

ACORN ENERGY, INC.  
Form 10-Q  
August 09, 2012  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q  
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2012

Commission file number: 0-19771

ACORN ENERGY, INC.  
(Exact name of registrant as specified in charter)

Delaware  
(State or other jurisdiction of incorporation or  
organization)

22-2786081  
(I.R.S. Employer Identification No.)

3903 Centerville Road, Wilmington, Delaware  
(Address of principal executive offices)

19807  
(Zip Code)

302-656-1707  
(Registrant's telephone number, including area code)

4 West Rockland Road, Montchanin, Delaware 19710  
(Former address)

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 2, 2012
Common Stock, \$0.01 par value per share	17,926,752 shares

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ACORN ENERGY, INC.  
 Quarterly Report on Form 10-Q  
 for the Quarterly Period Ended June 30, 2012

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Certain statements contained in this report are forward-looking in nature. These statements are generally identified by the inclusion of phrases such as “we expect”, “we anticipate”, “we believe”, “we estimate” and other phrases of similar

meaning. Whether such statements ultimately prove to be accurate depends upon a variety of factors that may affect our business and operations. Many of these factors are described in our most recent Annual Report on Form 10-K as filed with Securities and Exchange Commission.

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## PART I

ACORN ENERGY, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)  
 (IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	As of December 31, 2011	As of June 30, 2012
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$34,280	\$14,753
Short-term deposits	18,000	18,015
Restricted deposit	2,223	1,888
Funds held in escrow	5,961	5,961
Accounts receivable	4,965	4,476
Unbilled revenue	3,778	3,997
Inventory	2,144	2,652
Other current assets	922	2,765
Total current assets	72,273	54,507
Property and equipment, net	635	842
Severance assets	2,620	2,716
Restricted deposit	271	269
Intangible assets, net	4,780	10,056
Goodwill	4,637	6,562
Deferred taxes	440	423
Other assets	149	99
Total assets	\$85,805	\$75,474
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Short-term bank credit and current maturities of long-term debt	\$677	\$149
Accounts payable	2,052	2,164
Accrued payroll, payroll taxes and social benefits	1,907	2,139
Deferred revenue	2,876	1,597
Other current liabilities	4,544	3,139
Total current liabilities	12,056	9,188
Long-term liabilities:		
Accrued severance	3,837	3,949
Long-term debt	141	75
Other long-term liabilities	204	210
Total long-term liabilities	4,182	4,234
Commitments and contingencies		
Equity:		
Acorn Energy, Inc. shareholders		
Common stock - \$0.01 par value per share:		



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Authorized – 30,000,000 shares; Issued –18,325,529 and 18,728,672 shares at December 31, 2011 and June 30, 2012, respectively	183	187
Additional paid-in capital	84,614	84,244
Warrants	427	55
Accumulated deficit	(13,022	) (20,312
Treasury stock, at cost – 801,920 shares at December 31, 2011 and June 30, 2012	(3,036	) (3,036
Accumulated other comprehensive income	485	484
Total Acorn Energy, Inc. shareholders' equity	69,651	61,622
Non-controlling interests	(84	) 430
Total equity	69,567	62,052
Total liabilities and equity	\$85,805	\$75,474

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

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ACORN ENERGY, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)  
(IN THOUSANDS, EXCEPT NET INCOME (LOSS) PER SHARE DATA)

declare all borrowings outstanding, together with accrued and unpaid interest, to be immediately due and payable; or

require us to apply all of our available cash to repay the borrowings.

If we were unable to repay or otherwise refinance these borrowings when due, we cannot assure you that sufficient assets will remain to repay the 9.75% Senior Notes.

**Our internal controls for financial reporting and our disclosure controls and procedures may not prevent all possible errors that could occur.**

Our Chief Executive Officer and Chief Financial Officer evaluate on a quarterly basis our internal controls for financial reporting and our disclosure controls and procedures, which includes a review of the objectives, design, implementation and effect of the controls in respect of the information generated for use in our periodic reports. In the course of our controls evaluation, we seek to identify data errors, control problems and to confirm that appropriate corrective action, including process improvements, were being undertaken. The overall goals of these various evaluation activities are to monitor our internal controls for financial reporting and our disclosure controls and procedures and to make modifications as necessary. Our intent in this regard is that our internal controls for financial reporting and our disclosure controls and procedures will be maintained as dynamic systems that change (including with improvements and corrections) as conditions warrant.

A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be satisfied. Our management has concluded that our internal controls for financial reporting and our disclosure controls and procedures are designed to give a reasonable assurance that they are effective to achieve their objectives. We cannot provide absolute assurance that we have detected all possible control issues. These inherent limitations include the possibility that judgments in our decision-making could be faulty, and that isolated breakdowns could occur because of simple human error or mistake. The design of our system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed absolutely in achieving our stated goals under all potential future or unforeseeable conditions. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud could occur and not be detected. Breakdowns in our internal controls and procedures could occur in the future, and any such breakdowns could have an adverse effect on us.

