DRC RESOURCES CORP /FI
Form 6-K
November 15, 2004

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 6-K

REPORT OF FOREIGN PRIVATE ISSUER

PURSUANT TO RULE 13a-16 or 15d-16 OF

THE SECURITIES EXCHANGE ACT OF 1934

For the month of November, 2004

Commission File Number 1-31722

DRC RESOURCES CORPORATION

(Exact name of registrant as specified in its charter)

595 Howe Street, Suite #601, Vancouver, British Columbia, Canada V6C 2T5

(604) 687-1629

(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover Form 20-F or Form 40-F.

Form 20-F __X__ Form 40-F ___

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101 (b)(1): ___

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7): ___

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes _X__ No ___

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-713___.

EXHIBIT INDEX

The following is a list of Exhibits included as part of this Report on Form 6-K.

1

MD&A 3rd Quarter 2004, dated November 12, 2004

2

3rd Quarter 2004 Audited Financial Statements

SIGNATURES

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

DRC RESOURCES CORPORATION
(Registrant)

Date: November 15, 2004	**By:**	***Christopher J. Bradbrook***
		Christopher J. Bradbrook,
		President and Chief Executive Officer

DRC RESOURCES CORPORATION

2004

THIRD QUARTER REPORT

Content

#601 - 595 Howe Street, Vancouver, B. C. V6C 2T5

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E-mail address: drcresources@uniserve.com

Website: drcresources.com

TSX Symbol   DRC

To Our Shareholders:

It is a pleasure to be able to write my very first message to DRC Resources shareholders as President and CEO. During the 3rd quarter ended September 30, 2004 the Company made significant progress in several key areas.

Work continued towards finalizing all requirements to initiate the 2000 metre exploration decline at the Company s Afton copper-gold Project near Kamloops, British Columbia. Subsequent to the end of the period we were pleased to be able to announce (on October 26, 2004) that mobilization of equipment and contractors had begun. The final contract for the exploration decline and ancillary underground development was awarded to Procon Mining and Tunnelling Ltd. (Procon). Procon is a British Columbia-based mining contractor with extensive experience in underground mine development.

This is an important step in the advancement of the project, as it will support the work required to complete a bankable feasibility study and conduct additional exploration work. Total costs for this work are expected to be approximately US$14.5 million. Definition diamond drilling, bulk sampling and technical studies will be carried out concurrently with development of the decline, and are designed to provide the information necessary to better define mineralization and to upgrade resources to the reserve category. The feasibility study will include commissioning an independent mine engineering consulting group to finalize a plan for placing the Afton Copper-Gold Project into production.

In July we were pleased to announce the results of 6 diamond drill holes on the Company s 100% owned Ajax Property, located 10 km east of the Afton Property. This drilling indicated the presence of a large copper-gold system which was intersected over a strike length of approximately 400 meters and to a vertical depth of 300 meters below surface. The results of this work are particularly encouraging as they indicate mineralization continues much deeper than the base of the shallow pits where copper-gold ore was mined in the early 1990 s.

In August the Company s Form 20F Registration Statement filing was accepted by the United States Securities and Exchange Commission. This now allows the Company s shares to trade in the United States. The 20F Registration is an extremely important step in the evolution of DRC Resources, and an important tool to enable us to achieve our goal of realizing shareholder value and gives us access to the world s largest pool of investors. We continue to be excited about the prospects for the Company and look forward to articulating our enthusiasm to investors throughout North America.

For the immediate future, DRC s main focus will continue to be the exploration and development of the Afton Copper-Gold Project. Specifically we look forward to making meaningful progress on the exploration decline and to begin delineation and exploration drilling in and near the mineralized zone. We will also be accelerating our investor relations effort throughout, Canada, the United States and Europe to introduce the Company and its investment potential to new investors.

To date the Company has outlined a Measured and Indicated Mineral Resource of 68.7 Million Tonnes grading 1.68% Copper Equivalent or 2.61g/t Gold Equivalent (1.08% Cu, 0.85 g/t Au, 2.62 g/t Ag, 0.12 g/t Pd), which contains approximately 1.6 billion pounds of copper, and 1.9 million ounces of gold. A 2004 advanced scoping study completed by Behre Dolbear and Company Ltd., indicates that this project would have initial capital expenditures of US$120 million and (at conservative metal prices of US$0.85 per pound copper, and US$375 per ounce gold) when viewed as a primary copper mine, could potentially produce the metal at a cash (direct) operating cost of US$0.15 per pound of copper, and when viewed as a primary gold mine, could produce the metal at negative cash operating cost per ounce of gold. According to the British Columbia Ministry of Energy & Mines, the Afton Project is the largest advanced exploration project in South Central B.C. The Company is also exploring its nearby, 100%-owned, Ajax and Pothook properties.

DRC is in excellent financial condition with cash of US$21 million and no debt. The company has only 13.7 million shares outstanding and 15.2 million shares fully diluted.

On behalf of the Board of Directors, I would like to welcome our new shareholders and thank our long-term investors for their continued interest and support. Management will continue its best efforts to ensure that investor confidence in the Afton Project is rewarded.

Chris Bradbrook

President & CEO

November 12, 2004

MANAGEMENT S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITIONS AND RESULTS OF OPERATION AT SEPTEMBER 30, 2004

DATED NOVEMBER 12, 2004

Management s Discussion and Analysis (MD&A) of financial condition and results of operation of DRC Resources Corporation (the Company or DRC) for the third quarter ended September 30, 2004 should be read in conjunction with the Company s consolidated financial statements and corresponding notes for the period ending September 30, 2004. The focus of this discussion is on material changes and information relating to the current period and may exclude certain information disclosed in the previous period s discussion.

DRC prepares and files its consolidated financial statements and MD&A in Canadian (CDN) dollars and in accordance with Canadian generally accepted accounting principles (GAAP).

Overview

DRC Resources Corporation with head office located in Vancouver, British Columbia, was incorporated in 1980. The Company is a development stage resource company engaged in the acquisition, evaluation, exploration and development of mineral interests. The Company s presently issued 13,691,766 million issued shares are listed on the Toronto Stock Exchange (TSX symbol DRC). The Company s main project, the Afton Copper-Gold Project, and also the Ajax Project are located 10 kilometres west of Kamloops, British Columbia. The Company also owns a mineral interest in Ontario which is being maintained with no further work program presently planned.

The Company s business is managed by directors and executives with professional backgrounds and many years experience in the mining industry, augmented by independent geological and mining professionals (qualified persons) retained to advise the Company on its main project.

In evaluating the Company s financial condition and performance, management looks at DRC s relative position in the context of reporting mineral exploration companies in Canada. In that context, management sees the Company as emerging from junior to advanced exploration stage, in which its decision making capabilities will undergo more rigorous testing as DRC moves toward the development and production stages on its advanced Afton Copper-Gold Project. How effectively the Company meets the new issues and challenges will depend upon the management of priorities for the development of the Afton Copper-Gold Project. Management perceives the advancement of DRC s status as due to selection of highly qualified technical advisors, on-site attention of management to conduct exploration work, understanding of what constitutes a successful exploration attempt and careful cash management. All of those qualities must continue and be improved to meet the challenges of higher cost activities (underground vs. surface exploration). While a generally improved economic climate in the mining industry has greatly assisted in the money raising area, the main risks to achievement of objectives will be increased competition for both expert personnel and contract labour which is expected to result in a general increase in costs and, possibly, delay in getting jobs done. Hence, staffing and cost management are expected to be the main challenges to company stewardship in the near term.

Progress and Outlook

On August 23, 2004, the Company announced that its Form 20F Registration Statement filing was accepted by the United States Securities and Exchange Commission under Section 12(g) of the Securities Exchange Act of 1934. The Registration Statement (CIK #0000800166, File No. 1-31722), which allows the Company s shares to trade in the United States, can be viewed at www.sec.gov.

The 12(g) Registration and the Standard & Poor s Investor Relations Program (www.advisorinsight.com) permits the introduction of DRC Resources Corporation and its Afton Copper-Gold Project to a large investor base, and raises the Company s profile within the North American investment community.

DRC Resources has changed the Auditors for the Company to comply with the financial filing requirements for United States registered companies. DeVisser Gray, a Vancouver-based Chartered Accounting firm registered under the Canadian Public Accountability Board (CPAB) and the United States Public Company Accounting Oversite Board (PCAOB) has been appointed as the Company s Auditors.

During the third quarter 2004 the Company focused on the design, budget requirements and personnel to implement a plan to excavate an underground exploration decline for the Afton Copper-Gold Project (Afton Project), located near Kamloops, British Columbia. As a mineral exploration company, the future liquidity of DRC will be affected principally by the level of exploration expenditures and by its ability to raise capital through the equity markets. Completion of a $24.15 million financing at the beginning of November, 2003 put the Company in a cash position more than sufficient to fund planned exploration expenditures and meet ongoing obligations as they become due.

The Company is moving forward with its plan to advance the Afton Project through the feasibility stage by carrying out an underground exploration and development program as recommended in the February 2004 update of Behre Dolbear & Company s advanced Scoping Study that included an economic evaluation of the Afton Project, Kamloops, B.C in compliance with National Policy 43-101 (filed on SEDAR).

The Advanced Scoping Study confirmed that one of several possible mining methods had the potential for development of an underground bulk tonnage mining operation at Afton. The relevant project statistics are outlined below:

Afton Project Statistics

Mineral Resource	Measured and Indicated[1]	68,700,000 tonnes	1.68% Cu_{Eq}
	Inferred Resource	7,450,000 tonnes	1.61% Cu_{Eq}
Mineral Resource Within the	Measured and Indicated	46,983,000 tonnes	1.72% Cu_{Eq}
Proposed Mine Plan	Inferred Resource	4,543,000 tonnes	1.72% Cu_{Eq}
Total Resource Material to be Recovered by the Mine Plan			
	All Categories[2]	51,526,000 tonnes	1.72% Cu_{Eq}
Metallurgical Recovery	Copper		90%
	Gold		90%
	Silver		75%
	Palladium		74%
Mining Method			Underground Panel (Block) Caving
Production Rate (Mine & Mill)			9,000 tonnes per day
Mine Life			17.8 years
Average Annual Production	Copper		29,350 tonnes
	Gold		71,000 ounces
	Silver		178,100 ounces
	Palladium		7,700 ounces
Initial Capital Cost[3]			$140,034,000
Working Capital and Initial Inventory			$9,700,000
On-going Capital			$191,351,000
Unit Operating Cost	(at full production)		$9.77/tonne milled
Net Present Value	0%		$418,206,437
	5%		$203,578,770
	7.5%		$140,373,936
	10%		$94,306,153
Internal Rate of Return	(pre-tax)		26.68%
	(after tax)		19.94%
Payback Period			3.7 years

Notes:	1	Afton Main Zone Only (@ 0.7% Cu_{Eq} cut-off grade)
	2	See Note on Page 17, Section 3.0
	3	Currency used throughout is $Canadian

Metal	Price Used US$)	Recovery
Copper	$0.85/lb.	90%
Gold	$375/oz.	90%
Silver	$5.25/oz.	75%
Palladium	$200/oz.	74%

Significant additional expenditure will be required to establish that development of the Afton Project is feasible as a large high-grade copper-gold mine. Rising copper demand and prices have increased interest in advanced projects such as the Afton and are expected to make production financing obtainable.

DRC employs a comprehensive QA/QC program including the use of standards and internal and external check samples. Behre Dolbear has reviewed the QA/QC program and is of the opinion that it meets or exceeds industry standards. Industry-accepted methods were used for grade estimation using ordinary kriging (a method of determining a weighted average in such a way that the geostatistical estimation variance of the weighted average is minimized). The assays were composited into 10 metre down-hole composites. Reasonableness of grade interpolation was reviewed by visual inspection of sections displaying block model grades, drill-hole composites and geology with good agreement being observed. In accordance with National Instrument 43-101, both the updated Mineral Resource Study and the updated advanced Scoping Study were filed on SEDAR.

The resources developed by DRC Resources are not reserves and, until such time as resources are proven to be reserves, there is a risk that the Company may not achieve ongoing operations from which it may derive significant income.

The Company has held and is continuing discussions with senior members of the mining and minerals processing industries with the objective of moving the Afton Project through the feasibility stage to production. The Company is in process of confidential discussions concerning production financing with a number of mining companies, smelters and financial institutions.

Michael W.P. Hibbitts, Vice President of Exploration & Development, a qualified person, has been charged with responsibility for managing the design, implementation and supervision of the underground exploration program to advance the Afton Project through the feasibility stage. In June, 2004 the Company invited 5 major Canadian mining contract companies to tender for excavation of a 2000 metre decline (tunnel) and Ancillary Underground Development for the Afton Copper-Gold Project. The main purpose of the decline is to provide underground access for the definition diamond drill program, bulk sampling and technical studies, which will be carried on concurrently with development of the decline, in order to complete the Afton Feasibility Study.

Subsequent to the end of the third quarter the Company awarded the contract for the Exploration Decline and Ancillary Underground Development for the Afton Copper-Gold Project to Procon Mining & Tunnelling Ltd., a Canadian mining contractor with its head office in British Columbia, with over 10 years of experience in underground mine development. Its corporate clients include major Canadian and international mining companies.

Mobilization for the excavation of the Afton Exploration Decline is scheduled to begin in early November, 2004. All development work is scheduled to be completed by November 15, 2005.

Selected Quarterly Information

The selected financial data appearing below for the third quarter ending September 30, 2004, 2003, and 2002 are set forth in Canadian dollars and extracted from the Consolidated Financial Statements (filed on SEDAR).

DRC s financial statements are prepared in accordance with generally accepted accounting principles (GAAP) that apply in Canada. The selected financial data appearing in the first table below is presented in accordance with Canadian GAAP and should be read in conjunction with, and is qualified in its entirety by reference to DRC Resources audited Consolidated Financial Statements.

	Quarter Ended September 30, 2004	**Quarter Ended September 30, 2003**	**Quarter Ended September 30, 2002**
Operating Revenue	85,525	21,496	30,085
Net Income (Loss)	(146,626)	(105,943)	(62,734)
Income (Loss) per Share	(0.01)	(0.01)	(0.01)
Total Assets	30,729,760	6,098,807	6,773,988
Net Assets	29,697,423	5,876,397	6,507,589
Deferred Income Taxes	892,880	206,266	183,537
Cash Dividends per share	Nil	Nil	Nil
Deficit	(3,075,938)	(2,161,588)	(1,652,298)
Capital Stock	32,773,361	8,037,985	8,159,887
Weighted Average Number of Shares	13,356,110	9,197,028	8,771,266

During the third quarter of 2004, $1,368,000 was received by the Company for the exercise of 455,000 stock options. With approximately $26 million in cash assets, DRC currently has sufficient funds to meet its obligations and to carry out its exploration plans for at least the next 24 months. There is no assurance that DRC will in the future be able to obtain all the financing it requires on acceptable terms and conditions, or at all. The only sources of future funds presently available to DRC are the sale of equity capital or the offering of an interest in its properties to be earned by another person or firm carrying out further exploration or development of the properties.

