

KEY ENERGY SERVICES INC

Form 10-Q

May 11, 2017

Table of Contents

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

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Form 10-Q

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(Mark One)

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

For the Quarterly Period Ended March 31, 2017

or

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

Commission file number: 001-08038

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KEY ENERGY SERVICES, INC.  
(Exact name of registrant as specified in its charter)

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Delaware 04-2648081  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

1301 McKinney Street, Suite 1800, Houston, Texas 77010  
(Address of principal executive offices) (Zip Code)

(713) 651-4300  
(Registrant's telephone number, including area code)

None  
(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

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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. No

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes  No

As of May 5, 2017, the number of outstanding shares of common stock of the registrant was 20,096,462.

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Table of Contents

KEY ENERGY SERVICES, INC.  
 QUARTERLY REPORT ON FORM 10-Q  
 For the Quarter Ended March 31, 2017

Part I — Financial Information

Item 1. <u>Financial Statements</u>	<u>4</u>
Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>21</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>28</u>
Item 4. <u>Controls and Procedures</u>	<u>29</u>

Part II — Other Information

Item 1. <u>Legal Proceedings</u>	<u>30</u>
Item 1A. <u>Risk Factors</u>	<u>30</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>30</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>30</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>30</u>
Item 5. <u>Other Information</u>	<u>30</u>
Item 6. <u>Exhibits</u>	<u>30</u>

**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Statements that are not historical in nature or that relate to future events and conditions are, or may be deemed to be, forward-looking statements. These forward-looking statements are based on our current expectations, estimates and projections and management’s beliefs and assumptions concerning future events and financial trends affecting our financial condition and results of operations. In some cases, you can identify these statements by terminology such as “may,” “will,” “should,” “predicts,” “expects,” “believes,” “anticipates,” “projects,” “potential” or “continue” or the negative or other comparable terminology. These statements are only predictions and are subject to substantial risks and uncertainties and are not guarantees of performance. Future actions, events and conditions and future results of operations may differ materially from those expressed in these statements. In evaluating those statements, you should carefully consider the information above as well as the risks outlined in “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2016 and in the other reports we file with the Securities and Exchange Commission.

We undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date of this report except as required by law. All of our written and oral forward-looking statements are expressly qualified by these cautionary statements and any other cautionary statements that may accompany such forward-looking statements.

Important factors that may affect our expectations, estimates or projections include, but are not limited to, the following:

- conditions in the oil and natural gas industry, especially oil and natural gas prices and capital expenditures by oil and natural gas companies;

• volatility in oil and natural gas prices;  
• our ability to implement price increases or maintain pricing on our core services;  
• risks that we may not be able to reduce, and could even experience increases in, the costs of labor, fuel, equipment and supplies employed in our businesses;  
• industry capacity;  
• asset impairments or other charges;  
• the periodic low demand for our services and resulting operating losses and negative cash flows;  
• our highly competitive industry as well as operating risks, which are primarily self-insured, and the possibility that our insurance may not be adequate to cover all of our losses or liabilities;  
• significant costs and potential liabilities resulting from compliance with applicable laws, including those resulting from environmental, health and safety laws and regulations, specifically those relating to hydraulic fracturing, as well as climate change legislation or initiatives;

Table of Contents

our historically high employee turnover rate and our ability to replace or add workers, including executive officers and skilled workers;

our ability to incur debt or long-term lease obligations;

our ability to implement technological developments and enhancements;

severe weather impacts on our business;

our ability to successfully identify, make and integrate acquisitions and our ability to finance future growth of our operations or future acquisitions;

our ability to achieve the benefits expected from disposition transactions;

the loss of one or more of our larger customers;

our ability to generate sufficient cash flow to meet debt service obligations;

the amount of our debt and the limitations imposed by the covenants in the agreements governing our debt, including our ability to comply with covenants under our debt agreements;

an increase in our debt service obligations due to variable rate indebtedness;

our inability to achieve our financial, capital expenditure and operational projections, including quarterly and annual projections of revenue and/or operating income and our inaccurate assessment of future activity levels, customer demand, and pricing stability which may not materialize (whether for Key as a whole or for geographic regions and/or business segments individually);

risks affecting our international operations, including risks affecting our ability to execute our plans to withdraw from international markets outside North America;

our ability to respond to changing or declining market conditions, including our ability to reduce the costs of labor, fuel, equipment and supplies employed and used in our businesses;

our ability to maintain sufficient liquidity;

adverse impact of litigation; and

other factors affecting our business described in “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2016 and in the other reports we file with the Securities and Exchange Commission.

Table of Contents

## PART I — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

Key Energy Services, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(in thousands, except share amounts)

	March 31, 2017 (unaudited)	December 31, 2016 (unaudited)
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 82,710	\$ 90,505
Restricted cash	15,628	24,707
Accounts receivable, net of allowance for doubtful accounts of \$902 and \$168, respectively	62,939	71,327
Inventories	22,282	22,269
Other current assets	25,040	25,762
Total current assets	208,599	234,570
Property and equipment	408,405	408,716
Accumulated depreciation	(24,339 )	(3,565 )
Property and equipment, net	384,066	405,151
Intangible assets, net	506	520
Other non-current assets	11,075	17,740
<b>TOTAL ASSETS</b>	<b>\$ 604,246</b>	<b>\$ 657,981</b>
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 13,037	\$ 10,357
Current portion of long-term debt	2,500	2,500
Other current liabilities	89,740	103,938
Total current liabilities	105,277	116,795
Long-term debt	244,623	245,477
Workers' compensation, vehicular and health insurance liabilities	23,686	23,313
Deferred tax liabilities	—	35
Other non-current liabilities	29,645	29,744
Commitments and contingencies		
Equity:		
Preferred stock, \$0.01 par value; 10,000,000 shares authorized, none issued	—	—
Common stock, \$0.01 par value; 100,000,000 shares authorized, 20,096,462 shares issued and outstanding	201	201
Additional paid-in capital	256,445	252,421
Accumulated other comprehensive loss	1,472	239
Retained deficit	(57,103 )	(10,244 )
Total equity	201,015	242,617
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$ 604,246</b>	<b>\$ 657,981</b>

See the accompanying notes which are an integral part of these condensed consolidated financial statements.

Table of Contents

Key Energy Services, Inc. and Subsidiaries  
 Condensed Consolidated Statements of Operations  
 (in thousands, except per share data)  
 (unaudited)

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
REVENUES	\$101,452	\$ 111,088
COSTS AND EXPENSES:		
Direct operating expenses	87,306	90,598
Depreciation and amortization expense	21,301	35,752
General and administrative expenses	30,996	46,245
Impairment expense	187	—
Operating loss	(38,338 )	(61,507 )
Interest expense, net of amounts capitalized	7,710	21,584
Other income, net	(240 )	(1,231 )
Reorganization items, net	1,340	—
Loss before income taxes	(47,148 )	(81,860 )
Income tax benefit	289	246
NET LOSS	\$(46,859 )	\$(81,614 )
Loss per share:		
Basic and diluted	\$(2.33 )	\$(0.51 )
Weighted average shares outstanding:		
Basic and diluted	20,096	160,047

See the accompanying notes which are an integral part of these condensed consolidated financial statements.

Table of Contents

Key Energy Services, Inc. and Subsidiaries  
 Condensed Consolidated Statements of Comprehensive Income  
 (in thousands)  
 (unaudited)

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
NET LOSS	\$(46,859)	\$(81,614 )
Other comprehensive income:		
Foreign currency translation income	1,233	532
COMPREHENSIVE LOSS	\$(45,626)	\$(81,082 )

See the accompanying notes which are an integral part of these condensed consolidated financial statements.



Table of Contents

Key Energy Services, Inc. and Subsidiaries  
Condensed Consolidated Statements of Cash Flows  
(in thousands)  
(unaudited)

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$(46,859)	\$(81,614 )
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization expense	21,301	35,752
Impairment expense	187	—
Bad debt expense	622	665
Accretion of asset retirement obligations	59	142
Loss (income) from equity method investments	(19 )	83
Amortization and write-off of deferred financing costs and premium	121	1,306
Deferred income tax benefit	(32 )	(252 )
Loss (gain) on disposal of assets, net	(194 )	1,934
Share-based compensation	4,024	2,313
Excess tax expense from share-based compensation	—	2,508
Changes in working capital:		
Accounts receivable	7,964	30,653
Other current assets	164	5,038
Accounts payable, accrued interest and accrued expenses	(11,004 )	(20,895 )
Share-based compensation liability awards	—	(189 )
Other assets and liabilities	11,019	(7,508 )
Net cash used in operating activities	(12,647 )	(30,064 )
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Capital expenditures	(2,440 )	(2,701 )
Proceeds from sale of fixed assets	—	7,435
Net cash provided by (used in) investing activities	(2,440 )	4,734
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Repayments of long-term debt	(625 )	(787 )
Restricted cash	9,079	(18,605 )
Payment of deferred financing costs	(350 )	—
Repurchases of common stock	—	(143 )
Excess tax expense from share-based compensation	—	(2,508 )
Net cash provided by (used in) financing activities	8,104	(22,043 )
Effect of changes in exchange rates on cash	(812 )	(1,277 )
Net decrease in cash and cash equivalents	(7,795 )	(48,650 )
Cash and cash equivalents, beginning of period	90,505	204,354
Cash and cash equivalents, end of period	\$82,710	\$ 155,704

See the accompanying notes which are an integral part of these condensed consolidated financial statements.



Table of Contents

Key Energy Services, Inc. and Subsidiaries

NOTES TO CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS

NOTE 1. GENERAL

Key Energy Services, Inc., and its wholly owned subsidiaries (collectively, “Key,” the “Company,” “we,” “us,” “its,” and “our”) provide a full range of well services to major oil companies, foreign national oil companies and independent oil and natural gas production companies. Our services include rig-based and coiled tubing-based well maintenance and workover services, well completion and recompletion services, fluid management services, fishing and rental services, and other ancillary oilfield services. Additionally, certain of our rigs are capable of specialty drilling applications. We operate in most major oil and natural gas producing regions of the continental United States and we have operations in Russia, which we are attempting to sell. In addition, we have a technology development and control systems business based in Canada.