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

Our corporate headquarters are located at 10811 South Westview Circle Drive, Suite 100, Building C, Houston, Texas 77043, which also serves as administrative and financial offices and warehouse space and storage. We maintain domestic marketing offices in Denver, Colorado and New Orleans, Louisiana. We also lease office and warehouse space in two separate locations in Calgary, Alberta, Canada, where our Canadian operations are headquartered. We consider our business facilities adequate and suitable for our present and anticipated future needs, but may seek to expand our facilities from time to time.

The following table sets forth the locations of our offices and warehouses, the approximate square footage of space we maintain at such locations, our use of such space and whether it is owned or leased by us.

Location	Approximate Square Footage	Use	Owned/Leased
Houston, Texas	80,125	Administrative; Financial; Marketing; Operations; Warehouse	Leased
Denver, Colorado	1,513	Marketing	Leased
New Orleans, Louisiana	364	Marketing	Leased
Calgary, Alberta, Canada	23,270	Administrative; Financial; Marketing; Operations	Leased
Calgary, Alberta, Canada	42,985	Warehouse	Leased

**Item 3. Legal Proceedings**

We are involved from time to time in ordinary, routine claims and lawsuits incidental to our business. In the opinion of management, uninsured losses, if any, resulting from the ultimate resolutions of these matters should not be material to our financial position or results of operations. However, it is not possible to predict or determine the outcomes of the legal actions brought against us or by us, or to provide an estimate of all additional losses, if any, that may arise. At December 31, 2010, we did not have any amounts accrued related to litigation claims.

**Item 4. Reserved**

**PART II**

**Item 5. Market for Registrant's Common Equity, Securities Related Stockholder Matters and Issuer Purchases of Equity Market Information**

Our common stock is privately held and there is no established public trading market for our common stock. As of December 31, 2010, there was one holder of record of our 100 shares of common stock, \$0.001 par value.



**Dividend Policy**

We have not declared or paid any cash dividends on our common stock during our two most recent fiscal years. We do not intend to declare or pay any cash dividends on our common stock in the foreseeable future. Covenants within our 9.75% Senior Notes restrict our ability to pay cash dividends on our capital stock. Future declaration and payment of cash dividends, if any, on our common stock will be determined in light of factors deemed relevant by our board of directors, including our earnings, operations, capital requirements and financial condition and restrictions in our financing agreements.

**Item 6. Selected Consolidated Financial Data (In Thousands)**

As a result of the Merger, which was completed on February 14, 2007, our capital structure and our basis of accounting differ from those prior to the Merger. Our financial data in respect of all reporting periods after February 13, 2007 reflect the Merger under the purchase method of accounting. The financial information for the periods before the Merger is referred to as Predecessor Period and financial information for the periods after the Merger is referred to as the Successor Period. The adjustments to our assets and liabilities as a result of the Merger have impacted net income subsequent to the Merger. The increase in the basis of the assets has resulted in non-cash charges in periods subsequent to the Merger, principally related to the step-up in the value of our seismic data library and other intangible assets. The book value of our seismic data library was increased by approximately \$275.2 million to its then fair market value of \$395.6 million. As a result of this step up in value and of our maximum four-year straight-line amortization of seismic data, our data amortization expense has increased in the Successor Period. In addition, we recorded identifiable intangible assets with a fair value of \$53.4 million of which \$52.5 million is amortizable over their useful lives ranging from 1 to 10 years. As a result of this step up in value, amortization expense of acquired intangible assets has increased in the Successor Period.

The following table summarizes certain historical consolidated financial data of Seitel and is qualified in its entirety by the more detailed consolidated financial statements and notes thereto included herein.

	SUCCESSOR PERIOD			Feb. 14, 2007- Dec. 31, 2007	PREDECESSOR PERIOD	
	Year Ended December 31,				Jan. 1, 2007 - Feb. 13, 2007	Year Ended Dec. 31, 2006
	2010	2009	2008			
<b>Statement of Operations Data:</b>						
Revenue	\$ 175,556	\$ 115,345	\$ 172,403	\$ 129,802	\$ 19,010	\$ 191,919
<b>Expenses and costs:</b>						
Depreciation and amortization	175,592	150,199	168,629	146,072	11,485	88,662
Impairment of intangible asset			225			
Gain on sale of seismic data						(231)
Cost of sales	97	290	462	218	8	234
Selling, general and administrative	31,831	25,090	36,316	33,393	3,577	35,930
Merger			357	2,657	17,457	1,449
	207,520	175,579	205,989	182,340	32,527	126,044
Income (loss) from operations	(31,964)	(60,234)	(33,586)	(52,538)	(13,517)	65,875
Interest expense, net	(40,536)	(40,696)	(40,017)	(38,844)	(2,284)	(19,520)
Foreign currency exchange gains (losses)	441	1,008	(4,059)	3,173	(102)	259
Gain on sale of marketable securities	4,188					27
Other income	446	151	40	39	12	