Operating Results

During the third quarter 2004 the main focus of the Company has been the final engineering design for the underground workings and tendering the underground exploration decline for the Afton Project in Kamloops, B.C. as described in the Progress and Outlook section above.

The Company has expended over $5.5 million on the Afton Project exploration program to date which includes, but is not limited to, the cost of an economic evaluation by the Company s mine engineering consultants, Behre Dolbear & Company Ltd., metallurgical test work, geophysical surveys, upgrading access roads, and the surface diamond drill exploration program consisting of 109 diamond drill holes for a total of 53,000 metres (175,000 ft).

The advanced Scoping Study on the Afton Main Mineral Zone prepared by Behre Dolbear and Company Ltd., is based on a Mineral Resource (all categories) of 76 million tonnes and indicates that panel cave mining and conventional flotation technology are viable methods of application for mining and processing of 51.5 Million Tonnes of the Mineral Resource. The Study indicates an estimated life of mine cash operating cost of US$0.15 per pound of copper and a total operating cost of less than US$0.40 per pound of copper, both costs being net of precious metal credits. A copper price of US$0.85 per pound was used in the economic calculation for this study. Persistence of the current robust metals market, in which copper prices have exceeded US$1.20 per pound, would enhance the economic potential of the Afton Project. The Company is proceeding directly to the feasibility stage and implementing the final design of the underground workings.

The present estimate of $17,952,000 (including a 30% contingency) for exploration and development costs over the next 18 months through feasibility compares closely with the scoping study by the Company s principal project consultant, Behre Dolbear & Company Ltd. ($17,748,000 without contingencies), to cover all required underground development, diamond drilling, standby consulting professionals and the internal administrative, planning and supervisory group costs. Recent reviews and engineering recommendations for changes to the underground exploration program indicate a potential for reducing overall costs by some 20%. The change involves reducing the length of the decline and placement in a more advantageous location for the underground exploration program. A $12 million exploration expenditures program is budgeted for the next 12 months.

The Company invited tenders for the decline construction contract in late second quarter and, subsequent to the end of the third quarter, awarded the contract to Procon Mining & Tunnelling Ltd. (as described in the Progress and Outlook section above).

This program will be funded out of available working capital. It is expected that budgeted costs may be modified and adjusted downward to reflect the exact method of underground development implemented.

DRC s exploration program in 2004 is also designed to test several other areas of the Afton Project property, the Pothook and Ajax mineral zones by surface diamond drilling where indicated. The exploration programs will be paid for out of working capital.

DRC Resources completed 6 diamond drill holes on the Company s 100% owned Ajax Property, located 10 km east of the Afton Property, Kamloops, B.C. The purpose of the diamond drill program was to test for sulphide mineralization between the two Ajax open pits and below the previously mined depths. Drilling intersected a large near surface copper sulphide system with an associated gold credit between and deeper than the previously mined Ajax East and Ajax West pits. The Ajax Property, consisting of 77 mineral claims, covering 4500 acres, is connected by an existing 10 km mine haulage road to the Afton Copper-Gold Property to the west. (For drill holes location, refer to maps on Company s website: www.drcresources.com)

The results of the exploration program represent a significant departure from the shallow surface pits where the copper-gold ore was mined by the previous operator in the early nineteen nineties. The exploration drill program has outlined copper-gold mineralization with an interpreted vertical depth of 300 metres below surface and with an apparent thickness of 400 metres, which is consistent with the zone mined in the two open pits. Three of the six drill holes were drilled over a strike length of approximately 400 metres. Three drill holes completed to the northwest of the Ajax East and West pits did not intersect the mineralized zone as the holes were collared too far in the foot wall of the zone.

The Ajax East and West pits have been described as porphyry deposits in geological publications. The Company is encouraged by the size and depth of the system and intends to continue to explore for a higher grade core.

Significant assay results for three drill holes intersecting the mineral zone over a length of 400 metres and to a depth of 300 metres below surface are as follows:

ASSAY INTERSECTIONS FOR AX-01 @ -55°/121°

Core Length (m)	Depth (m)	Copper (%)	Gold (g/t)
51	75-126	0.232	0.145
121	156-277	0.240	0.169
63	307-370	0.362	0.165
31.2	421-452.2	0.249	0.126

ASSAY INTERSECTIONS FOR AX-02 @ -52°/120°

Core Length (m)	Depth (m)	Copper (%)	Gold (g/t)
194	26-220	0.223	0.141
123	277-400	0.221	0.082

ASSAY INTERSECTION FOR AX-04 @ -55°/120°

Core Length (m)	Depth (m)	Copper (%)	Gold (g/t)
278	27-305	0.233	0.159

Note: Certain technical reports outlining the above have been filed on SEDAR. A direct link to SEDAR may be found on the Company s website: www.drcresources.com.

Summary of Quarterly Information

The selected financial data appearing below for the last completed 8 quarterly periods beginning December 31, 2002 and ending September 30, 2004 are set forth in Canadian dollars and extracted from the audited and interim Consolidated Financial Statements (filed on SEDAR).

DRC s financial statements are prepared in accordance with generally accepted accounting principles (GAAP) that apply in Canada. The selected financial data appearing in the first table below is presented in accordance with Canadian GAAP.

The following selected financial data should be read in conjunction with, and is qualified in its entirety by reference to DRC s audited and interim Consolidated Financial Statements.

The Afton and Ajax exploration programs are the only significant expenditures in progress. All exploration has been funded by external financing through issue of securities of DRC. The Company has no current ongoing mining operations. Income is derived solely from interest on available working capital that is earmarked for expenditure in exploration and development.

Foreign currency fluctuations had a very limited negative effect on DRC other income and expenses. It should be noted that forecasts of revenues described in the Scoping Study on the Afton project could be negatively impacted by a rising Canadian dollar (or devaluing US dollar), since all such future concentrate product sales would be conducted in US currency, while production costs would be incurred in Canadian dollars.

For purposes of illustrating management explanation and discussion of the Company s financial condition and results of operations, please refer to the following table of comparative selected quarterly financial information.

Quarter Ending	**Sep 30**	**June 30**	**Mar 31**	**Dec 31**	**Sep 30**	**June 30**	**Mar 31**	**Dec 31**
	2004	**2004**	**2004**	**2003**	**2003**	**2003**	**2003**	**2002**
Net Operating Revenue (Loss)	85,525	199,034	171,306	108,482	21,613	(8,747)	(4,615)	114,260
(Loss) Before Taxes	(140,903)	(18,310)	71,505	(415,702)	(70,410)	(141,907)	(103,856)	(368,551)
(Loss) per Share	(0.01)	(0.01)	(0.01)	(0.04)	(0.01)	(0.02)	(0.01)	(0.04)

Net Income(Loss)	(146,126)	(20,442)	62,395	(1,218,371)	(105,943)	(182,930)	(119,800)	(185,907)
(Loss) per Share	(0.01)	(0.01)	(0.01)	(0.13)	(0.01)	(0.02)	(0.01)	(0.02)

Liquidity & Capital Resources

Working Capital at Quarter-end

DRC Resources had working capital of $26,186,696, $3,480,065 and $3,467,864 and no debt at September 30th in, respectively, the years 2004, 2003 and 2002. Net equity financings of $4,904,120 in 2000, $1,935,515 in 2002 and $22,500,250 in 2003 were the principal sources of working capital.

During the third quarter 2004 interest income, a small oil and gas royalty and foreign exchange gains (loss) provided for approximately 37.71% of the Company s administrative costs. In the same period in 2003 and 2002 interest and royalty income provided for, respectively, approximately 14.09% and 22.54% of the Company s administrative costs.

In 2000 DRC Resources working capital increased significantly due to funding provided by a $5 million Special Warrants Private Placement Offering, which put the Company in a position to make a commitment to a large exploration program on its Afton Copper-Gold Project. In 2002 a $2.1 million private placement of flow-through shares was added to exploration funding and in 2003 a $24.15 million private place of common shares significantly increased the working capital.

Interest income on its working capital combined with a favourable exploration cost experience on the Afton Copper-Gold Project leave DRC with working capital adequate to meet its administrative costs and property maintenance programs through the year 2005. DRC s working capital is sufficient to meet all its present requirements as an exploration company. In order to be in a position to move to the development stage of its Afton Copper-Gold Project, DRC realized that it would be expected to raise as much as 10% of the expected capital requirement of about $140 million, in order to attract an institutional lender or mine financing partner, such as a smelter, to the project. The $24.15 million financing in November 2003 achieved this objective, with the result that the Company is now engaged in discussions concerning project financing, project participation and concentrate sales arrangements with a number of mining companies, international smelters and financial institutions that have expressed an interest in the Afton Copper-Gold Project.

Contractual Obligation for Acquisition of the Afton Copper-Gold Property

By Option to Purchase Agreement (the Option) dated September 22, 1999, DRC Resources acquired the exclusive right for 90 days to purchase a 100% undivided working interest in the Afton 1 11, incl. mineral claims, Record Nos. 372023 372026 incl. and 372641 372647 incl. (the Original Claims) as to 50% from Westridge Enterprises Ltd., a non-reporting British Columbia company wholly owned by John H. Kruzick, a director, the President and CEO of the Company at that time, and as to 50% from Indo-Gold Development Ltd., a non-reporting British Columbia company owned by John Ball, a geologist. The Option provided for consideration to be a 10% Net Profit Royalty to and a property management agreement with the optionors, with exercise to be by carrying out exploration work and paying Common Shares of DRC Resources as follows:

Due Date[1]	***Option Payment***	**Status**	**Exploration ($)**	**Status**
On regulatory approval	1,000,000 Shares	Paid		
Year 1 (2000)	-		400,000	Performed
Year 2 (2001)	200,000 Shares	Paid	600,000	Performed

Year 3 (2002)	200,000 Shares	Paid	1,000,000	Performed
Year 4 (2003)	200,000 Shares	Paid	1,000,000	Performed
Year 5 (2004)	200,000 Shares		1,000,000	Performed
Year 6 (2005)	200,000 Shares		1,000,000	Performed
Year 7 (2006)			500,000	
Year 8 (2007)			500,000	
Year 9 (2008)			500,000	
TOTALS	2,000,000 Shares		6,500,000	

Note: (1)

The initial option payment was due and paid following acceptance of the filing of the Formal Option by the then governing regulatory body, the Canadian Venture Exchange. Subsequent option payments are due to be paid in full on or before the anniversary of the Due Date on November 10th in all future years unless otherwise agreed upon by both parties.

Contractual Obligation for the Development of the Afton Copper-Gold Project

The Company entered into a consulting services agreement with Mr. Michael W.P. Hibbitts, Vice President of Exploration and Development on March 22, 2004. The terms of the contract are as follows:

- Term: Month to Month.
- Cash compensation: a base retainer fee $11,000 per month served.
- Stock Options: He was granted options to purchase 100,000 common share at an exercise price of $6.50 in accordance with DRC Resources Stock Option Plan.
- Expenses: He will be reimbursed all reasonable out-of-pocket expenses incurred by him in carrying out his duties
- Bonus: He will be paid a cash payment of $18,000 upon performing the services and completing the feasibility study on the Afton Project according to the agreed timeline.
- Transportation: He will be provided with a truck for use on and in connection with the Afton Project

Other than relatively nominal property maintenance costs on projects does not have any other commitments for material expenditures in either the near or long term.

The Company s source of liquidity is its cash and cash equivalents. However, this is supplemented by interest earned and these sources of cash are considered sufficient to meet near-term financial requirements.

Off-Balance Sheet Arrangements

The Company has service contracts with two persons who are directors and/or members of administrative, supervisory or management bodies.

Since founding DRC Resources, John H. Kruzick has provided the Company s direction and management as a consultant through a private company, Westridge Enterprises Ltd., controlled by him and paid on a per diem services basis with reimbursed for out-of-pocket expenses. By Services Agreement made and approved April 23, 2003 and amended October 13, 2004 by the Board of Directors, John H. Kruzick s engagement as

Chairman of the Board was formalized on a retainer basis on the following terms and conditions:

- Term: Five years commencing April 2003 through March 2007.
- Cash compensation: He was paid a base retainer fee $500 per day served during year 2003 (beginning in April, 2003). The base retainer fee is to be increased annually as deemed appropriate for services performed subject to approval by a majority of the board of directors.
- Director s Fees: As member of the Board of Directors he is to be entitled to any approved directors fees.
- Retainer during Illness: He will be paid the per diem fee on the basis of 20 days per month for up to six months from the date when any illness renders him unable to fulfill his duties.
- Benefits During Illness: he will receive benefits other than contract fees for up to 2 years after any illness renders him unable to fulfill his duties.
- Stock Options: He may be granted options to purchase its stock in accordance with DRC Resources Stock Option Plan.
- Expenses: He will be reimbursed all reasonable out-of-pocket expenses incurred by him in carrying out his duties.
- Termination: The Board of Directors may terminate Kruzick s employment at any time, with or without cause.
- Termination by Company Without Cause: If his services are terminated without cause, Mr. Kruzick will receive accrued service fees and a lump sum payment equal to the average monthly fee paid for the previous year times the number years he has been with the Company.
- Termination Without Cause by Kruzick: If Mr. Kruzick terminates his employment without cause prior to the expiration of the Agreement, he will be paid all accrued, but unpaid fees and expenses.
- Termination With Cause by DRC Resources: If Mr. Kruzick s employment is terminated by DRC Resources for cause, other than moral turpitude or dishonesty on Kruzick s part, prior to the expiration of this Agreement, he will be paid a lump sum severance payment equal to the compensation of one month of service fees for each year of past contract services rendered (based on the average monthly fee paid for the previous year), together with any accrued, but unpaid expenses
- Reporting: Mr. Kruzick is to be a permanent member and chairman of the Executive Committee, report to the Board of Directors at regular quarterly Board meetings and at the annual general meeting of DRC Resources and otherwise be accountable to the Board of Directors.

