-out for Intelie is measured at fair value, based on level 3 inputs, with any change to fair value recorded in the Condensed Consolidated Statements of Comprehensive Loss in each reporting period. As of September 30, 2018, the fair value of the earn-out was \$7.7 million. During the three and nine months ended September 30, 2018, RigNet recognized accreted interest expense on the Intelie earn-out of \$0.1 million with corresponding increases to other liabilities. Portions of the earn-out are payable in RigNet stock on the first, second and third anniversary of the closing of the acquisition based on certain post-closing performance targets under the acquisition agreement.

The goodwill of \$10.7 million arising from the acquisition consists largely of growth prospects, synergies and other benefits that the Company believes will result from combining the operations of the Company and Intelie, as well as other intangible assets that do not qualify for separate recognition, such as assembled workforce in place at the date of acquisition. None of the goodwill recognized is expected to be deductible for income tax purposes. The acquisition of Intelie, including goodwill, is included in the Company's condensed consolidated financial statements as of the acquisition date and is reflected in the Applications and Internet-of-Things segment.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	<u>Weighted Average Estimated Useful Life (Years)</u>	<u>Fair Market Values</u> (in thousands)
Current assets		\$ 589
Property and equipment		73
Trade name	7	\$ 2,300
Technology	7	8,400
Customer relationships	7	320
Total identifiable intangible assets		11,020
Goodwill		10,744
Current liabilities		(460)
Deferred tax liability		(3,825)
Total purchase price		<u>\$ 18,141(a)</u>

(a) Includes \$7.6 million in contingent consideration earn-out estimated as of the date of acquisition.

Actual and Pro Forma Impact of the 2018 Acquisitions

The 2018 acquisitions of Auto-Comm, SAFCON and Intelie contributed revenue and net income of \$7.0 million and \$0.8 million, respectively, for the three months ended September 30, 2018. The 2018 acquisitions of Auto-Comm, SAFCON and Intelie contributed revenue and net income of \$13.2 million and \$1.6 million, respectively, for the nine months ended September 30, 2018.

The following table represents supplemental pro forma information as if the 2018 acquisitions had occurred on January 1, 2017.

	<u>Three Months Ended September 30, 2018</u>	<u>Three Months Ended September 30, 2017</u>	<u>Nine Months Ended September 30, 2018</u>	<u>Nine Months Ended September 30, 2017</u>
	(in thousands, except per share amounts)			
Revenue	\$ 64,770	\$ 55,308	\$ 183,067	\$ 161,023
Expenses	67,568	59,245	195,161	171,041
Net loss	<u>\$ (2,798)</u>	<u>\$ (3,937)</u>	<u>\$ (12,094)</u>	<u>\$ (10,018)</u>
Net loss attributable to RigNet, Inc. common stockholders	<u>\$ (2,847)</u>	<u>\$ (3,976)</u>	<u>\$ (12,203)</u>	<u>\$ (10,135)</u>
Net loss per share attributable to RigNet, Inc. common stockholders:				
Basic	<u>\$ (0.15)</u>	<u>\$ (0.22)</u>	<u>\$ (0.66)</u>	<u>\$ (0.56)</u>
Diluted	<u>\$ (0.15)</u>	<u>\$ (0.22)</u>	<u>\$ (0.66)</u>	<u>\$ (0.56)</u>

The Company incurred acquisition-related costs of \$0.9 million and \$2.1 million in the three and nine months ended September 30, 2018, respectively, reported in general and administrative costs.

Energy Satellite Services

On July 28, 2017, RigNet acquired substantially all the assets of Energy Satellite Services (ESS). ESS is a supplier of wireless communications services via satellite networks primarily to the midstream sector of the oil and gas industry for remote pipeline monitoring. The assets acquired enhance RigNet's Supervisory Control and Data Acquisition (SCADA) customer portfolio, and strengthen the Company's US land and Internet-of-Things (IoT) market position. The Company paid \$22.2 million in cash for the ESS assets. ESS is based in Texas.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The assets and liabilities of ESS have been recorded at their estimated fair values at the date of acquisition. The excess of the purchase price over the estimated fair values of the underlying net tangible and identifiable intangible assets and liabilities has been recorded as goodwill.

The goodwill of \$8.5 million arising from the acquisition consists largely of growth prospects, synergies and other benefits that the Company believes will result from combining the operations of the Company and ESS, as well as other intangible assets that do not qualify for separate recognition, such as assembled workforce in place at the date of acquisition. The goodwill recognized is expected to be deductible for income tax purposes. The acquisition of ESS, including goodwill, is included in the Company's condensed consolidated financial statements as of the acquisition date and is reflected in the Applications and Internet-of-Things segment.

	<u>Weighted Average Estimated Useful Life (Years)</u>	<u>Fair Market Values</u> (in thousands)
Accounts receivable		\$ 392
Property and equipment		1,000
Covenant not to compete	5	\$3,040
Customer relationships	7	<u>9,870</u>
Total identifiable intangible assets		12,910
Goodwill		8,465
Accounts payable		(567)
Total purchase price		<u>\$22,200</u>

Data Technology Solutions

On July 24, 2017, RigNet acquired substantially all the assets of Data Technology Solutions (DTS). DTS provides comprehensive communications and IT services to the onshore, offshore, and maritime industries, as well as disaster relief solutions to global corporate clients. The Company paid \$5.1 million in cash for the DTS assets. DTS is based in Louisiana.

The assets and liabilities of DTS have been recorded at their estimated fair values at the date of acquisition. The excess of the purchase price over the estimated fair values of the underlying net tangible and identifiable intangible assets and liabilities has been recorded as goodwill.

The goodwill of \$0.7 million arising from the acquisition consists largely of growth prospects, synergies and other benefits that the Company believes will result from combining the operations of the Company and DTS, as well as other intangible assets that do not qualify for separate recognition, such as assembled workforce in place at the date of acquisition. The goodwill recognized is expected to be deductible for income tax purposes. The acquisition of DTS, including goodwill, is included in the Company's condensed consolidated financial statements as of the acquisition date and is reflected in the Managed Services segment.

	<u>Fair Market Values</u> (in thousands)
Property and equipment	\$ 4,553
Goodwill	704
Accounts payable	<u>(152)</u>
Total purchase price	<u>\$ 5,105</u>

Cyphre Security Solutions

On May 18, 2017, RigNet completed its acquisition of Cyphre Security Solutions (Cyphre®) for an estimated aggregate purchase price of \$12.0 million. Of this aggregate purchase price, RigNet paid \$4.9 million in cash in May 2017, \$3.3 million in stock and expects to pay \$3.8 million of contingent consideration for intellectual property, estimated as of the date of acquisition. Cyphre is a cybersecurity company that provides advanced enterprise data protection leveraging BlackTIE® hardware-based encryption featuring low latency protection for files at rest and in transit for both public and private cloud. Cyphre is based in Texas.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The contingent consideration for Cyphre is measured at fair value, based on level 3 inputs, with any change to fair value recorded in the Condensed Consolidated Statements of Comprehensive Loss in each reporting period. As of September 30, 2018, the fair value of the contingent consideration was \$4.0 million. During the three and nine months ended September 30, 2018, RigNet recognized accreted interest expense on the Cyphre contingent consideration of \$0.1 million with corresponding increases to other liabilities.

The assets and liabilities of Cyphre have been recorded at their estimated fair values at the date of acquisition. The excess of the purchase price over the estimated fair values of the underlying net tangible and identifiable intangible assets and liabilities has been recorded as goodwill.

The goodwill of \$4.6 million arising from the acquisition consists largely of growth prospects, synergies and other benefits that the Company believes will result from combining the operations of the Company and Cyphre, as well as other intangible assets that do not qualify for separate recognition, such as assembled workforce in place at the date of acquisition. The goodwill recognized is expected to be deductible for income tax purposes. The acquisition of Cyphre, including goodwill, is included in the Company's condensed consolidated financial statements as of the acquisition date and is reflected in the Applications and Internet-of-Things segment.

	Weighted Average Estimated Useful Life (Years)	Fair Market Values (in thousands)
Property and equipment		\$ 18
Trade name	7	\$1,590
Technology	7	5,571
Customer relationships	7	<u>332</u>
Total identifiable intangible assets		7,493
Goodwill		4,591
Accrued expenses		<u>(100)</u>
Total purchase price		<u>\$12,002(a)</u>

(a) Includes \$3.8 million in contingent consideration estimated as of the date of acquisition.

Actual and Pro Forma Impact of the 2017 Acquisitions

The 2017 acquisitions of ESS, DTS and Cyphre contributed \$2.4 million of revenue for the three and nine months ended September 30, 2017. The 2017 acquisitions contributed \$0.6 million and \$0.3 million to net income for the three and nine months ended September 30, 2017, respectively.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following table represents supplemental pro forma information as if the 2017 acquisitions had occurred on January 1, 2017.

	<u>Three Months Ended</u> <u>September 30,</u> <u>2017</u>	<u>Nine Months Ended</u> <u>September 30,</u> <u>2017</u>
	(in thousands, except per share amounts)	
Revenue	\$ 52,150	\$ 158,085
Expenses	55,993	165,484
Net loss	<u>\$ (3,843)</u>	<u>\$ (7,399)</u>
Net loss attributable to RigNet, Inc. common stockholders	<u>\$ (3,882)</u>	<u>\$ (7,516)</u>
Net loss per share attributable to RigNet, Inc. common stockholders:		
Basic	<u>\$ (0.21)</u>	<u>\$ (0.42)</u>
Diluted	<u>\$ (0.21)</u>	<u>\$ (0.42)</u>

Note 3 – Business and Credit Concentrations

The Company is exposed to various business and credit risks including interest rate, foreign currency, credit and liquidity risks.

Interest Rate Risk

The Company has significant interest-bearing liabilities at variable interest rates which generally price monthly. The Company's variable borrowing rates are tied to LIBOR resulting in interest rate risk (see Note 6 – Long-Term Debt). The Company presently does not use financial instruments to hedge interest rate risk, but evaluates this on a regular basis and may utilize financial instruments in the future if deemed necessary.