The accompanying unaudited condensed consolidated financial statements were prepared using generally accepted accounting principles in the United States of America (“GAAP”) for interim financial information and in accordance with the rules and regulations of the Securities and Exchange Commission (the “SEC”). The condensed December 31, 2016 balance sheet was prepared from audited financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2016 (the “2016 Form 10-K”). Certain information relating to our organization and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted in this Quarterly Report on Form 10-Q. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our 2016 Form 10-K.

The unaudited condensed consolidated financial statements contained in this report include all normal and recurring material adjustments that, in the opinion of management, are necessary for a fair presentation of our financial position, results of operations and cash flows for the interim periods presented herein. The results of operations for the three months ended March 31, 2017 are not necessarily indicative of the results expected for the full year or any other interim period, due to fluctuations in demand for our services, timing of maintenance and other expenditures, and other factors.

On October 24, 2016, Key and certain of our domestic subsidiaries filed voluntary petitions for reorganization under chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware pursuant to a prepackaged plan of reorganization (“the Plan”). The Plan was confirmed by the Bankruptcy Court on December 6, 2016, and the Company emerged from the bankruptcy proceedings on December 15, 2016 (“the Effective Date”).

Upon emergence on the Effective Date, the Company adopted fresh start accounting which resulted in the creation of a new entity for financial reporting purposes. As a result of the application of fresh start accounting, as well as the effects of the implementation of the Plan, the Consolidated Financial Statements on or after December 16, 2016 are not comparable with the Consolidated Financial Statements prior to that date.

References to “Successor” or “Successor Company” relate to the financial position and results of operations of the reorganized Company subsequent to December 15, 2016. References to “Predecessor” or “Predecessor Company” refer to the financial position and results of operations of the Company on and prior to December 15, 2016.

We have evaluated events occurring after the balance sheet date included in this Quarterly Report on Form 10-Q and through the date on which the unaudited condensed consolidated financial statements were issued, for possible disclosure of a subsequent event.

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES

The preparation of these unaudited condensed consolidated financial statements requires us to develop estimates and to make assumptions that affect our financial position, results of operations and cash flows. These estimates may also impact the nature and extent of our disclosure, if any, of our contingent liabilities. Among other things, we use estimates to (i) analyze assets for possible impairment, (ii) determine depreciable lives for our assets, (iii) assess future tax exposure and realization of deferred tax assets, (iv) determine amounts to accrue for contingencies, (v) value tangible and intangible assets, (vi) assess workers’ compensation, vehicular liability, self-insured risk accruals and other insurance reserves, (vii) provide allowances for our uncollectible accounts receivable, (viii) value our asset

retirement obligations, and (ix) value our equity-based compensation. We review all significant estimates on a recurring basis and record the effect of any necessary adjustments prior to publication of our financial statements. Adjustments made with respect to the use of estimates relate to improved information not previously available. Because of the limitations inherent in this process, our actual results may differ materially from these estimates. We believe that the estimates used in the preparation of these interim financial statements are reasonable.

## Table of Contents

There have been no material changes or developments in our evaluation of accounting estimates and underlying assumptions or methodologies that we believe to be a “Critical Accounting Policy or Estimate” as disclosed in our 2016 Form 10-K.

### Recent Accounting Developments

ASU 2016-18. In November 2016, the FASB issued ASU No. 2016-18 Statement of Cash Flows (Topic 230), Restricted Cash. This standard provides guidance on the presentation of restricted cash and restricted cash equivalents in the statement of cash flows. Restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period amounts shown on the statements of cash flows. The amendments of this ASU should be applied using a retrospective transition method and are effective for reporting periods beginning after December 15, 2017, with early adoption permitted. Other than the revised statement of cash flows presentation of restricted cash, the adoption of this standard is not expected to have an impact on our consolidated financial statements.

ASU 2016-15. In August 2016 the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments (a consensus of the FASB Emerging Issues Task Force) (ASU 2016-15), that clarifies how entities should classify certain cash receipts and cash payments on the statement of cash flows. The guidance also clarifies how the predominance principle should be applied when cash receipts and cash payments have aspects of more than one class of cash flows. The guidance will be effective for annual periods beginning after December 15, 2017 and interim periods within those annual periods. Early adoption is permitted. The Company is evaluating the effect of this standard on its consolidated financial statements.

ASU 2016-13. In June 2016, the FASB issued ASU 2016-13, Measurement of Credit Losses on Financial Instruments, that will change how companies measure credit losses for most financial assets and certain other instruments that aren’t measured at fair value through net income. The standard will replace today’s “incurred loss” approach with an “expected loss” model for instruments measured at amortized cost. For available-for-sale debt securities, entities will be required to record allowances rather than reduce the carrying amount. The amendments in this update will be effective for annual periods beginning after December 15, 2019 and interim periods within those annual periods. Early adoption is permitted for annual periods beginning after December 15, 2018. The Company is evaluating the effect of this standard on our consolidated financial statements.

ASU 2016-09. In March 2016, the FASB Issued ASU 2016-09 Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. This standard changes how companies account for certain aspects of share-based payment awards to employees, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The Company adopted the accounting guidance as of January 1, 2017 on a prospective basis. In accordance with the standard, the Company has made an election to account for forfeitures of equity awards as they occur. With the exception of excess tax benefits and deficiencies related to the vesting of share-based compensation now being recognized as an income tax expense or benefit on the income statement rather than additional paid in capital on the balance sheet, the adoption of this guidance did not have a material impact our consolidated financial statements.

ASU 2016-02. In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which will replace the existing lease guidance. The new standard is intended to provide enhanced transparency and comparability by requiring lessees to record right-of-use assets and corresponding lease liabilities on the balance sheet. Additional disclosure requirements include qualitative disclosures along with specific quantitative disclosures with the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. ASU 2016-02 is effective for the Company for annual reporting periods beginning after December 15, 2018, including interim periods within those fiscal years, with early adoption permitted. The new standard is required to be applied with a modified retrospective approach to each prior reporting period presented. We are currently evaluating the standard to determine the impact of its adoption on the consolidated financial statements.

ASU 2014-09. In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). The objective of this ASU is to establish the principles to report useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue from contracts with customers. The core principle is to 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. ASU 2014-09 must be adopted using either a full retrospective method or a modified retrospective method. During a July 2015 meeting, the FASB affirmed a proposal to defer the effective date of the new revenue standard for all entities by one year. As a result, ASU 2014-09 is effective for the Company for interim and annual reporting periods beginning after December 15, 2017 with early adoption permitted for interim and annual reporting periods beginning after December 15, 2016. We are currently evaluating the standard to determine the impact of its adoption on the consolidated financial statements, however, management believes that the impact to the financial statements will not be material.

**NOTE 3. ASSETS HELD FOR SALE**

In April 2015, we announced our decision to exit markets in which we participate outside of North America. Our strategy is to sell or relocate the assets of the businesses operating in these markets. During the fourth quarter of 2015, the

Table of Contents

assets and related liabilities of our Russian business unit which is included in our International reporting segment met the criteria for assets held for sale. We recorded a \$0.2 million impairment during the three months ended March 31, 2017 to reduce the carrying value of these assets to fair market value. We expect this sale to occur in the first half of 2017.

The following assets and related liabilities are classified as held for sale on our March 31, 2017 condensed consolidated balance sheet (in thousands):

## Current assets:

Cash and cash equivalents	\$ 1,844
Accounts receivable	1,068
Inventories	216
Other current assets	198
Total current assets	3,326
Property and equipment, net	493
Total assets	\$3,819

## Current liabilities:

Accounts payable	\$ 232
Total current liabilities	232
Net Assets	\$3,587

## NOTE 4. EQUITY

A reconciliation of the total carrying amount of our equity accounts for the three months ended March 31, 2017 is as follows (in thousands):

	COMMON STOCKHOLDERS					
	Common Stock Number of Shares	Common Stock Amount at Par	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Retained Deficit	Total
Balance at December 31, 2016	20,096	\$ 201	\$ 252,421	\$ 239	\$(10,244)	\$242,617
Foreign currency translation	—	—	—	1,233	—	1,233
Share-based compensation	—	—	4,024	—	—	4,024
Net loss	—	—	—	—	(46,859 )	(46,859 )
Balance at March 31, 2017	20,096	\$ 201	\$ 256,445	\$ 1,472	\$(57,103)	\$201,015

## NOTE 5. OTHER BALANCE SHEET INFORMATION

The table below presents comparative detailed information about other current assets at March 31, 2017 and December 31, 2016 (in thousands):

	March 31, 2017	December 31, 2016
Other current assets:		
Prepaid current assets	\$ 10,694	\$ 10,291
Reinsurance receivable	8,078	7,922
Current assets held for sale	3,326	3,667
Other	2,942	3,882
Total	\$ 25,040	\$ 25,762

Table of Contents

The table below presents comparative detailed information about other non-current assets at March 31, 2017 and December 31, 2016 (in thousands):

	March 31, December 31,	
	2017	2016
Other non-current assets:		
Reinsurance receivable	\$ 8,547	\$ 8,393
Deposits	1,323	8,292
Equity method investments	579	560
Non-current assets held for sale	493	360
Other	133	135
Total	\$ 11,075	\$ 17,740

The table below presents comparative detailed information about other current liabilities at March 31, 2017 and December 31, 2016 (in thousands):

	March 31, December 31,	
	2017	2016
Other current liabilities:		
Accrued payroll, taxes and employee benefits	\$ 15,975	\$ 23,224
Accrued operating expenditures	12,888	16,669
Income, sales, use and other taxes	8,716	10,748
Self-insurance reserve	33,917	35,484
Accrued interest	6,294	1,419
Accrued insurance premiums	1,469	2,347
Unsettled legal claims	5,195	5,398
Accrued severance	167	2,219
Current liabilities held for sale	232	371
Other	4,887	6,059
Total	\$ 89,740	\$ 103,938

The table below presents comparative detailed information about other non-current liabilities at March 31, 2017 and December 31, 2016 (in thousands):

	March 31, December 31,	
	2017	2016
Other non-current liabilities:		
Asset retirement obligations	\$ 8,900	\$ 9,035
Environmental liabilities	3,275	3,446
Accrued sales, use and other taxes	16,892	16,735
Other	578	528
Total	\$ 29,645	\$ 29,744

**NOTE 6. INTANGIBLE ASSETS**

The components of our other intangible assets as of March 31, 2017 and December 31, 2016 are as follows (in thousands):

	March 31, December 31,	
	2017	2016
Trademark:		
Gross carrying value	520	520
Accumulated amortization (14 )	—	—



Net carrying value	506	520
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11

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Table of Contents

The weighted average remaining amortization periods and expected amortization expense for the next five years for our definite lived intangible assets are as follows:

Weighted average remaining amortization period (years)	Expected amortization expense (in thousands)				
	Remainder of 2017	2018	2019	2020	2021 2022
Trademark	8.8	43	58	58	58 58

Amortization expense for our intangible assets was less than \$0.1 million and \$0.5 million for the three months ended March 31, 2017 and 2016, respectively.