Since May 12, 1981, Sharon L. Ross has provided the Company with secretarial and office administrative services as a consultant through a private company, Allshare Holdings Ltd., controlled by her and paid on a per diem services basis with reimbursed for out-of-pocket expenses. By Services Agreement made and approved April 23, 2003 by the Board of Directors, Sharon L. Ross engagement as Corporate Secretary to perform the duties customary to that position was formalized on the following terms and conditions:

- Term: Five years commencing April 2003 through March 2007.
- Cash compensation: She was paid a base fee of $35 per hour served during year 2003 (beginning in April, 2003), The base fee is to be increased annually as deemed appropriate for services performed subject to approval by a majority of the board of directors.
- Director s Fees: As member of the Board of Directors she is to be entitled to any approved directors fees.
- Retainer during Illness: Mrs. Ross will be paid the per diem fee on the basis of 128 hours per month for up to six months from the date when any illness renders her unable to fulfill her duties.
- Benefits During Illness: She will receive benefits other than contract fees for up to 2 years after any illness renders her unable to fulfill her duties.
- Stock Options: She may be granted options to purchase its stock in accordance with DRC s Stock Option Plan.
- Expenses: She will be reimbursed all reasonable out-of-pocket expenses incurred by her in carrying out her duties.
- Termination: the Board of Directors may terminate Mrs. Ross engagement at any time, with or without cause.
- Termination by Company Without Cause: If her services are terminated without cause, Mrs. Ross will receive accrued service fees and a lump sum payment equal to the average monthly fee paid for the previous year times the number years she has been with the Company.
- Termination Without Cause by Ross: If Mrs. Ross terminates her engagement without cause prior to the expiration of the Agreement, she will be paid all accrued, but unpaid fees and expenses.
- Termination With Cause by DRC Resources: If Mrs. Ross engagement is terminated by DRC Resources for cause, other than moral turpitude or dishonesty on her part, prior to the expiration of the Agreement, she will be paid a lump sum severance payment equal to the compensation of one month of service fees for each year of past contract services rendered (based on the average monthly fee paid for the previous year), together with any accrued, but unpaid expenses
- Function and Reporting: Mrs. Ross reports to the President, is to be a member and act as secretary of the Executive Committee of the Board of Directors, is to consult with the Executive Committee, as required, in respect of extraordinary matters arising in the course of day-to-day business and be accountable to the Board of Directors.

Related Party Transactions

During the quarter ending September 30, 2004, the Company paid $17,731 compared to $15,886 in the same period of 2003, for secretarial and accounting services invoiced by Allshare Holdings Ltd., a private company in which a director has a 50% interest. During the quarter ending September 30, 2004 the Company paid $39,750 compared to $36,000 in the same period of 2003 for consulting and deferred exploration costs invoiced by Westridge Enterprises Ltd., a private company owned by a director of the Company. A related person of the President was paid $21,600 for consulting services during the quarter ending September 30, 2004 compared to $15,875 for the same period in 2003. An officer of the Company was paid $ 35,060 for the quarter ended September 30, 2004 for consulting services for exploration and development of the Company s mineral projects.

Risks

Mineral exploration is a high risk business and there is no assurance that economic mineral deposits will be found on any of DRC s mineral interests. Positive surface indications and drill results are no guarantee that an economic mineral deposit exists at depth. Fluctuating mineral commodity prices and exchange rates may adversely affect the economics of a mineral deposit. Financial markets can sometimes be negative toward junior exploration companies.

Capital

The information below relating to the capital structure of the Company is at October 26, 2004.

Authorized share capital: 40,000,000 common shares without par value

Issued and outstanding: 13,691,766 common shares without par value

Incentive Stock Options Outstanding:

Number of Options	Exercise Price	Expiry Date

50,000	$3.50	December 5, 2004
100,000	$6.50	April 13, 2006
345,000	$7.50	November 6, 2005
(Broker s Compensation Options)		
600,000	$4.60	October 12, 2009
50,000	$4.60	October 13, 2006
(Service Compensation Options)		

Subsequent Events

On October 18, 2004, Mr. Christopher J. Bradbrook was appointed President and Chief Executive Officer of the Company to replace Mr. John H. Kruzick who was appointed Chairman of the Board and will remain an integral part of the Company s management team. Mr. Bradbrook brings a wealth of expertise and experience to DRC Resources, as a result of his more than 25-year career in the mining industry, in which his principal roles have encompassed many aspects of the industry, including: exploration, mine development, corporate development work, financial analysis, investor relations, and marketing.

Additional Information

Additional information on the Company may be found on SEDAR at www.sedar.com or the Company s website at www.drcresources.com .

Disclaimer

The information contained herein is prepared by the company and believed to be accurate but has not been independently audited or verified and is provided for informational purposes. This information is not to be construed as an offer nor as a recommendation to buy or sell securities. DRC Resources Corporation, its officers and directors assume no responsibility for use of this information in any way whatsoever and do not guarantee its accuracy.

Cautionary Note

It should be noted that some of the statements contained in this presentation are not historical facts but may be forward-looking statements. Estimates and statements that describe the Company s future plans, objectives or goals are examples of forward-looking statements and such statements may include words to the effect that the Company or management expects a stated condition or result to occur. Since forward-looking statement address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results in each case could differ materially from those currently anticipated in such statements by reason of factors such as the productivity of the Company s mining properties, changes in general economic conditions and conditions in the financial markets, changes in demand and prices for the minerals, legislative, environmental and other regulatory, political and competitive developments in areas in which the Company operates.

US Investors Should Note: *The United States Securities and Exchange Commission permits mining companies, in their filings with the SEC to disclose only those mineral deposits that a company can economically and legally extract or produce. We may use certain terms in our publications such as resources , that are prescribed by Canadian regulatory policy and guidelines but are not provided for in the SEC guidelines on publications and filings.*

ize:10pt;">The Company uses a controlled disbursement account for its main cash account. Under this system, outstanding checks can be in excess of the cash balances at the bank before the

disbursement account is funded, creating a book overdraft. Book overdrafts on this account are presented as a current liability in accounts payable in the consolidated balance sheets.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable arise from product sales, product rentals and services, and are stated at estimated net realizable value. This value incorporates an allowance for doubtful accounts to reflect any loss anticipated on accounts receivable balances. The Company regularly evaluates its accounts receivable to estimate amounts that will not be collected and records the appropriate provision for doubtful accounts as a charge to operating expenses. The allowance for doubtful accounts is based on a combination of the age of the receivables, individual customer circumstances, credit conditions, and historical write-offs and collections. The Company writes off specific accounts receivable when they are determined to be uncollectible.

The majority of the Company’s customers are engaged in the energy industry. The cyclical nature of the energy industry may affect customers’ operating performance and cash flows, which directly impact the Company’s ability to collect on outstanding obligations. Additionally, certain customers are located in international areas that are inherently subject to risks of economic, political, and civil instability, which can impact the collectability of receivables.

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Changes in the allowance for doubtful accounts are as follows (in thousands):

	Year ended December 31,		
	2015	2014	2013
Balance, beginning of year	$847	$872	$714
Charged to provision for doubtful accounts	1,132	481	570
Write-offs	(790)	(506)	(412)
Balance, end of year	$1,189	$847	$872

Inventories

Inventories consist of raw materials, work-in-process, and finished goods and are stated at the lower of cost, determined using the weighted-average cost method, or market. Finished goods inventories include raw materials, direct labor, and production overhead. The Company regularly reviews inventories on hand and current market conditions to determine if the cost of finished goods inventories exceed current market prices and impairs the cost basis of the inventory accordingly. Historically, the Company recorded a provision for excess and obsolete inventory. Impairment or provisions are based primarily on forecasts of product demand, historical trends, market conditions, production, or procurement requirements and technological developments and advancements.

At December 31, 2015, the Company recorded impairment to all inventory items recognized with allowance for excess and obsolete inventory.

Property and Equipment

Property and equipment are stated at cost. The cost of ordinary maintenance and repair is charged to operating expense, while replacement of critical components and major improvements are capitalized. Depreciation or amortization of property and equipment, including assets held under capital leases, is calculated using the straight-line method over the asset’s estimated useful life as follows:

Buildings and leasehold improvements	2-30 years
Machinery, equipment, and rental tools	7-10 years
Furniture and fixtures	3 years
Transportation equipment	2-5 years
Computer equipment and software	3-7 years

Property and equipment are reviewed for impairment on an annual basis or whenever events or changes in circumstances indicate the carrying value of an asset or asset group may not be recoverable. Indicative events or circumstances include, but are not limited to, matters such as a significant decline in market value or a significant change in business climate. An impairment loss is recognized when the carrying value of an asset exceeds the estimated undiscounted future cash flows from the use of the asset and its eventual disposition. The

amount of impairment loss recognized is the excess of the asset’s carrying value over its fair value. Assets to be disposed of are reported at the lower of the carrying value or the fair value less cost to sell. Upon sale or other disposition of an asset, the Company recognizes a gain or loss on disposal measured as the difference between the net carrying value of the asset and the net proceeds received.

Internal Use Computer Software Costs

Direct costs incurred to purchase and develop computer software for internal use are capitalized during the application development and implementation stages. These software costs have been for enterprise-level business and finance software that is customized to meet the Company’s specific operational needs. Capitalized costs are included in property and equipment and are amortized on a straight-line basis over the estimated useful life of the software beginning when the software project is substantially complete and placed in service. Costs incurred during the preliminary project stage and costs for training, data conversion, and maintenance are expensed as incurred.

The Company amortizes software costs using the straight-line method over the expected life of the software, generally

3 to 7 years. The unamortized amount of capitalized software was $6.3 million at December 31, 2015.

Goodwill

Goodwill is the excess of cost of an acquired entity over the amounts assigned to identifiable assets acquired and liabilities assumed in a business combination. Goodwill is not subject to amortization, but is tested for impairment annually during the fourth quarter, or more frequently if an event occurs or circumstances change that would indicate a potential impairment. These circumstances may include an adverse change in the business climate or a change in the assessment of future operations of a reporting unit.

The Company assesses whether a goodwill impairment exists using both qualitative and quantitative assessments. The qualitative assessment involves determining whether events or circumstances exist that indicate it is more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill. If, based on this qualitative assessment, it is determined that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, the Company does not perform a quantitative assessment.

If the qualitative assessment indicates that it is more likely than not that the fair value of a reporting unit is less than its carrying amount or if the Company elects not to perform a qualitative assessment, a quantitative assessment or two-step impairment test is performed to determine whether goodwill impairment exists at the reporting unit.

The first step is to compare the estimated fair value of each reporting unit with goodwill to its carrying amount, including goodwill. To determine fair value estimates, the Company uses the income approach based on discounted cash flow analyses, combined, when appropriate, with a market-based approach. The market-based approach considers valuation comparisons of recent public sale transactions of similar businesses and earnings multiples of publicly traded businesses operating in industries consistent with the reporting unit. If the fair value of a reporting unit is less than its carrying amount, the second step of the impairment test is performed to determine the amount of impairment loss, if any. The second step compares the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill. If the carrying amount of the reporting unit's goodwill exceeds its implied fair value, an impairment loss is recognized in an amount equal to that excess.

Other Intangible Assets

The Company's other intangible assets have finite and indefinite lives and consist of customer relationships, trademarks, brand names, and purchased patents.

The cost of intangible assets with finite lives is amortized using the straight-line method over the estimated period of economic benefit, ranging from 2 to 20 years. Asset lives are adjusted whenever there is a change in the estimated period of economic benefit. No residual value has been assigned to these intangible assets.

Intangible assets with finite lives are tested for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. These conditions may include a change in the extent or manner in which the asset is being used or a change in future operations. The Company assesses the recoverability of the carrying amount by preparing estimates of future revenue, margins, and cash flows. If the sum of expected future cash flows (undiscounted and without interest charges) is less than the carrying amount, an impairment loss is recognized. The impairment loss recognized is the amount by which the carrying amount exceeds the fair value. Fair value of these assets may be determined by a variety of methodologies, including discounted cash flow models.

Intangible assets with indefinite lives are not subject to amortization, but are tested for impairment annually during

the fourth quarter, or more frequently if an event occurs or circumstances change that would indicate a potential impairment. These circumstances may include, but are not limited to, a significant adverse change in the business climate, unanticipated competition, or a change in projected operations or results of a reporting unit.

The Company assesses whether an indefinite lived intangible impairment exists using both qualitative and quantitative assessments. The qualitative assessment involves determining whether events or circumstances exist that indicate it is more likely than not that the fair value of the indefinite lived intangible is less than its carrying amount. If, based on this qualitative assessment, it is determined that it is not more likely than not that the fair value of the indefinite lived intangible is less than its carrying amount, the Company does not perform a quantitative assessment.

If the qualitative assessment indicates that it is more likely than not that the indefinite-lived intangible asset is impaired or if the Company elects to not perform a qualitative assessment, the Company then performs the quantitative impairment test. The quantitative impairment test for an indefinite-lived intangible asset consists of a comparison of the fair value of the asset with its carrying amount. If the carrying amount of an intangible asset exceeds its fair value, an impairment loss is recognized in an amount equal to that excess. Fair value of these assets may be determined by a variety of methodologies, including discounted cash flows.

Business Combinations

The Company includes the results of operations of its acquisitions in its consolidated results, prospectively from the date of acquisition. Acquisitions are accounted for by applying the acquisitions method. The Company allocates the fair value of purchase consideration to the assets acquired, liabilities assumed, and any non-controlling interests in the acquired entity generally based on their fair values at the acquisition date. The excess of the fair value of purchase consideration over the fair value of these assets acquired, liabilities assumed, and any non-controlling interests in the acquired entity is recorded as goodwill. The primary items that generate goodwill include the value of the synergies between the acquired company and Flotek and the value of the acquired assembled workforce. Acquisition-related expenses are recognized separately from the business acquisition and are recognized as expenses as incurred.

Fair Value Measurements

The Company categorizes financial assets and liabilities using a three-tier fair value hierarchy, based on the nature of the inputs used to determine fair value. Inputs refer broadly to assumptions market participants would use to value an asset or liability and may be observable or unobservable. The hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (level 1) and the lowest priority to unobservable inputs (level 3). “Level 1” measurements are measurements using quoted prices in active markets for identical assets and liabilities. “Level 2” measurements are measurements using quoted prices in markets that are not active or that are based on quoted prices for similar assets or liabilities. “Level 3” measurements are measurements that use significant unobservable inputs which require a company to develop its own assumptions. When determining the fair value of assets and liabilities, the Company uses the most reliable measurement available.