Foreign Currency Risk

The Company has exposure to foreign currency risk, as a portion of the Company's activities are conducted in currencies other than U.S. dollars. Currently, the Norwegian Kroner, the British Pound Sterling and the Brazilian Real are the currencies that could materially impact the Company's financial position and results of operations. The Company presently does not hedge these risks, but evaluates financial risk on a regular basis and may utilize financial instruments in the future if deemed necessary. Foreign currency translations are reported as accumulated other comprehensive loss in the Company's condensed consolidated financial statements.

Credit Risk

Credit risk, with respect to accounts receivable, is due to the limited number of customers concentrated in the oil and gas, maritime, pipeline, engineering and construction industries. The Company mitigates the risk of financial loss from defaults through defined collection terms in each contract or service agreement and periodic evaluations of the collectability of accounts receivable. The Company provides an allowance for doubtful accounts which is adjusted when the Company becomes aware of a specific customer's inability to meet its financial obligations or as a result of changes in the overall aging of accounts receivable.

Liquidity Risk

The Company maintains cash and cash equivalent balances with major financial institutions which, at times, exceed federally insured limits. The Company monitors the financial condition of the financial institutions and has not experienced losses associated with these accounts during 2018 or 2017. Liquidity risk is managed by continuously monitoring forecasted and actual cash flows and by matching the maturity profiles of financial assets and liabilities (see Note 6 – Long-Term Debt).

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 4 – Goodwill and Intangibles

Goodwill

Goodwill resulted from prior acquisitions as the consideration paid for the acquired businesses exceeded the fair value of acquired identifiable net tangible and intangible assets. Goodwill is reviewed for impairment at least annually with additional evaluations being performed when events or circumstances indicate that the carrying value of these assets may not be recoverable.

Due to the change in segments (see Note 12 – Segment Information) and reporting units during the third quarter of 2017, the Company re-allocated goodwill to each reporting unit based on relative fair value.

The Company acquired \$1.0 million of goodwill in the Systems Integration segment from the Auto-Comm and SAFCON acquisitions completed on April 18, 2018 (see Note 2 – Business Combinations).

The Company acquired \$10.7 million of goodwill in the Apps & IoT segment from the Intelie acquisition completed on March 23, 2018 (see Note 2 – Business Combinations).

The Company acquired \$8.5 million of goodwill in the Apps & IoT segment from the ESS acquisition completed on July 28, 2017 (see Note 2 – Business Combinations).

The Company acquired \$0.7 million of goodwill in the Managed Services segment from the DTS acquisition completed on July 24, 2017 (see Note 2 – Business Combinations).

The Company acquired \$4.6 million of goodwill in the Apps & IoT segment from the Cyphre acquisition completed on May 18, 2017 (see Note 2 – Business Combinations).

The Company performs its annual impairment test as of July 31st of each year, with the most recent annual test being performed as of July 31, 2018. As of July 31, 2018, the fair values of the Company's reporting units are in excess of their carrying values.

Managed Services had \$22.9 million of goodwill as of September 30, 2018, and fair value exceeded carrying value by 34.7% as of the July 31, 2018 annual impairment test. Apps & IoT had \$22.4 million of goodwill as of September 30, 2018, and fair value exceeded carrying value by 48.1% as of the July 31, 2018 annual impairment test. Systems Integration had \$1.0 million of goodwill as of September 30, 2018, and fair value exceeded carrying value by 126.5% as of the July 31, 2018 annual impairment test. Any future downturn in our business could adversely impact the key assumptions in our impairment test. While we believe that there appears to be no indication of current or future impairment, historical operating results may not be indicative of future operating results and events and circumstances may occur causing a triggering event in a period as short as three months.

No impairment indicators have been identified in any reporting unit as of September 30, 2018 and December 31, 2017.

As of September 30, 2018 and December 31, 2017, goodwill was \$46.3 million and \$37.1 million, respectively. Goodwill increases or decreases in value due to the effect of foreign currency translation, and increases with acquisitions.

Intangibles

Intangibles consist of customer relationships, brand name, backlog, technology and licenses acquired as part of the Company's acquisitions. Intangibles also include internal-use software. The Company's intangibles have useful lives ranging from 5.0 to 7.0 years and are amortized on a straight-line basis. Impairment testing is performed when events or circumstances indicate that the carrying value of the assets may not be recoverable.

No impairment indicators have been identified in any reporting unit as of September 30, 2018.

As of September 30, 2018 and December 31, 2017, intangibles were \$34.5 million and \$30.4 million, respectively. During the three months ended September 30, 2018 and 2017, the Company recognized amortization expense of \$2.6 million and \$1.9 million, respectively. During the nine months ended September 30, 2018 and 2017, the Company recognized amortization expense of \$7.2 million and \$4.7 million, respectively.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following table sets forth expected amortization expense of intangibles for the remainder of 2018 and the following years (in thousands):

2018	\$ 2,126
2019	7,132
2020	6,181
2021	5,893
2022	5,498
Thereafter	7,655
	<u>\$34,485</u>

Note 5 – Restricted Cash

As of September 30, 2018 and December 31, 2017, the Company had restricted cash of \$0.1 million and \$1.5 million, in current and long-term assets, respectively. The restricted cash in long-term assets was primarily used to collateralize a performance bond in the Managed Services segment (see Note 6 – Long-Term Debt).

Note 6 – Long-Term Debt

As of September 30, 2018 and December 31, 2017, the following credit facilities and long-term debt arrangements with financial institutions were in place:

	<u>September 30,</u> <u>2018</u>	<u>December 31,</u> <u>2017</u>
	(in thousands)	
Term loan, net of unamortized deferred financing costs	\$ 10,891	\$ 14,503
Revolving loan	60,150	43,400
Capital lease	116	211
	<u>71,157</u>	<u>58,114</u>
Less: Current maturities of long-term debt	(4,827)	(4,814)
Current maturities of capital lease	(116)	(127)
	<u>\$ 66,214</u>	<u>\$ 53,173</u>

Credit Agreement

On November 6, 2017, the Company entered into its third amended and restated credit agreement with four participating financial institutions. The credit agreement provides for a \$15.0 million term loan facility (Term Loan) and an \$85.0 million revolving credit facility (RCF) and matures on November 6, 2020.

The RCF contains a sub-limit of up to \$25.0 million for commercial and stand-by letters of credit and performance bonds. The facilities under the credit agreement are secured by substantially all the assets of the Company.

Under the credit agreement, both the Term Loan and RCF bear interest at a rate of LIBOR plus a margin ranging from 1.75% to 2.75% based on a consolidated leverage ratio defined in the credit agreement. Interest is payable monthly and principal installments of \$1.25 million under the Term Loan are due quarterly. The weighted average interest rate for the three months ended September 30, 2018 and 2017 were 4.9% and 3.2%, respectively. The weighted average interest rate for the nine months ended September 30, 2018 and 2017 were 4.7% and 3.1%, respectively, with an interest rate of 5.0% at September 30, 2018.

Term Loan

As of September 30, 2018, the Term Loan had an outstanding principal balance of \$11.3 million, excluding the impact of unamortized deferred financing costs.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

RCF

As of September 30, 2018, \$60.2 million in draws remain outstanding under the RCF.

Covenants and Restrictions

The Company's credit agreement contains certain covenants and restrictions, including restricting the payment of cash dividends under default and maintaining certain financial covenants such as a consolidated leverage ratio, defined in the credit agreement, of less than or equal to 2.75 to 1.0 and a consolidated fixed charge coverage ratio of not less than 1.25 to 1.0 as of September 30, 2018. If any default occurs related to these covenants that is not cured or waived, the unpaid principal and any accrued interest can be declared immediately due and payable. As of September 30, 2018, and December 31, 2017, the Company believes it was in compliance with all covenants.

Performance Bonds and Letters of Credit

On September 14, 2012, NesscoInvsat Limited, a subsidiary of RigNet, secured a performance bond facility. On November 6, 2017, this facility became a part of the third amended and restated credit agreement and falls under the \$25.0 million sub-limit of the RCF for commercial and standby letters of credit and performance bonds.

As of September 30, 2018, there were no outstanding standby letters of credit. There were \$2.2 million of performance bonds outstanding.

In June 2016, the Company secured a performance bond facility with a lender in the amount of \$1.5 million for its Managed Services segment. This facility has a maturity date of June 2021. The Company maintains restricted cash on a dollar for dollar basis to secure this facility.

Debt Maturities

The following table sets forth the aggregate principal maturities of long-term debt, net of deferred financing cost amortization, for the remainder of 2018 and the following years (in thousands):

2018	\$ 1,238
2019	4,914
2020	65,005
Total debt, including current maturities	<u>\$71,157</u>

Note 7 – Fair Value Disclosures

The Company uses the following methods and assumptions to estimate the fair value of financial instruments:

- **Cash and Cash Equivalents** — Reported amounts approximate fair value based on quoted market prices (Level 1).
- **Restricted Cash** — Reported amounts approximate fair value.
- **Accounts Receivable** — Reported amounts, net of the allowance for doubtful accounts, approximate fair value due to the short-term nature of these assets.
- **Accounts Payable, Including Income Taxes Payable and Accrued Expenses** — Reported amounts approximate fair value due to the short-term nature of these liabilities.
- **Long-Term Debt** — The carrying amount of the Company's floating-rate debt approximates fair value since the interest rates paid are based on short-term maturities and recent quoted rates from financial institutions. The estimated fair value of debt was calculated based upon observable (Level 2) inputs regarding interest rates available to the Company at the end of each respective period.

The Company's non-financial assets, such as goodwill, intangibles and property, plant and equipment, are measured at fair value, based on level 3 inputs, when there is an indicator of impairment and recorded at fair value only when an impairment charge is recognized.