## NOTE 7. DEBT

As of March 31, 2017 and December 31, 2016, the components of our debt were as follows (in thousands):

	March 31, 2017	December 31, 2016
Term Loan Facility due 2021	\$249,375	\$ 250,000
Unamortized debt issuance costs	(2,252 )	(2,023 )
Total	247,123	247,977
Less current portion	(2,500 )	(2,500 )
Long-term debt	\$244,623	\$ 245,477

## ABL Facility

On December 15, 2016, the Company and Key Energy Services, LLC, as borrowers (the “ABL Borrowers”), entered into the ABL Facility with the financial institutions party thereto from time to time as lenders (the “ABL Lenders”), Bank of America, N.A., as administrative agent for the lenders, and Bank of America, N.A. and Wells Fargo Bank, National Association, as co-collateral agents for the lenders. The ABL Facility provides for aggregate initial commitments from the ABL Lenders of \$100 million, and matures on June 15, 2021.

The ABL Facility provides the ABL Borrowers with the ability to borrow up to an aggregate principal amount equal to the lesser of (i) the aggregate revolving commitments then in effect and (ii) the sum of 85% of the value of eligible accounts receivable plus (b) 80% of the value of eligible unbilled accounts receivable, subject to a limit equal to the greater of (x) \$35 million and (y) 25% of the Commitments. The amount that may be borrowed under the ABL Facility is subject to increase or reduction based on certain segregated cash or reserves provided for by the ABL Facility. In addition, the percentages of accounts receivable and unbilled accounts receivable included in the calculation described above is subject to reduction to the extent of certain bad debt write-downs and other dilutive items provided in the ABL Facility.

Borrowings under the ABL Facility will bear interest, at the ABL Borrowers’ option, at a per annum rate equal to (i) LIBOR for 30, 60, 90, 180, or, with the consent of the ABL Lenders, 360 days, plus an applicable margin that varies from 2.5% to 4.5% depending on the Borrowers’ fixed charge coverage ratio at such time or (ii) a base rate equal to the sum of (a) the greatest of (x) the prime rate, (y) the federal funds rate, plus 0.50% or (z) 30-day LIBOR, plus 1.0% plus (b) an applicable margin that varies from 1.50% to 3.50% depending on the Borrowers’ fixed charge coverage ratio at such time. In addition, the ABL Facility provides for unused line fees of 1.00% to 1.25% per year, depending on utilization, letter of credit fees and certain other factors.

The ABL Facility may in the future be guaranteed by certain of the Company’s existing and future subsidiaries (the “ABL Guarantors,” and together with the ABL Borrowers, the “ABL Loan Parties”). To secure their obligations under the ABL Facility, each of the ABL Loan Parties has granted or will grant, as applicable, to the Administrative Agent a first-priority security interest for the benefit of the ABL Lenders in its present and future accounts receivable, inventory and related assets and proceeds of the foregoing (the “ABL Priority Collateral”). In addition, the obligations of the ABL Loan Parties under the ABL Facility are secured by second-priority liens on the Term Priority Collateral (as described below under “Term Loan Facility”).

The revolving loans under the ABL Facility may be voluntarily prepaid, in whole or in part, without premium or penalty, subject to breakage or similar costs.

The ABL Facility contains certain affirmative and negative covenants, including covenants that restrict the ability of the ABL Loan Parties to take certain actions including, among other things and subject to certain significant exceptions, the incurrence of debt, the granting of liens, the making of investments, entering into transactions with affiliates, the payment of dividends and

Table of Contents

the sale of assets. The ABL Facility also contains a requirement that the ABL Borrowers comply, during certain periods, with a fixed charge coverage ratio of 1.00 to 1.00.

As of March 31, 2017, we have no borrowings outstanding and \$35.4 million in letters of credit outstanding with borrowing capacity of \$26.1 million available subject to covenant constraints under our ABL Facility.

Term Loan Facility

On December 15, 2016, the Company entered into the Term Loan Facility among the Company, as borrower, certain subsidiaries of the Company named as guarantors therein, the financial institutions party thereto from time to time as Lenders (collectively, the “Term Loan Lenders”) and Cortland Capital Market Services LLC and Cortland Products Corp., as agent for the Lenders. The Term Loan Facility had an initial outstanding principal amount of \$250 million. The Term Loan Facility will mature on December 15, 2021, although such maturity date may, at the Company’s request, be extended by one or more of the Term Loan Lenders pursuant to the terms of the Term Loan Facility.

Borrowings under the Term Loan Facility will bear interest, at the Company’s option, at a per annum rate equal to (i) LIBOR for one, two, three, six, or, with the consent of the Term Loan Lenders, 12 months, plus 10.25% or (ii) a base rate equal to the sum of (a) the greatest of (x) the prime rate, (y) the Federal Funds rate, plus 0.50% and (z) 30-day LIBOR, plus 1.0% plus (b) 9.25%.

The Term Loan Facility is guaranteed by certain of the Company’s existing and future subsidiaries (the “Term Loan Guarantors,” and together with the Company, the “Term Loan Parties”). To secure their obligations under the Term Loan Facility, each of the Term Loan Parties has granted or will grant, as applicable, to the agent a first-priority security interest for the benefit of the Term Loan Lenders in substantially all of each Term Loan Party’s assets other than certain excluded assets and the ABL Priority Collateral (the “Term Priority Collateral”). In addition, the obligations of the Term Loan Parties under the Term Loan Facility are secured by second-priority liens on the ABL Priority Collateral (as described above under “ABL Facility”).

The loans under the Term Loan Facility may be prepaid at the Company’s option, subject to the payment of a prepayment premium in certain circumstances as provided in the Term Loan Facility. If a prepayment is made prior to the first anniversary of the loan, such prepayment must be made with make-whole amount with the calculation of the make-whole amount as specified in the Term Loan Facility. If a prepayment is made after the first anniversary of the loan but prior to the second anniversary, such prepayment must be made at 106% of the principle amount, if a prepayment is made after the second anniversary but prior to the third anniversary, such prepayment must be made at 103% of the principle amount. After the third anniversary, if a prepayment is made, no prepayment premium is due. The Company is required to make principal payments in the amount of \$625,000 per quarter commencing with the quarter ending March 31, 2017. In addition, pursuant to the Term Loan Facility, the Company must prepay or offer to prepay, as applicable, term loans with the net cash proceeds of certain debt incurrences and asset sales, excess cash flow, and upon certain change of control transactions, subject in each case to certain exceptions.

The Term Loan Facility contains certain affirmative and negative covenants, including covenants that restrict the ability of the Term Loan Parties to take certain actions including, among other things and subject to certain significant exceptions, the incurrence of debt, the granting of liens, the making of investments, entering into transactions with affiliates, the payment of dividends and the sale of assets. The Term Loan Facility also contains financial covenants requiring that the Company maintain an asset coverage ratio of at least 1.35 to 1.0 and that Liquidity (as defined in the Term Loan Facility) must not be less than \$37.5 million (of which at least \$20.0 million must be in cash or cash equivalents held in deposit accounts) as of the last day of any fiscal quarter, subject to certain exceptions and cure rights.

The weighted average interest rates on the outstanding borrowings under the Term Loan Facility for the three months ended March 31, 2017 was as follows:

Three  
Months  
Ended  
March 31,  
2017

Term Loan Facility 11.27 %



Table of Contents

## NOTE 8. OTHER INCOME

The table below presents comparative detailed information about our other income and expense, shown on the condensed consolidated statements of operations as “other income, net” for the periods indicated (in thousands):

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
Interest income	\$ (198 )	\$ (132 )
Foreign exchange gain	(9 )	(252 )
Other, net	(33 )	(847 )
Total	\$ (240 )	\$ (1,231 )

## NOTE 9. INCOME TAXES

We are subject to U.S. federal income tax as well as income taxes in multiple state and foreign jurisdictions. Our effective tax rates were 0.6% and 0.3% for the three months ended March 31, 2017 and 2016, respectively. The variance between our effective rate and the U.S. statutory rate is due to the mix of pre-tax profit between the U.S. and international taxing jurisdictions with varying statutory rates, the impact of permanent differences, including goodwill impairment expense, and other tax adjustments, such as valuation allowances against deferred tax assets and tax expense or benefit recognized for uncertain tax positions.

We have historically calculated the provision for income taxes during interim reporting periods by applying an estimate of the annual effective tax rate for the full fiscal year to year-to-date ordinary income or loss. Management believes the use of the annual effective tax rate method to be appropriate for prior interim reporting periods. However, we adopted a year-to-date effective tax rate method for recording income taxes for the three-month period ended March 31, 2017. The adoption of this method was based on our expectations at March 31, 2017 that a small change in our estimated annual ordinary income could result in a large change in the estimated annual effective tax rate. We will re-evaluate our use of this method each quarter until such time a return to the annualized effective tax rate method is deemed appropriate.