Revenue Recognition

Revenue for product sales and services is recognized when all of the following criteria have been met: (i) persuasive evidence of an arrangement exists, (ii) products are shipped or services are rendered to the customer and significant risks and rewards of ownership have passed to the customer, (iii) the price to the customer is fixed and determinable, and (iv) collectability is reasonably assured. Products and services are sold with fixed or determinable prices and do not include right of return provisions or other significant post-delivery obligations. Deposits and other funds received in advance of delivery are deferred until the transfer of ownership is complete. Shipping and handling costs are reflected in cost of revenue. Taxes collected are not included in revenue; rather, taxes are accrued for future remittance to governmental authorities.

For certain contracts related to the EOGA division and the Logistics division of the ECT segment, the Company recognizes revenue under the percentage-of-completion method of accounting, measured by the percentage of “costs incurred to date” to the “total estimated costs of completion.” This percentage is applied to the “total estimated revenue at completion” to calculate proportionate revenue earned to date. Contracts for services are inclusive of direct labor and material costs, as well as, indirect costs of operations. General and administrative costs are charged to expense as incurred. Changes in job performance metrics and estimated profitability, including contract bonus or penalty provisions and final contract settlements, are recognized in the period such revisions appear probable. Known or anticipated losses on contracts are recognized in full when amounts are probable and estimable.

Drilling revenue is recognized upon receipt of a signed and dated field billing ticket from the customer. Customers are charged contractually agreed amounts for oilfield rental equipment damaged or lost-in-hole (“LIH”). LIH proceeds are recognized as revenue and the associated carrying value is charged to cost of sales. LIH revenue totaled $3.8 million, $4.7 million, and $5.9 million for the years ended December 31, 2015, 2014, and 2013, respectively.

The Company generally is not contractually obligated to accept returns, except for defective products. Typically products determined to be defective are replaced or the customer is issued a credit memo. Based on historical return rates, no provision is made for returns at the time of sale. All costs associated with product returns are expensed as incurred.

Foreign Currency Translation

Financial statements of foreign subsidiaries are prepared using the currency of the primary economic environment of the foreign subsidiaries as the functional currency. Assets and liabilities of foreign subsidiaries are translated into U.S. dollars at exchange rates in effect as of the end of identified reporting periods. Revenue and expense transactions are translated using the average monthly exchange rate for the reporting period. Resultant translation adjustments are recognized as other comprehensive income (loss) within stockholders’ equity.

Comprehensive Income (Loss)

Comprehensive income (loss) encompasses all changes in stockholders’ equity, except those arising from investments from and distributions to stockholders. The Company’s comprehensive income (loss) includes net income (loss) and foreign currency translation adjustments.

Research and Development Costs

Expenditures for research activities relating to product development and improvement are charged to expense as incurred.

Income Taxes

The Company has two U.S. tax filing groups which file separate U.S. Federal tax returns. Taxable income of one return cannot be offset by tax attributes, including net operating losses, of the other return. During the year ended December 31, 2015, the Company restructured its legal entities such that there will be only one U.S. tax filing group filing a single U.S. consolidated federal income tax return beginning in 2016.

The Company uses the liability method in accounting for income taxes. Deferred tax assets and liabilities are recognized for temporary differences between financial statement carrying amounts and the tax bases of assets and liabilities and are measured using the tax rates expected to be in effect when the differences reverse. Deferred tax assets and liabilities are recognized related to the anticipated future tax effects of temporary differences between the financial statement basis and the tax basis of the Company's assets and liabilities using statutory tax rates at the applicable year end. Deferred tax assets are also recognized for operating loss and tax credit carry forwards. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the results of operations in the period that includes the enactment date. A valuation allowance is used to reduce deferred tax assets when uncertainty exists regarding their realization.

A valuation allowance is recorded to reduce previously recorded tax assets when it becomes more likely than not that such assets will not be realized. The Company evaluates, at least annually, net operating loss carry forwards and other net deferred tax assets and considers all available evidence, both positive and negative, to determine whether a valuation allowance is necessary relative to net operating loss carry forwards and other net deferred tax assets. In making this determination, the Company considers cumulative losses in recent years as significant negative evidence. The Company considers recent years to mean the current year plus the two preceding years. The Company considers the recent cumulative income or loss position of its filings groups as objectively verifiable evidence for the projection of future income, which consists primarily of determining the average of the pre-tax income of the current and prior two years after adjusting for certain items not indicative of future performance. Based on this analysis, the Company determines whether a valuation allowance is necessary.

U.S. Federal income taxes are not provided on unremitted earnings of subsidiaries operating outside the U.S. because it is the Company's intention to permanently reinvest undistributed earnings in the subsidiary. These earnings would become subject to income tax if they were remitted as dividends or loaned to a U.S. affiliate. Determination of the amount of unrecognized deferred U.S. income tax liability on these unremitted earnings is not practicable.

The Company has performed an evaluation and concluded that there are no significant uncertain tax positions requiring recognition in the Company's financial statements.

The Company's policy is to record interest and penalties related to income tax matters as income tax expense.

Earnings (Loss) Per Share

Basic earnings (loss) per common share is calculated by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share is calculated by dividing net income (loss) attributable to common stockholders, adjusted for the effect of assumed conversions of convertible notes and preferred stock, by the weighted average number of common shares outstanding, including potentially dilutive common share equivalents, if the effect is dilutive. Potentially dilutive common shares equivalents consist of incremental shares of common stock issuable upon exercise of stock options and warrants, settlement of restricted stock units, and conversion of convertible notes and convertible preferred stock.

Debt Issuance Costs

Costs related to debt issuance are capitalized and amortized as interest expense over the term of the related debt using the straight-line method, which approximates the effective interest method. Upon the repayment of debt, the Company accelerates the recognition of an appropriate amount of the costs as interest expense.

Capitalization of Interest

Interest costs are capitalized for qualifying in-process software development projects. Capitalization of interest commences when activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred. Interest costs are capitalized until the assets are ready for their intended use. Capitalized interest is added to the cost of the underlying assets and amortized over the estimated useful lives of the assets.

Stock-Based Compensation

Stock-based compensation expense for share-based payments, related to stock option and restricted stock awards, is recognized based on their grant-date fair values. The Company recognizes compensation expense, net of estimated forfeitures, on a straight-line basis over the requisite service period of the award. Estimated forfeitures are based on historical experience.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and reported amounts of revenue and expenses. Actual results could differ from these estimates.

Significant items subject to estimates and assumptions include application of the percentage-of-completion method of revenue recognition, the carrying amount and useful lives of property and equipment and intangible assets, impairment assessments, share-based compensation expense, and valuation allowances for accounts receivable, inventories, and deferred tax assets.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation. The reclassifications did not impact net income.

New Accounting Pronouncements

(a) Application of New Accounting Standards

Effective January 1, 2015, the Company adopted the accounting guidance in Accounting Standards Update (“ASU”) No. 2014-08, “Presentation of Financial Statements and Property, Plant, and Equipment - Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity,” which amends the definition of a discontinued operation by raising the threshold for a disposal to qualify as discontinued operations. The ASU will also require entities to provide additional disclosures about discontinued operations as well as disposal transactions that do not meet the discontinued operations criteria. Implementation of this

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standard did not have a material effect on the consolidated financial statements.
Effective January 1, 2015, the Company adopted the accounting guidance in ASU No. 2014-12, "Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period." The ASU requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Implementation of this standard did not have a material effect on the consolidated financial statements or the Company's current awards under its existing stock-based compensation plans.
(b) New Accounting Requirements and Disclosures
In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, "Revenue from Contracts with Customers." The ASU will supersede most of the existing revenue recognition requirements in U.S. GAAP and will require entities to recognize revenue at an amount that reflects the consideration to which the Company expects to be entitled in exchange for transferring goods or services to a customer. The new standard also requires significantly expanded disclosures regarding the qualitative and quantitative information of an entity's nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. In August 2015, the FASB issued ASU No. 2015-14, which deferred the effective date by one year to annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted, but not before the original effective date of reporting periods beginning after December 15, 2016. The Company is currently evaluating the impact the pronouncement will have on the consolidated financial statements and related disclosures.
In January 2015, the FASB issued ASU No. 2015-01, "Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items." This ASU eliminates from U.S. GAAP the concept of extraordinary items and the need for an entity to separately classify, present, and disclose extraordinary events and transactions, while retaining certain presentation and disclosure guidance for items that are unusual in nature or occur infrequently. The pronouncement is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period and may be applied retrospectively, with early application permitted. The Company is currently evaluating the impact the pronouncement will have on the consolidated financial statements and related disclosures.
In February 2015, the FASB issued ASU No. 2015-02, "Amendments to the Consolidation Analysis." The amendment eliminates the deferral of certain consolidation standards for

entities considered to be investment companies and modifies the consolidation analysis performed on certain types of legal entities. The pronouncement is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period and may be applied retrospectively, with early application permitted. The Company is currently evaluating the impact the pronouncement will have on the consolidated financial statements and related disclosures.
In April 2015, the FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs." The accounting guidance requires that debt issuance costs related to a recognized debt liability be reported on the Consolidated Statements of Financial Condition as a direct deduction from the carrying amount of that debt liability. The pronouncement is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period with early application permitted for financial statements that have not been previously issued. In August 2015, the FASB issued ASU No. 2015-15, which provides additional guidance related to the presentation or subsequent measurement of debt issuance costs related to line-of-credit arrangements. An entity may present debt issuance costs as an asset and subsequently amortize the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings. The Company is currently evaluating the impact these pronouncements will have on the consolidated financial statements and related disclosures.
In July 2015, the FASB issued ASU No. 2015-11, "Simplifying the Measurement of Inventory." This standard requires management to measure inventory at the lower of cost or net realizable value. Net realizable value is the estimated

selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The pronouncement is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period and should be applied retrospectively, with early application permitted. The Company is currently evaluating the impact the pronouncement will have on the consolidated financial statements and related disclosures.

In September 2015, the FASB issued ASU 2015-16, “Simplifying the Accounting for Measurement-Period Adjustments.” This standard replaces the requirement that an acquirer in a business combination account for measurement period adjustments retrospectively with a requirement that an acquirer recognize adjustments to the provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The acquirer is required to record, in the same period’s financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. The

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pronouncement is effective for annual reporting periods beginning after December 15, 2015, including interim periods within that reporting period. The guidance is to be applied prospectively to adjustments to provisional amounts that occur after the effective date of the guidance. The Company is currently evaluating the impact the pronouncement will have on the consolidated financial statements and related disclosures.

In November 2015, the FASB issued ASU 2015-17, "Balance Sheet Classification of Deferred Taxes." This standard eliminates the current requirement for organizations to present deferred tax assets and liabilities as current and noncurrent in a classified balance sheet. Instead, organizations will be required to classify all deferred tax assets and liabilities as noncurrent. The pronouncement is effective for annual reporting periods beginning after December 15, 2016, and interim periods within those annual periods. The Company is currently evaluating the impact the pronouncement will have on the consolidated financial statements and related disclosures.

Note 3 — Impairment of Inventory and Rental Equipment

During the three months ended June 30, 2015, as a result of decreased rig activity and its impact on management's expectations for future market activity, the Company refocused the Drilling Technologies segment to businesses and markets that have the best opportunity for profitable growth in the future. In addition, the Company has shifted the focus of the Production Technologies segment to oil production markets and away from coal bed methane markets. As a result of these changes in focus and projected declines in asset utilization, the Company recorded a pre-tax impairment charge during the three months ended June 30, 2015, as follows (in thousands):

Drilling Technologies:	
Inventories	$17,241
Rental equipment	2,327
Production Technologies:	
Inventories	804
Total impairment	$20,372

Note 4 — Acquisitions

On January 27, 2015, the Company acquired 100% of the assets of International Artificial Lift, LLC ("IAL") for $1.3 million in cash consideration and 60,024 shares of the Company's common stock. IAL, a development-stage company at acquisition, specializes in the design, manufacturing and service of next-generation hydraulic pumping units that serve to increase and maximize production for oil and natural gas wells.

On April 1, 2014, the Company acquired 100% of the membership interests in SiteLark, LLC ("SiteLark") for $0.4 million in cash consideration and 5,327 shares of the Company's common stock. SiteLark provides reservoir engineering and modeling services for a variety of hydrocarbon applications. Its services include proprietary software that assists engineers with reservoir simulation, reservoir engineering and waterflood optimization.

On January 1, 2014, the Company acquired 100% of the membership interests in Eclipse IOR Services, LLC ("EOGA"), a leading Enhanced Oil Recovery ("EOR") design and injection firm, for $5.3 million in cash consideration, net of cash received, and 94,354 shares of the Company's common stock. EOGA's enhanced oil recovery processes and its use of polymers to improve the performance of EOR projects has been combined with the Company's existing EOR products and services.

On May 10, 2013, the Company acquired Florida Chemical Company, Inc. ("Florida Chemical"), one of the world's largest processors of citrus oils and a pioneer in solvent, chemistry synthesis, and flavor and fragrance applications from citrus oils. Florida Chemical has been an innovator in creating high performance, bio-based products for a

variety of industries, including applications in the oil and gas industry. The acquisition brings a portfolio of high performance renewable and sustainable chemistries that perform well in the oil and gas industry as well as non-energy related markets. This expanded the Company's business into consumer and industrial chemistry technologies which provide products for the flavor and fragrance industry and the specialty chemical industry. These technologies are used by beverage and food companies, fragrance companies, and companies providing household and industrial cleaning products.
The Company acquired 100% of the outstanding shares of Florida Chemical's common stock. The purchase consideration transferred was as follows (in thousands):

Cash	$49,500
Common stock (3,284,180 shares)	52,711
Repayment of debt	4,227
Total purchase price	$106,438

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The allocation of the purchase consideration was based upon the estimated fair value of the tangible and identifiable intangible assets acquired and liabilities assumed in the acquisition. The allocation was made to major categories of assets and liabilities based on management's best estimates,

supported by independent third-party analyses. The excess of the purchase price over the estimated fair value of tangible and identifiable intangible assets acquired, and liabilities assumed was allocated to goodwill.

The allocation of purchase consideration is as follows (in thousands):

Cash	$331
Net working capital, net of cash	15,574
Property and equipment:	
Personal property	13,400
Real property	6,750
Other assets	205
Other intangible assets:	
Customer relationships	29,270
Trade names	12,670
Proprietary technology	14,080
Goodwill	39,328
Deferred tax impact of valuation adjustment	(25,170)
Total purchase price allocation	$106,438

The following unaudited pro forma financial information presents results of operations as if the acquisition had occurred as of January 1, 2013. This financial information does not purport to represent the results of operations which would actually have been obtained had the acquisition been completed as of January 1, 2013, or the results of operations

that may be obtained in the future. Also, this financial information does not reflect the cost of any integration activities or benefits from the merger and synergies that may be derived from any integration activities, both of which may have a material effect on the consolidated results of operations in the periods following the completion of the merger.