The earn-out for Intelie is measured at fair value, based on level 3 inputs, with any change to fair value recorded in the Condensed Consolidated Statements of Comprehensive Loss in each reporting period. As of September 30, 2018, the fair value of the earn-out was \$7.7 million. During the three and nine months ended September 30, 2018, RigNet recognized accreted interest expense on the Intelie earn-out of \$0.1 million with corresponding increases to other liabilities.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The contingent consideration for Cyphre is measured at fair value, based on level 3 inputs, with any change to fair value recorded in the Condensed Consolidated Statements of Comprehensive Loss in each reporting period. As of September 30, 2018, the fair value of the contingent consideration was \$4.0 million. During the three and nine months ended September 30, 2018, RigNet recognized accreted interest expense on the Cyphre contingent consideration of \$0.1 million with corresponding increases to other liabilities. During the three and nine months ended September 30, 2017, RigNet recognized accreted interest expense on the Cyphre contingent consideration of \$0.1 million.

The earn-out for Orgtec S.A.P.I. de C.V., d.b.a. TECNOR (TECNOR), acquired in February 2016, was measured at fair value, based on level 3 inputs, with any change to fair value recorded in the Condensed Consolidated Statements of Comprehensive Loss in each reporting period. The fair value of the earn-out of \$8.0 million was paid in July 2018. The \$2.1 million change in fair value in the nine months ended September 30, 2018 is primarily related to the second quarter 2018 negotiations with the sellers of TECNOR on the amount of the earn-out.

Additionally, the Company has agreed to pay the sellers of TECNOR up to \$1.0 million in either cash or RigNet stock payable in 2019 for the collection of certain accounts receivable balances. As of June 30, 2018, the fair value for the agreement to collect certain accounts receivable was \$0.8 million. As of September 30, 2018, the fair value for the agreement to collect certain accounts receivable was zero. The \$0.8 million reduction of fair value in the third quarter 2018 related to the reduction of the portion of the contingent consideration related to the subsequent collection of certain accounts receivable balances.

During the three and nine months ended September 30, 2018, RigNet recognized accreted interest expense on the TECNOR earn-out liability of \$0.1 million with corresponding increases to other liabilities. During the three and nine months ended September 30, 2017, RigNet recognized accreted interest expense on the TECNOR earn-out liability of \$0.1 million and \$0.4 million, respectively.

Note 8 – Income Taxes

The Company's effective income tax rate was (12.6%) and 0.1% for the three and nine months ended September 30, 2018, respectively. The Company's effective income tax rate was (22.2%) and (11.5%) for the three and nine months ended September 30, 2017, respectively. The Company's effective tax rate is affected by factors including changes in valuation allowances, fluctuations in income across jurisdictions with varying tax rates, and changes in income tax reserves, including related penalties and interest.

The Company has computed the provision for taxes for the current and comparative periods using the actual year-to-date effective tax rate. The Company's financial projections for those periods did not provide the level of detail necessary to calculate a forecasted effective tax rate.

In October 2018, the Company has received an IRS notice informing us of an audit of the Company's 2016 income tax return. It is unclear if the audit and the appeals process, if necessary, will be completed within the next twelve months. The Company is in the early stages of the audit and is unable to quantify any potential settlement or outcome of the audit at this time.

The Company believes that it is reasonably possible that a decrease of up to \$3.3 million in unrecognized tax benefits, including related interest and penalties, may be necessary within the coming year due to lapse in statute of limitations.

On December 22, 2017 the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (The Tax Act), making broad and complex changes to the U.S. tax code.

The SEC staff issued SAB 118, which provides guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for companies to complete the accounting under ASC 740. In accordance with SAB 118, a company must reflect the income tax effects of those aspects of the Tax Act for which the accounting under ASC 740 is complete. To the extent that a company's accounting for certain income tax effects of the Tax Act is incomplete but it is able to determine a reasonable estimate, it must record a provisional estimate in the financial statements. If a company cannot determine a provisional estimate to be included in the financial statements, it should continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the enactment of the Tax Act.

The Company has completed the accounting for the income tax effects of the Tax Act. As noted in the Company's 2017 Annual Report on Form 10-K filed with the SEC on March 6, 2018, the Company was able to make reasonable estimates and recorded provisional adjustments. The Company has now completed the adjustments which are recorded as follows:

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Reduction of US Federal Corporate Tax Rate: In the fourth quarter of 2017, the Company recorded a provisional decrease of \$8.2 million to deferred tax expense related to the US federal corporate tax rate reduction. The Company will not make any additional measurement-period adjustments and considers this item complete.

Deemed Repatriation Transition Tax: In the fourth quarter of 2017, the Company recorded a provisional Transition Tax obligation of \$3.8 million, which was fully offset by current losses and foreign tax credits. On August 1, 2018 the Department of Treasury and the Internal Revenue Service issued proposed regulations which provide additional guidance on the provisions of the Transition Tax under Section 965, including the election not to apply net operating loss deductions against the Transition Tax. The Company elected to apply foreign tax credits against the Transition Tax rather than current year operating losses. The final Transition Tax obligation of \$4.0 million is fully offset by foreign tax credits. The Company considers this item complete.

Global Intangible Low Taxed Income (GILTI): In the fourth quarter of 2017, the Company was not able to reasonably estimate the effects for GILTI. Therefore, no provisional adjustment was recorded. Under U.S. GAAP, the Company is allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (the period cost method) or (2) factoring such amounts into a company's measurement of its deferred taxes (the deferred method). The Company's selection of an accounting policy related to the new GILTI tax rules will depend, in part, on analyzing its global income to determine whether it expects to have future U.S. inclusions in taxable income related to GILTI and, if so, what the impact is expected to be. The Company has elected to treat any future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (the period cost method). The Company considers this item complete.

As stated previously, the Company has finalized its evaluation of the U.S. Tax Act and deems it complete.

Note 9 – Stock-Based Compensation

During the nine months ended September 30, 2018, the Company granted a total of 439,150 stock-based awards to certain directors, officers and employees of the Company under the 2010 Omnibus Incentive Plan (2010 Plan). Of these, the Company granted (i) 144,005 restricted stock units (RSUs) to certain officers and employees that generally vest over a four year period of continued employment, with 25% of the RSUs vesting on each of the first four anniversaries of the grant date, (ii) 11,188 RSUs to certain officers and employees that generally vest over a two year period of continued employment, with 50% of the RSUs vesting on each of the first two anniversaries of the grant date, (iii) 48,179 RSUs to outside directors that vest in 2019, (iv) 157,442 unrestricted stock grants to certain officers and employees that vested immediately and (v) 78,336 performance share units (PSUs) to certain officers and employees that generally cliff vest on the third anniversary of the grant date and are subject to continued employment and certain performance based targets. The ultimate number of PSUs issued is based on a multiple determined by certain performance-based targets.

The fair value of RSUs and PSUs is determined based on the closing trading price of the Company's common stock on the grant date of the award. Compensation expense is recognized on a straight-line basis over the requisite service period of the entire award, net of forfeitures.

During the nine months ended September 30, 2018, the Company also granted 59,703 stock options with an exercise price of \$13.50 to certain officers and employees of the Company under the 2010 Plan. Options granted have a contractual term of ten years and vest over a four year period of continued employment, with 25% of the options vesting on each of the first four anniversaries of the grant date.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The fair value of each stock option award is estimated on the grant date using a Black-Scholes option valuation model, which uses certain assumptions as of the date of grant. The assumptions used for the stock option grants made during the nine months ended September 30, 2018, were as follows:

	<u>Nine Months Ended</u> <u>September 30,</u> <u>2018</u>
Expected volatility	48%
Expected term (in years)	7
Risk-free interest rate	2.8%
Dividend yield	—

Based on these assumptions, the weighted average grant date fair value of stock options granted during the nine months ended September 30, 2018 was \$7.14 per option.

During the nine months ended September 30, 2018, 79,579 RSUs and 44,749 stock options were forfeited.

Stock-based compensation expense related to the Company's stock-based compensation plans for the three months ended September 30, 2018 and 2017 was \$1.1 million and \$1.0 million, respectively. Stock-based compensation expense related to the Company's stock-based compensation plans for the nine months ended September 30, 2018 and 2017 was \$4.4 million and \$2.9 million, respectively. As of September 30, 2018, there was \$3.4 million of total unrecognized compensation cost related to unvested options, RSUs and restricted stock expected to vest. This cost is expected to be recognized over a remaining weighted-average period of 1.8 years.

Note 10 – Earnings (loss) per Share

Basic earnings (loss) per share (EPS) are computed by dividing loss attributable to RigNet common stockholders by the number of basic shares outstanding. Basic shares equal the total of the common shares outstanding, weighted for the average days outstanding for the period. Basic shares exclude the dilutive effect of common shares that could potentially be issued due to the exercise of stock options or vesting of restricted stock and RSUs. Diluted EPS is computed by dividing loss attributable to RigNet common stockholders by the number of diluted shares outstanding. Diluted shares equal the total of the basic shares outstanding and all potentially issuable shares, other than antidilutive shares, if any, weighted for the average days outstanding for the period. The Company uses the treasury stock method to determine the dilutive effect. In periods when a net loss is reported, all common stock equivalents are excluded from the calculation because they would have an anti-dilutive effect, meaning the loss per share would be reduced. Therefore, in periods when a loss is reported, basic and dilutive loss per share are the same.

For the three and nine months ended September 30, 2018, there were approximately 932,048 and 620,666 potentially issuable shares, respectively, excluded from the Company's calculation of diluted EPS that were excluded because the Company incurred a loss in the period and to include them would have been anti-dilutive.

For the three and nine months ended September 30, 2017, there were approximately 723,296 and 644,858 potentially issuable shares, respectively, excluded from the Company's calculation of diluted EPS that were excluded because the Company incurred a loss in the period and to include them would have been anti-dilutive.

Note 11 – Commitments and Contingencies

Legal Proceedings

In August 2017, the Company filed litigation in Harris County District Court and arbitration against one of its former Chief Executive Officers for, among other things, breach of fiduciary duty, misappropriation of trade secrets, unfair competition and breach of contract. That former executive filed counterclaims against the Company and one of its independent directors. The parties entered into a settlement agreement resolving all claims amongst themselves in May 2018 and dismissed the litigation and arbitration proceedings. The Company incurred legal expense of approximately \$0.7 million in connection with this dispute for the nine months ended September 30, 2018.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Global Xpress (GX) Dispute

Inmarsat plc (Inmarsat), a satellite telecommunications company, and the Company are in a dispute relating to a January 2014 agreement regarding the purchase by the Company of up to \$65.0 million, under certain conditions, of GX capacity from Inmarsat over several years (GX dispute). Inmarsat initiated arbitration regarding the GX dispute in October 2016. The parties dispute whether Inmarsat has met its contractual obligations with respect to the service under the agreement. In July 2017, pursuant to its contractual rights under the agreement, the Company delivered a notice of termination of the agreement to Inmarsat. In addition, the Company has filed certain counterclaims against Inmarsat. The parties have agreed to divide the arbitration into two phases, with the first phase to decide if RigNet's purchase obligation ever commenced and the second phase to address RigNet's counterclaims against Inmarsat. The parties attended an arbitration hearing on the first phase in June 2018 and are currently awaiting the decision of the arbitration panel.

