

ISRAMCO INC  
Form 10-Q  
November 09, 2018

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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**FORM 10-Q**

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**Check  
One**

Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended **September 30, 2018**

or

Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934

**Commission File Number 0-12500**

**ISRAMCO, INC**

(Exact Name of registrant as Specified in its Charter)

**Delaware**

(State or other Jurisdiction of Incorporation or Organization)

**13-3145265**

I.R.S. Employer Number

**1001 West Loop South, Suite 750, HOUSTON, TX 77027**

(Address of Principal Executive Offices)

**713-621-5946**

(Registrant's Telephone Number, Including Area Code)

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

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller Reporting Company
Emerging growth company	

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

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

As of November 9, 2018, Isramco, Inc., had 2,717,648 outstanding shares of common stock, par value \$0.01 per share.

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**Forward Looking Statements**

CERTAIN STATEMENTS MADE IN THIS QUARTERLY REPORT ON FORM 10-Q ARE “FORWARD-LOOKING STATEMENTS” WITHIN THE MEANING OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995. FORWARD-LOOKING STATEMENTS CAN BE IDENTIFIED BY TERMINOLOGY SUCH AS “MAY”, “WILL”, “SHOULD”, “EXPECTS”, “INTENDS”, “ANTICIPATES”, “BELIEVES”, “ESTIMATES”, “PREDICTS”, OR “CONTINUE” OR THE NEGATIVE OF THESE TERMS OR OTHER COMPARABLE TERMINOLOGY AND INCLUDE, WITHOUT LIMITATION, STATEMENTS BELOW REGARDING EXPLORATION AND DRILLING PLANS, FUTURE GENERAL AND ADMINISTRATIVE EXPENSES, FUTURE GROWTH, FUTURE EXPLORATION, FUTURE GEOPHYSICAL AND GEOLOGICAL DATA, GENERATION OF ADDITIONAL PROPERTIES, RESERVES, NEW PROSPECTS AND DRILLING LOCATIONS, FUTURE CAPITAL EXPENDITURES, SUFFICIENCY OF WORKING CAPITAL, ABILITY TO RAISE ADDITIONAL CAPITAL, PROJECTED CASH FLOWS FROM OPERATIONS, OUTCOME OF ANY LEGAL PROCEEDINGS, DRILLING PLANS, THE NUMBER, TIMING OR RESULTS OF ANY WELLS, INTERPRETATION AND RESULTS OF SEISMIC SURVEYS OR SEISMIC DATA, FUTURE PRODUCTION OR RESERVES, LEASE OPTIONS OR RIGHTS, PARTICIPATION OF OPERATING PARTNERS, CONTINUED RECEIPT OF ROYALTIES, AND ANY OTHER STATEMENTS REGARDING FUTURE OPERATIONS, FINANCIAL RESULTS, OPPORTUNITIES, GROWTH, BUSINESS PLANS AND STRATEGY. BECAUSE FORWARD-LOOKING STATEMENTS INVOLVE RISKS AND UNCERTAINTIES, THERE ARE IMPORTANT FACTORS THAT COULD CAUSE ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE EXPRESSED OR IMPLIED BY THESE FORWARD-LOOKING STATEMENTS. ALTHOUGH THE COMPANY BELIEVES THAT EXPECTATIONS REFLECTED IN THE FORWARD-LOOKING STATEMENTS ARE REASONABLE, IT CANNOT GUARANTEE FUTURE RESULTS, PERFORMANCE OR ACHIEVEMENTS. MOREOVER, NEITHER THE COMPANY NOR ANY OTHER PERSON ASSUMES RESPONSIBILITY FOR THE ACCURACY AND COMPLETENESS OF THESE FORWARD-LOOKING STATEMENTS. THE COMPANY IS UNDER NO DUTY TO UPDATE ANY FORWARD-LOOKING STATEMENTS AFTER THE DATE OF THIS REPORT TO CONFORM SUCH STATEMENTS TO ACTUAL RESULTS.

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Table of Contents**PART I - Financial Information****ITEM 1. Financial Statements****ISRAMCO INC.****CONSOLIDATED BALANCE SHEETS**

(In thousands, except share and per share amounts)

(Unaudited)

	<b>As of</b>	<b>As of</b>
	<b>September</b>	<b>December</b>
	<b>30, 2018</b>	<b>31, 2017</b>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 10,591	\$ 30,009
Accounts receivable, net of allowances for doubtful accounts of \$2,117 and \$2,431	20,531	12,549
Restricted and designated cash	704	802
Inventories	502	475
Derivative asset	260	-
Prepaid expenses and other	1,574	2,711
Total Current Assets	34,162	46,546
Property and Equipment, at cost – successful efforts method:		
Oil and Gas properties	244,277	243,812
Advanced payment for equipment	462	564
Production service equipment and other equipment and property	66,982	59,108
Total Property and Equipment	311,721	303,484
Accumulated depreciation, depletion, amortization and impairment	(255,446 )	(251,355 )
Net Property and Equipment	56,275	52,129
Derivative asset	1,102	187
Restricted cash – long term	23,045	9,674
Investments	261	261
Total Assets	\$ 114,845	\$ 108,797
<b>LIABILITIES AND SHAREHOLDERS' DEFICIT</b>		
Current Liabilities:		
Accounts payable and accrued expenses	\$ 14,879	\$ 13,515

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Short term debt and current maturities of long-term debt, net of discount of \$763 and \$828	21,437	18,517
Short term debt related party	2,800	-
Payables due to related party	50	60
Accrued interest	1,096	1,027
Derivative liability	-	457
Total Current Liabilities	40,262	33,576
Long term debt, net of discount of \$1,574 and \$2,131	61,426	77,369
Other Long-term Liabilities:		
Asset retirement obligations	22,045	21,670
Total Liabilities	123,733	132,615
Commitments and contingencies		
Shareholders' Deficit:		
Common stock \$0.01 par value; authorized 7,500,000 shares; issued 2,746,915 shares; outstanding 2,717,648 shares	27	27
Additional paid-in capital	23,853	23,853
Accumulated deficit	(25,049 )	(40,970 )
Treasury stock, 29,267 shares at cost	(164 )	(164 )
Total Isramco, Inc. Shareholders' Deficit	(1,333 )	(17,254 )
Non controlling interest	(7,555 )	(6,564 )
Total Deficit	(8,888 )	(23,818 )
Total Liabilities and Shareholders' Deficit	\$ 114,845	\$ 108,797

See notes to the unaudited consolidated financial statements.