Pro forma financial information is as follows (in thousands, except per share data):

	Year ended December 31, 2013
Revenue	$395,407
Net income	38,271
Earnings per common share:	
Basic	$0.73
Diluted	$0.70

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Pro forma adjustments include, but are not limited to, adjustments for amortization expense for acquired finite lived intangible assets, depreciation expense for the fair value of acquired property and equipment, interest expense for increased long-term debt and revolving credit facility borrowings required for the acquisition, and income tax expense on Florida Chemical income before income taxes. In addition, pro forma adjustments eliminate historical amortization, depreciation, and interest expense from the pro forma results of operations.
The acquisition was financed through increased long-term debt of $25 million, additional borrowings on the Company's revolving credit facility of $28.7 million and the issuance of 3.3 million shares of the Company's common stock. Results of Florida Chemical's operations are included in the Company's consolidated financial statements from the date of acquisition. The Company's consolidated statements of operations for the year ended December 31, 2013 include

$50.9 million of revenue and $10.0 million of income from operations related to the operations of Florida Chemical. The Company incurred $1.4 million of acquisition costs in connection with the transaction which have been expensed as incurred and included in selling, general and administrative expenses.
During the quarter ended September 30, 2014, the Company identified and recorded a final adjustment related to the acquisition of Florida Chemical. Current deferred tax assets were increased by $1.2 million with a corresponding decrease to goodwill within the consumer and industrial chemistry technologies reporting unit. This final adjustment was not significant relative to the total consideration paid for Florida Chemical and, therefore, the final adjustment has not been retrospectively applied to the Company's balance sheet as of December 31, 2013. This adjustment, if recorded in 2013, would have had no impact on the 2013 consolidated statements of operations and cash flows.

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Note 5 — Supplemental Cash Flow Information

Supplemental cash flow information is as follows (in thousands):

	Year ended December 31,		
	2015	2014	2013
Supplemental non-cash investing and financing activities:			
Value of common stock issued in acquisitions	$1,014	$2,043	$52,711
Final Florida Chemical acquisition adjustment	—	1,162	—
Value of common stock issued in payment of accrued liability	—	600	—
Equipment acquired through capital leases	—	—	754
Exercise of stock options by common stock surrender	1,332	1,198	3,907
Supplemental cash payment information:			
Interest paid	$1,398	$1,285	$1,859
Income taxes paid, net of refunds	1,547	22,389	17,783

Note 6 — Revenue

The Company differentiates revenue and cost of revenue based on whether the source of revenue is attributable to products, rentals or services. Revenue and cost of revenue by source are as follows (in thousands):

	Year ended December 31,		
	2015	2014	2013
Revenue:			
Products	$283,493	$354,356	$282,639
Rentals	35,242	65,549	62,042
Services	15,624	29,252	26,384
	$334,359	$449,157	$371,065
Cost of Revenue:			
Products	$187,511	$214,417	$180,800
Rentals	16,052	31,285	24,987
Services	8,668	12,385	9,916
Depreciation	7,018	8,111	7,835
	$219,249	$266,198	$223,538

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Note 7 — Inventories
Inventories are as follows (in thousands):

	December 31, 2015	2014
Raw materials	$44,997	$50,195
Work-in-process	3,069	3,129
Finished goods	37,426	32,634
Inventories, net	$85,492	$85,958

Changes in the reserve for excess and obsolete inventory are as follows (in thousands):

	Year ended December 31, 2015	2014	2013
Balance, beginning of year	$—	$2,744	$2,752
Charged to costs and expenses	—	358	1,330
Deductions	—	(3,102)	(1,338)
Balance, end of the year	$—	$—	$2,744

During the year ended December 31, 2015, the Company recorded an $18.6 million write-down of inventory to recognize the impairment from refocusing the Drilling Technologies and Production Technologies segments and for all items identified as excess and obsolete inventory. At December 31, 2014, the Company recorded a $2.0 million write-down of inventory to recognize impairment of all items identified and included in the reserve for excess and obsolete inventory.

Note 8 — Property and Equipment
Property and equipment are as follows (in thousands):

	December 31 2015	2014
Land	$7,145	$6,780
Buildings and leasehold improvements	34,351	33,765
Machinery, equipment and rental tools	85,611	80,731
Equipment in progress	12,304	7,299
Furniture and fixtures	2,749	2,528
Transportation equipment	7,462	6,566
Computer equipment and software	11,382	7,605
Property and equipment	161,004	145,274
Less accumulated depreciation	(69,091)	(59,163)
Property and equipment, net	$91,913	$86,111

Depreciation expense, including expense recorded in cost of revenue, totaled $13.2 million, $13.1 million, and $11.2 million for the years ended December 31, 2015, 2014, and 2013, respectively.
During the year ended December 31, 2015, an impairment of $2.3 million was recognized related to rental equipment. No impairments were recognized in 2014 and 2013 related to property and equipment.

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Note 9 — Goodwill
The Company has five reporting units, Energy Chemistry Technologies, Consumer and Industrial Chemistry Technologies, Downhole Tools, Teledrift, and Production Technologies, of which four had an existing goodwill balance at December 31, 2015. For segment reporting purposes, Downhole Tools and the Teledrift reporting units are included within the Drilling Technologies segment.
During May 2013, as a result of the Florida Chemical acquisition, the Company recognized $39.3 million of goodwill. During the fair value assessment process, the Company identified two separate reporting units, one of which was consolidated within the Energy Chemistry Technologies segment and the other was identified as the Consumer and Industrial Chemistry Technologies reporting unit and segment. The Company recognized $18.7 million of additional goodwill within the Energy Chemistry Technologies reporting unit and $20.6 million of goodwill within the Consumer and Industrial Chemistry Technologies reporting unit. During the year ended December 31, 2014, the Company recorded a final adjustment related to the acquisition of Florida Chemical that reduced goodwill by $1.2 million (see Note 4). The net addition to goodwill will not be deductible for income tax purposes.
Goodwill is tested for impairment annually in the fourth quarter, or more frequently if circumstances indicate a potential impairment. During the second quarter of 2015, the drilling rig count and revenue of the Drilling Technologies segment continued to decline. An impairment of inventory and rental equipment was recorded (see Note 3). The drop off in business resulting from declines in oil prices and the active drilling rig count was an event or circumstance that caused the Company to test its recorded goodwill within the Teledrift reporting unit within the Drilling Technologies segment (deterioration in the operating environment and overall

financial performance of the reporting unit). No impairment of goodwill was recorded as a result of this testing.
During annual goodwill impairment testing during the year ended December 31, 2015, the Company assessed the qualitative factors and concluded it was not more likely than not that there was an impairment of goodwill for the Consumer and Industrial Chemistry Technologies reporting unit. However, the Company was not able to conclude that it was not more likely than not that fair value of the Energy Chemistry Technologies, Teledrift, and Production Technologies reporting units exceeded the carrying value of the respective reporting units. Therefore, the Company performed the Step 1 impairment test for each of these reporting units. The results of the Step 1 test indicated that the fair values of the Energy Chemistry Technologies and Production Technologies reporting units exceeded the carry amounts of their respective reporting units. Therefore, no further testing was required for these two reporting units. The Step 1 impairment test for the Teledrift reporting unit indicated that the fair value of the reporting unit was less than its carrying value; therefore, the Company performed the Step 2 impairment test. The results of the Step 2 impairment test indicated that the implied fair value of goodwill exceeded the carrying value of the goodwill for the Teledrift reporting unit. As a result of the Company’s annual testing of goodwill for all reporting units, the Company did not record any loss due to impairment of goodwill in 2015.
During annual goodwill impairment testing during the years ended December 31, 2014 and 2013, the Company first assessed qualitative factors to determine whether it was necessary to perform the two-step goodwill impairment test that the Company has historically used. The Company concluded that it was not more likely than not that goodwill was impaired as of the fourth quarter of 2014 and 2013, and therefore, further testing was not required.

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Changes in the carrying value of goodwill for each reporting unit are as follows (in thousands):

	Energy Chemistry Technologies	Consumer and Industrial Chemistry Technologies	Downhole Tools	Teledrift	Production Technologies	Total
Balance at December 31, 2013:						
Goodwill	$30,296	$20,642	$43,009	$46,396	$5,861	$146,204
Accumulated impairment losses	—	—	(43,009)	(31,063)	(5,861)	(79,933)
Goodwill balance, net	30,296	20,642	—	15,333	—	66,271
Activity during the year 2014:						
Goodwill impairment recognized	—	—	—	—	—	—
Acquisition goodwill recognized	6,022	(1,162)	—	—	—	4,860
Balance at December 31, 2014:						
Goodwill	36,318	19,480	43,009	46,396	5,861	151,064
Accumulated impairment losses	—	—	(43,009)	(31,063)	(5,861)	(79,933)
Goodwill balance, net	36,318	19,480	—	15,333	—	71,131
Activity during the year 2015:						
Goodwill impairment recognized	—	—	—	—	—	—
Acquisition goodwill recognized	—	—	—	—	1,689	1,689
Balance at December 31, 2015:						
Goodwill	36,318	19,480	43,009	46,396	7,550	152,753
Accumulated impairment losses	—	—	(43,009)	(31,063)	(5,861)	(79,933)
Goodwill balance, net	$36,318	$19,480	$—	$15,333	$1,689	$72,820

Note 10 — Other Intangible Assets

Other intangible assets are as follows (in thousands):

	December 31, 2015		2014	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization
Finite lived intangible assets:				
Patents and technology	$20,960	$5,809	$20,061	$4,569
Customer lists	52,607	14,640	52,607	11,829
Trademarks and brand names	7,191	3,360	7,191	2,706
Total finite lived intangible assets acquired	80,758	23,809	79,859	19,104
Deferred financing costs	1,665	858	1,655	512
Total amortizable intangible assets	82,423	$24,667	81,514	$19,616
Indefinite lived intangible assets:				
Trademarks and brand names	11,630		11,630	
Total other intangible assets	$94,053		$93,144	
Carrying value:				
Other intangible assets, net	$69,386		$73,528	

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Intangible assets acquired are amortized on a straight-line basis over two to 20 years. Amortization of intangible assets acquired totaled \$4.8 million, \$4.8 million, and \$3.9 million for the years end ended December 31, 2015, 2014, and 2013, respectively.

Amortization of deferred financing costs totaled \$0.3 million, \$0.3 million, and \$0.2 million for the years ended December 31, 2015, 2014, and 2013, respectively.

Estimated future amortization expense for other intangible assets, including deferred financing costs, at December 31, 2015 is as follows (in thousands):

Year ending December 31,	
2016	$4,925
2017	4,770
2018	4,499
2019	4,297
2020	4,277
Thereafter	34,988
Other intangible assets, net	$57,756

During the years ended December 31, 2015, 2014 and 2013, no impairments were recognized related to other intangible assets.

Note 11 — Long-Term Debt and Credit Facility

Long-term debt is as follows (in thousands):

	December 31, 2015	2014
Long-term debt:		
Borrowings under revolving credit facility	$25,148	$8,500
Term loan	25,398	35,541
Total long-term debt	50,546	44,041
Less current portion of long-term debt	(32,291)	(18,643)
Long-term debt, less current portion	$18,255	$25,398

Credit Facility

On May 10, 2013, the Company and certain of its subsidiaries (the “Borrowers”) entered into an Amended and Restated Revolving Credit, Term Loan and Security Agreement (the “Credit Facility”) with PNC Bank, National Association (“PNC Bank”). The Company may borrow under the Credit Facility for working capital, permitted acquisitions, capital expenditures and other corporate purposes. Under terms of the Credit Facility, as amended, the Company (a) may borrow up to \$75 million under a revolving credit facility and (b) has borrowed \$50 million under a term loan.

The Credit Facility is secured by substantially all of the Company’s domestic real and personal property, including accounts receivable, inventory, land, buildings, equipment and other intangible assets. The Credit Facility contains customary representations, warranties, and both affirmative and negative covenants. The Credit Facility includes a financial covenant to maintain a fixed charge coverage ratio of 1.10 to 1.00. The numerator of the ratio includes (a) Adjusted EBITDA (consolidated earnings before interest, taxes, depreciation and amortization adjusted to exclude stock compensation expense and impairment expense of up to \$23 million in 2015) minus(b) unfunded capital expenditures (excluding up to \$7.5 million in 2015 and \$5.0 million in 2016 associated with the construction of the Company’s Global Research and Innovation facility) and (c) cash taxes paid.