The Company assesses the realizability of its deferred tax assets each period by considering whether it is more likely than not that all or a portion of the deferred tax assets will not be realized. Due to the history of losses in recent years and the continued challenges affecting the oil and gas industry, management continues to believe it is more likely than not that we will not be able to realize our net deferred tax assets. There has been no change in our position, and no release of our net deferred tax asset valuation allowance was made during the three months ended March 31, 2017. As of March 31, 2017, we had \$0.3 million of unrecognized tax benefits, net of federal tax benefit, which, if recognized, would impact our effective tax rate. We record interest and penalties related to unrecognized tax benefits as income tax expense. We have accrued a liability of less than \$0.1 million for the payment of interest and penalties as of March 31, 2017. We believe that it is reasonably possible that \$0.2 million of our currently remaining unrecognized tax positions may be recognized in the next twelve months as a result of a lapse of statute of limitations and settlement of ongoing audits.

## NOTE 10. COMMITMENTS AND CONTINGENCIES

## Litigation

Various suits and claims arising in the ordinary course of business are pending against us. We conduct business throughout the continental United States and may be subject to jury verdicts or arbitrations that result in outcomes in favor of the plaintiffs. We are also exposed to various claims abroad. We continually assess our contingent liabilities, including potential litigation liabilities, as well as the adequacy of our accruals and our need for the disclosure of these items, if any. We establish a provision for a contingent liability when it is probable that a liability has been incurred and the amount is reasonably estimable. We have \$5.2 million of other liabilities related to litigation that is deemed probable and reasonably estimable as of March 31, 2017. We do not believe that the disposition of any of these matters will result in an additional loss materially in excess of amounts that have been recorded.

In November 2015, the Santa Barbara County District Attorney filed a criminal complaint against two former employees and Key, specifically alleging three counts of violations of California Labor Code section 6425(a) against Key. The complaint sought unspecified penalties against Key related to an October 12, 2013 accident which resulted in the death of one Key employee at a drilling site near Santa Maria, California. An arraignment was held on February 10, 2016, where Key and its former employees pleaded not guilty to all charges.

Table of Contents

On or about January 10, 2017, Key entered into a settlement with the Santa Barbara County District Attorney. Key agreed to plead no contest to one felony count (Count 2), a violation of California Labor Code 6425(a). The Santa Barbara County District Attorney also agreed to recommend total restitution, fines, fees, and surcharges not to exceed \$450,000. The court dismissed the remaining charges (Counts 1 and 3) against Key. The parties agreed to postpone sentencing in the matter until January 20, 2018. The parties agreed that if Key pays all of the total restitution, fines, fees, and surcharges by January 20, 2018, the Santa Barbara County District Attorney will not object to Key withdrawing its plea to a felony count on Count 2 and entering a plea to a misdemeanor.

**Self-Insurance Reserves**

We maintain reserves for workers' compensation and vehicle liability on our balance sheet based on our judgment and estimates using an actuarial method based on claims incurred. We estimate general liability claims on a case-by-case basis. We maintain insurance policies for workers' compensation, vehicle liability and general liability claims. These insurance policies carry self-insured retention limits or deductibles on a per occurrence basis. The retention limits or deductibles are accounted for in our accrual process for all workers' compensation, vehicular liability and general liability claims. As of March 31, 2017 and December 31, 2016, we have recorded \$57.6 million and \$58.7 million, respectively, of self-insurance reserves related to workers' compensation, vehicular liabilities and general liability claims. Partially offsetting these liabilities, we had \$16.6 million and \$16.3 million of insurance receivables as of March 31, 2017 and December 31, 2016, respectively. We believe that the liabilities we have recorded are appropriate based on the known facts and circumstances and do not expect further losses materially in excess of the amounts already accrued for existing claims.

**Environmental Remediation Liabilities**

For environmental reserve matters, including remediation efforts for current locations and those relating to previously disposed properties, we record liabilities when our remediation efforts are probable and the costs to conduct such remediation efforts can be reasonably estimated. As of March 31, 2017 and December 31, 2016, we have recorded \$3.3 million and \$3.4 million, respectively, for our environmental remediation liabilities. We believe that the liabilities we have recorded are appropriate based on the known facts and circumstances and do not expect further losses materially in excess of the amounts already accrued.

**NOTE 11. LOSS PER SHARE**

Basic loss per share is determined by dividing net loss attributable to Key by the weighted average number of common shares actually outstanding during the period. Diluted loss per common share is based on the increased number of shares that would be outstanding assuming conversion of potentially dilutive outstanding securities using the treasury stock and "as if converted" methods.

The components of our loss per share are as follows (in thousands, except per share amounts):

	Successor	Predecessor
	Three	Three
	Months	Months
	Ended	Ended
	March 31,	March 31,
	2017	2016

**Basic and Diluted EPS Calculation:****Numerator**

Net loss	\$(46,859)	\$(81,614 )
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**Denominator**

Weighted average shares outstanding	20,096	160,047
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Basic and diluted loss per share	\$(2.33 )	\$(0.51 )
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Stock options, stock appreciation rights ("SARs") and warrants are included in the computation of diluted earnings per share using the treasury stock method. Restricted stock awards are legally considered issued and outstanding when granted and are included in basic weighted average shares outstanding.





Table of Contents

The company has issued potentially dilutive instruments such as restricted stock units (“RSUs”), stock options, SARs and warrants. However, the company did not include these instruments in its calculation of diluted loss per share during the periods presented, because to include them would be anti-dilutive. The following table shows potentially dilutive instruments (in thousands):

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
RSUs	677	62
Stock options	677	812
SARs	—	240
Warrants	1,838	—
Total	3,192	1,114

No events occurred after March 31, 2017 that would materially affect the number of weighted average shares outstanding.

**NOTE 12. SHARE-BASED COMPENSATION**

We recognized employee share-based compensation expense of \$2.8 million and \$2.4 million during the three months ended March 31, 2017 and 2016, respectively. Additionally, we recognized share-based compensation expense related to our outside directors of \$0.3 million and zero during the three months ended March 31, 2017 and 2016, respectively. Our employee share-based awards vest in equal installments over a four-year period. The unrecognized compensation cost related to our unvested share-based awards as of March 31, 2017 is estimated to be \$19.2 million and is expected to be recognized over a weighted-average period of 2.2 years.

We recognized compensation expense related to our stock options of \$0.9 million and zero during the three months ended March 31, 2017 and 2016, respectively. Our employee stock options vest in equal installments over a four-year period. The unrecognized compensation cost related to our unvested stock options as of March 31, 2017 is estimated to be \$6.4 million and is expected to be recognized over a weighted-average period of 2.2 years.

**NOTE 13. TRANSACTIONS WITH RELATED PARTIES**

The Company has purchased equipment and services from a few affiliates of certain directors. The dollar amounts related to these related party activities are not material to the Company’s condensed consolidated financial statements.

**NOTE 14. ESTIMATED FAIR VALUE OF FINANCIAL INSTRUMENTS**

Cash, cash equivalents, accounts receivable, accounts payable and accrued liabilities. These carrying amounts approximate fair value because of the short maturity of the instruments or because the carrying value is equal to the fair value of those instruments on the balance sheet date.

Term Loan Facility due 2021. Because the variable interest rates of these loans approximate current market rates, the fair values of the loans borrowed under this facility approximate their carrying values.

**NOTE 15. SEGMENT INFORMATION**

Our reportable business segments are U.S. Rig Services, Fluid Management Services, Coiled Tubing Services, Fishing and Rental Services and International. We also have a “Functional Support” segment associated with overhead and other costs in support of our reportable segments. Our U.S. Rig Services, Fluid Management Services, Coiled Tubing Services, Fishing and Rental Services operate geographically within the United States. The International reportable segment includes our current and former operations in Mexico and Russia. Our Canadian subsidiary is also reflected in our International reportable segment. During the fourth quarter of 2016, we completed the sale of our business in Mexico and we are currently in discussions to sell our business in Russia. We evaluate the performance of our segments based on gross margin measures. All inter-segment sales pricing is based on current market conditions.

## Table of Contents

### U.S. Rig Services

Our U.S. Rig Services include the completion of newly drilled wells, workover and recompletion of existing oil and natural gas wells, well maintenance, and the plugging and abandonment of wells at the end of their useful lives. We also provide specialty drilling services to oil and natural gas producers with certain of our larger rigs that are capable of providing conventional and horizontal drilling services. Our rigs encompass various sizes and capabilities, allowing us to service all types of wells. Many of our rigs are outfitted with our proprietary KeyView® technology, which captures and reports well site operating data and provides safety control systems. We believe that this technology allows our customers and our crews to better monitor well site operations, improves efficiency and safety, and adds value to the services that we offer.

The completion and recompletion services provided by our rigs prepare wells for production, whether newly drilled, or recently extended through a workover operation. The completion process may involve selectively perforating the well casing to access production zones, stimulating and testing these zones, and installing tubular and downhole equipment. We typically provide a well service rig and may also provide other equipment to assist in the completion process. Completion services vary by well and our work may take a few days to several weeks to perform, depending on the nature of the completion.

The workover services that we provide are designed to enhance the production of existing wells and generally are more complex and time consuming than normal maintenance services. Workover services can include deepening or extending wellbores into new formations by drilling horizontal or lateral wellbores, sealing off depleted production zones and accessing previously bypassed production zones, converting former production wells into injection wells for enhanced recovery operations and conducting major subsurface repairs due to equipment failures. Workover services may last from a few days to several weeks, depending on the complexity of the workover.

Maintenance services provided with our rig fleet are generally required throughout the life cycle of an oil or natural gas well. Examples of these maintenance services include routine mechanical repairs to the pumps, tubing and other equipment, removing debris and formation material from wellbores, and pulling rods and other downhole equipment from wellbores to identify and resolve production problems. Maintenance services are generally less complicated than completion and workover related services and require less time to perform.