Table of Contents**ISRAMCO INC.****CONSOLIDATED STATEMENTS OF OPERATIONS**

(In thousands, except share and per share amounts)

(Unaudited)

	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>		
	<b>2018</b>	<b>2017</b>	<b>2018</b>	<b>2017</b>	
<b>Revenues and other</b>					
Oil and gas sales	\$ 12,655	\$ 11,223	\$ 35,422	\$ 33,020	
Production services	9,420	5,073	23,110	13,230	
Office services	130	139	397	418	
Gain on divestiture	509	25	981	2,703	
Other	132	114	421	382	
Total revenues and other	22,846	16,574	60,331	49,753	
<b>Operating expenses</b>					
Lease operating expense, transportation and taxes	2,482	2,631	7,142	7,113	
Depreciation, depletion and amortization	1,447	1,540	4,193	4,480	
Accretion expense	195	231	653	679	
Production services	8,607	4,609	21,552	13,382	
Loss (gain) from plug and abandonment	(2	) -	210	26	
General and administrative	1,251	1,103	3,821	3,491	
Total operating expenses	13,980	10,114	37,571	29,171	
<b>Operating income</b>	<b>8,866</b>	<b>6,460</b>	<b>22,760</b>	<b>20,582</b>	
<b>Other expenses</b>					
Interest expense, net	1,218	1,216	3,768	3,611	
Loss (gain) from derivative contracts, net	(186	) 225	(1,334	) 777	
Capital loss (gain)	-	(33	) 11	(33	)
Total other expenses	1,032	1,408	2,445	4,355	
<b>Income before income taxes</b>	<b>7,834</b>	<b>5,052</b>	<b>20,315</b>	<b>16,227</b>	
<b>Income tax expense</b>	<b>(1,941</b>	<b>) (1,872</b>	<b>) (5,385</b>	<b>) (6,074</b>	
<b>Net income</b>	<b>\$5,893</b>	<b>\$3,180</b>	<b>\$14,930</b>	<b>\$10,153</b>	
Net loss attributable to non-controlling interests	(285	) (296	) (991	) (1,127	
<b>Net income attributable to Isramco</b>	<b>\$6,178</b>	<b>\$3,476</b>	<b>\$15,921</b>	<b>\$11,280</b>	
<b>Earnings per share – basic:</b>	<b>\$2.27</b>	<b>\$1.28</b>	<b>\$5.86</b>	<b>\$4.15</b>	
<b>Earnings per share – diluted:</b>	<b>\$2.27</b>	<b>\$1.28</b>	<b>\$5.86</b>	<b>\$4.15</b>	

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Weighted average number of shares outstanding basic:	2,717,648	2,717,648	2,717,648	2,717,648
Weighted average number of shares outstanding diluted:	2,717,648	2,717,648	2,717,648	2,717,648

See notes to the unaudited consolidated financial statements.



Table of Contents**ISRAMCO INC.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(In thousands)

(Unaudited)

	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2018</b>	<b>2017</b>	<b>2018</b>	<b>2017</b>
Net income	\$5,893	\$3,180	\$14,930	\$10,153
Comprehensive income	5,893	3,180	14,930	10,153
Comprehensive loss attributable to non-controlling interests	(285 )	(296 )	(991 )	(1,127 )
<b>Comprehensive Income attributable to Isramco</b>	<b>\$6,178</b>	<b>\$3,476</b>	<b>\$15,921</b>	<b>\$11,280</b>

See notes to the unaudited consolidated financial statements.

Table of Contents**ISRAMCO INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

(Unaudited)

	<b>Nine months Ended</b>	
	<b>September 30, 2018</b>	<b>2017</b>
<b>Cash Flows From Operating Activities:</b>		
Net income	\$ 14,930	\$ 10,153
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion, amortization and impairment	4,193	4,480
Bad debt expense	58	120
Accretion expense	653	679
Gain on divestiture	(981 )	(2,703 )
Changes in deferred taxes	-	794
Net unrealized (gain) loss on derivative contracts	(1,632 )	55
Loss (gain) on sale of equipment and other	11	(33 )
Amortization of debt cost	622	596
Changes in components of working capital and other assets and liabilities		
Accounts receivable	(8,040 )	(4,277 )
Prepaid expenses, other receivables and other current assets	1,137	1,186
Due to related party	(10 )	24
Inventories	(27 )	160
Accounts payable and accrued expenses	1,006	1,609
Net cash provided by operating activities	11,920	12,843
<b>Cash flows from investing activities:</b>		
Addition to property and equipment, net	(8,185 )	(2,503 )
Proceeds from sale of oil and gas properties and equipment	965	2,705
Proceeds from sale of equipment	-	49
Investment in Apache Flats	-	(31 )
Net cash provided by (used in) investing activities	(7,220 )	220
<b>Cash flows from financing activities:</b>		
Repayments of long term debt	(13,200)	(7,200)
Net proceeds from related party loan	2,800	-
Repayments of short - term debt, net	(445 )	(520 )
Net cash used in financing activities	(10,845)	(7,720)

<b>Net increase (decrease) in cash, cash equivalents, and restricted cash</b>	(6,145 )	5,343
<b>Cash, cash equivalents, and restricted cash at beginning of period</b>	40,485	33,913
<b>Cash, cash equivalents, and restricted cash at end of period</b>	\$34,340	\$39,256

See notes to the unaudited consolidated financial statements.

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**Isramco Inc.**

**Notes to Consolidated Financial Statements**

**(Unaudited)**

**Note 1 - Financial Statement Presentation**

Isramco, Inc. and its subsidiaries and affiliated companies (together referred to as “We”, “Our”, “Isramco” or the “Company”) is predominately an independent oil and natural gas company engaged in the exploration, development and production of oil and natural gas properties located onshore in the United States and ownership of various royalty interests in oil and gas concessions located offshore Israel. The Company also operates a production services company that provides well maintenance and workover services, well completion, and recompletion services.

The accompanying unaudited financial statements and notes of Isramco have been prepared pursuant to the rules and regulations of the United States Securities and Exchange Commission (the “Commission”). Pursuant to such rules and regulations, certain disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. The accompanying financial statements and notes should be read in conjunction with the accompanying financial statements and notes included in Isramco’s Annual Report on Form 10-K for the year ended December 31, 2017.

The accompanying unaudited interim financial statements furnished in this report reflect all adjustments that are, in the opinion of management, necessary to fairly present Isramco’s results of operations and cash flows for the nine-month periods ended September 30, 2018 and 2017 and Isramco’s financial position as of September 30, 2018.

**Use of Estimates**

In preparing financial statements in accordance with accounting principles generally accepted in the United States, management makes informed judgments and estimates that affect the reported amounts of assets, liabilities, revenues, and expenses. Management evaluates its estimates and related assumptions regularly, including those related to the value of properties and equipment; proved reserves; intangible assets; asset retirement obligations; litigation reserves; environmental liabilities; liabilities, and costs; income taxes; and fair values. Changes in facts and circumstances or additional information may result in revised estimates, and actual results may differ from these estimates.