The Credit Facility also includes a financial covenant to maintain a ratio of funded debt to Adjusted EBITDA of not greater than 4.0 to 1.0, and an annual limit on capital expenditures of approximately $36 million. The Credit Facility restricts the payment of cash dividends on common stock. In the event of default, PNC Bank

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may accelerate the maturity date of any outstanding amounts borrowed under the Credit Facility.
The Credit Facility includes a provision that 25% of EBITDA minus cash paid for taxes, dividends, debt payments, and unfunded capital expenditures, not to exceed $3.0 million for any year, be paid within 60 days of the fiscal year end. For the year ended December 31, 2015, there was no additional payment required based on this provision.
Each of the Company's domestic subsidiaries is fully obligated for Credit Facility indebtedness as a borrower or as a guarantor.
(a) Revolving Credit Facility
Under the revolving credit facility, the Company may borrow up to $75 million through May 10, 2018. This includes a sublimit of $10 million that may be used for letters of credit. The revolving credit facility is secured by substantially all the Company's domestic accounts receivable and inventory.
At December 31, 2015, eligible accounts receivable and inventory securing the revolving credit facility provided total borrowing capacity of $62.9 million under the revolving credit facility. Available borrowing capacity, net of outstanding borrowings, was $37.8 million at December 31, 2015.
The interest rate on advances under the revolving credit facility varies based on the level of borrowing under the Credit Facility. Rates range (a) between PNC Bank's base lending rate plus 0.5% to 1.0% or (b) between the London Interbank Offered Rate (LIBOR) plus 1.5% to 2.0%. PNC Bank's base lending rate was 3.50% at December 31, 2015.
The Company is required to pay a monthly facility fee of 0.25% per annum on any unused amount under the commitment based on daily averages. At December 31, 2015, $25.1 million was outstanding under the revolving credit facility, with $4.1 million borrowed as base rate loans at an interest rate of 4.00% and $21.0 million borrowed as LIBOR loans at an interest rate of 1.75%.
Borrowing under the revolving credit facility is classified as current debt as a result of the required lockbox arrangement and the subjective acceleration clause.
(b) Term Loan
The Company increased borrowing to $50 million under the term loan on May 10, 2013. Monthly principal payments of $0.6 million are required. The unpaid balance of the term loan is due on May 10, 2018. Prepayments are permitted, and may be required in certain circumstances. Amounts repaid under the term loan may not be reborrowed. The term loan is secured by substantially all of the Company's domestic land, buildings, equipment, and other intangible assets.
The interest rate on the term loan varies based on the level of borrowing under the Credit Facility. Rates range (a) between PNC Bank's base lending rate plus 1.25% to 1.75% or (b) between LIBOR plus 2.25% to 2.75%. At December 31, 2015,

$25.4 million was outstanding under the term loan, with $0.4 million borrowed as base rate loans at an interest rate of 4.75% and $25.0 million borrowed as LIBOR loans at an interest rate of 2.50%.
Repaid Convertible Notes
On February 15, 2013, the Company repurchased the remaining $5.2 million of outstanding Convertible Senior Unsecured Notes ("2008 Notes") for cash equal to the original principal amount, plus accrued and unpaid interest. These 2008 Notes were either tendered by the holder pursuant to the Company's tender offer or were redeemed by the Company pursuant to provisions of the indenture for the 2008 Notes. Following this repurchase, the Company no longer has any outstanding convertible senior notes.
The convertible notes were guaranteed by substantially all of the Company's wholly owned subsidiaries. Flotek Industries, Inc., the parent company, is a holding company with no independent assets or operations. The guarantees provided by the Company's subsidiaries were full and unconditional, and joint and several. Any subsidiaries of the Company that were not guarantors were deemed to be "minor" subsidiaries in accordance with SEC Regulation S-X, Rule 3-10, "Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered."
Share Lending Agreement
Concurrent with the offering of the 2008 Notes, the Company entered into a share lending agreement (the "Share Lending Agreement") with the underwriter (the "Borrower"). The Company loaned 3.8 million shares of its common stock (the "Borrowed Shares") to the Borrower for a period commencing February 11, 2008 and ending on the date the

2008 Notes were paid. The Borrower was permitted to use the Borrowed Shares only for the purpose of directly or indirectly facilitating the sale of the 2008 Notes and for the establishment of hedge positions by holders of the 2008 Notes. The Company did not require collateral to mitigate any inherent or associated risk of the Share Lending Agreement.

The Company did not receive any proceeds for the Borrowed Shares, but did receive a nominal loan fee of $0.0001 for each share loaned. The Borrower retained all proceeds from sales of Borrowed Shares pursuant to the Share Lending Agreement. Upon conversion or replacement of the 2008 Notes, the number of Borrowed Shares proportionate to the converted or repaid notes were to be returned to the Company. The Borrowed Shares were issued and outstanding for corporate law purposes. Accordingly, holders of Borrowed Shares possessed all of the rights of a holder of the Company’s outstanding shares, including the right to vote the shares on all matters submitted to a vote of stockholders and the right to receive any dividends or other distributions declared or paid on outstanding shares of common stock. Under the Share Lending Agreement, the Borrower agreed to pay to the Company, within one business day after a payment date, an

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amount equal to any cash dividends that the Company paid on the Borrowed Shares, and to pay or deliver to the Company, upon termination of the loan of Borrowed Shares, any other distribution, in liquidation or otherwise, that the Company made on the Borrowed Shares.
To the extent the Borrowed Shares loaned under the Share Lending Agreement were not sold or returned to the Company, the Borrower agreed to not vote any borrowed shares of which the Borrower was the owner of record. The Borrower also agreed, under the Share Lending Agreement, to not transfer or dispose of any borrowed shares unless such transfer or disposition was pursuant to a registration statement that was effective under the Securities Act of 1933, as amended. Investors that purchased shares from the Borrower, and all

subsequent transferees of such purchasers, were entitled to the same voting rights, with respect to owned shares, as any other holder of common stock.
Through December 31, 2012, the Borrower returned 1,360,442 shares of the Company's borrowed common stock. On January 22, 2013, the remaining 2,439,558 shares of the Company's common stock were returned to the Company and the Share Lending Agreement was terminated. No consideration was paid by the Company for the return of the Borrowed Shares.
Shares that had been loaned under the Share Lending Agreement were not considered outstanding for the purpose of computing and reporting earnings per common share.

Debt Maturities
Maturities of long-term debt at December 31, 2015 are as follows (in thousands):

Year ending December 31,	Revolving Credit Facility	Term Loan	Total
2016	$25,148	$7,143	$32,291
2017	—	7,143	7,143
2018	—	11,112	11,112
Total	$25,148	$25,398	$50,546

Note 12 — Fair Value Measurements
Fair value is defined as the amount that would be received for selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company categorizes financial assets and liabilities into the three levels of the fair value hierarchy. The hierarchy prioritizes the inputs to valuation techniques used to measure fair value and bases categorization within the hierarchy on the lowest level of input that is available and significant to the fair value measurement.

- Level 1 — Quoted prices in active markets for identical assets or liabilities;
- Level 2 — Observable inputs other than Level 1, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and
- Level 3 — Significant unobservable inputs that are supported by little or no market activity or that are based on the reporting entity's assumptions about the inputs.

Liabilities Measured at Fair Value on a Recurring Basis
At December 31, 2015 and 2014, no liabilities were required to be measured at fair value on a recurring basis. There were no transfers in or out of either Level 1, Level 2, or Level 3 fair value measurements during the years ended December 31, 2015, 2014, and 2013.
Assets Measured at Fair Value on a Nonrecurring Basis

The Company’s non-financial assets, including property and equipment, goodwill, and other intangible assets are measured at fair value on a non-recurring basis and are subject to fair value adjustment in certain circumstances. No impairment of any of these assets was recognized during the years ended December 31, 2015, 2014, and 2013.

Fair Value of Other Financial Instruments

The carrying amounts of certain financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, approximate fair value due to the short-term nature of these accounts. The Company had no cash equivalents at December 31, 2015 or 2014.

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The carrying value and estimated fair value of the Company’s long-term debt are as follows (in thousands):

	December 31,			
	2015		2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Borrowings under revolving credit facility	$25,148	$25,148	$8,500	$8,500
Term loan	25,398	25,398	35,541	35,541

The carrying value of borrowings under the revolving credit facility and the term loan approximate their fair value because the interest rate is variable.

Note 13 — Earnings (Loss) Per Share

Basic earnings (loss) per common share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per common share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding combined with dilutive common share equivalents outstanding, if the effect is dilutive.

Because a net loss was realized during the year ended December 31, 2015, potentially dilutive securities were excluded from the diluted earnings per share calculation, as inclusion would have an anti-dilutive effect on net loss per share. Securities convertible into shares of common stock that were not considered in calculating earnings (loss) per common share were 777,400 stock options and 386,049 restricted stock units.

In connection with the sale of the 2008 Notes, the Company entered into a Share Lending Agreement for 3.8 million shares of the Company’s common stock (see Note 11). Contractual undertakings of the Borrower had the effect of substantially

eliminating the economic dilution that otherwise would result from the issuance of the Borrowed Shares, and all shares outstanding under the Share Lending Agreement were contractually obligated to be returned to the Company. As a result, shares loaned under the Share Lending Agreement were not considered outstanding for the purpose of computing and reporting earnings per common share. The Share Lending Agreement was terminated on January 22, 2013 upon the return of all Borrowed Shares to the Company.

On February 15, 2013, the Company repurchased the remaining $5.2 million of outstanding 2008 Notes for cash. Following this repurchase, the Company no longer has any outstanding convertible senior notes. For the year ended December 31, 2013, the Company’s convertible notes were excluded from the calculation of diluted earnings per common share as inclusion was anti-dilutive. In addition, for the year ended December 31, 2013, approximately 0.1 million stock options with an exercise price in excess of the average market price of the Company’s common stock were excluded from the calculation of diluted earnings per common share.

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Basic and diluted earnings (loss) per common share are as follows (in thousands, except per share data):

	Year ended December 31,		
	2015	2014	2013
Net income (loss) attributable to common stockholders	$(13,462)	$53,603	$36,178
Weighted average common shares outstanding - Basic	54,459	54,511	51,346
Assumed conversions:			
Incremental common shares from warrants	—	121	1,355
Incremental common shares from stock options	—	880	1,133
Incremental common shares from restricted stock units	—	14	7
Weighted average common shares outstanding - Diluted	54,459	55,526	53,841
Basic earnings (loss) per common share	$(0.25)	$0.98	$0.70
Diluted earnings (loss) per common share	$(0.25)	$0.97	$0.67

Note 14 — Income Taxes

Components of the income tax (benefit) expense are as follows (in thousands):

	Year ended December 31,		
	2015	2014	2013
Current:			
Federal	$(3,529)	$21,468	$15,225
State	283	684	3,322
Foreign	3,520	1,627	1,432
Total current	274	23,779	19,979
Deferred:			
Federal	(7,756)	2,573	1,336
State	(173)	(1,071)	(543)
Foreign	1	—	—
Total deferred	(7,928)	1,502	793
Income tax (benefit) expense	$(7,654)	$25,281	$20,772

The components of income (loss) before income taxes are as follows (in thousands):

	Year ended December 31,		
	2015	2014	2013
United States	$(26,982)	$78,884	$56,950
Foreign	5,866	—	—
Income (loss) before taxes	$(21,116)	$78,884	$56,950

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A reconciliation of the U.S. federal statutory tax rate to the effective income tax rate is as follows:

	Year ended December 31,		
	2015	2014	2013
Federal statutory tax (benefit) expense rate	(35.0)%	35.0%	35.0%
State income taxes, net of federal benefit	0.8	2.3	2.8
Non-U.S. income taxed at different rates	(1.9)	—	—
Return to accrual adjustments	(2.5)	(0.9)	0.2
Change in valuation allowance	1.3	—	—
Domestic production activities deduction	—	(2.5)	(2.6)
Other	1.1	(1.9)	1.1
Effective income tax (benefit) expense rate	(36.2)%	32.0%	36.5%

Fluctuations in effective tax rates have historically been impacted by permanent tax differences with no associated income tax impact and changes in state apportionment factors, including the effect on state deferred tax assets and liabilities. Changes in the effective tax rate during 2015 also included the benefit of non-U.S. income taxed at lower rates, and the Company not qualifying for the domestic production activities deduction. The benefit of operating in foreign tax jurisdictions is primarily derived from operations in Canada.

Deferred income taxes reflect the tax effect of temporary differences between the carrying value of assets and liabilities for financial reporting purposes and the value reported for income tax purposes, at the enacted tax rates expected to be in effect when the differences reverse. The components of deferred tax assets and liabilities are as follows (in thousands):

	December 31,	
	2015	2014
Deferred tax assets:		
Net operating loss carryforwards	$15,210	$10,183
Allowance for doubtful accounts	432	369
Inventory valuation reserves	3,734	1,896
Equity compensation	4,250	4,146
Goodwill	6,869	8,963
Accrued compensation	73	75
Foreign tax credit carryforward	865	—
Other	67	1
Total gross deferred tax assets	31,500	25,633
Valuation allowance	(1,093)	(809)
Total deferred tax assets, net	30,407	24,824
Deferred tax liabilities:		
Property and equipment	(12,876)	(12,066)
Intangible assets	(18,249)	(18,786)
Convertible debt	(3,011)	(4,126)
Prepaid insurance and other	(216)	(225)
Total gross deferred tax liabilities	(34,352)	(35,203)
Net deferred tax (liabilities) assets	$(3,945)	$(10,379)

FLOTEK INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Deferred taxes are presented in the balance sheets as follows (in thousands):

	December 31, 2015	2014
Current deferred tax assets	$2,649	$2,696
Non-current deferred tax assets	17,229	12,907
Non-current deferred tax liabilities	(23,823)	(25,982)
Net deferred tax (liabilities) assets	$(3,945)	$(10,379)

During the year ended December 31, 2014, the Company recorded a final adjustment related to the acquisition of Florida Chemical that increased current deferred tax assets by $1.2 million (see Note 4).

As of December 31, 2015, the Company had U.S. net operating loss carryforwards of $39.7 million, expiring in various amounts in 2028 through 2035. The ability to utilize net operating losses and other tax attributes could be subject to a significant limitation if the Company were to undergo an "ownership change" for purposes of Section 382 of the Tax Code.

The Company's corporate organizational structure requires the filing of two separate consolidated U.S. Federal income tax returns. Taxable income of one group ("Group A") cannot be offset by tax attributes, including net operating losses of the other group ("Group B"). During the year ended December 31, 2015, the Company restructured its legal entities such that there will be only one U.S. tax filing group filing a single U.S. consolidated federal income tax return beginning in 2016.

The Company considers all available evidence, both positive and negative, to determine whether a valuation allowance is necessary for deferred tax assets. The Company considers cumulative losses in recent years as significant negative evidence. The Company considers recent years to mean the

current year plus the two preceding years. As of December 31, 2015, the Company maintains a valuation allowance of $1.1 million for deferred tax assets in certain state and foreign jurisdictions.

The Company has not calculated U.S. taxes on unremitted earnings of certain non-U.S. subsidiaries due to the Company's intent to reinvest the unremitted earnings of the non-U.S. subsidiaries. At December 31, 2015, the Company had approximately $5.9 million in unremitted earnings outside the U.S. which were not included for U.S. tax purposes. U.S. income tax liability would be incurred if these funds were remitted to the U.S. It is not practicable to estimate the amount of the deferred tax liability on such unremitted earnings.

The Company has performed an evaluation and concluded that there are no significant uncertain tax positions requiring recognition in the Company's financial statements. The evaluation was performed for the tax years which remain subject to examination by tax jurisdictions as of December 31, 2015 which are the years ended December 31, 2012 through December 31, 2015 for U.S. federal taxes and the years ended December 31, 2011 through December 31, 2015 for state tax jurisdictions.

At December 31, 2015, the Company has no unrecognized tax benefits.

Note 15 — Convertible Preferred Stock and Stock Warrants

In August 2009, the Company sold convertible preferred stock with detachable warrants to purchase shares of the Company's common stock. In February 2011, the Company exercised its contractual right to mandatorily convert all outstanding shares of convertible preferred stock into shares of common stock. Currently, the Company has no issued or outstanding shares of preferred stock.

During the years ended December 31, 2014 and 2013, warrants were exercised to purchase 1,277,250 and 267,000 shares, respectively, of the Company's common stock at $1.21 per share generating cash proceeds of $1.5 million and $0.3 million, respectively. The Company no longer has any outstanding warrants.