The Company has incurred legal expenses of \$2.1 million in connection with the GX dispute for the nine months ended September 30, 2018. The Company may continue to incur significant legal fees, related expenses and management time in the future. The Company cannot predict the ultimate outcome of the GX dispute, the total costs to be incurred or the potential impact on personnel.

Based on the information available at this time and management's understanding of the GX dispute, the Company does not deem the likelihood of a material loss related to this dispute to be probable, so it has not accrued any liability related to the dispute. At this stage of the arbitration, the range of possible loss is not reasonably estimable, but could range from zero to the maximum amount payable under the contract for the services plus expenses.

Other Litigation

The Company, in the ordinary course of business, is a claimant or a defendant in various legal proceedings, including proceedings as to which the Company has insurance coverage and those that may involve the filing of liens against the Company or its assets.

Sales Tax Audit

The Company has received a routine sales tax audit notice from a state where the Company has operations. Per the notice, the audit can cover up to a four-year period. The Company is in the early stages of the audit, and does not have any estimates of further exposure, if any, for the tax years under review.

Operating Leases

The Company leases office space under lease agreements expiring on various dates through 2025. For the three months ended September 30, 2018 and 2017, the Company recognized expense under operating leases of \$0.7 million and \$0.9 million, respectively. For the nine months ended September 30, 2018 and 2017, the Company recognized expense under operating leases of \$2.1 million and \$2.9 million, respectively.

As of September 30, 2018, future minimum lease obligations for the remainder of 2018 and future years were as follows (in thousands):

2018	\$ 611
2019	1,648
2020	974
2021	786
2022	739
Thereafter	1,843
	<u>\$6,601</u>

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Commercial Commitments

The Company enters into contracts for satellite bandwidth and other network services with certain providers.

As of September 30, 2018, the Company had the following commercial commitments related to satellite and network services for the remainder of 2018 and the future years thereafter (in thousands):

2018	\$ 5,824
2019	10,109
2020	1,010
2021	109
	<u>\$17,052</u>

The Company is no longer reporting \$65.0 million in the above table for capacity from Inmarsat's GX network. Please see paragraph "Global Xpress (GX) Dispute" above for details of the ongoing arbitration and the Company's notice to terminate the contract with Inmarsat.

Note 12 – Segment Information

Segment information is prepared consistent with the components of the enterprise for which separate financial information is available and regularly evaluated by the chief operating decision-maker for the purpose of allocating resources and assessing performance.

RigNet considers its business to consist of the following segments:

- **Managed Services.** The Managed Services segment provides remote communications, telephony and technology services for offshore and onshore drilling rigs and production facilities, support vessels, and other remote sites.
- **Applications and Internet-of-Things (Apps & IoT).** The Apps & IoT segment provides applications over-the-top of the Managed Services including Supervisory Control and Data Acquisition (SCADA) provided primarily for pipelines and Software as a Service (SaaS) offerings including BlackTIE encryption, weather monitoring primarily in the North Sea (METOCEAN), real-time predictive analytics (Intelie Pipes and Intelie LIVE) and certain other value-added services such as Adaptive Video Intelligence (AVI).
- **Systems Integration.** The Systems Integration segment provides design and implementation services for customer telecommunications systems. Solutions are delivered based on the customer's specifications, adhering to international industry standards and best practices. Project services may include consulting, design, engineering, project management, procurement, testing, installation, commissioning and maintenance.

Corporate and eliminations primarily represents unallocated executive and support activities, interest expense, income taxes and eliminations.

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The Company's business segment information as of and for the three and nine months ended September 30, 2018 and 2017, is presented below.

	Three Months Ended September 30, 2018				
	Managed Services	Applications and Internet-of-Things	Systems Integration	Corporate and Eliminations	Consolidated Total
			(in thousands)		
Revenue	\$ 44,943	\$ 7,463	\$ 12,364	\$ —	\$ 64,770
Cost of revenue (excluding depreciation and amortization)	27,930	3,677	9,127	—	40,734
Depreciation and amortization	5,641	1,661	605	506	8,413
Selling, general and administrative	3,779	520	380	11,965	16,644
Operating income (loss)	<u>\$ 7,593</u>	<u>\$ 1,605</u>	<u>\$ 2,252</u>	<u>\$ (12,471)</u>	<u>\$ (1,021)</u>
Capital expenditures	6,413	109	—	—	6,522

	Three Months Ended September 30, 2017				
	Managed Services	Applications and Internet-of-Things	Systems Integration	Corporate and Eliminations	Consolidated Total
			(in thousands)		
Revenue	\$ 40,243	\$ 4,985	\$ 5,616	\$ —	\$ 50,844
Cost of revenue (excluding depreciation and amortization)	24,902	3,394	4,089	—	32,385
Depreciation and amortization	5,263	835	615	1,286	7,999
Selling, general and administrative	3,013	363	280	9,755	13,411
Operating income (loss)	<u>\$ 7,065</u>	<u>\$ 393</u>	<u>\$ 632</u>	<u>\$ (11,041)</u>	<u>\$ (2,951)</u>
Capital expenditures	5,655	198	—	—	5,853

	Nine Months Ended September 30, 2018				
	Managed Services	Applications and Internet-of-Things	Systems Integration	Corporate and Eliminations	Consolidated Total
			(in thousands)		
Revenue	\$128,705	\$ 19,375	\$ 30,530	\$ —	\$ 178,610
Cost of revenue (excluding depreciation and amortization)	78,982	9,927	21,752	—	110,661
Depreciation and amortization	17,012	3,344	1,922	2,478	24,756
Selling, general and administrative	13,017	1,304	1,260	37,433	53,014
Operating income (loss)	<u>\$ 19,694</u>	<u>\$ 4,800</u>	<u>\$ 5,596</u>	<u>\$ (39,911)</u>	<u>\$ (9,821)</u>
Total assets	165,532	47,694	23,609	14,403	251,238
Capital expenditures	18,709	377	—	645	19,731

	Nine Months Ended September 30, 2017				
	Managed Services	Applications and Internet-of-Things	Systems Integration	Corporate and Eliminations	Consolidated Total
			(in thousands)		
Revenue	\$122,531	\$ 9,846	\$ 15,701	\$ —	\$ 148,078
Cost of revenue (excluding depreciation and amortization)	75,798	6,844	12,656	—	95,298
Depreciation and amortization	17,509	849	1,813	2,696	22,867
Selling, general and administrative	12,435	1,149	1,179	22,606	37,369
Operating income (loss)	<u>\$ 16,789</u>	<u>\$ 1,004</u>	<u>\$ 53</u>	<u>\$ (25,302)</u>	<u>\$ (7,456)</u>
Total assets	184,678	33,353	15,857	3,960	237,848
Capital expenditures	13,081	198	—	645	13,924

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following table presents revenue earned from the Company's domestic and international operations for the three and nine months ended September 30, 2018 and 2017. Revenue is based on the location where services are provided or goods are sold. Due to the mobile nature of RigNet's customer base and the services provided, the Company works closely with its customers to ensure rig or vessel moves are closely monitored to ensure location of service information is properly reflected.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(in thousands)			
Domestic	\$18,876	\$17,136	\$ 52,510	\$ 46,110
International	45,894	33,708	126,100	101,968
Total	\$64,770	\$50,844	\$178,610	\$148,078

The following table presents goodwill and long-lived assets, net of accumulated depreciation, for the Company's domestic and international operations as of September 30, 2018 and December 31, 2017.

	September 30,	December 31,
	2018	2017
	(in thousands)	
Domestic	\$ 67,663	\$ 68,942
International	73,932	58,895
Total	\$ 141,595	\$ 127,837

Note 13 – Related Party

The Company has a reseller arrangement with Darktrace, which is an artificial intelligence company in cybersecurity that is partially owned by Kohlberg Kravis Roberts & Co. L.P. (KKR). KKR is a significant stockholder of the Company. Under the arrangement, the Company will sell Darktrace's cybersecurity audit services with the Company's cybersecurity offerings. In the three and nine months ended September 30, 2018, the Company purchased \$0.1 million from Darktrace in the ordinary course of business.

Note 14 – Restructuring Costs – Cost Reduction Plans

During the three and nine months ended September 30, 2018, the Company incurred a net pre-tax restructuring expense of \$0.7 million reported as general and administrative expense in the Corporate segment associated with the reduction of 17 employees.

During the three and nine months ended September 30, 2017, the Company incurred a net pre-tax restructuring expense of \$0.8 million reported as general and administrative expense in the Corporate segment associated with the reduction of 31 employees.

Item 2. Management's Discussion And Analysis Of Financial Condition And Results Of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the accompanying unaudited condensed consolidated financial statements as of September 30, 2018 and for the three and nine months ended September 30, 2018 and 2017 included elsewhere herein, and with our Annual Report on Form 10-K for the year ended December 31, 2017. The following discussion and analysis contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under "Risk Factors" in Item 1A of our Annual Report and elsewhere in this quarterly report. See "Forward-Looking Statements" below.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that are subject to a number of risks and uncertainties, many of which are beyond the Company's control. Forward-Looking statements may include statements about:

- new regulations, delays in drilling permits or other changes in the oil and gas industry;
- competition and competitive factors in the markets in which we operate;
- demand for our services and solutions;
- the advantages of our services compared to others;
- changes in technology and customer preferences and our ability to adapt our product and services offerings;
- our ability to develop and maintain positive relationships with our customers;
- our ability to retain and hire necessary employees and appropriately staff our marketing, sales and distribution efforts;
- our cash needs and expectations regarding cash flow from operations and capital expenditures;
- our expectations regarding the deductibility of goodwill for tax purposes;
- our strategy and acquisitions;
- our ability to develop and market additional products and services;
- our ability to manage and grow our business and execute our business strategy, including developing and marketing additional Applications and Internet-of-Things solutions, expanding our market share, increasing secondary and tertiary customer penetration at remote sites, enhancing systems integration and extending our presence into complementary remote communication segments through organic growth and strategic acquisitions;
- our ability to pursue, consummate and integrate merger and acquisition opportunities successfully;
- the GX dispute;
- the amount and timing of contingent consideration payments arising from our acquisitions;
- our cost reduction, restructuring activities and related expenses; and
- our financial performance, including our ability to expand Adjusted EBITDA through our operational leverage.