Consolidated interim period results are not necessarily indicative of results of operations or cash flows for the full year and accordingly, certain information normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States has been condensed or omitted. The Company has evaluated events or transactions through the date of issuance of these consolidated financial statements.

### **Concentrations of Credit Risk**

Financial instruments, which potentially expose Isramco to concentrations of credit risk, consist primarily of interest rate swaps, cash equivalents, trade and joint interest accounts receivable. Isramco's customer base includes several of the major United States oil and gas operating and production companies as well as major power companies in Israel. Although Isramco is directly affected by the well-being of the oil and gas production industry, management does not believe a significant credit risk existed as of September 30, 2018. Isramco continues to monitor and review credit exposure of its marketing counter-parties.

Tamar Royalties LLC, a wholly owned subsidiary of Isramco Inc., entered into certain swap and cap agreements with Deutsche Bank AG London Branch to hedge the risk of interest rate volatility. See Note 4 for details.

Our production services segment customers include major oil and natural gas production companies and independent oil and natural gas production companies. We perform ongoing credit evaluations of our customers and usually do not require material collateral. We maintain reserves for potential credit losses when necessary. Our results of operations and financial position should be considered in light of the fluctuations in demand experienced by oilfield service companies as changes in oil and gas producers' expenditures and budgets occur. These fluctuations can impact our results of operations and financial position as supply and demand factors directly affect utilization and hours which are the primary determinants of our net cash provided by operating activities.

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Isramco maintains deposits in banks, which may exceed the amount of federal deposit insurance available. Management periodically assesses the financial condition of the institutions and believes that any possible deposit loss is minimal.

### **Risk Management Activities**

The Company follows Accounting Standards Codification (ASC) 815, *Derivatives and Hedging*. From time to time, the Company may hedge a portion of its forecasted oil and natural gas production or may hedge interest rates on variable interest rate loans. Derivative contracts entered into by the Company have consisted of transactions in which the Company hedges the variability of cash flow related to a forecasted transaction. The Company has elected not to designate any of its positions for hedge accounting. Accordingly, the Company records the net change in the mark-to-market valuation of these positions, as well as payments and receipts on settled contracts, in “Net loss (gain) on derivative contracts” in the consolidated statements of operations. Currently, the Company has no derivative contracts in place to hedge against fluctuations in oil and natural gas prices.

### **Fair Value**

Fair value accounting applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements. Fair value measurements are determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, these accounting requirements establish a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity’s own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that we have the ability to access.

Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs for the asset or liability, and are typically based on an entity's own assumptions, as there is little, if any, related market activity.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability. We utilize the fair value hierarchy in our accounting for interest rate swaps (Level 2).

### **Consolidation**

The consolidated financial statements include the accounts of Isramco and its subsidiaries. Inter-company balances and transactions have been eliminated in consolidation.

### **Cash, cash equivalents and restricted cash**

The Company adopted the FASB accounting standard ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force) on January 1, 2018 using a full retrospective approach. ASU 2016-18 requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents are included with cash and cash equivalents in reconciling the beginning-of-period and end-of-period total amounts shown on the Company's consolidated statements of cash flows. We believe the adoption of ASU 2016-18 did not have a material impact on the Company's Consolidated Financial Statements.

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The Company considers highly liquid investments purchased with a maturity period of three months or less at the date of purchase to be cash equivalents. Restricted cash and restricted cash – long term are included with cash, cash equivalents, and restricted cash on the Company’s consolidated statements of cash flows.

Consolidated balance sheets amount included as cash, cash equivalents, and restricted cash on the Company’s consolidated statements of cash flows:

	<b>As of</b>	<b>As of</b>
	<b>September</b>	<b>December</b>
	<b>30, 2018</b>	<b>31, 2017</b>
Cash and cash equivalents	\$ 10,591	\$ 30,009
Restricted and designated cash	704	802
Restricted cash – long term	23,045	9,674
Total Current Assets	\$ 34,340	\$ 40,485

**Impairment**

We review our property and equipment in accordance with Accounting Standards Codification (ASC) 360, *Property, Plant, and Equipment* (ASC 360). ASC 360 requires us to evaluate property and equipment as an event occurs or circumstances change that would more likely than not reduce the fair value of the property and equipment below the carrying amount. If the carrying amount of property and equipment is not recoverable from its undiscounted cash flows, then we would recognize an impairment loss for the difference between the carrying amount and the current fair value. Further, we evaluate the remaining useful lives of property and equipment at each reporting period to determine whether events and circumstances warrant a revision to the remaining depreciation periods.

**Asset Retirement Obligation**

ASC 410, *Asset Retirement and Environmental Obligations* (ASC 410) requires that the fair value of an asset retirement cost, and corresponding liability, should be recorded as part of the cost of the related long-lived asset and subsequently allocated to expense using a systematic and rational method. The Company records asset retirement obligations to reflect the Company’s legal obligations related to future plugging and abandonment of its oil and natural gas wells and gas gathering systems. The Company estimates the expected cash flow associated with the obligation and discounts the amounts using a credit-adjusted, risk-free interest rate. At least annually, the Company reassesses the obligation to determine whether a change in the estimated obligation is necessary. The Company evaluates whether there are indicators that suggest the estimated cash flows underlying the obligation have materially



changed. Should those indicators suggest the estimated obligation may have materially changed on an interim basis (quarterly), the Company will accordingly update its assessment.

### **Gain on divestiture**

In February 2018, the Company sold an oil and gas property for a net gain of \$472,000. The gain consists of \$454,000 cash plus \$19,000 in relieved asset retirement obligation, offset by a net book value of \$1,000. In September 2018, the Company sold an oil and gas property for a net gain of \$509,000.

### **Commitments and Contingencies**

As is common within the oil and natural gas industry, we have entered into various commitments and operating agreements related to the exploration and development of and production from proved oil and natural gas properties. It is our belief that such commitments will be met without a material adverse effect on our financial position, results of operations or cash flows.

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Aggregate maturities of contractual obligations at September 30, 2018 are due in future years as follows (in thousands):

Principal Payments on Long-term debt:

2018	\$5,700
2019	21,900
2020	17,100
2021	14,700
2022	14,400
2023	11,400
Total	\$85,200

**Note 2 - Supplemental Cash Flow Information**

The Israeli taxing authority withheld taxes of \$5,385,000 and \$5,261,000 during the nine months ended September 30, 2018 and 2017 respectively.

Cash payments for interest were \$3,252,000 and \$2,980,000 for the nine-month periods ended September 30, 2018 and 2017 respectively.

The consolidated statement of cash flows for the nine-month period ended September 30, 2018 excludes the following non-cash transactions:

Increase in property and equipment of \$165,000 included in accounts payable.