Our rig fleet is also used in the process of permanently shutting-in oil or natural gas wells that are at the end of their productive lives. These plugging and abandonment services generally require auxiliary equipment in addition to a well servicing rig. The demand for plugging and abandonment services is not significantly impacted by the demand for oil and natural gas because well operators are required by state regulations to plug wells that are no longer productive.

### Fluid Management Services

We provide transportation and well-site storage services for various fluids utilized in connection with drilling, completions, workover and maintenance activities. We also provide disposal services for fluids produced subsequent to well completion. These fluids are removed from the well site and transported for disposal in saltwater disposal wells owned by us or a third party. In addition, we operate a fleet of hot oilers capable of pumping heated fluids used to clear soluble restrictions in a wellbore. Demand and pricing for these services generally correspond to demand for our well service rigs.

### Coiled Tubing Services

Coiled Tubing Services involve the use of a continuous metal pipe spooled onto a large reel which is then deployed into oil and natural gas wells to perform various applications, such as wellbore clean-outs, nitrogen jet lifts, through-tubing fishing, and formation stimulations utilizing acid and chemical treatments. Coiled tubing is also used for a number of horizontal well applications such as milling temporary isolation plugs that separate frac zones, and various other pre- and post-hydraulic fracturing well preparation services.

### Fishing and Rental Services

We offer a full line of fishing services and rental equipment designed for use in providing drilling and workover services. Fishing services involve recovering lost or stuck equipment in the wellbore utilizing a broad array of “fishing tools.” Our rental tool inventory consists of drill pipe, tubulars, handling tools (including our patented Hydra-Wall® pipe-handling units and services), pressure-control equipment, pumps, power swivels, reversing units, foam air units, frac stack equipment used to support hydraulic fracturing operations and the associated flowback of frac fluids,

proppants, oil and natural gas. We also provide well testing services.

Demand for our fishing and rental services is closely related to capital spending by oil and natural gas producers, which is generally a function of oil and natural gas prices.

#### International

In April 2015, we announced our decision to exit markets in which we participate outside of North America. During the fourth quarter of 2016, we completed the sale of our business in Mexico and we are currently in discussions to sell our business in Russia. We provided rig-based services such as the maintenance, workover, recompletion of existing oil wells, completion of newly-

Table of Contents

drilled wells and plugging and abandonment of wells at the end of their useful lives in each of our international markets. In addition, in Mexico we provided drilling, coiled tubing, wireline and project management and consulting services. We also have a technology development and control systems business based in Canada which is focused on the development of hardware and software related to oilfield service equipment controls, data acquisition and digital information flow.

**Functional Support**

Our Functional Support segment includes unallocated overhead costs associated with administrative support for our U.S. and International reporting segments.

**Financial Summary**

The following tables set forth our unaudited segment information as of and for the three months ended March 31, 2017 and 2016 (in thousands):

Successor Company as of and for the three months ended March 31, 2017

	U.S. Rig Services	Fluid Management Services	Coiled Tubing Services	Fishing and Rental Services	International	Functional Support	Reconciling (E)liminations	Total
Revenues from external customers	\$60,291	\$ 17,895	\$ 5,341	\$15,855	\$ 2,070	\$ —	\$ —	\$101,452
Intersegment revenues	46	284	22	920	—	—	(1,272)	—
Depreciation and amortization	7,324	5,808	1,413	5,950	525	281	—	21,301
Impairment expense	—	—	—	—	187	—	—	187
Other operating expenses	55,054	19,024	6,213	13,782	3,658	20,571	—	118,302
Operating loss	(2,087 )	(6,937 )	(2,285 )	(3,877 )	(2,300 )	(20,852 )	—	(38,338 )
Reorganization items, net	—	—	—	—	—	1,340	—	1,340
Interest expense, net of amounts capitalized	—	—	—	—	—	7,710	—	7,710
Loss before income taxes	(2,091 )	(7,165 )	(2,278 )	(3,674 )	(2,242 )	(29,698 )	—	(47,148 )
Long-lived assets(1)	172,549	92,019	23,766	85,764	1,344	130,686	(110,481)	395,647
Total assets	295,921	11,638	35,129	348,879	142,599	6,683	(236,603)	604,246
Capital expenditures	2,026	118	—	27	116	153	—	2,440

Table of Contents

Predecessor Company as of and for the three months ended March 31, 2016

	U.S. Rig Services	Fluid Management Services	Coiled Tubing Services	Fishing and Rental Services	International	Functional Support	Reconciling Eliminations	Total
Revenues from external customers	\$58,988	\$22,670	\$9,531	\$16,283	\$3,616	\$—	\$—	\$111,088
Intersegment revenues	245	309	40	987	140	—	(1,721)	—
Depreciation and amortization	14,905	5,880	2,986	7,182	2,237	2,562	—	35,752
Other operating expenses	50,449	23,062	12,694	13,113	6,439	31,086	—	136,843
Operating loss	(6,366 )	(6,272 )	(6,149 )	(4,012 )	(5,060 )	(33,648 )	—	(61,507 )
Interest expense, net of amounts capitalized	—	—	—	—	—	21,584	—	21,584
Loss before income taxes	(6,362 )	(6,268 )	(6,076 )	(4,014 )	(4,497 )	(54,643 )	—	(81,860 )
Long-lived assets(1)	482,588	123,400	52,113	120,984	53,894	174,785	(135,972)	871,792
Total assets	1,323,797	262,688	131,421	482,133	175,044	(737,293)	(411,744)	1,226,046
Capital expenditures	140	820	101	1,084	364	192	—	2,701

(1) Long-lived assets include fixed assets, intangibles and other non-current assets.

(2) Functional Support is geographically located in the United States.

## NOTE 16. CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

The senior notes of the Predecessor company were registered securities. As a result of these registered securities, we are required to present the following condensed consolidating financial information pursuant to SEC Regulation S-X Rule 3-10, "Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered." Our ABL Facility and Term Loan Facility of the Successor Company are not registered securities, so the presentation of condensed consolidating financial information is not required for the Successor period.

## CONDENSED CONSOLIDATING UNAUDITED STATEMENTS OF OPERATIONS

	Predecessor Three Months Ended March 31, 2016				
	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
	(in thousands)				
Revenues	\$—	\$107,472	\$3,756	\$ (140 )	\$111,088
Direct operating expense	—	86,807	3,923	(132 )	90,598
Depreciation and amortization expense	—	34,534	1,218	—	35,752
General and administrative expense	193	43,598	2,454	—	46,245
Operating loss	(193 )	(57,467 )	(3,839 )	(8 )	(61,507 )
Interest expense, net of amounts capitalized	21,584	—	—	—	21,584
Other income, net	(645 )	(143 )	(558 )	115	(1,231 )
Loss before income taxes	(21,132 )	(57,324 )	(3,281 )	(123 )	(81,860 )
Income tax (expense) benefit	(6 )	—	252	—	246
Net loss	\$(21,138)	\$(57,324 )	\$(3,029 )	\$ (123 )	\$(81,614 )

Table of Contents

## CONDENSED CONSOLIDATING UNAUDITED STATEMENTS OF CASH FLOWS

	Predecessor				
	Three Months Ended March 31, 2016				
	Parent	Guarantor	Non-Guarantor	Eliminations	Consolidated
	Company	Subsidiaries	Subsidiaries		
	(in thousands)				
Net cash provided by (used in) operating activities	\$—	\$ (31,902 )	\$ 1,838	\$ —	\$ (30,064 )
Cash flows from investing activities:					
Capital expenditures	—	(2,701 )	—	—	(2,701 )
Intercompany notes and accounts	—	21,596	—	(21,596)	—
Other investing activities, net	—	7,435	—	—	7,435
Net cash provided by investing activities	—	26,330	—	(21,596)	4,734
Cash flows from financing activities:					
Repayments of long-term debt	(787 )	—	—	—	(787 )
Restricted stock	(18,605 )	—	—	—	(18,605 )
Repurchases of common stock	(143 )	—	—	—	(143 )
Intercompany notes and accounts	(21,596 )	—	—	21,596	—
Other financing activities, net	(2,508 )	—	—	—	(2,508 )
Net cash used in financing activities	(43,639 )	—	—	21,596	(22,043 )
Effect of changes in exchange rates on cash	—	—	(1,277 )	—	(1,277 )
Net increase (decrease) in cash and cash equivalents	(43,639 )	(5,572 )	561	—	(48,650 )
Cash and cash equivalents at beginning of period	191,065	10,024	3,265	—	204,354
Cash and cash equivalents at end of period	\$ 147,426	\$ 4,452	\$ 3,826	\$ —	\$ 155,704

Table of Contents

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## OVERVIEW

Key Energy Services, Inc., and its wholly owned subsidiaries (collectively, "Key," the "Company," "we," "us," "its," and "our") provide a full range of well services to major oil companies, foreign national oil companies and independent oil and natural gas production companies. Our services include rig-based and coiled tubing-based well maintenance and workover services, well completion and recompletion services, fluid management services, fishing and rental services, and other ancillary oilfield services. Additionally, certain of our rigs are capable of specialty drilling applications. We operate in most major oil and natural gas producing regions of the continental United States, and we have operations in Russia, which we are attempting to sell. In addition, we have a technology development and control systems business based in Canada.

The following discussion and analysis should be read in conjunction with the accompanying unaudited condensed consolidated financial statements and related notes as of and for the three months ended March 31, 2017 and 2016, included elsewhere herein, and the audited consolidated financial statements and notes thereto included in our 2016 Form 10-K and "Part 1A. Risk Factors" of our 2016 Form 10-K.

We operate in five business segments: U.S. Rig Services, Fluid Management Services, Coiled Tubing Services, Fishing and Rental Services and International. We also have a "Functional Support" segment associated with managing our U.S. and International business segments. See "Note 15. Segment Information" in "Item 1. Financial Statements" of Part I of this report for a summary of our business segments.