In some cases, forward-looking statements can be identified by terminology such as "may," "could," "should," "would," "expect," "plan," "project," "intend," "will," "anticipate," "believe," "estimate," "predict," "potential," "pursue," "target," "continue," the negative of such terms or other comparable terminology that convey uncertainty of future events or outcomes. All of these types of statements, other than statements of historical fact included in this Quarterly Report on Form 10-Q, are forward-looking statements.

The forward-looking statements contained in this Quarterly Report on Form 10-Q are largely based on Company expectations, which reflect estimates and assumptions made by Company management. These estimates and assumptions reflect management's best judgment based on currently known market conditions and other factors. Although the Company believes such estimates and assumptions to be reasonable, they are inherently uncertain and involve a number of risks and uncertainties beyond its control. In addition, management's assumptions may prove to be inaccurate. The Company cautions that the forward-looking statements contained in this Quarterly Report on Form 10-Q are not guarantees of future performance, and it cannot assure any reader that such statements will be realized or the forward-looking statements or events will occur. Future results may differ materially from those anticipated or

implied in forward-looking statements due to factors listed in the “Risk Factors” section of our Annual Report on Form 10-K for the year ended December 31, 2017 and elsewhere in this Quarterly Report on Form 10-Q. If one or more of these factors materialize, or if any underlying assumptions prove incorrect, our actual future results, performance or achievements may vary materially from any projected future results, performance or achievements expressed or implied by these forward-looking statements. The forward-looking statements speak only as of the date made, and other than as required by law, the Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

Our Operations

We are a global technology company that provides customized communications services, applications, real-time machine learning, and cybersecurity solutions to enhance customer decision-making and business performance. We deliver a digital transformation bundle that accelerates technology adoption and empowers customers to be always connected, always secure, and always learning.

Customers use our private networks to manage information flows and execute mission-critical operations primarily in remote areas where conventional telecommunications infrastructure is either unreliable or unavailable. We provide our clients what is often the sole means of communications for their remote operations.

Managed Service and Applications and Internet-of-Things customers are primarily served under fixed-price contracts, either on a monthly or day rate basis or for equipment sales. Our contracts are generally in the form of Master Service Agreements, or MSAs, with specific services being provided under individual service orders that have a term of up to three years with renewal options for offshore contracts that are generally longer-term contracts with few cancellation provisions, while land-based locations are generally shorter term or terminable on short notice without a penalty. Service orders are executed under the MSA for individual remote sites or groups of sites, and generally permit early termination on short notice without penalty in the event of force majeure, breach of the MSA or cold stacking of a drilling rig (when a rig is taken out of service and is expected to be idle for a protracted period of time). Systems Integration customers are served primarily under fixed-price, long-term contracts.

Segment information is prepared consistent with the components of the enterprise for which separate financial information is available and regularly evaluated by the chief operating decision-maker for the purpose of allocating resources and assessing performance.

- **Managed Services.** Our Managed Services segment provides remote communications, telephony and technology services for offshore and onshore drilling rigs and production facilities, support vessels, and other remote sites.
- **Applications and Internet-of-Things (Apps & IoT).** Our Apps & IoT segment provides applications over-the-top of the Managed Services including Supervisory Control and Data Acquisition (SCADA) provided primarily for pipelines and Software as a Service (SaaS) offerings including BlackTIE® encryption, weather monitoring primarily in the North Sea (METOCEAN), real-time predictive analytics (Intelie Pipes™ and Intelie LIVE) and certain other value-added services such as Adaptive Video Intelligence (AVI).
- **Systems Integration.** Our Systems Integration segment provides design and implementation services for customer telecommunications systems. Solutions are delivered based on the customer’s specifications, adhering to international industry standards and best practices. Project services may include consulting, design, engineering, project management, procurement, testing, installation, commissioning and maintenance.

Cost of revenue consists primarily of satellite charges, voice and data termination costs, network operations expenses, internet connectivity fees, equipment purchases for Systems Integration projects and direct service labor. Satellite charges consist of the costs associated with obtaining satellite bandwidth (the measure of capacity) used in the transmission of service to and from leased satellites. Direct service labor consists of field technicians, our Network Operations Center (NOC) employees, and other employees who directly provide services to customers. Network operations expenses consist primarily of costs associated with the operation of our NOC, which is maintained 24 hours a day, seven days a week. Depreciation and amortization is recognized on all property, plant and equipment either installed at a customer’s site or held at our corporate and regional offices, as well as intangibles arising from acquisitions and internal use software. Selling and marketing expenses consist primarily of salaries and commissions, travel costs and marketing communications. General and administrative expenses consist of expenses associated with our management, finance, contract, support and administrative functions.

Profitability generally increases or decreases at a managed services site as we add or lose customers and value-added services. Assumptions used in developing the rates for a site may not cover cost variances from inherent uncertainties or unforeseen obstacles, including both physical conditions and unexpected problems encountered with third party service providers.

Recent Developments

We have committed to upgrade our Gulf of Mexico microwave network. In conjunction with a major U.S. carrier, this upgrade will add 4G and 5G LTE capabilities to the existing network. Additionally, we are buying an office in Lafayette, Louisiana that will consolidate three separate legacy facilities. Gulf of Mexico LTE network buildout project and the purchase of the Lafayette, Louisiana office will increase capital expenditures for the remainder of 2018 and into 2019.

In August 2018, we announced the appointment of Lee M. Ahlstrom as Senior Vice President and Chief Financial Officer.

In July 2018, we paid an earn-out of \$8.0 million in connection with the February 2016 acquisition of TECNOR. The \$2.1 million change in fair value in the nine months ended September 30, 2018 is primarily related to the second quarter 2018 negotiations with the sellers of TECNOR on the amount of the earn-out. Additionally, we have agreed to pay the sellers of TECNOR up to \$1.0 million in either cash or RigNet stock payable in 2019 for the collection of certain accounts receivable balances. As of September 30, 2018, the fair value for the agreement to collect certain accounts receivable was zero. The \$0.8 million reduction of fair value in the third quarter 2018 related to the reduction of the portion of the contingent consideration related to the subsequent collection of certain accounts receivable balances.

On April 18, 2018, we completed the separate acquisitions of Automation Communications Engineering Corp. (Auto-Comm) and Safety Controls, Inc. (SAFCON) for an aggregate purchase price of \$6.7 million. Of this aggregate purchase price, we paid \$2.6 million in cash and \$4.1 million in stock. Auto-Comm provides a broad range of communications services, for both onshore and offshore remote locations, to the oil and gas industry. Auto-Comm brings over 30 years of systems integration experience in engineering and design, installation, testing, and maintenance. SAFCON offers a diverse set of safety, security, and maintenance services to the oil and gas industry. Auto-Comm and SAFCON have developed strong relationships with major energy companies that complement the relationships that we have established over the years. Auto-Comm and SAFCON are based in Louisiana.

On March 23, 2018, we completed the acquisition of Intelie Soluções Em Informática S.A (Intelie), for an estimated aggregate purchase price of \$18.1 million. Of this aggregate purchase price, we paid R\$10.6 million (BRL) (or approximately \$3.2 million) in cash, \$7.3 million in stock and expect to pay \$7.6 million worth of RigNet stock as contingent consideration earn-out, estimated as of the date of acquisition. The initial estimate of the earn-out payable was preliminary and remains subject to change based on the achievement of certain post-closing performance targets under the acquisition agreement. The maximum earn-out is \$17.0 million. Intelie is a real-time, predictive analytics company that combines an operational understanding with a machine learning approach. Intelie facilitates innovation via Intelie Pipes, a distributed query language with a complex event processor to aggregate and normalize real-time data from a myriad of data sources. This technology enables the Intelie LIVE platform to solve data integration, data quality, data governance and monitoring problems. Intelie LIVE is an operational intelligence platform that empowers clients to make timely, data-driven decisions in mission-critical real-time operations, including drilling, and longer-term, data-intensive projects, such as well planning. While primarily applicable to oil and gas, Intelie Live has broad applicability across many industry verticals. Intelie is based in Brazil.

As of September 30, 2018, we have backlog for our percentage of completion projects of \$41.4 million.

Known Trends and Uncertainties

Operating Matters

Uncertainties in the oil and gas industry may continue to impact our profitability. The fundamentals of the oil and gas industry we serve remain challenged into 2018, particularly offshore. Oil prices declined significantly throughout 2015 and into 2016 from the highs in mid-year 2014 due to lower-than-expected global oil demand growth, increased supply from U.S. unconventional sources and increased production from several international countries. Although oil prices and U.S. drilling rig counts have increased in 2017 and 2018 since their 2016 lows, the oil and gas environment continues to be challenged with operators focusing on projects with shorter pay-back periods that generally require less capital investment and lower costs from service providers and drilling contractors. The offshore drilling contracting environment remains challenged, with major offshore drilling contractors having experienced significant pressure on day rates, which in turn may have a negative impact on the rates we are able to charge customers. The price of Brent crude, a key indicator of activity for the oil and gas industry has increased throughout 2018 and has averaged \$72.74 per barrel through the nine months ending September 30, 2018. As a result, drilling contractors are expecting gradual demand recovery. Generally, a prolonged lower oil price environment decreases exploration and development drilling investment, utilization of drilling rigs and the activity of the global oil and gas industry that we serve.