Asset retirement obligation relieved of \$19,000 due to sale of oil and gas properties.

The consolidated statement of cash flows for the nine-month period ended September 30, 2017 excludes the following non-cash transactions:

Net additions to equipment of \$33,000 included in accounts payable.

Increase in property and equipment of \$27,000 due to additional asset retirement obligation.

Asset retirement obligation relieved of \$18,000 due to sale of oil and gas properties.

Insurance premiums financed through issuance of short term debt of \$835,000.

### **Note 3 – Revenue from Contracts with Customers**

#### Adoption of new revenue recognition and disclosure guidance

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which generally requires an entity to identify performance obligations in its contracts, estimate the amount of consideration to be received in the transaction price, allocate the transaction price to each separate performance obligation, and recognize revenue as obligations are satisfied. Additionally, the standard requires expanded disclosures related to revenue recognition. Subsequent to the issuance of ASU 2014-09, the FASB issued additional guidance to assist entities with implementation efforts, including the issuance of ASU 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net), pertaining to the presentation of revenues on a gross basis (revenues presented separately from associated expenses) versus a net basis. This guidance requires an entity to record revenue on a gross basis if it controls a promised good or service before transferring it to a customer, whereas an entity is required to record revenue on a net basis if its role is to arrange for another entity to provide the goods or services to a customer.

The Company adopted the new revenue recognition and presentation guidance on January 1, 2018, using a full retrospective transition approach. We believe that adoption of the new guidance had no cumulative effect impact on the Company's retained earnings at January 1, 2018.

The new guidance does not have a material impact on the timing of the Company's revenue recognition or its financial position, results of operations, net income, or cash flows.

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Below is a discussion of the nature, timing, and presentation of revenues arising from the Company's major revenue-generating arrangements:

**Oil and Gas Sales United States** – Revenues on sales of oil, natural gas liquids (“NGLs”), gas and purchased oil and gas are recognized when control of the product is transferred to the purchaser and payment can be reasonably assured. Sales prices for oil, NGL and gas production are negotiated based on factors normally considered in the industry, such as an index or spot price, distance from the well to the pipeline or market, commodity quality and prevailing supply and demand conditions. As such, the prices of oil, NGLs and gas generally fluctuate based on the relevant market index rates. Sales under the Company's oil contracts are generally considered performed when the Company sells oil production at the wellhead and receives an agreed-upon index price, net of any price differentials. The Company recognizes revenue when control transfers to the purchaser at the wellhead based on the net price received. Sales under the Company's gas processing contracts are recognized when the Company delivers gas to a midstream processing entity at the wellhead or the inlet of the midstream processing entity's system. The midstream processing entity gathers and processes the gas and remits proceeds to the Company for the resulting sales of NGLs and gas. In many cases, the Company elects to take its NGLs and residue gas in-kind at the tailgate of the midstream entity's processing plant and subsequently market the products itself. When the Company elects to take-in-kind, it delivers NGLs and gas to a third-party purchaser at a contractually agreed-upon delivery point and receives a specified index price from the purchaser.

**Natural Gas Sales Israel** – We own all ownership units in Tamar Royalties LLC, a Delaware limited liability company. Tamar Royalties LLC owns an overriding royalty interest of 1.5375% before payout and increasing to 2.7375% after payout in the Tamar Field (collectively the “Tamar Royalty”) offshore Israel. An overriding royalty interest is an ownership interest in the oil and gas leasehold estate equating to a certain percentage of production or production revenues, calculated free of the costs of production and development of the underlying lease(s), but subject to its proportionate share of certain post production costs. An overriding royalty interest is a non-possessory interest in the oil and gas leasehold estate and, accordingly, we have no control over the operations, drilling, expenses, timing, production, sales, or any other aspect of development or production of the Tamar Field.

Natural gas from the Tamar Field is currently sold to the Israel Electric Corporation (“IEC”) and numerous other Israeli purchasers, including independent power producers, cogeneration facilities, local distribution companies and certain industrial companies. Currently, many of the Tamar's gas purchase and sale agreements provide for sales at a 7 to 15-year term, while some contracts have extension options of up to 2 years. Depending on the specific contract, prices may vary and are based on an initial base price subject to price adjustment provisions, including price indexation and a price floor. The IEC contract provides for price reopeners (sometimes referred to as “price review” clauses) in the eighth and eleventh years of the contract, subject to limits on the amount of increase or decrease from the existing contractual price.

Revenues from natural gas sales in Israel are recognized when control of the product is transferred to a purchaser and payment can reasonably be assured. The Company receives monthly overriding royalty payments from Isramco Negev 2 Limited Partnership, a related party. We generally receive payment two months after the hydrocarbons have been

produced. The revenue is recognized in the month that the hydrocarbons are produced.

**Production Services** – Our production services business earns revenues for well servicing, plugging and abandonment services, workover and fluid hauling services pursuant to master service agreements based on purchase orders or other contractual arrangements with the client. Production services jobs are generally short-term (less than 30 days) and are charged at current market rates for the labor, equipment and materials necessary to complete the job. Production services jobs are varied in nature, but typically represent a single performance obligation, either for a particular job, a series of distinct jobs, or a period of time during which we stand ready to provide services as our client needs them. Revenue is recognized for these services over time, as the services are performed. We typically bill clients for our production servicing on an hourly basis for the period that the rig or truck is actively working. Generally, the Company accounts for production services as a single performance obligation satisfied over time. Revenue for certain jobs spanning multiple days is recognized over time upon the completion of each day's work based upon a completed field ticket, which includes the charges for the services performed, mobilization of the equipment to the location and personnel. Additional revenue is generated through labor charges and the sale of consumable supplies that are incidental to the service being performed. Such amounts are recognized ratably over the period during which the corresponding goods and services are consumed.

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Disaggregation of revenues (in thousands):

	<b>Nine Months Ended September 30, 2018      2017</b>	
Oil and Gas sales		
United States	\$ 12,008	\$ 11,100
Israel	23,414	21,920
Production Services	23,330	13,230
Total revenues from contracts with customers	\$ 58,752	\$ 46,250

**Performance obligations**

The Company satisfies the performance obligations under its crude oil and natural gas sales contracts upon delivery of its production and related transfer of title to customers. Upon delivery of production, the Company has a right to receive consideration from its customers in amounts that correspond with the value of the production transferred. The Company satisfies the performance obligations under production services arrangements by completing the contracted job, at which time the Company has the right to receive consideration from its customers in agreed upon amounts.

All of the Company's outstanding production services and crude oil sales contracts at September 30, 2018 are short-term in nature with contract terms of less than one year. For such contracts, the Company has utilized the practical expedient in Accounting Standards Codification ("ASC") 606-10-50-14 exempting the Company from disclosure of the transaction price allocated to remaining performance obligations, if any, if the performance obligation is part of a contract that has an original expected duration of one year or less.