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Income (loss) from continuing operations before income taxes	(67,425)	(99,771)	(77,622)	(88,170)	(15,891)	46,641
Provision (benefit) for income taxes	(4,008)	(2,974)	(3,548)	(11,057)	452	(715)
Income (loss) from continuing operations	(63,417)	(96,797)	(74,074)	(77,113)	(16,343)	47,356
Loss from discontinued operations, net of tax						(142)
Net income (loss)	\$ (63,417)	\$ (96,797)	\$ (74,074)	\$ (77,113)	\$ (16,343)	\$ 47,214

	SUCCESSOR PERIOD				PREDECESSOR PERIOD
	2010	2009	As of December 31,		2006
			2008	2007	
<b>Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 89,971	\$ 26,270	\$ 42,678	\$ 43,443	\$ 107,495
Seismic data library, net	106,104	200,389	279,257	349,039	123,123
Total assets	491,009	522,019	643,825	743,101	305,435
Total debt	405,604	405,732	405,499	406,481	189,038
Stockholder's equity (deficit)	(7,022)	46,361	115,785	220,958	37,491
Common shares outstanding	100	100	100	100	155,184

**Item 7. Management's Discussion and Analysis Of Financial Condition And Results Of Operations**

The following discussion should be read in conjunction with our consolidated financial statements and the related notes to the financial statements included elsewhere in this document.

**Overview**

**General**

Our products and services are used by oil and gas companies to assist in oil and gas exploration and development and management of hydrocarbon reserves. We own an extensive library of onshore and offshore seismic data that we offer for license to oil and gas companies. Oil and gas companies use seismic data in oil and gas exploration and development efforts to increase the probability of drilling success. We believe that our library of onshore seismic data is the largest available for licensing in North America. We generate revenue primarily by licensing data from our data library and from new data creation products, which are substantially underwritten or paid for by our clients. By participating in underwritten, nonexclusive surveys or purchasing licenses to existing data, oil and gas companies can obtain access to surveys at reduced costs as compared to acquiring seismic data on a proprietary basis.

Our primary areas of focus are onshore United States and Canada and, to a lesser extent, offshore U.S. Gulf of Mexico. These markets continue to experience major changes. Major integrated oil and gas companies and national oil companies have become more active in the U.S. market, primarily in the resource plays, through joint ventures, asset purchases and corporate transactions. The larger independent oil and gas companies continue to be responsible for a significant portion of current U.S. drilling activity. Our offshore seismic data is primarily located in the shallow waters of the U.S. Gulf of Mexico and generates a small percentage of our revenue.

Our clients continue to seek our services to create data in the United States and Canada. On March 10, 2011, our clients' commitment for underwriting on new data creation projects was \$64.0 million. Licensing data "off the shelf" does not require the longer planning and lead times like new data creation and thus is more likely to fluctuate quarter to quarter.

In 2010, we experienced a recovery in demand for our seismic data, principally in the unconventional resource plays. We expect increased demand in the oil-rich plays and liquids-rich natural gas plays while activity in natural gas shales is expected to remain steady.

**Principal Factors Affecting Our Business**

Our business is dependent upon a variety of factors, many of which are beyond our control. The following are those that we consider to be principal factors affecting our business.

**Demand for Seismic Data:** Demand for our products and services is cyclical due to the nature of the oil and gas industry. In particular, demand for our seismic data services depends upon exploration, production, development and field management spending by oil and gas companies and, in the case of new data creation, the willingness of these companies to forgo ownership in the seismic data. Capital expenditures by oil and gas companies depend upon several factors, including actual and forecasted oil and natural gas commodity prices, prospect availability and the companies' own short-term and strategic plans. These capital expenditures may also be affected by worldwide economic or industry-wide conditions. The 2009 economic downturn resulted in lower commodity prices and reduced exploration capital expenditures, which, in turn, caused demand for seismic data to decline. Demand for seismic data improved in 2010, primarily in the unconventional resource plays; however, there continues to be uncertainty as to the impact on demand for seismic data in conventional areas.

**Availability of Capital for Our Customers:** Some of our customers are independent oil and gas companies and private prospect-generating companies that rely primarily on private capital markets to fund their exploration, production, development and field management activities. The reduction in cash flows being experienced by our customers resulting from lower commodity prices, along with the reduced availability of credit and increased costs of borrowing due to the tightening of the credit markets, could have a material impact on the ability of such companies to obtain funding necessary to purchase our seismic data.

**Merger and Acquisition Activity:** Merger and acquisition activity continues to occur within our client base. This activity could have a negative impact on seismic companies that operate in markets with a limited number of participating clients. However, we believe that, over time, this activity could have a positive impact on our business, as it should generate re-licensing fees, result in increased vitality in the trading of mineral interests and result in the creation of new independent customers through the rationalization of staff within those companies affected by this activity.