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For the periods referenced below, we were serving the following managed service sites listed in the table below:

	3rd Quarter 2018	2nd Quarter 2018	1st Quarter 2018	4th Quarter 2017	3rd Quarter 2017
Selected Operational Data:					
Offshore drilling rigs (1)	191	190	188	182	184
Offshore Production	332	320	310	304	316
Maritime	187	177	176	172	165
Other sites (2)	640	610	525	513	510
Total	<u>1,350</u>	<u>1,297</u>	<u>1,199</u>	<u>1,171</u>	<u>1,175</u>

(1) Includes jack up, semi-submersible and drillship rigs

(2) Includes U.S. and International land sites, completion sites, man-camps, remote offices, and supply bases and offshore-related supply bases, shore offices, tender rigs and platform rigs

In addition, uncertainties that could impact our profitability include service responsiveness to remote locations, communication network complexities, political and economic instability in certain regions, cyber-attacks, export restrictions, licenses and other trade barriers. These uncertainties may result in the delay of service initiation, which may negatively impact our results of operations. Additional uncertainties that could impact our operating cash flows include the availability and cost of satellite bandwidth, timing of collecting our receivables, and our ability to increase our contracted services through sales and marketing efforts while leveraging the contracted satellite and other communication service costs.

Sales Tax Audit

We have received a routine sales tax audit notice from a state where we have operations. Per the notice, the audit can cover up to a four-year period. We are in the early stages of the audit and do not have any estimates of further exposure, if any, for the tax years under review.

Global Xpress (GX) Dispute

We and Inmarsat are in a dispute relating to a January 2014 agreement regarding the purchase of up to \$65.0 million, under certain conditions, of GX capacity from Inmarsat over several years. Inmarsat initiated arbitration regarding the GX dispute in October 2016. The parties dispute whether Inmarsat has met its contractual obligations with respect to the service under the agreement. In July 2017, pursuant to our contractual rights under the agreement, we delivered a notice of termination of the agreement to Inmarsat. In addition, we have filed certain counterclaims against Inmarsat. The parties have agreed to divide the arbitration into two phases, with the first phase to decide if our purchase obligation ever commenced and the second phase to address our counterclaims against Inmarsat. The parties attended an arbitration hearing on the first phase in June 2018 and are currently awaiting the decision of the arbitration panel.

We have incurred legal expenses of \$2.1 million in connection with the GX dispute for the nine months ended September 30, 2018. We may continue to incur significant legal fees, related expenses and management time in the future. We cannot predict the ultimate outcome of the GX dispute, the total costs to be incurred or the potential impact on personnel.

Based on the information available at this time and our understanding of the GX dispute, we do not deem the likelihood of a material loss related to this dispute to be probable, so we have not accrued any liability related to the dispute. At this stage of the arbitration, the range of possible loss is not reasonably estimable, but could range from zero to the maximum amount payable under the contract for the services plus expenses.

Results of Operations

The following table sets forth selected financial and operating data for the periods indicated.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(in thousands)			
Revenue	\$64,770	\$50,844	\$178,610	\$148,078
Expenses:				
Cost of revenue (excluding depreciation and amortization)	40,734	32,385	110,661	95,298
Depreciation and amortization	8,413	7,999	24,756	22,867
Selling and marketing	2,728	2,400	9,866	5,968
General and administrative	13,916	11,011	43,148	31,401
Total expenses	65,791	53,795	188,431	155,534
Operating loss	(1,021)	(2,951)	(9,821)	(7,456)
Other expense, net	(1,465)	(480)	(2,813)	(1,859)
Loss before income taxes	(2,486)	(3,431)	(12,634)	(9,315)
Income tax benefit (expense)	(312)	(762)	11	(1,075)
Net loss	(2,798)	(4,193)	(12,623)	(10,390)
Less: Net income attributable to non-controlling interest	49	39	109	117
Net loss attributable to RigNet, Inc. stockholders	<u>\$ (2,847)</u>	<u>\$ (4,232)</u>	<u>\$ (12,732)</u>	<u>\$ (10,507)</u>
Other Non-GAAP Data:				
Adjusted EBITDA	\$ 8,730	\$ 7,843	\$ 24,247	\$ 21,121

The following represents selected financial operating results for our segments:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(in thousands)			
Managed Services:				
Revenue	\$44,943	\$40,243	\$128,705	\$122,531
Cost of revenue (excluding depreciation and amortization)	27,930	24,902	78,982	75,798
Depreciation and amortization	5,641	5,263	17,012	17,509
Selling, general and administrative	3,779	3,013	13,017	12,435
Managed Services operating income	<u>\$ 7,593</u>	<u>\$ 7,065</u>	<u>\$ 19,694</u>	<u>\$ 16,789</u>
Applications and Internet-of-Things:				
Revenue	\$ 7,463	\$ 4,985	\$ 19,375	\$ 9,846
Cost of revenue (excluding depreciation and amortization)	3,677	3,394	9,927	6,844
Depreciation and amortization	1,661	835	3,344	849
Selling, general and administrative	520	363	1,304	1,149
Applications & Internet-of-Things operating income	<u>\$ 1,605</u>	<u>\$ 393</u>	<u>\$ 4,800</u>	<u>\$ 1,004</u>
Systems Integration:				
Revenue	\$12,364	\$ 5,616	\$ 30,530	\$ 15,701
Cost of revenue (excluding depreciation and amortization)	9,127	4,089	21,752	12,656
Depreciation and amortization	605	615	1,922	1,813
Selling, general and administrative	380	280	1,260	1,179
Systems Integration and Automation operating income	<u>\$ 2,252</u>	<u>\$ 632</u>	<u>\$ 5,596</u>	<u>\$ 53</u>

NOTE: Consolidated balances include the segments above along with corporate activities and intercompany eliminations.

Three Months Ended September 30, 2018 and 2017

Revenue. Revenue increased by \$13.9 million, or 27.4%, to \$64.8 million for the three months ended September 30, 2018 from \$50.8 million for the three months ended September 30, 2017. Revenue increased in all segments. The 2018 acquisitions of Auto-Comm, SAFCON and Intelie contributed revenue of \$7.0 million for the three months ended September 30, 2018. The Systems Integration segment increased \$6.7 million, or 120.2%, primarily due to \$5.1 million from the acquisition of Auto-Comm and SAFCON, and increased activity against a growing backlog of Systems Integration projects. The Managed Services segment increased \$4.7 million, or 11.7%, due to increased site count, the Gulf of Mexico LTE network buildout project and \$0.5 million from the acquisition of Auto-Comm and SAFCON. The Apps & IoT segment increased \$2.5 million, or 49.7%, due to our focus on growth of the application layer and IoT space, including \$0.8 million from the acquisition of Intelie and \$0.6 million from the acquisition of Auto-Comm and SAFCON.

Cost of Revenue (excluding depreciation and amortization). Cost of revenue (excluding depreciation and amortization) increased by \$8.3 million, or 25.8%, to \$40.7 million for the three months ended September 30, 2018 from \$32.4 million for the three months ended September 30, 2017. Cost of revenue (excluding depreciation and amortization) increased in the Systems Integration segment by \$5.0 million due to the acquisition of Auto-Comm and SAFCON and increased activity of Systems Integration projects. Cost of revenue (excluding depreciation and amortization) increased in the Managed Services segment by \$3.0 million to serve our increased site count. Cost of revenue (excluding depreciation and amortization) increased in the Apps & IoT segment by \$0.3 million as we invested in our strategy of expanding of the application layer and IoT space including the acquisition of Intelie.

Depreciation and Amortization. Depreciation and amortization expense increased by \$0.4 million to \$8.4 million for the three months ended September 30, 2018 from \$8.0 million for the three months ended September 30, 2017. The increase is primarily attributable to additions to property, plant and equipment and intangibles from acquisitions and capital expenditures.

Selling and Marketing. Selling and marketing expense increased \$0.3 million to \$2.7 million for the three months ended September 30, 2018 from \$2.4 million for the three months ended September 30, 2017. This increase was due to investments made towards our growth strategy including increased sales personnel and marketing strategy costs.

General and Administrative. General and administrative expenses increased by \$2.9 million to \$13.9 million for the three months ended September 30, 2018 from \$11.0 million for the three months ended September 30, 2017. General and administrative costs increased primarily due to increased personnel costs, bad debt expense, legal expenses, acquisitions and acquisition-related costs.

Income Tax Expense. Our effective income tax rate was (12.6%) and (22.2%) for the three months ended September 30, 2018 and 2017, respectively. Our effective tax rate is affected by factors including changes in valuation allowances, fluctuations in income across jurisdictions with varying tax rates, and changes in income tax reserves, including related penalties and interest.

Nine months Ended September 30, 2018 and 2017

Revenue. Revenue increased by \$30.5 million, or 20.6%, to \$178.6 million for the nine months ended September 30, 2018 from \$148.1 million for the nine months ended September 30, 2017. Revenue increased in all segments. The 2018 acquisitions of Auto-Comm, SAFCON and Intelie contributed revenue of \$13.2 million for the nine months ended September 30, 2018. The Systems Integration segment increased \$14.8 million, or 94.4%, primarily due to \$9.8 million from the acquisition of Auto-Comm and SAFCON and increased activity against a growing backlog of Systems Integration projects. The Apps & IoT segment increased \$9.5 million, or 96.8%, due to our focus on growth of the application layer and IoT space including \$1.6 million from the acquisition of Intelie, \$0.8 million from the acquisition of Auto-Comm and SAFCON and \$4.7 million from owning ESS for the full nine months ended September 30, 2018 compared to two months in 2017. The Managed Services segment increased \$6.2 million, or 5.0%, due to increased site count coupled with \$1.0 Million from the acquisition of Auto-Comm and SAFCON and \$2.3 million from owning DTS for the full nine months ended September 30, 2018 compared to two months in 2017.