The majority of the Company's operated natural gas production is sold at lease locations to midstream customers under multi-year term contracts. For such contracts having a term greater than one year, the Company has utilized the practical expedient in ASC 606-10-50-14A which indicates an entity is not required to disclose the transaction price allocated to remaining performance obligations, if any, if variable consideration is allocated entirely to a wholly unsatisfied performance obligation. Under our sales contracts, whether for crude oil or natural gas, each unit of production delivered to a customer represents a separate performance obligation; therefore, future volumes to be delivered are wholly unsatisfied at period-end and disclosure of the transaction price allocated to remaining performance obligations is not applicable.

**Contract balances**

Under the Company's crude oil and natural gas sales contracts or arrangements that give rise to service revenues, the Company recognizes revenue after its performance obligations have been satisfied, at which point the Company has an unconditional right to receive payment. Accordingly, the Company's commodity sales contracts and service arrangements generally do not give rise to contract assets or contract liabilities under ASC Topic 606. Instead, the Company's unconditional rights to receive consideration are presented as a receivable within "Accounts receivable, net of allowances for doubtful accounts", in its condensed consolidated balance sheets.

### **Revenues from previously satisfied performance obligations**

To record revenues for commodity sales in the United States and Israel, at the end of each period the Company estimates the amount of production delivered and sold to customers and the prices to be received for such sales. Differences between estimated revenues and actual amounts received for all prior months are recorded in the month payment is received from the customer and are reflected in our consolidated financial statements within the caption "Oil and gas sales". Revenues recognized during the nine months ended September 30, 2018 related to performance obligations satisfied in prior reporting periods were not material.

To record revenues for un-billed production services, at the end of each period the Company estimates the services rendered. Differences between estimated revenues and actual amounts received for all prior months are recorded in the month invoices are created and reflected in our consolidated financial statement with the caption "Production services". Revenues recognized during the nine months ended September 30, 2018 related to performance obligations satisfied in prior reporting periods were not material.

Table of Contents**Note 4 - Financial Instruments and Fair Value**

Pursuant to ASC 820, Fair Value Measurements and Disclosures (ASC 820) the Company's determination of fair value incorporates not only the credit standing of the counterparties involved in transactions with the Company resulting in receivables on the Company's consolidated balance sheets, but also the impact of the Company's non-performance risk on its own liabilities. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The Company believes that it utilizes market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable. The Company classifies fair value balances based on the observability of those inputs.

On June 16, 2015, Tamar Royalties LLC ("Tamar Royalties"), a wholly owned subsidiary of the Company, engaged in an interest rate swap agreement ("IRS Agreement") with the Deutsche Bank AG London Branch ("DBAG"). An interest rate swap is an agreement between two parties (known as counterparties) where one stream of future interest payments is exchanged for another based on a specified notional principal amount. Interest rate swaps often exchange fixed interest payments for floating interest payments that are linked to interest rates.

As previously disclosed on the Company's Form 8-K filed May 22, 2015, Tamar Royalties entered into a \$120,000,000 credit facility with Deutsche Bank, which facility is discussed further in Note 5 "Long-Term Debt and Interest Expense". Under the terms of this facility, Tamar Royalties, is required to hedge at least seventy-five percent (75%) of the outstanding balance under this facility against fluctuations in LIBOR, with at least thirty seven and one-half percent (37.5%) of the outstanding balance being hedged through swaps. The notional value of these hedges corresponds to the amortization schedule covering the facility and previously disclosed in the aforementioned Form 8-K. Accordingly, on June 16, 2015, Tamar Royalties and DBAG entered into the IRS Agreement whereby the Company hedged \$119,250,000 of the \$120,000,000 initial borrowing as follows:

(a) Tamar Royalties hedged 37.5% of the perpetual outstanding balance under the facility, being an initial notional amount of \$45,000,000, with a fixed rate swap whereby the Company will pay DBAG a fixed interest rate of 4.63%, and DBAG will pay the Company a monthly floating interest rate of USD-LIBOR-BBA plus a spread of 2.75%.

(b) Tamar Royalties hedged the remaining 62.5% of the perpetual outstanding balance less \$750,000, being an initial notional amount of \$74,250,000, against fluctuations in LIBOR by capping the fluctuations in LIBOR at 1.50%. Pursuant to the IRS Agreement, the Company will pay DBAG a fixed interest rate of 0.91%, and DBAG will pay the Company the greater of (i) USD-LIBOR-BBA minus a cap strike of 1.5% and (ii) zero.



As a result of these financial instruments, the Company recorded a net gain from derivative contracts in the amount of \$1,334,000 consisting of \$1,632,000 of unrealized gain and \$298,000 loss in cash settlements for the nine months ended September 30, 2018. The Company recorded a net loss from derivative contracts in the amount of \$777,000 consisting of \$55,000 of unrealized loss and \$722,000 loss in cash settlements for the nine months ended September 30, 2017.

Financial Instruments as of September 30, 2018 and December 31, 2017 consisted of the following (in thousands):

Financial Instrument	Fair Value Input Level	September 30, 2018		December 31, 2017	
		Carrying Value	Fair Value	Carrying Value	Fair Value
<b>ST Assets/Liabilities:</b>					
Interest rate swaps	Level 2	\$260	\$260	\$(457)	\$(457)
<b>LT Assets:</b>					
Interest rate swaps	Level 2	1,102	1,102	187	187
		\$1,362	\$1,362	\$(270)	\$(270)

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Our interest rate swaps are measured at fair value using Level 2 inputs. The fair of our interest rate swaps is based on the net present value of expected future cash flows related to both variable and fixed-rate legs of the swap agreement. This measurement is computed using the forward London Interbank Offered Rate (“LIBOR”) yield curve, a market-based observable input.

**Note 5 - Long-Term Debt and Interest Expense**

Long-term debt as of September 30, 2018 and December 31, 2017 consisted of the following (in thousands):

	<b>As of</b>	<b>As of</b>
	<b>September</b>	<b>December</b>
	<b>30, 2018</b>	<b>31, 2017</b>
Bank loan		
Principal amount	\$ 85,200	\$ 98,400
Less: unamortized discount and debt costs	(2,337 )	(2,959 )
Total long-term debt	82,863	95,441
Less: current maturities, net of current unamortized discount	(21,437 )	(18,072 )
Long-term debt, net of current maturities	\$ 61,426	\$ 77,369

**Bank Loan and Credit Facility**

## The Deutsche Bank Facility

On May 18, 2015, Tamar Royalties, a newly formed, wholly-owned, special purpose subsidiary of the Company, entered into a term loan credit agreement (the “DB Facility”) with Deutsche Bank Trust Company Americas (“Deutsche Bank”), as facility agent for the lenders and as collateral agent for the secured parties, and with the lenders party thereto. The DB Facility provides for borrowings in the amount of \$120,000,000 on a committed basis and is secured by, among other things, an overriding royalty interest in the Tamar Field, a natural gas field in the Mediterranean Sea, equal to 1.5375%, but is subject to increase to 2.7375% upon the Tamar project payout (the “Royalty Interest”). In connection with the DB Facility, and pursuant to a royalties sale and contribution agreement, the Company contributed the Royalty Interest to Tamar Royalties in exchange for all of the ownership units of Tamar Royalties.