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FLOTEK INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 16 — Common Stock
The Company's Certificate of Incorporation, as amended November 9, 2009, authorizes the Company to issue up to 80 million shares of common stock, par value $0.0001 per share, and 100,000 shares of one or more series of preferred stock, par value $0.0001 per share.
A reconciliation of the changes in common shares issued is as follows:

	Year ended December 31,	
	2015	2014
Shares issued at the beginning of the year	54,633,726	58,265,911
Issued in acquisitions	60,024	99,681
Issued in payment of accrued liability	—	27,101
Issued upon exercise of warrants	—	1,277,250
Issued as restricted stock award grants	758,904	525,120
Issued upon exercise of stock options	767,560	311,954
Retirement of treasury shares	—	(5,873,291)
Shares issued at the end of the year	56,220,214	54,633,726

Stock-Based Incentive Plans
Stockholders approved long term incentive plans in 2014, 2010, 2007, 2005, and 2003 (the "2014 Plan," the "2010 Plan," the "2007 Plan," the "2005 Plan" and the "2003 Plan," respectively) under which the Company may grant equity awards to officers, key employees, and non-employee directors in the form of stock options, restricted stock, and certain other incentive awards. The maximum number of shares that may be issued under the 2014 Plan, 2010 Plan, and 2007 Plan are 2.7 million, 6.0 million, and 2.2 million, respectively. At December 31, 2015, the Company had a total of 1.1 million shares remaining to be granted under the 2014 Plan, 2010 Plan, and 2007 Plan. Shares may no longer be granted under the 2005 Plan and 2003 Plan.
Stock Options
All stock options are granted with an exercise price equal to the market value of the Company's common stock on the date of grant. Options expire no later than ten years from the date of grant and generally vest in four years or less. Proceeds received from stock option exercises are credited to common stock and additional paid-in capital, as appropriate. The Company uses historical data to estimate pre-vesting option forfeitures. Estimates are adjusted when actual forfeitures differ from the estimate. Stock-based compensation expense is recorded for all equity awards expected to vest.

The fair value of stock options at the date of grant is calculated using the Black-Scholes option pricing model. The risk free interest rate is based on the implied yield of U.S. Treasury zero-coupon securities that correspond to the expected life of the option. Volatility is estimated based on historical and implied volatilities of the Company's stock and of identified companies considered to be representative peers of the Company. The expected life of awards granted represents the period of time the options are expected to remain outstanding. The Company uses the "simplified" method which is permitted for companies that cannot reasonably estimate the expected life of options based on historical share option exercise experience. The Company does not expect to pay dividends on common stock. No options were granted to employees during 2015, 2014, and 2013.
The Black-Scholes option valuation model was developed to estimate the fair value of traded options that have no vesting restrictions and are fully-transferable. Because option valuation models require the use of subjective assumptions, changes in these assumptions can materially affect the fair value calculation. The Company's options are not characteristic of traded options; therefore, the option valuation models do not necessarily provide a reliable measure of the fair value of options.

FLOTEK INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Stock option activity for the year ended December 31, 2015 is as follows:

Options	Shares		Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding as of January 1, 2015	1,544,960		$ 4.81		
Exercised	(767,560	)	1.79		
Forfeited	—		—		
Expired	—		—		
Outstanding as of December 31, 2015	777,400		$ 7.80	1.31	$2,828,951
Vested or expected to vest at December 31, 2015	777,400		$ 7.80	1.31	$2,828,951
Options exercisable as of December 31, 2015	777,400		$ 7.80	1.31	$2,828,951

The total intrinsic value of stock options exercised during the years ended December 31, 2015, 2014, and 2013 was $8.4 million, $6.0 million, and $5.6 million, respectively. No stock options vested during the year ended December 31, 2015. The total fair value of stock options vesting during the year ended December 31, 2014 was less than $0.1 million and was $4.2 million for the year ended December 31, 2013.

At December 31, 2015, the Company had recognized all compensation expense related to stock options.

Restricted Stock

The Company grants employees either time-vesting or performance-based restricted shares in accordance with terms

specified in the Restricted Stock Agreements ("RSAs"). Time-vesting restricted shares vest after a stipulated period of time has elapsed subsequent to the date of grant, generally three to four years. Certain time-vested shares have also been issued with a portion of the shares granted vesting immediately. Performance-based restricted shares are issued with performance criteria defined over a designated performance period and vest only when, and if, the outlined performance criteria are met. During the year ended December 31, 2015, approximately 45% of the restricted shares granted were time-vesting and 55% were performance-based. Grantees of restricted shares retain voting rights for the granted shares.

Restricted stock share activity for the year ended December 31, 2015 is as follows:

Restricted Stock Shares	Shares		Weighted-Average Fair Value at Date of Grant
Non-vested at January 1, 2015	826,518		$18.78
Granted	406,650		16.15
RSAs converted from 2014 restricted stock units	352,254		24.66
Vested	(653,211	)	20.90
Forfeited	(32,995	)	22.72
Non-vested at December 31, 2015	899,216		$18.21

FLOTEK INDUSTRIES, INC.
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The weighted-average grant-date fair value of restricted stock granted during the years ended December 31, 2015, 2014, and 2013 was $16.15, $27.29, and $15.17 per share, respectively. The total fair value of restricted stock that vested during the years ended December 31, 2015, 2014, and 2013 was $13.7 million, $10.2 million, and $8.4 million, respectively.
At December 31, 2015, there was $11.6 million of unrecognized compensation expense related to non-vested restricted stock. The unrecognized compensation expense is

expected to be recognized over a weighted-average period of 1.6 years.
Restricted Stock Units
During the year ended December 31, 2015, the Company granted performance-based restricted stock units ("RSUs") that will be converted into 386,049 shares of common stock. These shares, which will be issued as RSAs, will vest in equal one-half tranches on December 31, 2016 and 2017.

Restricted stock unit share activity for the year ended December 31, 2015 is as follows:

Restricted Stock Unit Shares	Shares		Weighted-Average Fair Value at Date of Grant
RSU share equivalents at January 1, 2015	352,254		$24.66
2014 RSUs converted to RSAs in 2015	(352,254	)	24.66
Share equivalents earned in 2015	386,049		21.96
RSU share equivalents at December 31, 2015	386,049		$21.96

At December 31, 2015, there was $5.7 million of unrecognized compensation expense related to 2015 restricted stock units. The unrecognized compensation expense is expected to be recognized over a weighted-average period of 2.0 years.
Employee Stock Purchase Plan
The Company's Employee Stock Purchase Plan (ESPP) was approved by stockholders on May 18, 2012. The Company registered 500,000 shares of its common stock, currently held as treasury shares, for issuance under the ESPP. The purpose of the ESPP is to provide employees with an opportunity to purchase shares of the Company's common stock through accumulated payroll deductions. The ESPP allows participants to purchase common stock at a purchase price equal to 85% of the fair market value of the common stock on the last business day of a three-month offering period which coincides with calendar quarters. Payroll deductions may not exceed 10% of an employee's compensation and participants may not purchase more than 1,000 shares in any one offering period. The fair value of the discount associated with shares purchased under the plan is recognized as share-based compensation expense and was $0.2 million, $0.2 million, and $0.1 million during the years ended December 31, 2015, 2014, and 2013, respectively. The total fair value of the shares purchased under the plan during the years ended December 31, 2015, 2014, and 2013 was $1.0 million, $1.1 million, and $0.9 million, respectively. The employee payment associated with participation in the plan was satisfied through payroll deductions.

Share-Based Compensation Expense
Non-cash share-based compensation expense related to stock options, restricted stock, restricted stock unit grants, and stock purchased under the Company's ESPP was $14.7 million, $10.5 million, and $10.9 million during the years ended December 31, 2015, 2014, and 2013, respectively.
Treasury Stock
The Company accounts for treasury stock using the cost method and includes treasury stock as a component of

stockholders' equity. During the years ended December 31, 2015, 2014, and 2013, the Company purchased 473,304 shares, 243,005 shares, and 448,121 shares, respectively, of the Company's common stock at market value as payment of income tax withholding owed by employees upon the vesting of restricted shares and the exercise of stock options. Shares issued as restricted stock awards to employees that were forfeited are accounted for as treasury stock. During the years ended December 31, 2015, 2014, and 2013, shares surrendered for the exercise of stock options were 106,810, 46,208, and 237,267, respectively. These surrendered shares are also accounted for as treasury stock. During the year ended December 31, 2013, JP Morgan Chase & Co. returned 2,439,558 shares of the Company's common stock that had been borrowed under the Share Lending Agreement. These shares were then included in treasury stock.

FLOTEK INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Retirement of Treasury Stock

On December 31, 2014, the Company retired 5,873,291 shares of its treasury stock with an aggregate cost of $32.6 million. The retirement was recorded as reductions of $32.6 million in treasury stock, $1,000 in common stock, and $32.6 million in additional paid-in capital.

All retired treasury shares were canceled and returned to the status of authorized but unissued shares. The retirement of treasury stock had no impact on the Company's total consolidated stockholders' equity.

Stock Repurchase Program

In November 2012, the Company's Board of Directors authorized the repurchase of up to $25 million of the Company's common stock. Repurchases may be made in the open market or through privately negotiated transactions.

During the year ended December 31, 2015, the Company repurchased 799,723 shares of its outstanding common stock on the open market at a cost of $9.7 million, inclusive of transaction costs, or an average price of $12.13 per share. During the year ended December 31, 2014, the Company repurchased 621,176 shares of its outstanding common stock on the open market at a cost of $10.4 million, inclusive of transaction costs, or an average price of $16.74 per share.

In June 2015, the Company's Board of Directors authorized the repurchase of up to an additional $50 million of the Company's common stock. Repurchases may be made in open market or through privately negotiated transactions. Through December 31, 2015, the Company has not repurchased any of its common stock under this authorization.

As of December 31, 2015, the Company has $54.9 million remaining under its share repurchase program.

Note 17 — Commitments and Contingencies

Class Action Litigation

In November 2015, four putative securities class action lawsuits were filed in the United States District Court for the Southern District of Texas against the Company and certain of its officers. The lawsuits claim in part that the Company made false and/or misleading statements, as well as failed to disclose material adverse facts about the Company's business, operations and prospects. The complaint seeks an award of damages in an unspecified amount on behalf of a putative class consisting of persons who purchased the Company's common stock between October 23, 2014 and November 9, 2015, inclusive.

In January 2016, three derivative lawsuits were filed, two in the District Court of Harris County, Texas and one in the United States District Court for the Southern District of Texas, on behalf of the Company against certain of its officers and its current directors. The lawsuits allege violations of law, breaches of fiduciary duty, and unjust enrichment against the defendants.

The Company believes that the class action lawsuits and the derivative lawsuits are without merit, and it intends to vigorously defend against all claims asserted. Discovery has not yet commenced. At this time, the Company is unable to reasonably estimate the outcome of this litigation.

In addition, the Company has received notice from the U.S. Securities and Exchange Commission that it has opened an inquiry related to similar issues to those raised in the above-described litigation.

Other Litigation

The Company is subject to routine litigation and other claims that arise in the normal course of business. Management is not

aware of any pending or threatened lawsuits or proceedings that are expected to have a material effect on the Company's financial position, results of operations, or liquidity.

Operating Lease Commitments

The Company has operating leases for office space, vehicles, and equipment. Future minimum lease payments under operating leases at December 31, 2015 are as follows (in thousands):

Year ending December 31,	Minimum Lease

	Payments
2016	$3,136
2017	2,746
2018	2,504
2019	2,233
2020	2,024
Thereafter	14,469
Total	$27,112

Rent expense under operating leases totaled $2.6 million, $2.2 million, and $1.7 million during the years ended December 31, 2015, 2014, and 2013, respectively.

401(k) Retirement Plan

The Company maintains a 401(k) retirement plan for the benefit of eligible employees in the U.S. All employees are eligible to participate in the plan upon employment. On January 1, 2015, the Company implemented a new matching program. The Company matches contributions at 100% of up to 2% of an employee’s compensation and, if greater, the Company matches contributions at 50% from 4% to 8% of an employee’s compensation.

FLOTEK INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

During the years ended December 31, 2015, 2014, and 2013, compensation expense included $1.0 million, $0.7 million and $0.6 million, respectively, related to the Company's 401(k) match.

Concentrations and Credit Risk

The majority of the Company's revenue is derived from the oil and gas industry. Customers include major oilfield services companies, major integrated oil and natural gas companies, independent oil and natural gas companies, pressure pumping service companies, and state-owned national oil companies. This concentration of customers in one industry increases credit and business risks.

The Company is subject to significant concentrations of credit risk within trade accounts receivable as the Company does not generally require collateral as support for trade receivables. In addition, the majority of the Company's cash is maintained at a major financial institution and balances often exceed insurable amounts.

Note 18 — Business Segment, Geographic and Major Customer Information

Segment Information

Operating segments are defined as components of an enterprise for which separate financial information is available that is regularly evaluated by chief operating decision-makers in deciding how to allocate resources and assess performance. The operations of the Company are categorized into four reportable segments: Energy Chemistry Technologies, Consumer and Industrial Chemistry Technologies, Drilling Technologies, and Production Technologies.

- Energy Chemistry Technologies designs, develops, manufactures, packages, and markets specialty chemistries used in oil and natural gas well drilling, cementing, completion, stimulation, and production. In addition, the Company's chemistries are used in specialized enhanced and improved oil recovery markets ("EOR" or "IOR"). Activities in this segment also include construction and management of automated material handling facilities and management of loading facilities and blending operations for oilfield services companies.
- Consumer and Industrial Chemistry Technologies designs, develops, and manufactures products that are sold to companies in the flavor and fragrance industry and the specialty chemical industry. These technologies are used by beverage and food companies, fragrance companies, and companies providing household and industrial cleaning products.
- Drilling Technologies rents, sells, inspects, manufactures, and markets downhole drilling equipment used in energy, mining, and industrial drilling activities.
- Production Technologies assembles and markets production-related equipment, including the Petrovalve® product line of rod pump components, hydraulic pumping units, electric submersible pumps, gas separators, valves, and services that support natural gas and oil production activities.

The Company evaluates performance based upon a variety of criteria. The primary financial measure is segment operating income. Various functions, including certain sales and marketing activities and general and administrative activities, are provided centrally by the corporate office. Costs associated with corporate office functions, other corporate income and expense items, and income taxes are not allocated to reportable segments.