Cost of Revenue (excluding depreciation and amortization). Cost of revenue (excluding depreciation and amortization) increased by \$15.4 million, or 16.1%, to \$110.7 million for the nine months ended September 30, 2018 from \$95.3 million for the nine months ended September 30, 2017. Cost of revenue (excluding depreciation and amortization) increased in the Systems Integration segment by \$9.1 million due to the acquisition of Auto-Comm and SAFCON and increased activity of Systems Integration projects. Cost of revenue (excluding depreciation and amortization) increased in the Managed Services segment by \$3.2 million due to serving an increased site count. Cost of revenue (excluding depreciation and amortization) increased in the Apps & IoT segment by \$3.1 million as we invested in our strategy of expanding of the application layer and IoT space including the acquisition of Intelie and ESS.

Depreciation and Amortization. Depreciation and amortization expense increased by \$1.9 million to \$24.8 million for the nine months ended September 30, 2018 from \$22.9 million for the nine months ended September 30, 2017. The increase is primarily attributable to additions to property, plant and equipment and intangibles from acquisitions and capital expenditures.

Selling and Marketing. Selling and marketing expense increased \$3.9 million to \$9.9 million for the nine months ended September 30, 2018 from \$6.0 million for the nine months ended September 30, 2017. This increase was due to investments made towards our growth strategy including increased sales personnel and marketing strategy costs.

General and Administrative. General and administrative expenses increased by \$11.7 million to \$43.1 million for the nine months ended September 30, 2018 from \$31.4 million for the nine months ended September 30, 2017. General and administrative costs increased primarily due to increased personnel costs, bad debt expense, legal expenses, acquisitions and acquisition-related costs.

Income Tax Expense. Our effective income tax rate was 0.1% and (11.5%) for the nine months ended September 30, 2018 and 2017, respectively. Our effective tax rate is affected by factors including changes in valuation allowances, fluctuations in income across jurisdictions with varying tax rates, and changes in income tax reserves, including related penalties and interest.

Liquidity and Capital Resources

At September 30, 2018, we had working capital, including cash and cash equivalents, of \$55.8 million.

Based on our current expectations, we believe our liquidity and capital resources will be sufficient for the conduct of our business and operations for the foreseeable future. We may also use a portion of our available cash to finance growth through the acquisition of, or investment in, businesses, products, services or technologies complementary to our current business, through mergers, acquisitions, joint ventures or otherwise, or to pay down outstanding debt.

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During the next twelve months, we expect our principal sources of liquidity to be cash flows from operating activities, cash and cash equivalents on hand and availability under our credit facility.

While we believe we have sufficient liquidity and capital resources to meet our current operating requirements and expansion plans, we may elect to pursue additional expansion opportunities within the next year which could require additional financing, which may include debt or equity offerings.

Beyond the next twelve months, we expect our principal sources of liquidity to be cash flows provided by operating activities, cash and cash equivalents on hand, availability under our credit facility and additional financing activities we may pursue, which may include debt or equity offerings.

	Nine Months Ended September 30,	
	2018	2017
(in thousands)		
Condensed Consolidated Statements of Cash Flows Data:		
Cash and cash equivalents including restricted cash, January 1,	\$ 36,141	\$ 58,805
Net cash provided by operating activities	1,352	20,888
Net cash used in investing activities	(23,511)	(45,117)
Net cash provided by (used) in financing activities	6,157	(1,052)
Changes in foreign currency translation	2,175	919
Cash and cash equivalents including restricted cash, September 30,	<u>\$ 22,314</u>	<u>\$ 34,443</u>

Currently, the Norwegian Kroner, the British Pound Sterling and the Brazilian Real are the foreign currencies that could materially impact our liquidity. We presently do not hedge these risks, but evaluate financial risk on a regular basis and may utilize financial instruments in the future if deemed necessary. During the nine months ended September 30, 2018 and 2017, 91.4% and 90.2% of our revenue was denominated in U.S. dollars, respectively.

Operating Activities

Net cash provided by operating activities was \$1.4 million for the nine months ended September 30, 2018 compared to cash provided by operating activities of \$20.9 million for the nine months ended September 30, 2017. The decrease in cash from operating activities during 2018 of \$19.5 million was primarily due to the timing of collecting receivables coupled with increased operating loss.

Our cash provided by operations is subject to many variables including the volatility of the oil and gas industry and the demand for our services. Other factors impacting operating cash flows include the availability and cost of satellite bandwidth, as well as the timing of collecting our receivables. Our future cash flow from operations will depend on our ability to increase our contracted services through our sales and marketing efforts while leveraging our contracted satellite and other communication service costs.

Investing Activities

Net cash used in investing activities was \$23.5 million and \$45.1 million for the nine months ended September 30, 2018 and 2017, respectively.

Net cash used in investing activities during the nine months ended September 30, 2018 and 2017 included \$5.4 million and \$32.2 million for acquisitions, respectively, and \$18.8 million and \$13.2 million of capital expenditures, respectively. We expect capital expenditures for 2018 to be higher than 2017 as we build out our LTE network in the Gulf of Mexico and consolidate multiple Louisiana facilities into one facility.

Financing Activities

Net cash provided by financing activities was \$6.2 million for the nine months ended September 30, 2018. Cash provided by financing activities for the nine months ended September 30, 2018 included \$16.8 million in proceeds from borrowings and \$3.8 million in principal payments on our long-term debt. Additionally, we paid the \$8.0 million TECNOR earnout in July 2018, of which \$6.4 million is in cash flows from financing activities and \$1.6 million is in cash flows from operating activities.

Net cash used in financing activities was \$1.1 million for the nine months ended September 30, 2017. Cash used in financing activities for the nine months ended September 30, 2017 included \$16.7 million in principal payments on our long-term debt partially offset by draws of \$15.0 million on our RCF.

Credit Agreement

We have a \$15.0 million term loan facility (Term Loan) and an \$85.0 million revolving credit facility (RCF), which includes a \$25.0 million sublimit for the issuance of commercial and standby letters of credit and performance bonds.

Both the Term Loan and RCF bear an interest rate of LIBOR plus a margin ranging from 1.75% to 2.75%, based on a consolidated leverage ratio defined in the credit agreement. Interest is payable monthly and principal installments of \$1.25 million under the Term Loan are due quarterly, with the balance due November 6, 2020.

The weighted average interest rate for the three months ended September 30, 2018 and 2017 were 4.9% and 3.2%, respectively. The weighted average interest rate for the nine months ended September 30, 2018 and 2017 were 4.7% and 3.1%, respectively, with an interest rate of 5.0% at September 30, 2018. As of September 30, 2018, the outstanding principal amount of the Term Loan was \$11.3 million, excluding the impact of unamortized deferred financing costs. As of September 30, 2018, \$60.2 million in draws on the RCF remain outstanding.

The credit agreement contains certain covenants and restrictions, including restricting the payment of cash dividends when under default and maintaining certain financial covenants such as a consolidated leverage ratio, defined in the credit agreement, of less than or equal to 2.75 to 1.0 and a consolidated fixed charge coverage ratio of not less than 1.25 to 1.0. If any default occurs related to these covenants that was not cured or waived, the unpaid principal and any accrued interest can be declared immediately due and payable. The facilities under the credit agreement are secured by substantially all our assets. As of September 30, 2018, we believe we were in compliance with all covenants. We will continue to monitor our covenant compliance and intend to adjust our capital strategy, as needed. However, our ability to maintain compliance with these covenants is also dependent on our future financial performance and market conditions, which may vary from current expectations.

Off-Balance Sheet Arrangements

We do not engage in any off-balance sheet arrangements.

Non-GAAP Measure

Adjusted EBITDA should not be considered as an alternative to net loss, operating income (loss), basic or diluted loss per share or any other measure of financial performance calculated and presented in accordance with GAAP. Our Adjusted EBITDA may not be comparable to similarly titled measures of other companies because other companies may not calculate Adjusted EBITDA or similarly titled measures in the same manner as we do. We prepare Adjusted EBITDA to eliminate the impact of items that we do not consider indicative of our core operating performance. We encourage you to evaluate these adjustments and the reasons we consider them appropriate. Net loss is the most comparable GAAP measure to Adjusted EBITDA.

We define Adjusted EBITDA as net loss plus interest expense (benefit), income tax expense, depreciation and amortization, impairment of goodwill, intangibles, property, plant and equipment, (gain) loss on sales of property, plant and equipment, net of retirements, change in fair value of earn-outs and contingent consideration, stock-based compensation, acquisition costs, executive departure costs, restructuring charges and non-recurring items.

We believe Adjusted EBITDA is useful to investors in evaluating our operating performance for the following reasons:

- Investors and securities analysts use Adjusted EBITDA as a supplemental measure to evaluate the overall operating performance of companies, and we understand our investor and analyst's presentations include Adjusted EBITDA;
- By comparing our Adjusted EBITDA in different periods, our investors may evaluate our operating results without the additional variations caused by items that we do not consider indicative of our core operating performance and which are not necessarily comparable from year to year; and
- Adjusted EBITDA is an integral component of Consolidated EBITDA, as defined and used in the financial covenant ratios in the credit agreement.

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Our management uses Adjusted EBITDA:

- To indicate profit contribution;
- For planning purposes, including the preparation of our annual operating budget and as a key element of annual incentive programs;
- To allocate resources to enhance the financial performance of our business; and
- In communications with our Board of Directors concerning our financial performance.

Although Adjusted EBITDA is frequently used by investors and securities analysts in their evaluations of companies, Adjusted EBITDA has limitations as an analytical tool, and you should not consider it in isolation or as a substitute for analysis of our results of operations as reported under GAAP. Some of these limitations are:

- Adjusted EBITDA does not reflect our cash expenditures or future requirements for capital expenditures or other contractual commitments;
- Adjusted EBITDA does not reflect changes in, or cash requirements for, our working capital needs;
- Adjusted EBITDA does not reflect interest expense;
- Adjusted EBITDA does not reflect cash requirements for income taxes;
- Adjusted EBITDA does not reflect impairment of goodwill, intangibles, property, plant and equipment;
- Adjusted EBITDA does not reflect foreign exchange impact of intercompany financing activities;
- Adjusted EBITDA does not reflect (gain) loss on retirement of property, plant and equipment;
- Adjusted EBITDA does not reflect the stock-based compensation component of employee compensation;
- Adjusted EBITDA does not reflect acquisition costs;
- Adjusted EBITDA does not reflect change in fair value of earn-outs and contingent consideration;
- Adjusted EBITDA does not reflect executive departure costs;
- Adjusted EBITDA does not reflect restructuring charges;
- Although depreciation and amortization are non-cash charges, the assets being depreciated or amortized will often have to be replaced in the future, and Adjusted EBITDA does not reflect any cash requirements for these replacements; and
- Other companies in our industry may calculate Adjusted EBITDA or similarly titled measures differently than we do, limiting its usefulness as a comparative measure.