## PERFORMANCE MEASURES

The Baker Hughes U.S. rig count data, which is publicly available on a weekly basis, is often used as an indicator of overall Exploration and Production ("E&P") company spending and broader oilfield activity. In assessing overall activity in the U.S. onshore oilfield service industry in which we operate, we believe that the Baker Hughes U.S. land drilling rig count is the best available barometer of E&P companies' capital spending and resulting activity levels. Historically, our activity levels have been highly correlated to U.S. onshore capital spending by our E&P company customers as a group.

	WTI Cushing Oil(1)	NYMEX Henry Hub Natural Gas(1)	Average Baker Hughes U.S. Land Drilling Rigs(2)
2017:			
First Quarter	\$ 51.60	\$ 3.02	729
2016:			
First Quarter	\$ 33.35	\$ 1.99	524
Second Quarter	\$ 45.46	\$ 2.15	398
Third Quarter	\$ 44.85	\$ 2.88	461
Fourth Quarter	\$ 49.14	\$ 3.04	567

(1) Represents the average of the monthly average prices for each of the periods presented. Source: EIA and Bloomberg

(2) Source: [www.bakerhughes.com](http://www.bakerhughes.com)

Internally, we measure activity levels for our well servicing operations primarily through our rig and trucking hours. Generally, as capital spending by E&P companies increases, demand for our services also rises, resulting in increased rig and trucking services and more hours worked. Conversely, when activity levels decline due to lower spending by E&P companies, we generally provide fewer rig and trucking services, which results in lower hours worked.



Table of Contents

In the U.S., our rig activity occurs primarily on weekdays during daylight hours. Accordingly, we track U.S. rig activity on a “per U.S. working day” basis. Key’s U.S. working days per quarter, which exclude national holidays, are indicated in the table below. Our international rig activity and domestic trucking activity tend to occur on a 24/7 basis. Accordingly, we track our international rig activity and our domestic trucking activity on a “per calendar day” basis. The following table presents our quarterly rig and trucking hours from 2016 through the first quarter of 2017:

	Rig Hours		Total	Trucking Hours	Key’s U.S. Working Days(1)
2017:	U.S.	International	Total		
First Quarter	165,968	2,462	168,430	179,215	64
2016:					
First Quarter	153,417	5,715	159,132	217,429	63
Second Quarter	144,587	6,913	151,500	199,527	64
Third Quarter	163,206	6,170	169,376	198,362	64
Fourth Quarter	169,087	4,341	173,428	192,049	61
Total 2016	630,297	23,139	653,436	807,367	252

(1) Key’s U.S. working days are the number of weekdays during the quarter minus national holidays.

**MARKET AND BUSINESS CONDITIONS AND OUTLOOK**

Our core businesses depend on our customers’ willingness to make expenditures to produce, develop and explore for oil and natural gas. Industry conditions are influenced by numerous factors, such as oil and natural gas prices, the supply of and demand for oil and natural gas, domestic and worldwide economic conditions, and political instability in oil producing countries and available supply of and demand for the services we provide. Oil and natural gas prices began a rapid and substantial decline in the fourth quarter of 2014. Depressed commodity price conditions persisted and worsened during 2015 and that trend continued into 2016. As a result, the rig count and demand for our products and services declined substantially, and the prices we are able to charge our customers for our products and services have also declined substantially. While we have sought to anticipate activity declines and have reshaped our organizational and cost structure to mitigate the negative impact of these declines, we have continued to experience negative operating results and cash flows from operations. Although oil prices have improved off the low point of 2016 with the November 2016 decision by OPEC to curtail the cartel’s oil production, and our revenues improved through the first quarter of 2017, we have not experienced an increase in activity levels commensurate with in the increase in oil prices or the Baker Hughes U.S. land drilling rig count. We believe that stability in oil prices at an attractive price to our customers coupled with continued aging of horizontal wells and customers choosing to increase production through regular well maintenance will allow for demand for our services to continue to improve from the first quarter of 2017. We believe that an improvement in demand for our services will allow for increases in both activity and the price of our services over 2017. With increased demand for oilfield services broadly, however, the demand for qualified employees will also increase, which may impact our ability to meet the needs of our customers or to offset inflation in labor costs with price increases from our customers.

**RESULTS OF OPERATIONS**

The following tables set forth consolidated results of operations and financial information by operating segment and other selected information of the Successor Company and the Predecessor Company for the periods ending March 31, 2017 and 2016, respectively. Upon emergence on the Effective Date, the Company adopted fresh start accounting which resulted in the creation of a new entity for financial reporting purposes. As a result of the application of fresh start accounting, as well as the effects of the implementation of the Plan, the Consolidated Financial Statements on or after December 16, 2016 are not comparable with the Consolidated Financial Statements prior to that date. While the comparison of these periods is not presented according to generally accepted accounting principles in the United States (“GAAP”) and no comparable GAAP measures are presented, management believes that providing this financial information is the most relevant and useful method for making comparisons between the periods.



Table of Contents

The following table shows our consolidated results of operations for three months ended March 31, 2017 and 2016, respectively (in thousands):

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
REVENUES	\$101,452	\$111,088
COSTS AND EXPENSES:		
Direct operating expenses	87,306	90,598
Depreciation and amortization expense	21,301	35,752
General and administrative expenses	30,996	46,245
Impairment expense	187	—
Operating loss	(38,338 )	(61,507 )
Interest expense, net of amounts capitalized	7,710	21,584
Other income, net	(240 )	(1,231 )
Reorganization items, net	1,340	—
Loss before income taxes	(47,148 )	(81,860 )
Income tax benefit	289	246
NET LOSS	\$(46,859 )	\$(81,614 )

## Consolidated Results of Operations — Three Months Ended March 31, 2017 and 2016

## Revenues

Our revenues for the three months ended March 31, 2017 decreased \$9.6 million, or 8.7%, to \$101.5 million from \$111.1 million for the three months ended March 31, 2016. While the price of oil has improved since the first quarter of 2016, oil prices have remained low resulting in overall lower spending from our customers. These market conditions resulted in overall reduced customer activity and a reduction in the price received for our services. Internationally, we had lower revenue as a result of the sale our operations in Mexico. See “Segment Operating Results — Three Months Ended March 31, 2017 and 2016” below for a more detailed discussion of the change in our revenues.

## Direct Operating Expenses

Our direct operating expenses decreased \$3.3 million, to \$87.3 million (86.1% of revenues), for the three months ended March 31, 2017, compared to \$90.6 million (81.6% of revenues) for the three months ended March 31, 2016. The decrease is primarily related to a decrease in employee compensation costs and equipment expense as we sought to reduce our cost structure and as a result of lower activity levels.

## Depreciation and Amortization Expense

Depreciation and amortization expense decreased \$14.5 million, or 40.4%, to \$21.3 million during the three months ended March 31, 2017, compared to \$35.8 million for the three months ended March 31, 2016. The decrease is primarily attributable to the reduction of property, plant and equipment due to the implementation of fresh start accounting in the fourth quarter of 2016.

## General and Administrative Expenses

General and administrative expenses decreased \$15.2 million, to \$31.0 million (30.6% of revenues), for the three months ended March 31, 2017, compared to \$46.2 million (41.6% of revenues) for the three months ended March 31, 2016. The decrease is primarily due to lower employee compensation costs due to reduced staffing levels and reduction in wages and the \$5.0 million FCPA settlement accrual and \$2.4 million decrease in expenses related to the FCPA investigation, which was completed in 2016, partially offset by \$1.8 million in professional fees related to restructuring in 2017.

Table of Contents

## Impairment Expense

We recorded a \$0.2 million impairment during the three months ended March 31, 2017 to reduce the carrying value of the assets and related liabilities of our Russian business unit, which is being held for sale, to fair market value. We recorded no impairment expense during the three months ended March 31, 2016.

## Interest Expense, Net of Amounts Capitalized

Interest expense decreased \$13.9 million, or 64.3%, to \$7.7 million for the three months ended March 31, 2017, compared to \$21.6 million for the same period in 2016. The decrease is primarily related to the elimination of the Predecessor Company's senior secured notes in connection with our emergence from voluntary reorganization.

## Other Income, Net

During the three months ended March 31, 2017, we recognized other income, net, of \$0.2 million, compared to other income, net, of \$1.2 million for the three months ended March 31, 2016. Our foreign exchange gain relates to U.S. dollar-denominated transactions in our foreign locations and fluctuations in exchange rates between local currencies and the U.S. dollar.

The following table summarizes the components of other income, net for the periods indicated (in thousands):

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
Interest income	\$ (198 )	\$ (132 )
Foreign exchange gain	(9 )	(252 )
Other, net	(33 )	(847 )
Total	\$ (240 )	\$ (1,231 )

## Reorganization Items, Net

Reorganization item expenses were \$1.3 million for the three months ended March 31, 2017, and there were no reorganization item expenses for the same period in 2016. Reorganization items consist of professional fees incurred in connection with our emergence from voluntary reorganization.

## Income Tax Benefit

We recorded an income tax benefit of \$0.3 million on a pre-tax loss of \$47.1 million for the three months ended March 31, 2017, compared to an income tax benefit of \$0.2 million on a pre-tax loss of \$81.9 million for the same period in 2016. Our effective tax rate was 0.6% for the three months ended March 31, 2017, compared to 0.3% for the three months ended March 31, 2016. Our effective tax rates for such periods differ from the U.S. statutory rate of 35% due to a number of factors, including the mix of profit and loss between domestic and international taxing jurisdictions and the impact of permanent items, including expenses subject to statutorily imposed limitations such as meals and entertainment expenses, that affect book income but do not affect taxable income and discrete tax adjustments, such as valuation allowances against deferred tax assets and tax expense or benefit recognized for uncertain tax positions.