**North America Drilling Activity:** The 2009 economic downturn in North America resulted in reduced demand for natural gas that led to lower hydrocarbon prices resulting in a decrease in drilling activity in the first part of 2009 with land rig counts in North America reaching a low in May 2009. North America land drilling activity has been recovering since then, primarily driven by activity in domestic resource plays. However, weaker than expected natural gas prices and continued low domestic natural gas demand continue to cause uncertainty as to full recovery of conventional gas exploration.

**Government Regulation:** Our operations are subject to a variety of federal, provincial, state, foreign and local laws and regulations, including environmental and health and safety laws. We invest financial and managerial resources to comply with these laws and related permit requirements. Modification of existing laws or regulations and the adoption of new laws or regulations limiting or increasing exploration or production activities by oil and gas companies may have a material effect on our business operations.

### Non-GAAP Key Performance Measures

Management considers certain performance measures in evaluating and managing our financial condition and operating performance at various times and from time to time. Some of these performance measures are non-GAAP financial measures. Generally, a non-GAAP financial measure is a numerical measure of a company's performance, financial position or cash flows that either excludes or includes amounts that are not normally excluded or included in the most directly comparable measure calculated and presented in accordance with United States generally accepted accounting principles, or GAAP. These non-GAAP measures are not in accordance with, nor are they a substitute for, GAAP measures. These non-GAAP measures are intended to supplement our presentation of our financial results that are prepared in accordance with GAAP.

The following are the key performance measures considered by management.

#### Cash Resales

Cash resales represent new contracts for data licenses from our library, including data currently in progress, payable in cash. We believe this measure is important in gauging new business activity. We expect cash resales to generally follow a consistent trend over several quarters, while considering our normal seasonality. Volatility in this trend over several consecutive quarters could indicate changing market conditions.

The following is a reconciliation of this non-GAAP financial measure to the most directly comparable GAAP financial measure, total revenue (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Cash resales	\$ 137,605	\$ 49,268	\$ 117,305
Other revenue components:			
Acquisition revenue	40,500	37,403	55,990
Non-monetary exchanges	4,678	1,764	7,625
Revenue recognition adjustments	(11,005)	22,386	(15,060)
Solutions and other	3,778	4,524	6,543
<b>Total revenue</b>	<b>\$ 175,556</b>	<b>\$ 115,345</b>	<b>\$ 172,403</b>

**Cash EBITDA**

Cash EBITDA represents cash generated from licensing data from our seismic library net of recurring cash operating expenses. We believe this measure is helpful in determining the level of cash from operations we have available for debt service and funding of capital expenditures (net of the portion funded or underwritten by our customers). Cash EBITDA includes cash resales plus all other cash revenues other than from data acquisitions and gains on sales of marketable securities obtained as part of licensing our seismic data, less cost of goods sold and cash selling, general and administrative expenses (excluding non-recurring corporate expenses such as merger and acquisition transaction costs and severance costs).

The following is a quantitative reconciliation of this non-GAAP financial measure to the most directly comparable GAAP financial measure, operating loss (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Cash EBITDA	\$ 117,252	\$ 32,868	\$ 93,791
Add (subtract) other revenue components not included in cash EBITDA:			
Acquisition revenue	40,500	37,403	55,990
Non-monetary exchanges	4,678	1,764	7,625
Revenue recognition adjustments	(11,005)	22,386	(15,016)
Less:			
Gain on sale of marketable securities	(4,188)		
Depreciation and amortization	(175,592)	(150,199)	(168,629)
Impairment of intangible asset			(225)
Merger expenses			(357)
Merger and acquisition transaction costs			(6)
Severance and one-time costs associated with cost reduction measures	(176)	(1,170)	
Non-cash operating expenses	(3,433)	(3,286)	(6,759)
Operating loss	\$ (31,964)	\$ (60,234)	\$ (33,586)

**Growth of our Seismic Data Library**

We regularly add to our seismic data library through four different methods: (1) recording new data; (2) buying ownership of existing data for cash; (3) obtaining ownership of existing data sets through non-monetary exchanges; and (4) creating new value-added products from existing data within our library. For the years ended December 31, 2010, 2009 and 2008, we completed the addition of approximately 900 square miles, 700 square miles and 2,700 square miles, respectively, of seismic data to our library. For the period from January 1, 2011 to March 10, 2011 we completed the addition of approximately 300 square miles and as of March 10, 2011 we had approximately 1,900 square miles of seismic data in progress.

**Critical Accounting Policies**

We operate in one business segment, which is made up of seismic data acquisition, seismic data licensing, seismic data processing and seismic reproduction services.

We prepare our financial statements and the accompanying notes in conformity with GAAP, which requires management to make estimates and assumptions about future events that affect the reported amounts in the financial statements and the accompanying notes. We identify certain accounting policies as critical based on, among other things, their impact on the portrayal of our financial condition and results of operations and the degree of difficulty, subjectivity and complexity in their deployment. Notes B and C of the notes to the consolidated financial statements include a summary of the significant accounting policies used in the preparation of the accompanying consolidated financial statements. The following is a brief discussion of our most critical accounting policies.