Pursuant to the terms of its governing documents, Tamar Royalties will be managed by N.M.A. Energy Resources Ltd, a related party of the Company, and an independent manager, Donald J. Puglisi.

Pursuant to the terms of the DB Facility, Tamar Royalties borrowed \$120,000,000 in its initial borrowing under this facility. The initial borrowing under the DB Facility bears annual interest based on the LIBOR for a three-month interest period plus a spread of 2.75%. The \$120,000,000 initial borrowing under the DB Facility will be repaid over eight (8) years commencing July 1, 2015, in accordance with an amortization profile based on projected cash flows from the Royalty Interest. Tamar Royalties' obligations under the DB Facility are secured by a first ranking pledge of the shares of Tamar Royalties, first ranking pledge of all rights under the agreements creating the Royalty Interest, and a first priority security interest over the accounts created under the DB Facility.

So long as any amounts remain outstanding to the Lenders under the DB Facility, Tamar Royalties must, from and after the end of the Availability Period (as defined in the DB Facility), have a Historical Debt Service Coverage Ratio (as defined in the DB Facility) of not less than 1.00:1.00, a Loan Life Coverage Ratio (as defined in the DB Facility) of at least 1.1:1.00, and maintain a Required Reserve Amount (as defined in the DB Facility). The initial Required Reserve Amount was \$4,680,000. In addition, Tamar Royalties is required under the DB Facility to hedge against fluctuations in LIBOR as reflected in Note 4 "Financial Instruments and Fair Value".

The amortization schedule under the DB Facility was based on the projection that the Investment Repayment Date (as defined therein) would occur at some point before the end of the first quarter of 2018 and therefore, commencing from the Payment Date occurring on 1st April 2018, the amounts to be repaid on each payment date under the credit agreement increase to reflect the expected increase in the Royalties Receivables (as defined therein) as a result of the increase in the royalty percentage following the Investment Repayment Date.

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As noted above with regard to the payout of the Tamar Field, a disagreement between Tamar Royalties and Isramco Negev 2 Limited Partnership has emerged as to whether certain items may be included in the calculation of payout. The disagreement largely stems from the fact that the agreements governing the creation of the Tamar Royalty were formulated in the 1980s and do not have a clear and unequivocal definition as to what costs should be included in the payout calculation. The Company currently believes that the total scope of the disagreement is approximately forty five million dollars (\$45,000,000). Under the terms of the agreements creating the Tamar Royalty, the dispute is subject to arbitration in Israel. The Company expects that the matter will be resolved through this arbitration process. However, the Company cannot be assured of a favorable result resulting from this arbitration process. Accordingly, the Company continues to receive royalty payments at the lower rates as if the Investment Repayment Date has not occurred.

Therefore, as a result of the dispute with the Isramco Negev 2, Tamar Royalties will have a shortfall in its Royalties Receivables for the period (or part of the period) between 1st April 2018 and 1st April 2019, by which time, even if the Isramco Negev 2's claims regarding the Investment Repayment Date are accepted, the Investment Repayment Date is expected to occur.

As a result, the Company believes Tamar Royalties required an additional \$15,600,000 USD to cover payments under the amortization schedule of the DB Facility (the "Shortfall"), and the Company believes that curing the Shortfall was in the best interest of both Isramco Inc. and Tamar Royalties. Therefore, Isramco Inc. contributed the expected amount of the Shortfall, being \$15,600,000 USD, to Tamar Royalties as an additional capital contribution and such contribution was made pursuant to the terms and conditions of that certain Consent and Agreement dated February 27, 2018, between and among Tamar Royalties, as Borrower, Deutsche Bank Trust Company Americas, as Facility Agent and Collateral Agent, and the Lenders party thereto. As a result of the aforementioned contribution, together with the terms and conditions of the aforementioned consent and assignment, Tamar Royalties remains in compliance with all covenants of the DB Facility.

On January 2, 2018, the Company made a payment in the amount of \$3,427,000 consisting of \$2,400,000 and \$1,027,000 in principal and interest respectively.

On April 2, 2018, the Company made a payment in the amount of \$6,479,000 consisting of \$5,400,000 and \$1,079,000 in principal and interest respectively.

On July 2, 2018, the Company made a payment in the amount of \$6,546,000 consisting of \$5,400,000 and \$1,146,000 in principal and interest respectively.

On October 2, 2018, the Company made a payment in the amount of \$6,796,000 consisting of \$5,700,000 and \$1,096,000 in principal and interest respectively.

The Company incurred debt costs in obtaining the facility in the amount of \$2,011,000. Additionally, the lenders retained \$2,959,000 in fees. These costs, totaling \$4,970,000, are recorded as a reduction of the principal loan balance and are being amortized over the life of the loan using the effective interest method. Amortization of these costs for the nine-month period ended September 30, 2018 and 2017 totaled \$622,000 and \$596,000 respectively.

As of September 30, 2018, Tamar Royalties was in compliance with the financial covenants required under the DB Facility.

#### The Société Générale Facility

On June 30, 2015, Isramco Onshore LLC (“Isramco Onshore”), a newly formed, wholly-owned, subsidiary of Isramco, Inc. (the “Company”), entered into a secured Credit Agreement (the “SG Facility”) with The Société Générale, as Administrative Agent and Issuing Lender, SG Americas Securities LLC, as Sole Bookrunner, Lead Arranger and Documentation Agent, and the lenders party thereto from time to time, as Lenders. The SG Facility provides for a commitment by The Société Générale of \$150,000,000, subject to an initial borrowing base of \$40,000,000. The tenor of the SG Facility was four (4) years and the SG Facility was secured by certain onshore United States oil and gas properties. Pricing under the SG Facility was as follows: (i) for EuroDollar Rate (as defined in the SG Facility) loans range from the EuroDollar rate plus 1.75% to the EuroDollar rate plus 2.75% depending on borrowing base utilization; and (ii) for Reference Rate (as defined in the SG Facility) loans ranges from the Reference Rate plus 0.75% to the Reference Rate Spread plus 1.75% based on borrowing base utilization; and (iii) a quarterly commitment fee (as defined in the SG Facility) ranging from an annual rate of 0.38% to 0.5% of the undrawn borrowing base.