## Segment Operating Results — Three Months Ended March 31, 2017 and 2016

The following table shows operating results for each of our segments for the three months ended March 31, 2017 and 2016 (in thousands):

Successor Company for the three months ended March 31, 2017

	U.S. Rig Services	Fluid Management Services	Coiled Tubing Services	Fishing and Rental Services	International	Functional Support	Total
Revenues from external customers	\$60,291	\$ 17,895	\$ 5,341	\$15,855	\$ 2,070	\$ —	\$101,452
Operating expenses	62,378	24,832	7,626	19,732	4,370	20,852	139,790
Operating loss	(2,087 )	(6,937 )	(2,285 )	(3,877 )	(2,300 )	(20,852 )	(38,338 )



Table of Contents

Predecessor Company for the three months ended March 31, 2016

	U.S. Rig Services	Fluid Management Services	Coiled Tubing Services	Fishing and Rental Services	International	Functional Support	Total
Revenues from external customers	\$58,988	\$ 22,670	\$ 9,531	\$16,283	\$ 3,616	\$ —	\$111,088
Operating expenses	65,354	28,942	15,680	20,295	8,676	33,648	172,595
Operating loss	(6,366 )	(6,272 )	(6,149 )	(4,012 )	(5,060 )	(33,648 )	(61,507 )

#### U.S. Rig Services

Revenues for our U.S. Rig Services segment increased \$1.3 million, or 2.2%, to \$60.3 million for the three months ended March 31, 2017, compared to \$59.0 million for the three months ended March 31, 2016. The increase for this segment is primarily due to limited spending from our customers as a result of slightly improved, but still low oil prices. These market conditions resulted in a limited increase in customer activity and the price received for our services.

Operating expenses for our U.S. Rig Services segment were \$62.4 million for the three months ended March 31, 2017, which represented a decrease of \$3.0 million, or 4.6%, compared to \$65.4 million for the same period in 2016. These expenses decreased primarily due to a decrease in depreciation expense partially offset by an increase in employee compensation costs and equipment expense as a result of the recent increase activity levels.

#### Fluid Management Services

Revenues for our Fluid Management Services segment decreased \$4.8 million, or 21.1%, to \$17.9 million for the three months ended March 31, 2017, compared to \$22.7 million for the three months ended March 31, 2016. The decrease for this segment is primarily due to lower spending from our customers as a result of continued low oil prices. These market conditions resulted in reduced customer activity and a reduction in the price received for our services.

Operating expenses for our Fluid Management Services segment were \$24.8 million for the three months ended March 31, 2017, which represented a decrease of \$4.1 million, or 14.2%, compared to \$28.9 million for the same period in 2016. These expenses decreased primarily due to a decrease in employee compensation costs and equipment expense as we sought to reduce our cost structure and as a result of lower activity levels.

#### Coiled Tubing Services

Revenues for our Coiled Tubing Services segment decreased \$4.2 million, or 44.0%, to \$5.3 million for the three months ended March 31, 2017, compared to \$9.5 million for the three months ended March 31, 2016. The decrease for this segment is primarily due to lower spending from our customers as a result of continued low oil prices. These market conditions resulted in reduced customer activity and a reduction in the price received for our services.

Operating expenses for our Coiled Tubing Services segment were \$7.6 million for the three months ended March 31, 2017, which represented a decrease of \$8.1 million, or 51.4%, compared to \$15.7 million for the same period in 2016. These expenses decreased primarily due to a decrease in employee compensation costs and equipment expense as we sought to reduce our cost structure and as a result of lower activity levels and a decrease in depreciation expense.

#### Fishing and Rental Services

Revenues for our Fishing and Rental Services segment decreased \$0.4 million, or 2.6%, to \$15.9 million for the three months ended March 31, 2017, compared to \$16.3 million for the three months ended March 31, 2016. The decrease for this segment is primarily due to lower spending from our customers as a result of continued low oil prices. These market conditions resulted in reduced customer activity and a reduction in the price received for our services.

Operating expenses for our Fishing and Rental Services segment were \$19.7 million for the three months ended March 31, 2017, which represented a decrease of \$0.6 million, or 2.8%, compared to \$20.3 million for the same period in 2016. These expenses decreased primarily as a result of a decrease in depreciation expense and decrease in employee compensation cost as we sought to reduce our cost structure and as a result of lower activity levels.

#### International

Revenues for our International segment decreased \$1.5 million, or 42.8%, to \$2.1 million for the three months ended March 31, 2017, compared to \$3.6 million for the three months ended March 31, 2016. The decrease was primarily attributable to selling our operations in Mexico.

Operating expenses for our International segment decreased \$4.3 million, or 49.6%, to \$4.4 million for the three months ended March 31, 2017, compared to \$8.7 million for the three months ended March 31, 2016. These expenses decreased primarily as a result of a decrease in employee compensation costs and equipment expense, primarily due to selling our operations in Mexico.

Table of Contents

## Functional Support

Operating expenses for Functional Support, which represent expenses associated with managing our U.S. and International reporting segments, decreased \$12.8 million, or 38.0%, to \$20.9 million (20.6% of consolidated revenues) for the three months ended March 31, 2017 compared to \$33.6 million (30.3% of consolidated revenues) for the same period in 2016. The decrease is primarily due to lower employee compensation costs due to reduced staffing levels and reduction in wages and the \$5.0 million FCPA settlement accrual and \$2.4 million decrease in expenses related to the FCPA investigation, which was completed in 2016, partially offset by \$1.8 million in professional fees related to restructuring in 2017.

## LIQUIDITY AND CAPITAL RESOURCES

## Current Financial Condition and Liquidity

As of March 31, 2017, we had cash and cash equivalents of \$82.7 million compared to \$90.5 million as of December 31, 2016. Our working capital was \$103.3 million as of March 31, 2017, compared to \$117.8 million as of December 31, 2016. Our working capital decreased from the prior year end primarily as a result of a decrease in cash and cash equivalents, restricted cash, and accounts receivable partially offset by decrease in accrued liabilities. As of March 31, 2017, we had no borrowings outstanding and \$35.4 million in committed letters of credit outstanding under our ABL Facility.

The following table summarizes our cash flows for the three months ended March 31, 2017 and 2016 (in thousands):

	Successor Three Months Ended March 31, 2017	Predecessor Three Months Ended March 31, 2016
Net cash used in operating activities	\$(12,647)	\$(30,064)
Cash paid for capital expenditures	(2,440)	(2,701)
Proceeds received from sale of fixed assets	—	7,435
Repayments of long-term debt	(625)	(787)
Restricted cash	9,079	(18,605)
Payment of deferred financing costs	(350)	—
Other financing activities, net	—	(2,651)
Effect of exchange rates on cash	(812)	(1,277)
Net decrease in cash and cash equivalents	\$(7,795)	\$(48,650)

Cash used in operating activities was \$12.6 million for the three months ended March 31, 2017 compared to cash used in operating activities of \$30.1 million for the three months ended March 31, 2016. Cash used by operating activities for the three months ended March 31, 2017 was primarily related to net loss adjusted for noncash items and decrease in accrued liabilities partially offset by a cash inflow related to a decrease in accounts receivable. Cash used by operating activities for the three months ended March 31, 2016 was primarily related to net loss adjusted for noncash items and a decrease in accounts payable partially offset by a cash inflow related to a decrease in accounts receivable. Cash used in investing activities was \$2.4 million for the three months ended March 31, 2017 compared to cash provided by investing activities of \$4.7 million for the three months ended March 31, 2016. Cash inflows during these periods consisted primarily of proceeds from sales of fixed assets. Cash outflows during these periods consisted primarily of capital expenditures. Our capital expenditures primarily relate to maintenance of our equipment. Cash provided by financing activities was \$8.1 million for the three months ended March 31, 2017 compared to cash used in financing activities of \$22.0 million for the three months ended March 31, 2016. Overall financing cash inflows for the three months ended March 31, 2017 primarily relate to the decrease in restricted cash. Overall financing cash outflows for the three months ended March 31, 2016 primarily relate to the increase in restricted cash.

## Sources of Liquidity and Capital Resources

We believe that our internally generated cash flows from operations, current reserves of cash and availability under our ABL Facility are sufficient to finance our cash requirements for current and future operations, budgeted capital



expenditures, debt service and other obligations for the next twelve months.

26

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Table of Contents

At March 31, 2017, our annual debt maturities for our 2021 Term Loan Facility were as follows (in thousands):

Year	Principal Payments
2017	\$1,875
2018	2,500
2019	2,500
2020	2,500
2021 and thereafter	240,000
Total principal payments	\$249,375

**ABL Facility**

On December 15, 2016, the Company and Key Energy Services, LLC, as borrowers (the “ABL Borrowers”), entered into the ABL Facility with the financial institutions party thereto from time to time as lenders (the “ABL Lenders”), Bank of America, N.A., as administrative agent for the lenders, and Bank of America, N.A. and Wells Fargo Bank, National Association, as co-collateral agents for the lenders. The ABL Facility provides for aggregate initial commitments from the ABL Lenders of \$100 million and matures on June 15, 2021.

The ABL Facility provides the ABL Borrowers with the ability to borrow up to an aggregate principal amount equal to the lesser of (i) the aggregate revolving commitments then in effect and (ii) the sum of (a) 85% of the value of eligible accounts receivable plus (b) 80% of the value of eligible unbilled accounts receivable, subject to a limit equal to the greater of (x) \$35 million and (y) 25% of the Commitments. The amount that may be borrowed under the ABL Facility is subject to increase or reduction based on certain segregated cash or reserves provided for by the ABL Facility. In addition, the percentages of accounts receivable and unbilled accounts receivable included in the calculation described above is subject to reduction to the extent of certain bad debt write-downs and other dilutive items provided in the ABL Facility.

Borrowings under the ABL Facility bear interest, at the ABL Borrowers’ option, at a per annum rate equal to (i) LIBOR for 30, 60, 90, 180, or, with the consent of the ABL Lenders, 360 days, plus an applicable margin that varies from 2.50% to 4.50% depending on the Borrowers’ fixed charge coverage ratio at such time or (ii) a base rate equal to the sum of (a) the greatest of (x) the prime rate, (y) the federal funds rate, plus 0.50% or (z) 30-day LIBOR, plus 1.0% plus (b) an applicable margin that varies from 1.50% to 3.50% depending of the Borrowers’ fixed charge coverage ratio at such time. In addition, the ABL Facility provides for unused line fees of 1.00% to 1.25% per year, depending on utilization, letter of credit fees and certain other factors.