## Revenue Recognition

### *Revenue from Data Acquisition*

We generate revenue when we create a new seismic survey that is initially licensed by one or more of our customers to use the resulting data. The initial licenses may provide the customer with a limited exclusivity period. We consider the contracts signed up to the time we make a firm commitment to create the new seismic survey as underwriting. Underwriting revenue is recognized throughout the creation period using the proportional performance method based upon costs incurred and work performed to date as a percentage of total estimated costs and work required. Management believes that this method is the most reliable and representative measure of progress for our data creation projects. The customers paying for the initial exclusive licenses receive legally enforceable rights to any resulting product of the specific activities required to complete the survey. The customers also receive access to and use of the newly acquired, processed data.

### *Revenue from Non-Exclusive Data Licenses*

We recognize a substantial portion of our revenue from data licenses sold after any exclusive license period. Revenue from the non-exclusive licensing of seismic data is recognized when the following criteria are met:

we have an arrangement with the customer that is validated by a signed contract;

the sales price is fixed and determinable;

collection is reasonably assured;

the customer has selected the specific data or the contract has expired without full selection;

the data is currently available for delivery; and

the license term has begun.

Copies of the data are available to the customer immediately upon request.

For licenses that have been invoiced for which payment is due or has been received, but have not met the aforementioned criteria, the revenue is deferred along with the related direct costs (primarily sales commissions). This normally occurs under the library card, review and possession or review only license contracts because the data selection may occur over time. Additionally, if the contract allows licensing of data that is not currently available or enhancements, modifications or additions to the data are required per the contract, revenue is deferred until such time that the data is available.

### *Revenue from Non-Monetary Exchanges*

In certain cases, we will take ownership of a customer's seismic data or revenue interest (collectively referred to as "data") or receive advanced data processing services in exchange for a non-exclusive license to selected seismic data from our library or as partial consideration for the underwriting of new data acquisition. These exchanges are referred to as non-monetary exchanges. In non-monetary exchange transactions, we record a data library asset for the data received or processed at the time the contract is entered into or the data is completed, as applicable, and recognize revenue on the transaction in equal value in accordance with our policy on revenue from data licenses, that is, when the seismic data is selected by the customer, or revenue from data acquisition, as applicable. These transactions are valued at the fair value of the data received or delivered, whichever is more readily determinable.

## Seismic Data Library

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Costs associated with creating, acquiring or purchasing seismic data are capitalized and amortized principally on the income forecast method subject to a straight-line amortization period of four years, applied on a quarterly basis at the individual survey level.

### ***Data Library Amortization***

We amortize our seismic data library using the greater of the amortization that would result from the application of the income forecast method (subject to a minimum amortization rate) or a straight-line basis over the useful life of the data. Due to the subjectivity inherent in the income forecast amortization method, this amortization

policy ensures a minimum level of amortization will be recorded if sales of the specific data do not occur as expected and ensures that costs are fully amortized at the end of the data's useful life. With respect to each survey in the data library, the straight-line policy is applied from the time such survey is available for licensing to customers on a non-exclusive basis, since some data in the library may not be licensed until an exclusivity period has lapsed.

We apply the income forecast method by forecasting the ultimate revenue expected to be derived from a particular data library component over the estimated useful life of each survey comprising part of such component. We make this forecast annually and review it quarterly. If, during any such review, we determine that the ultimate revenue for a library component is expected to be significantly different than the original estimate of total revenue for such library component, we revise the amortization rate attributable to future revenue from each survey in such component.

The greater of the income forecast or straight-line amortization policy is applied quarterly on a cumulative basis at the individual survey level. Under this policy, we first record amortization using the income forecast method. The cumulative amortization recorded for each survey is then compared with the cumulative straight-line amortization. If the cumulative straight-line amortization is higher for any specific survey, additional amortization expense is recorded, resulting in accumulated amortization being equal to the cumulative straight-line amortization for such survey. This requirement is applied regardless of future-year revenue estimates for the library component of which the survey is a part and does not consider the existence of deferred revenue with respect to the library component or to any survey.

### ***Seismic Data Library Impairment***

We evaluate our seismic data library for impairment by grouping individual surveys into components based on our operations and geological and geographical trends. We believe that these library components constitute the lowest levels of independently identifiable cash flows. We evaluate our seismic data library investment for impairment whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. We consider the level of sales performance in each component compared to projected sales, as well as industry conditions, among others, to be key factors in determining when our seismic data should be evaluated for impairment. In evaluating sales performance of each component, we generally consider five consecutive quarters of actual performance below forecasted sales to be an indicator of potential impairment.