The following table presents a reconciliation of our net loss to Adjusted EBITDA.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(in thousands)			
Net loss	\$(2,798)	\$(4,193)	\$(12,623)	\$(10,390)
Interest expense	807	689	2,773	1,921
Depreciation and amortization	8,413	7,999	24,756	22,867
Loss on sales of property, plant and equipment, net of retirements	66	5	34	55
Stock-based compensation	1,086	1,007	4,368	2,949
Restructuring	664	767	664	767
Change in fair value of earn-out/contingent consideration	(750)	—	2,050	(846)
Executive departure costs	—	—	161	—
Acquisition costs	930	807	2,075	2,723
Income tax expense (benefit)	312	762	(11)	1,075
Adjusted EBITDA (non-GAAP measure)	<u>\$ 8,730</u>	<u>\$ 7,843</u>	<u>\$ 24,247</u>	<u>\$ 21,121</u>

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We evaluate Adjusted EBITDA generated from our operations to assess the potential recovery of historical capital expenditures, determine timing and investment levels for growth opportunities, extend commitments of satellite bandwidth cost, invest in new products and services, expand or open new offices and service centers, and assist purchasing synergies.

Adjusted EBITDA increased by \$0.9 million to \$8.7 million for the three months ended September 30, 2018, from \$7.8 million for the three months ended September 30, 2017. Adjusted EBITDA increased by \$3.1 million to \$24.2 million for the nine months ended September 30, 2018, from \$21.1 million for the nine months ended September 30, 2017.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We are subject to a variety of risks, including foreign currency exchange rate fluctuations relating to foreign operations and certain purchases from foreign vendors. In the normal course of business, we assess these risks and have established policies and procedures to manage our exposure to fluctuations in foreign currency values.

Our objective in managing our exposure to foreign currency exchange rate fluctuations is to reduce the impact of adverse fluctuations in earnings and cash flows associated with foreign currency exchange rates. We presently do not hedge these risks, but evaluate financial risk on a regular basis and may utilize financial instruments in the future if deemed necessary. During the nine months ended September 30, 2018 and 2017, 8.6% and 9.8%, respectively, of our revenues were earned in non-U.S. currencies. At September 30, 2018 and 2017, we had no significant outstanding foreign exchange contracts.

Our results of operations and cash flows are subject to fluctuations due to changes in interest rates primarily from our variable interest rate long-term debt. We presently do not hedge these risks, but evaluate financial risk on a regular basis and may utilize financial instruments in the future if deemed necessary. The following analysis reflects the annual impacts of potential changes in our interest rate to net loss attributable to us and our total stockholders' equity based on our outstanding long-term debt on September 30, 2018 and December 31, 2017, assuming those liabilities were outstanding for the previous twelve months:

	<u>September 30,</u> <u>2018</u>	<u>December 31,</u> <u>2017</u>
	(in thousands)	
Effect on Net Income (Loss) and Equity—Increase/Decrease:		
1% Decrease/increase in rate	\$ 712	\$ 581
2% Decrease/increase in rate	\$ 1,423	\$ 1,162
3% Decrease/increase in rate	\$ 2,135	\$ 1,743

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2018. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the Exchange Act), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company’s management, including its principal executive and Chief Financial Officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of September 30, 2018, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) of the Exchange Act that occurred during the quarter ended September 30, 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Management included in its assessment of internal control over financial reporting all consolidated entities, but excluded certain acquiree processes related to operations from Auto-Comm and SAFCON acquired by the company on April 18, 2018, and Intelie acquired by the Company on March 23, 2018.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

In August 2017, the Company filed litigation in Harris County District Court and arbitration against one of its former Chief Executive Officers for, among other things, breach of fiduciary duty, misappropriation of trade secrets, unfair competition and breach of contract. That former executive filed counterclaims against the Company and one of its independent directors. The parties entered into a settlement agreement resolving all claims amongst themselves in May 2018 and dismissed the litigation and arbitration proceedings. The Company has incurred legal expense of approximately \$0.7 million in connection with this dispute for the nine months ended September 30, 2018.

Inmarsat plc (Inmarsat), a satellite telecommunications company, and the Company are in a dispute relating to a January 2014 agreement regarding the purchase by the Company of up to \$65.0 million, under certain conditions, of GX capacity from Inmarsat over several years (GX dispute). Inmarsat initiated arbitration regarding the GX dispute in October 2016. The parties dispute whether Inmarsat has met its contractual obligations with respect to the service under the agreement. In July 2017, pursuant to its contractual rights under the agreement, the Company delivered a notice of termination of the agreement to Inmarsat. In addition, the Company has filed certain counterclaims against Inmarsat. The parties have agreed to divide the arbitration into two phases, with the first phase to decide if RigNet’s purchase obligation ever commenced and the second phase to address RigNet’s counterclaims against Inmarsat. The parties attended an arbitration hearing on the first phase in June 2018 and are currently awaiting the decision of the arbitration panel.

The Company has incurred legal expenses of \$2.1 million in connection with the GX dispute for the nine months ended September 30, 2018. The Company may continue to incur significant legal fees, related expenses and management time in the future. The Company cannot predict the ultimate outcome of the GX dispute, the total costs to be incurred or the potential impact on personnel.

Based on the information available at this time and management’s understanding of the GX dispute, the Company does not deem the likelihood of a material loss related to this dispute to be probable, so it has not accrued any liability related to the dispute. At this stage of the arbitration, the range of possible loss is not reasonably estimable, but could range from zero to the maximum amount payable under the contract for the services plus expenses.

The Company, in the ordinary course of business, is a claimant or a defendant in various other legal proceedings, including proceedings as to which the Company has insurance coverage and those that may involve the filing of liens against the Company or its assets.

Item 1A. Risk Factors

There have been no material changes from the risk factors disclosed in “Part I, Item 1A. Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2017.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None

Item 6. Exhibits

The exhibits required to be filed with this Quarterly Report on Form 10-Q are listed in the Exhibit Index attached hereto and are incorporated herein by reference.

INDEX TO EXHIBITS

2.1	Share Purchase Agreement between RigNet, Inc. and the shareholders of Orgtec S.A.P.I. de C.V., d.b.a. TECNOR dated November 3, 2015 (filed as Exhibit 2.2 to the Registrant's Quarterly Report on Form 10-Q filed with the SEC on May 9, 2016, and incorporated herein by reference)
2.2	Share Purchase and Sale Agreement between RigNet, Inc. and the shareholders of Intelie Solucoes Em Informatica S.A. dated January 15, 2018 (filed as Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed with the SEC on January 17, 2018, and incorporated herein by reference)
3.1	Amended and Restated Certificate of Incorporation, as amended (filed as Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2016, and incorporated herein by reference)
3.2	Amendment to Amended and Restated Certificate of Incorporation, effective May 18, 2016. (filed as Exhibit 3.2 to the Registrant's Quarterly Report on Form 10-Q filed with the SEC on August 8, 2016, and incorporated herein by reference)
3.3	Second Amended and Restated Bylaws of the Registrant, as amended (filed as Exhibit 3.3 to the Registrant's Annual Report on Form 10-K filed with the SEC on March 6, 2018, and incorporated herein by reference)
10.1	Registration Rights Agreement among Digital Oilfield Investments LP and RigNet, Inc. dated as of August 14, 2018 (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on August 20, 2018, and incorporated herein by reference)
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Schema Document
101.CAL	XBRL Calculation Linkbase Document
101.LAB	XBRL Label Linkbase Document
101.PRE	XBRL Presentation Linkbase Document
101.DEF	XBRL Definition Linkbase Document

+ Indicates management contract or compensatory plan.

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.

Date: November 9, 2018

RIGNET, INC.

By: /s/ LEE M. AHLSTROM

Lee M. Ahlstrom

Senior Vice President and Chief Financial Officer

(Principal Financial Officer)

CERTIFICATION OF
CHIEF EXECUTIVE OFFICER
OF RIGNET, INC.
PURSUANT TO 15 U.S.C. SECTION 7241, AS ADOPTED
PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002

I, Steven E. Pickett, certify that:

- a. I have reviewed this Quarterly Report on Form 10-Q of RigNet, Inc. (the "Registrant");
- b. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- c. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
- d. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
 - d. disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
- e. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's Board of Directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: November 9, 2018

By: /s/ STEVEN E. PICKETT
Steven E. Pickett
Chief Executive Officer and President

CERTIFICATION OF
CHIEF FINANCIAL OFFICER
OF RIGNET, INC.
PURSUANT TO 15 U.S.C. SECTION 7241, AS ADOPTED
PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002

I, Lee Ahlstrom, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of RigNet, Inc. (the "Registrant");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
 - d. disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's Board of Directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: November 9, 2018

By: /s/ LEE AHLSTROM
Lee Ahlstrom
Chief Financial Officer

CERTIFICATION OF
CHIEF EXECUTIVE OFFICER
OF RIGNET, INC.
PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED
PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Quarterly Report on Form 10-Q for the period ended September 30, 2018 filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven E. Pickett, Chief Executive Officer of RigNet, Inc. (the "Company"), hereby certify, to my knowledge, that:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 9, 2018

/s/ STEVEN E. PICKETT

Steven E. Pickett

Chief Executive Officer and President

CERTIFICATION OF
CHIEF FINANCIAL OFFICER
OF RIGNET, INC.
PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED
PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Quarterly Report on Form 10-Q for the period ended September 30, 2018 filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Lee Ahlstrom, Chief Financial Officer, of RigNet, Inc. (the "Company"), hereby certify, to my knowledge, that:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 9, 2018

/s/ LEE AHLSTROM

Lee Ahlstrom
Chief Financial Officer