The ABL Facility may in the future be guaranteed by certain of the Company’s existing and future subsidiaries (the “ABL Guarantors,” and together with the ABL Borrowers, the “ABL Loan Parties”). To secure their obligations under the ABL Facility, each of the ABL Loan Parties has granted or will grant, as applicable, to the Administrative Agent a first-priority security interest for the benefit of the ABL Lenders in its present and future accounts receivable, inventory and related assets and proceeds of the foregoing (the “ABL Priority Collateral”). In addition, the obligations of the ABL Loan Parties under the ABL Facility are secured by second-priority liens on the Term Priority Collateral (as described below under “Term Loan Facility”).

The revolving loans under the ABL Facility may be voluntarily prepaid, in whole or in part, without premium or penalty, subject to breakage or similar costs.

The ABL Facility contains certain affirmative and negative covenants, including covenants that restrict the ability of the ABL Loan Parties to take certain actions including, among other things and subject to certain significant exceptions, the incurrence of debt, the granting of liens, the making of investments, entering into transactions with affiliates, the payment of dividends and the sale of assets. The ABL Facility also contains a requirement that the ABL Borrowers comply, during certain periodic with a fixed charge coverage ratio of 1.00 to 1.00.

As of March 31, 2017, we have no borrowings outstanding under the ABL Facility and \$35.4 million of letters of credit outstanding with borrowing capacity of \$26.1 million available subject to covenant constraints under our ABL Facility.

**Term Loan Facility**

On December 15, 2016, the Company entered into the Term Loan Facility among the Company, as borrower, certain subsidiaries of the Company named as guarantors therein, the financial institutions party thereto from time to time as Lenders (collectively, the “Term Loan Lenders”) and Cortland Capital Market Services LLC and Cortland Products Corp., as agent for the Lenders. The Term Loan Facility had an outstanding principal amount of \$250 million as of the Effective Date.

The Term Loan Facility will mature on December 15, 2021, although such maturity date may, at the Company’s request, be extended by one or more of the Term Loan Lenders pursuant to the terms of the Term Loan Facility. Borrowings under the Term Loan Facility bear interest, at the Company’s option, at a per annum rate equal to (i) LIBOR for one, two, three, six, or, with

## Table of Contents

the consent of the Term Loan Lenders, 12 months, plus 10.25% or (ii) a base rate equal to the sum of (a) the greatest of (x) the prime rate, (y) the Federal Funds rate, plus 0.50% and (z) 30-day LIBOR, plus 1.0% plus (b) 9.25%. The Term Loan Facility is guaranteed by certain of the Company's existing and future subsidiaries (the "Term Loan Guarantors," and together with the Company, the "Term Loan Parties"). To secure their obligations under the Term Loan Facility, each of the Term Loan Parties has granted or will grant, as applicable, to the Agent a first-priority security interest for the benefit of the Term Loan Lenders in substantially all of each Term Loan Party's assets other than certain excluded assets and the ABL Priority Collateral (the "Term Priority Collateral"). In addition, the obligations of the Term Loan Parties under the Term Loan Facility are secured by second-priority liens on the ABL Priority Collateral (as described above under "ABL Facility").

The loans under the Term Loan Facility may be prepaid at the Company's option, subject to the payment of a prepayment premium in certain circumstances as provided in the Term Loan Facility. If a prepayment is made prior to the first anniversary of the loan, such prepayment must be made with make-whole amount with the calculation of the make-whole amount as specified in the Term Loan Facility. If a prepayment is made after the first anniversary of the loan but prior to the second anniversary, such prepayment must be made at 106% of the principle amount, if a prepayment is made after the second anniversary but prior to the third anniversary, such prepayment must be made at 103% of the principle amount. After the third anniversary, if a prepayment is made, no prepayment premium is due. The Company is required to make principal payments in the amount of \$625,000 per quarter commencing with the quarter ended March 31, 2017. In addition, pursuant to the Term Loan Facility, the Company must prepay or offer to prepay, as applicable, term loans with the net cash proceeds of certain debt incurrences and asset sales, excess cash flow, and upon certain change of control transactions, subject in each case to certain exceptions.

The Term Loan Facility contains certain affirmative and negative covenants, including covenants that restrict the ability of the Term Loan Parties to take certain actions including, among other things and subject to certain significant exceptions, the incurrence of debt, the granting of liens, the making of investments, entering into transactions with affiliates, the payment of dividends and the sale of assets. The Term Loan Facility also contains financial covenants requiring that the Company maintain an asset coverage ratio of at least 1.35 to 1.0 and that Liquidity (as defined in the Term Loan Facility) must not be less than \$37.5 million (of which at least \$20.0 million must be in cash or cash equivalents held in deposit accounts) as of the last day of any fiscal quarter, subject to certain exceptions and cure rights.

### Debt Compliance

At March 31, 2017, we were in compliance with all the financial covenants under our ABL Facility and the Term Loan Facility. Based on management's current projections, we expect to be in compliance with all the covenants under our ABL Facility and Term Loan Facility for the next twelve months. A breach of any of these covenants, ratios or tests could result in a default under our indebtedness.

### Capital Expenditures

During the three months ended March 31, 2017, our capital expenditures totaled \$2.4 million, primarily related to the ongoing maintenance of our equipment. Our capital expenditure plan for 2017 contemplates spending between \$10 million and \$20 million, subject to market conditions. This is primarily related to equipment replacement needs, including ongoing replacements to our rig services fleet. Our capital expenditure program for 2017 is subject to market conditions, including activity levels, commodity prices, industry capacity and specific customer needs as well as cash flows. Our focus for 2017 will be the maximization of our current equipment fleet, but we may choose to increase our capital expenditures in 2017 to expand our presence in a market. We currently anticipate funding our 2017 capital expenditures through a combination of cash on hand, operating cash flow, proceeds from sales of assets and borrowings under our ABL Facility. Should our operating cash flows or activity levels prove to be insufficient to fund our currently planned capital spending levels, management expects it will adjust our capital spending plans accordingly. We may also incur capital expenditures for strategic investments and acquisitions.

### Off-Balance Sheet Arrangements

At March 31, 2017 we did not, and we currently do not, have any off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There have been no material changes in our quantitative and qualitative disclosures about market risk from those disclosed in our 2016 Form 10-K. More detailed information concerning market risk can be found in “Item 7A. Quantitative and Qualitative Disclosures about Market Risk” in our 2016 Form 10-K.

28

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Table of Contents

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly Report on Form 10-Q, management performed, with the participation of our Chief Executive Officer and our Chief Financial Officer, an evaluation of the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Our disclosure controls and procedures are designed to ensure that information required to be disclosed by us in the reports we file or submit 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 is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on this evaluation, management concluded that our disclosure controls and procedures are effective as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the first quarter of 2017 that materially affected, or were reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

**PART II — OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

We are subject to various suits and claims that have arisen in the ordinary course of business. We do not believe that the disposition of any of our ordinary course litigation will result in a material adverse effect on our consolidated financial position, results of operations or cash flows. For additional information on legal proceedings, see “Note 10. Commitments and Contingencies” in “Item 1. Financial Statements” of Part I of this report, which is incorporated herein by reference.

In November 2015, the Santa Barbara County District Attorney filed a criminal complaint against two former employees and Key, specifically alleging three counts of violations of California Labor Code section 6425(a) against Key. The complaint sought unspecified penalties against Key related to an October 12, 2013 accident which resulted in the death of one Key employee at a drilling site near Santa Maria, California. An arraignment was held on February 10, 2016, where Key and its former employees pleaded not guilty to all charges.

On or about January 10, 2017, Key entered into a settlement with the Santa Barbara County District Attorney. Key agreed to plead no contest to one felony count (Count 2), a violation of California Labor Code 6425(a). The Santa Barbara County District Attorney also agreed to recommend total restitution, fines, fees, and surcharges not to exceed \$450,000. The court dismissed the remaining charges (Counts 1 and 3) against Key. The parties agreed to postpone sentencing in the matter until January 20, 2018. The parties agreed that if Key pays all of the total restitution, fines, fees, and surcharges by January 20, 2018, the Santa Barbara County District Attorney will not object to Key withdrawing its plea to a felony count on Count 2 and entering a plea to a misdemeanor.

**ITEM 1A. RISK FACTORS**

Reference is made to Part I, Item 1A. Risk Factors of the 2016 Form 10-K for information concerning risk factors.

**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 Exhibit Index, which follows the signature pages to this report and is incorporated by reference herein, sets forth a list of exhibits to this report.

Table of Contents

SIGNATURE

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.

/s/ J.

Date: May 11, 2017 By: MARSHALL  
DODSON  
J. Marshall  
Dodson  
Senior Vice  
President and  
Chief  
Financial  
Officer  
(As duly  
authorized  
officer and  
Principal  
Financial  
Officer)



EXHIBIT INDEX

Exhibit No. Description

- 3.1 Certificate of Incorporation of Key Energy Services, Inc. (incorporated herein by reference to Exhibit 3.1 to the Company's Form 8-A filed with the SEC on December 15, 2016, File No. 001-08038).
- 3.2 Amended and Restated By-laws of Key Energy Services, Inc. (incorporated herein by reference to Exhibit 3.2 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016, filed with the SEC on March 2, 2017, File No. 001-08038).
- 10.1 Joinder and Increase in Revolver Commitments Agreement, dated as of February 6, 2017, among Key Energy Services, Inc. and Key Energy Services, LLC, as borrowers, Siemens Financial Services, Inc. and Bank of America, N.A., as administrative agent (incorporated herein by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on February 6, 2017, File No. 001-08038)
- 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\*\* Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101\* Interactive Data File.

\* Filed herewith

\*\*Furnished herewith