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The SG Facility provided that Isramco Onshore hedge at least seventy-five percent (75%) of its crude oil production before borrowing under the SG Facility. As of March 31, 2018 and as of the date of issuance Isramco Onshore has not entered into such hedge agreements nor has it made a draw under the SG Facility. The Company incurred \$478,000 of financing costs in relation to this credit facility which were capitalized as a long-term asset and amortized over the term on the agreement on a straight-line basis until December 31, 2017 at which time the remaining balance totaling \$299,000 was expensed.

Isramco Onshore had various financial and operating covenants required by the SG Facility, including, among other things, the requirement that, during the term of the SG Facility, Isramco Onshore must have a Minimum Current Ratio (as defined in the SG Facility) of not less than 1.00:1.00, a Maximum Leverage Ratio (as defined in the SG Facility) of not less than 4.00:1.00 and a Minimum Interest Coverage Ratio (as defined in the SG Facility) of at least 2.50:1.00. In addition, the SG Facility provided for customary events of default, including, but not limited to, payment defaults, breach of representations or covenants, bankruptcy events and change of control.

On August 18, 2016, as a result of semi-annual borrowing base redetermination the borrowing base under SG Facility was reduced to zero. On February 28, 2017 the SG Facility was terminated.

### **Short-Term Debt**

As of September 30, 2018 and December 31, 2017 outstanding debt from short-term insurance financing agreements totaled \$0 and \$835,000 respectively. During the nine months ended September 30, 2018, the Company made cash payments totaling \$445,000.

### **Short-Term Debt – Related Party**

In September 2018 the Company issued an unsecured promissory note dated effective September 11, 2018, to I.O.C - Israel Oil Company LTD a related party in which the company may borrow up to \$7,000,000 at a rate of interest equal to seven and one-half percent (7.5%) and with a maturity date of September 2019. The company received \$2,800,000 under this related party note in September 2018 attendant with the creation of a new subsidiary, Arrow Midstream LLC. Amounts received under the aforementioned promissory note are dedicated to working capital and the purchase of equipment for Arrow Midstream LLC, a new wholly owned subsidiary of Isramco Inc. Arrow Midstream is focused on the transportation of liquefied petroleum products including, but not limited to, butane, propane, and similar products.

**Interest Expense**

The following table summarizes the amounts included in interest expense for the nine months ended September 30, 2018, and 2017:

	<b>Nine Months Ended</b>	
	<b>September 30,</b>	
	<b>2018</b>	<b>2017</b>
	<i>(In thousands)</i>	
Current debt, long-term debt and other - banks	\$3,768	\$3,611

**Note 6 - Tamar Field Proceeds**

We own an overriding royalty interest of 1.5375% in the Tamar Field, which will increase to 2.7375% after payout (collectively the "Tamar Royalty"). An overriding royalty interest is an ownership interest in the oil and gas leasehold estate equating to a certain percentage of production or production revenues, calculated free of the costs of production and development of the underlying lease(s), but subject to its proportionate share of certain post production costs. An overriding royalty interest is a non-possessory interest in the oil and gas leasehold estate and, accordingly, we have no control over the operations, drilling, expenses, timing, production, sales, or any other aspect of development or production of the Tamar Field. For additional information, please see the disclosure related to the Tamar Royalty set forth in the ITEM 1. BUSINESS section included in our Annual Report on Form 10-K for the year ended December 31, 2017, which disclosure is hereby incorporated herein by reference thereto.

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In 2009, two natural gas discoveries, known as “Tamar” and “Dalit”, were made within the area covered by the Michal and Matan Licenses, respectively. In December 2009, the Israeli Petroleum Commissioner granted Noble Energy, Inc. (“Noble”) and its partners, Isramco Negev 2-LP, Delek Drilling, Avner Oil & Gas, and Dor Gas (the “Tamar Consortium”), two leases (the “Leases”). The Leases are scheduled to expire in December 2038 and cover the Tamar and Dalit gas fields (collectively the “Tamar Field”). The Tamar Field is approximately 95 kilometers off the coast of the Israel, in the Israel exclusive economic zone of the Eastern Mediterranean, with a water depth of approximately 1,700 meters. On March 31, 2013 the Tamar Field commenced its initial production of the natural gas.

Since Isramco’s interest in the Tamar Field is an overriding royalty interest, there are no amounts capitalized with respect to Tamar Field.

During the nine months ended September 30, 2018, Tamar Field net sales attributable to Isramco amounted to 4,211,582 Mcf of natural gas and 5,532 Bbl of condensate with prices of \$5.50 per Mcf and \$65.72 per Bbl of condensate. Total revenues net of marketing and transportations expenses were \$23,414,000. The Israeli Tax Authority withheld \$5,385,000 of this revenue.

During the nine months ended September 30, 2017, Tamar Field net sales attributable to Isramco amounted to 4,058,476 Mcf of natural gas and 5,306 Bbl of condensate with prices of \$5.37 per Mcf and \$44.28 per Bbl of condensate. Total revenues net of marketing and transportations expenses were \$21,920,000. The Israeli Tax Authority withheld \$5,261,000 of this revenue.

With regard to the payout of the Tamar Field, a disagreement between the Company and Isramco Negev 2 Limited Partnership has emerged as to what costs should be included in the calculation of payout. In addition to actual costs for the development of the Tamar Field, Isramco, Negev 2 Limited Partnership has asserted that the following costs should be included in the calculation of payout: (i) Isramco Negev 2 Limited Partnership’s financing costs; (ii) the general and administrative expenses of Isramco Negev 2 Limited Partnership; (iii) the expected decommissioning costs of the Tamar Field; and (iv) expected future payments to be made in respect of the “Sheshinsky Levy” under Israeli law. In addition to the claim asserted by Isramco Negev 2 Limited Partnership, the Company has asserted counterclaims related to Isramco Negev 2 Limited Partnership’s inclusion into the payout calculation of charges related to gathering and transportation infrastructure. The disagreements primarily stem from the fact that the agreements governing the creation of the Tamar Royalty were formulated in the 1980s and do not have a clear and unequivocal definition as to what costs should be included in the payout calculation. The Company currently believes that the total scope of the claim asserted by Isramco Negev 2 Limited Partnership is approximately forty-five million dollars (\$45,000,000) and the counterclaims asserted by the Company have not been quantified. Under the terms of the agreements creating the Tamar Royalty, the dispute is subject to arbitration in Israel. The Company believes that the claims of Isramco Negev 2 Limited Partnership are erroneous and contrary to generally accepted industry practice. The Company expects that the matter will be favorably resolved through this arbitration process; however, the Company cannot be assured of a favorable result in this arbitration process.