The impairment evaluation is based first on a comparison of the undiscounted future cash flows over each component's remaining estimated useful life with the carrying value of each library component. If the undiscounted cash flows are equal to or greater than the carrying value of such component, no impairment is recorded. If undiscounted cash flows are less than the carrying value of any component, the forecast of future cash flows related to such component is discounted to fair value and compared with such component's carrying amount. The difference between the library component's carrying amount and the discounted future value of the expected revenue stream is recorded as an impairment charge.

For purposes of evaluating potential impairment losses, we estimate the future cash flows attributable to a library component by evaluating, among other factors, historical and recent revenue trends, oil and gas prospectivity in particular regions, general economic conditions affecting our customer base, expected changes in technology and other factors that we deem relevant. The cash flow estimates exclude expected future revenues attributable to non-monetary data exchanges and future data creation projects.

The estimation of future cash flows and fair value is highly subjective and inherently imprecise. Estimates can change materially from period to period based on many factors, including those described in the preceding paragraph. Accordingly, if conditions change in the future, we may record impairment losses relative to our seismic data library, which could be material to any particular reporting period.

### **Business Acquisitions and Goodwill**

We account for acquired businesses using the purchase method of accounting which requires that the assets acquired and liabilities assumed be recorded at the date of acquisition at their respective fair values. The cost to acquire a business is allocated to the underlying net assets of the acquired business in proportion to their respective fair values. Any excess of the purchase price over the estimated fair values of the net assets acquired is recorded as goodwill.

Goodwill is tested annually for impairment at the reporting unit level. If an indication of impairment exists, we are required to determine if such reporting unit's implied fair value is less than its carrying value in order to determine the amount, if any, of the impairment loss required to be recorded. Subsequent to the Merger, we established October 1 as our annual impairment testing date.

### Use of Estimates and Assumptions

In preparing our financial statements, a number of estimates and assumptions are made by management that affect the accounting for and recognition of assets, liabilities, revenues and expenses. These estimates and assumptions must be made because certain information that is used in the preparation of our financial statements is dependent on future events, cannot be calculated with a high degree of precision from data available or is not otherwise capable of being readily calculated based on generally accepted methodologies. In some cases, these estimates are particularly difficult to determine and we must exercise significant judgment.

The most difficult, subjective and complex estimates and assumptions that deal with the greatest amount of uncertainty are related to our accounting for our seismic data library and goodwill.

Accounting for our seismic data library requires us to make significant subjective estimates and assumptions relative to future sales and cash flows from such library. These cash flows impact amortization rates, as well as potential impairment charges. Any changes in these estimates or underlying assumptions will impact our income from operations prospectively from the date changes are made. To the extent that such estimates, or the assumptions used to make those estimates, prove to be significantly different than actual results, the carrying value of the seismic data library may be subject to higher prospective amortization rates, additional straight-line amortization or impairment losses.

Because we apply a minimum income forecast amortization rate of 70%, the effect of decreasing future sales by 10%, with all other factors remaining constant, would not increase amortization rates from 70% as of January 1, 2011. The effect of decreasing future sales by 20%, with all other factors remaining constant, would cause the range of amortization rates to be from 70% to 79% as of January 1, 2011.

In a portion of our seismic data library activities, we engage in certain non-monetary exchanges and record a data library asset for the seismic data received and recognize revenue on the transaction in accordance with our policy on revenue from data licenses or revenue from data acquisition, as applicable. These transactions are valued at the fair value of the data received by us or licenses granted by us, whichever is more readily determinable. In addition, we obtain third-party concurrence on the portfolio of all non-monetary exchanges for data of \$750,000 or more in order to support our estimate of the fair value of the transactions. Our estimate of the value of these transactions is highly subjective and based, in large part, on data sales transactions between us and a limited number of customers over a limited time period, and appraisals of the value of such transactions based on a relatively small market of private transactions over a limited period of time.

For our estimates of the fair value of goodwill, we prepare discounted cash flow analysis, which requires significant judgments and estimates about our future performance. If these projected cash flows change materially, we may be required to record impairment losses relative to goodwill.

Actual results could differ materially from the estimates and assumptions that we use in the preparation of our financial statements. To the extent management's estimates and assumptions change in the future, the effect on our reported results could be significant to any particular reporting period.

## Results of Operations

### Revenue

The following table summarizes the components of our revenue for the years ended December 31, 2010, 2009 and 2008 (in thousands):

	Year Ended December 31,		
	2010	2009	2008
<b>Acquisition revenue:</b>			
Cash underwriting	\$ 37,823	\$ 34,565	\$ 41,511
Underwriting from non-monetary exchanges	2,677	2,838	14,479
<b>Total acquisition revenue</b>	<b>40,500</b>	<b>37,403</b>	<b>55,990</b>
<b>Resale licensing revenue:</b>			
Cash resales	137,605	49,268	117,305
Non-monetary exchanges	4,678	1,764	7,625
Revenue recognition adjustments	(11,005)	22,386	(15,060)
<b>Total resale licensing revenue</b>	<b>131,278</b>	<b>73,418</b>	<b>109,870</b>
<b>Total seismic revenue</b>	<b>171,778</b>	<b>110,821</b>	<b>165,860</b>
<b>Solutions and other</b>	<b>3,778</b>	<b>4,524</b>	<b>6,543</b>
<b>Total revenue</b>	<b>\$ 175,556</b>	<b>\$ 115,345</b>	<b>\$ 172,403</b>