FLOTEK INDUSTRIES, INC.
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Summarized financial information of the reportable segments is as follows (in thousands):

As of and for the year ended December 31,	Energy Chemistry Technologies	Consumer and Industrial Chemistry Technologies	Drilling Technologies	Production Technologies	Corporate and Other	Total
2015						
Net revenue from external customers	$ 213,593	$ 56,374	$ 52,112	$ 12,280	$—	$334,359
Gross margin	81,936	14,371	16,702	2,101	—	115,110
Income (loss) from operations	43,902	8,742	(27,340)	(4,111)	(40,366)	(19,173)
Depreciation and amortization	4,791	2,202	8,539	750	1,742	18,024
Total assets	153,447	93,038	108,354	27,979	20,272	403,090
Capital expenditures	12,803	568	2,865	1,212	3,020	20,468
2014						
Net revenue from external customers	$ 268,761	$ 51,091	$ 113,302	$ 16,003	$—	$449,157
Gross margin	117,867	12,897	45,651	6,544	—	182,959
Income (loss) from operations	84,846	6,558	19,022	3,246	(32,784)	80,888
Depreciation and amortization	4,401	2,138	9,808	327	1,174	17,848
Total assets	156,596	87,412	147,584	21,843	9,841	423,276
Capital expenditures	6,983	115	9,626	942	2,241	19,907
2013						
Net revenue from external customers	$ 200,932	$ 42,927	$ 112,406	$ 14,800	$—	$371,065
Gross margin	88,536	10,659	43,156	5,176	—	147,527
Income (loss) from operations	65,396	6,260	18,306	3,060	(34,296)	58,726
Depreciation and amortization	3,160	1,126	9,632	250	941	15,109
Total assets	127,119	86,640	135,738	16,647	9,437	375,581
Capital expenditures	5,225	183	6,326	1,749	1,524	15,007

Geographic Information

Revenue by country is based on the location where services are provided and products are used. No individual country other than the United States ("U.S.") accounted for more than 10% of revenue. Revenue by geographic location is as follows (in thousands):

	Year ended December 31,		
	2015	2014	2013
U.S.	$273,624	$370,087	$319,649
Other countries	60,735	79,070	51,416
Total	$334,359	$449,157	$371,065

Long-lived assets held in countries other than the U.S. are not considered material to the consolidated financial statements.

FLOTEK INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Major Customers

Revenue from major customers, as a percentage of consolidated revenue, is as follows:

	Year ended December 31,		
	2015	2014	2013
Customer A	13.9%	*	*
Customer B	12.0%	16.1%	16.2%

* This customer did not account for more than 10% of revenue.

Approximately 95% of the revenue from major customers noted above was from the Energy Chemistry Technologies segment.

Note 19 — Quarterly Financial Data (Unaudited)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
	(in thousands, except per share data)				
2015					
Revenue	$82,373	$87,030	$87,942	$77,014	$334,359
Gross margin	26,527	29,252	31,227	28,104	115,110
Net income (loss)	(1,515)	(12,547)	1,975	(1,375)	(13,462)
Earnings (loss) per share(1):					
Basic	$(0.03)	$(0.23)	$0.04	$(0.03)	$(0.25)
Diluted	$(0.03)	$(0.23)	$0.04	$(0.03)	$(0.25)
2014					
Revenue	$102,575	$105,318	$116,761	$124,503	$449,157
Gross margin	43,681	42,310	46,078	50,890	182,959
Net income	12,018	11,041	14,272	16,272	53,603
Earnings per share(1):					
Basic	$0.22	$0.20	$0.26	$0.30	$0.98
Diluted	$0.22	$0.20	$0.26	$0.29	$0.97

(1) The sum of the quarterly earnings (loss) per share (basic and diluted) may not agree to the earnings (loss) per share for the year due to the timing of common stock issuances.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.
Not applicable.

Item 9A. Controls and Procedures.
Evaluation of Disclosure Controls and Procedures
The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in reports filed or submitted under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. The Company's disclosure controls and procedures are also designed to ensure such information is accumulated and communicated to management, including the principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosures. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance that control objectives are attained. The Company's disclosure controls and procedures are designed to provide such reasonable assurance.
The Company's management, with the participation of the principal executive and principal financial officers, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of December 31, 2015, as required by Rule 13a-15(e) of the Exchange Act. Based upon that evaluation, the principal executive and principal financial officers have concluded that the Company's disclosure controls and procedures were effective as of December 31, 2015.

Management's Report on Internal Control over Financial Reporting
The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) of the Exchange Act. The Company's management, including the principal executive and principal financial officers, assessed the effectiveness of internal control over financial reporting as of December 31, 2015, based on criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) ("COSO") in Internal Control – Integrated Framework. Upon evaluation, the Company's management has concluded that the Company's internal control over financial reporting was effective in connection with the preparation of the consolidated financial statements as of December 31, 2015.
The effectiveness of the Company's internal control over financial reporting as of December 31, 2015 has been audited by Hein & Associates LLP, an independent registered public accounting firm, as stated in their report which is included herein.
Changes in Internal Control over Financial Reporting
There have been no changes in the Company's system of internal control over financial reporting during the three months ended December 31, 2015 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information.
None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.
The information required by this Item is incorporated by reference to the Company's Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders to be filed with the SEC within 120 days of year end.
Item 11. Executive Compensation.
The information required by this Item is incorporated by reference to the Company's Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders to be filed with the SEC within 120 days of year end.
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.
The information required by this Item is incorporated by reference to the Company's Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders to be filed with the SEC within 120 days of year end.

Item 13. Certain Relationships and Related Transactions, and Director Independence.
The information required by this Item is incorporated by reference to the Company's Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders to be filed with the SEC within 120 days of year end.
Item 14. Principal Accountant Fees and Services.
The information required by this Item is incorporated by reference to the Company's Definitive Proxy Statement for the 2016 Annual Meeting of Stockholders to be filed with the SEC within 120 days of year end.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

EXHIBIT INDEX

Exhibit Number	Exhibit Title
2.1	Agreement and Plan of Merger dated May 10, 2013, by and among Flotek Industries, Inc., Flotek Acquisition Inc. and Florida Chemical Company, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Form 8-K filed on May 13, 2013).
3.1	Amended and Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to the Company's Form 10-Q for the quarter ended September 30, 2007).
3.2	Certificate of Designations for Series A Cumulative Convertible Preferred Stock dated August 11, 2009 (incorporated by reference to Exhibit 3.1 to the Company's Form 8-K filed on August 17, 2009).
3.3	Certificate of Amendment to the Amended and Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to the Company's Form 10-Q for the quarter ended September 30, 2009).
3.4	Amended and Restated Bylaws, dated December 9, 2014 (incorporated by reference to Exhibit 3.1 to the Company's Form 8-K filed on December 10, 2014).
4.1	Form of Certificate of Common Stock (incorporated by reference to Appendix E to the Company's Definitive Proxy Statement filed on September 27, 2001).
4.2	Form of Certificate of Series A Cumulative Convertible Preferred Stock (incorporated by reference to Exhibit A to the Certificate of Designations for Series A Cumulative Convertible Preferred Stock filed as Exhibit 3.1 to the Company's Form 8-K filed on August 17, 2009).
4.3	Form of Warrant to Purchase Common Stock of the Company, dated August 31, 2000 (incorporated by reference to Exhibit 4.3 to the Company's Registration Statement on Form SB-2 (File no. 333-129308) filed on October 28, 2005).
4.4	Form of Exercisable Warrant, dated August 11, 2009 (incorporated by reference to Exhibit 4.1 to the Company's Form 8-K filed on August 17, 2009).
4.5	Form of Contingent Warrant, dated August 11, 2009 (incorporated by reference to Exhibit 4.2 to the Company's Form 8-K filed on August 17, 2009).
4.6	Amendment to Warrant to Purchase Common Stock, dated June 14, 2012, by and among the Company and each of the holders party thereto (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on June 18, 2012).
4.7	Amendment to Amended and Restated Warrant to Purchase Common Stock, dated as of February 5, 2014 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on February 11, 2014).
10.1	2003 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.1 to the Company's Registration Statement on Form S-8 filed on October 27, 2005).
10.2	2005 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.2 to the Company's Registration Statement on Form S-8 filed on October 27, 2005).
10.3	2007 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.6 to the Company's Form 10-K for the year ended December 31, 2007).
10.4	Exclusive License Agreement, dated April 3, 2006, among the Company, USA Petrovalve, Inc. and Total Well Solutions, LLC (incorporated by reference to Exhibit 10.2 to the Company's Form 10-QSB for the quarter ended June 30, 2006).
10.5	Form of Unit Purchase Agreement, dated August 11, 2009 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on August 12, 2009).
10.6	Indenture, dated as of March 31, 2010, among the Company, the subsidiary guarantors named therein and U.S. Bank National Association (incorporated by reference to Exhibit 4.1 to the Company's Form 8-K filed on April 6, 2010).

10.7	2010 Long-Term Incentive Plan (incorporated by reference to Appendix A to the Company's Definitive Proxy Statement filed on July 13, 2010).
10.8	Form of Subscription Agreement (incorporated by reference to Exhibit 4.7 to the Company's Registration Statement on Form S-3 (File No. 333-174199) filed on May 13, 2011).
10.9	Non-Qualified Stock Option Agreement, dated April 8, 2011, between the Company and Steve Reeves (incorporated by reference to Exhibit 10.5 to the Company's Form 10-Q for the quarter ended June 30, 2011).
10.10	Non-Qualified Stock Option Agreement, dated April 8, 2011, between the Company and John W. Chisholm (incorporated by reference to Exhibit 10.7 to the Company's Form 10-Q for the quarter ended June 30, 2011).

Exhibit Number	Exhibit Title
10.11	Revolving Credit and Security Agreement dated as of September 23, 2011 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on September 26, 2011).
10.12	Guaranty dated September 23, 2011 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on September 26, 2011).
10.13	Security Agreement dated September 23, 2011 (incorporated by reference to Exhibit 10.3 to the Company's Form 8-K filed on September 26, 2011).
10.14	Intellectual Property Security Agreement dated September 23, 2011 (incorporated by reference to Exhibit 10.4 to the Company's Form 8-K filed on September 26, 2011).
10.15	Lien Subordination and Intercreditor Agreement dated as of September 23, 2011 (incorporated by reference to Exhibit 10.5 to the Company's Form 8-K filed on September 26, 2011).
10.16	Second Amendment to Revolving Credit and Security Agreement dated as of November 12, 2012 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on November 14, 2012).
10.17	Third Amendment to Revolving Credit and Security Agreement dated as of December 14, 2012 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on December 17, 2012).
10.18	Fourth Amendment to Revolving Credit Security Agreement dated as of December 27, 2012 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on December 28, 2012).
10.19	Employment Agreement, dated effective March 13, 2013 between the Company and H. Richard Walton (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on March 15, 2013).
10.20	Restricted Stock Agreement, dated effective March 13, 2013 between the Company and H. Richard Walton (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on March 15, 2013).
10.21	Registration Rights Agreement dated May 10, 2013, by and among Flotek Industries, Inc. and the stockholders party thereto (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on May 13, 2013).
10.22	Amended and Restated Revolving Credit, Term Loan and Security Agreement dated May 10, 2013 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on May 13, 2013).
10.23	First Amendment to Amended and Restated Revolving Credit, Term Loan and Security Agreement dated December 31, 2013 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on January 7, 2014).
10.24	Employment Agreement, dated effective February 5, 2014 between the Company and Joshua A. Snively, Sr. (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on February 11, 2014).
10.25	Restricted Stock Agreement, dated effective February 5, 2014 between the Company and Joshua A. Snively, Sr. (incorporated by reference to Exhibit 10.3 to the Company's Form 8-K filed on February 11, 2014).
10.26	2014 Long-Term Incentive Plan (incorporated by reference to Exhibit A to the Company's Definitive Proxy Statement filed on April 18, 2014).
10.27	Fifth Amended and Restated Service Agreement, dated as of April 15, 2014, between the Company, Protechnics II, Inc. and Chisholm Management, Inc. (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on April 21, 2014).
10.28	Letter Agreement, dated as of April 15, 2014, between the Company and John Chisholm (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on April 21, 2014).
10.29	Second Amendment to Amended and Restated Revolving Credit, Term Loan and Security Agreement dated December 5, 2014 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on December 10, 2014).
10.30	Employment Agreement, dated effective December 31, 2014 between the Company and Steve Reeves (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on January 7, 2015).
10.31	Employment Agreement, dated effective May 29, 2015 between the Company and H. Richard Walton (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on June 4, 2015).

10.32	Employment Agreement, dated effective May 1, 2015 between the Company and Robert M. Schmitz (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on June 4, 2015).
10.33	Third Amendment to Amended and Restated Revolving Credit, Term Loan and Security Agreement dated June 19, 2015 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on June 24, 2015).
10.34	Fourth Amendment to Amended and Restated Revolving Credit, Term Loan and Security Agreement dated July 21, 2015 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on July 23, 2015).
21*	List of Subsidiaries.
23*	Consent of Hein & Associates LLP.
31.1*	Rule 13a-14(a) Certification of Principal Executive Officer.

Exhibit Number	Exhibit Title
31.2*	Rule 13a-14(a) Certification of Principal Financial Officer.
32.1*	Section 1350 Certification of Principal Executive Officer.
32.2*	Section 1350 Certification of Principal Financial Officer.
101.INS**	XBRL Instance Document.
101.SCH**	XBRL Schema Document.
101.CAL**	XBRL Calculation Linkbase Document.
101.LAB**	XBRL Label Linkbase Document.
101.PRE**	XBRL Presentation Linkbase Document.
101.DEF**	XBRL Definition Linkbase Document.

* Filed herewith.

** Furnished with this Form 10-K, not filed.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FLOTEK INDUSTRIES, INC.

By: /s/ JOHN W. CHISHOLM
John W. Chisholm
President, Chief Executive Officer and Chairman of the Board

Date: January 27, 2016

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ JOHN W. CHISHOLM	President, Chief Executive Officer, and Chairman of the Board	January 27, 2016
John W. Chisholm	(Principal Executive Officer)	
/s/ ROBERT M. SCHMITZ	Chief Financial Officer	January 27, 2016
Robert M. Schmitz	(Principal Financial Officer and Principal Accounting Officer)	
/s/ KENNETH T. HERN	Director	January 27, 2016
Kenneth T. Hern		
/s/ JOHN S. REILAND	Director	January 27, 2016
John S. Reiland		
/s/ L.V. “BUD” MCGUIRE	Director	January 27, 2016
L.V. “Bud” McGuire		
/s/ L. MELVIN COOPER	Director	January 27, 2016
L. Melvin Cooper		
/s/ CARLA S. HARDY	Director	January 27, 2016
Carla S. Hardy		
/s/ TED D. BROWN	Director	January 27, 2016
Ted D. Brown		