## **Note 7 - Segment Information**

Isramco's primary business segments are vertically integrated within the oil and gas industry. These segments are separately managed due to distinct operational differences, unique technology, distribution and marketing requirements. The Company's two reporting segments are oil and gas exploration and production and production services. The oil and gas exploration and production segment explores for and produces natural gas, crude oil, condensate, and natural gas liquids ("NGLs"). The production services segment is engaged in rig-based and workover services, well completion and recompletion services, plugging and abandonment of wells and other ancillary oilfield services.

### **Oil and Gas Exploration and Production Segment**

Our Oil and Gas segment is engaged in the exploration, development and production of oil and natural gas properties located onshore in the United States and ownership of various royalty interests in oil and gas concessions located offshore Israel. We own varying working interests in oil and gas wells in Louisiana, Texas, New Mexico, Oklahoma, Wyoming, Utah and Colorado and currently serve as operator of approximately 422 producing wells located mainly in Texas in New Mexico.

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**Production Services Segment**

The Company began production services operations in October 2011. Our production servicing rig and truck fleet provides a range of production services, including the completion of newly-drilled wells, maintenance and workover of existing wells, fluid transportation, related oilfield services and plugging and abandonment of wells at the end of their useful lives to a diverse group of oil and gas exploration and production companies.

*Completion Service.* Newly drilled wells require completion services to prepare the well for production. Production servicing rigs are frequently used to complete newly drilled wells to minimize the use of higher cost drilling rigs in the completion process. The completion process may involve selectively perforating the well casing in the productive zones to allow oil or gas to flow into the well bore, stimulating and testing these zones, and installing the production string and other downhole equipment. The completion process typically ranges from a few days to several weeks, depending on the nature and type of the completion, and generally requires additional auxiliary equipment in addition to a production services rigs. The demand for completion services is directly related to drilling activity levels, which are sensitive to fluctuations in oil and gas prices.

*Well-servicing/Maintenance Services.* We provide maintenance services on the mechanical apparatus used to pump or lift oil from producing wells. These services include, among other activities, repairing and replacing pumps, sucker rods and tubing. We provide the rigs, equipment and crews for these tasks, which are performed on both oil and natural gas wells, but which are more commonly required on oil wells. Maintenance services typically take less than 48 hours to complete. Rigs generally are provided to customers on a call-out basis.

*Workover Services.* Producing oil and natural gas wells occasionally require major repairs or modifications, called “workovers.” Workovers may be required to remedy failures, modify well depth and formation penetration to capture hydrocarbons from alternative formations, clean out and recomplete a well when production has declined, repair leaks or convert a depleted well to an injection well for secondary or enhanced recovery projects. Workovers normally are carried out with pumps and tanks for drilling fluids, blowout preventers, and other specialized equipment for servicing rigs. A workover may last anywhere from a few days to several weeks.

*Fluid Services.* We own and operate 57 fluid service trucks equipped with an average fluid hauling capacity of up to 130 barrels a piece. Each fluid service truck is equipped to pump fluids from or into wells, pits, tanks and other storage facilities. The majority of our fluid service trucks are also used to transport water to fill frac tanks on well locations, to transport produced salt water to disposal wells, and to transport drilling and completion fluids to and from well locations.

*Plugging & Abandonment Services.* Production servicing rigs are also used in the process of permanently closing oil and gas wells no longer capable of producing in economic quantities. Many well operators bid for this work on a “turnkey” basis, requiring the service company to perform the entire job, including the sale or disposal of equipment salvaged from the well as part of the compensation received, and complying with state regulatory requirements. Plugging and abandonment work can provide favorable operating margins and is less sensitive to oil and gas pricing

than drilling and workover activity since well operators must plug a well in accordance with state regulations when it is no longer productive. We perform plugging and abandonment work throughout our core areas of operation in conjunction with equipment provided by us or by other service companies.

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We typically bill clients for our production servicing on an hourly basis for the period that the rig is actively working. As of September 30, 2018, our fleet of production servicing rigs totaled 33 rigs, which we operate through 5 locations in Texas and New Mexico.

	<b>Oil and Gas</b>			
<i>(in thousands)</i>	<b>Exploration</b>	<b>Production</b>	<b>Eliminations</b>	<b>Total</b>
	<b>&amp;</b>	<b>Services</b>		
	<b>Production</b>			
<b>Three Months Ended September 30, 2018:</b>				
<b>Sales revenues</b>				
United States	\$ 4,215	\$ 9,420	\$ -	\$13,635
Israel	8,440	-	-	8,440
Intersegment revenues	-	132	(132 )	-
Office services and other	801	-	(30 )	771
<b>Total revenues and other</b>	<b>13,456</b>	<b>9,552</b>	<b>(162 )</b>	<b>22,846</b>
<b>Operating costs and expenses</b>	<b>3,842</b>	<b>8,853</b>	<b>(162 )</b>	<b>12,533</b>
Depreciation, depletion, and amortization	563	884	-	1,447
Interest expenses, net	(56 )	1,274 )	-	1,218
Gain on derivative contracts	(186 )	-	-	(186 )
Other income, net	-	-	-	-
<b>Total expenses and other</b>	<b>4,163</b>	<b>11,011</b>	<b>(162 )</b>	<b>15,012</b>
Income (loss) before income taxes	\$ 9,293	\$ (1,459 )	\$ -	\$7,834
<b>Net Income (loss)</b>	<b>7,080</b>	<b>(1,187 )</b>	<b>-</b>	<b>5,893</b>
Net loss attributable to noncontrolling interests	-	(285 )	-	(285 )
Net income (loss) attributable to Isramco	7,080	(902 )	-	6,178
<b>Total Assets</b>	<b>\$ 65,300</b>	<b>\$ 49,545</b>	<b>\$ -</b>	<b>\$114,845</b>
<b>Expenditures for Long-lived Assets</b>	<b>\$ 196</b>	<b>\$ 3,070</b>	<b>\$ -</b>	<b>\$3,266</b>

	<b>Oil and Gas</b>			
<i>(in thousands)</i>	<b>Exploration</b>	<b>Production</b>	<b>Eliminations</b>	<b>Total</b>
	<b>&amp;</b>	<b>Services</b>		
	<b>Production</b>			
<b>Three Months Ended September 30, 2017:</b>				
<b>Sales revenues</b>				
United States	\$ 3,597	\$ 5,073	\$ -	\$8,670
Israel	7,626	-	-	7,626
Office services and other	308	-	(30 )	278

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Total revenues and other	11,531	5,073	(30	)	16,574
Operating costs and expenses	3,798	4,806	(30	)	8,574
Depreciation, depletion, and amortization	762	778	-		1,540
Interest expenses, net	227	989	-		1,216
Loss on derivative contracts	225	-	-		225