Total revenue was \$175.6 million for the year ended December 31, 2010 compared to \$115.3 million for the year ended December 31, 2009. This \$60.2 million, or 52%, increase was primarily due to an increase in total resale licensing revenue. Acquisition revenue increased from \$37.4 million in 2009 to \$40.5 million in 2010, with the second half of 2010 reflecting resumed acquisition activity in both the U.S. and Canada following reduced activity in 2009 caused by the economic downturn. Acquisition revenue in 2010 related to resource plays in the Haynesville area in east Texas, the Eagle Ford area in south Texas and the Niobrara area in Colorado, as well as the Montney and Horn River areas in Canada. Total resale licensing revenue was \$131.3 million in 2010 compared to \$73.4 million in 2009. The \$57.9 million or 79% increase in total resale licensing revenue reflected increased activity by our clients resulting from improving industry conditions and an increase in drilling activity in North America. Cash resales were \$137.6 million in 2010, up 179% compared to \$49.3 million in 2009. Cash resales attributable to 3D data located in unconventional resource plays increased 261% from 2009 to 2010 while cash resales related to conventional 3D data increased 114% during the same period. For the year ended December 31, 2010, 68% of our cash resales were from resource plays with the remaining 32% from conventional 3D, 2D and offshore data. This compares to 53% and 47%, respectively, for the year ended December 31, 2009. Non-monetary exchanges fluctuate year to year depending upon the data available for trade and totaled \$4.7 million in 2010 compared to \$1.8 million in 2009. Revenue recognition adjustments are non-cash adjustments to revenue and reflect the net amount of (i) revenue deferred as a result of all of the revenue recognition criteria not being met and (ii) the subsequent revenue recognition once the criteria are met. In 2010, the deferral of new licensing contracts exceeded the amount of revenue recognized from previously deferred contracts primarily as a result of cash resales on data that are still in the acquisition phase requiring deferral since the data products are not yet available for delivery as well as an increase in the value of library card contracts entered into in the period. Solutions and other revenue decreased \$0.7 million in 2010 compared to 2009 due to the completion of a data management project in 2009 and due to the mix of seismic revenue and the types of products delivered.

Total revenue was \$115.3 million for the year ended December 31, 2009 compared to \$172.4 million for the year ended December 31, 2008. This \$57.1 million, or 33.1%, decline was due to a decrease in acquisition revenue and lower total resale licensing revenue. Acquisition revenue decreased in both the U.S. and Canada from \$56.0 million in 2008 to \$37.4 million in 2009 because of our planned reduction in new data acquisition resulting from the poor industry conditions and economic uncertainty in 2009. Total resale licensing revenue was \$73.4 million in 2009 compared to \$109.9 million in 2008. Resale licensing revenue in 2009 was impacted by weak natural gas prices and the slowdown in drilling activity in North America with oil and gas companies curtailing their exploration and development spending as compared to 2008. Cash resales were \$49.3 million in 2009, down



58% compared to \$117.3 million in 2008, as clients' general concerns about the economic environment and liquidity delayed spending on seismic data. For the year 2009, core cash resales (U.S. 3D and Canada 2D and 3D data) were \$46.0 million, down 56% from the 2008 level of \$104.2 million. Non-core cash resales (U.S. 2D and offshore data) decreased 75% from \$13.1 million in 2008 to \$3.3 million in 2009. Non-monetary exchanges fluctuate year to year depending upon the data available for trade and totaled \$1.8 million in 2009 compared to \$7.6 million in 2008. Revenue recognition adjustments fluctuated between 2009 and 2008 resulting from a reduction in deferrals related to new contracts due to a fewer amount of library card contracts entered into in 2009 as compared to 2008. Solutions and other revenue decreased from \$6.5 million in 2008 to \$4.5 million in 2009 primarily resulting from the lower level of seismic revenue and the types of products delivered.

At December 31, 2010, we had a deferred revenue balance of \$37.1 million compared to the December 31, 2009 balance of \$26.7 million. The deferred revenue balance was related to (i) data licensing contracts on which selection of specific data had not yet occurred, (ii) deferred revenue on data acquisition projects and (iii) contracts in which the data products are not yet available or the revenue recognition criteria has not yet been met. The deferred revenue will be recognized when selection of specific data is made by the customer, upon expiration of the data selection period specified in the data licensing contracts, as work progresses on the data acquisition contracts, as the data products become available or as all of the revenue recognition criteria are met. Deferred revenue will be recognized no later than the following, based on the expiration of the selection period or our estimate of progress on acquisition projects and the availability of data products, although some revenue may be recognized earlier (in thousands):

2011	\$ 31,457
2012	5,307
2013 and thereafter	357

#### Depreciation and Amortization

Depreciation and amortization was comprised of the following (in thousands):

	Year Ended December 31,		
	2010	2009	2008
<b>Amortization of seismic data:</b>			
Income forecast	\$ 87,617	\$ 65,424	\$ 101,301
Straight-line	80,190	77,031	59,288
<b>Total amortization of seismic data</b>	<b>167,807</b>	<b>142,455</b>	<b>160,589</b>
Depreciation of property and equipment	2,081	2,256	2,345
Amortization of acquired intangibles	5,704	5,488	5,695
<b>Total</b>	<b>\$ 175,592</b>	<b>\$ 150,199</b>	<b>\$ 168,629</b>

Total seismic data library amortization amounted to \$167.8 million, \$142.5 million and \$160.6 million in 2010, 2009 and 2008, respectively. The amount of seismic data library amortization fluctuates based on the level and location of specific seismic surveys licensed (including licensing resulting from new data acquisition) and selected by our customers during any period as well as the amount of straight-line amortization required under our accounting policy.

Seismic data amortization as of percentage of total seismic revenue is summarized as follows:

Components of Amortization	Year Ended December 31,		
	2010	2009	2008
Income forecast	51%	59%	61%
Straight-line	47%	70%	36%
<b>Total</b>	<b>98%</b>	<b>129%</b>	<b>97%</b>

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The percentage of income forecast amortization to total seismic revenue was 51% for the year ended December 31, 2010; 59% for the year ended December 31, 2009; and 61% for the year ended December 31, 2008. In all three years, we had resale revenue recognized which was from data whose costs were fully amortized. In 2010, 37% of resales did not attract amortization, as compared to 24% in 2009 and 19% in 2008. Straight-line amortization represents the expense required under our accounting policy to ensure our data value is fully

amortized within four years of when the data becomes available for sale. The \$3.2 million increase in straight-line amortization from 2009 to 2010 was due to the distribution of revenue among the various seismic surveys, resulting in more straight-line amortization in 2010. The \$17.7 million increase in straight-line amortization from 2008 to 2009 was due to lower revenues and the distribution of revenue among the various seismic surveys, resulting in more straight-line amortization in 2009.

For the year ended December 31, 2010, the rates utilized under the income forecast method was 70% for all components. For the year ended December 31, 2009, the rates utilized under the income forecast method ranged from 70% to 74%. For the year ended December 31, 2008, the amortization rates utilized under the income forecast method ranged from 70% to 73%. The rate of amortization with respect to each component is decreased or increased if our estimate of future cash sales from such component is materially increased or decreased, subject to a minimum amortization rate of 70%. Additionally, certain seismic surveys have been fully amortized; consequently, no amortization expense is required on revenue recorded for these seismic surveys. As of January 1, 2011, the amortization rates to be utilized under the income forecast method is 70% for all components.

We expect the level of straight-line amortization for the year ending December 31, 2011 to decrease compared to the year ended December 31, 2010, because a significant portion of our data library will become fully amortized in the first quarter of 2011 as this represents four years from the date of the Merger.

In connection with the Merger, we recorded acquired intangible assets of \$53.4 million, of which \$52.5 million are amortizable over their useful lives ranging from 1 to 10 years. Amortization related to customer relationships, internally developed software and covenants not to compete totaled \$5.7 million, \$5.5 million, and \$5.7 million for the years ended December 31, 2010, 2009 and 2008, respectively.

#### Impairment of Intangible Asset

During the year ended December 31, 2008, we recorded an impairment charge of \$0.2 million related to a customer relationship intangible asset from our October 2007 purchase of a small data fulfillment company in Canada. The impairment was necessary as a result of the loss of significant customer business and current-period and projected operating losses associated with the customer relationship intangible asset. The impairment was determined by comparing estimated future cash flows attributable to the customer relationship to the carrying value of the asset. The resulting impairment reduced the customer relationship intangible asset to \$0. Subsequently in 2009, we sold this data fulfillment company.

#### Goodwill and Indefinite Lived Intangibles

We performed our annual assessment of the recoverability of goodwill and indefinite lived intangibles on October 1, 2010, and concluded that no impairment of goodwill or indefinite lived intangibles was indicated. This evaluation utilized discounted cash flow analysis and multiple analyses of our historical and forecasted operating results. Our prior year assessments resulted in no impairment charges as well.

#### Selling, General and Administrative Expenses

Selling, general and administrative ( SG&A ) expenses were \$31.8 million in 2010, \$25.1 million in 2009 and \$36.3 million in 2008. SG&A expense is made up of the following expense categories (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Cash SG&A expenses	\$ 28,398	\$ 21,804	\$ 29,557
Non-cash equity compensation expense	3,157	3,034	6,492
Non-cash rent expense	276	252	267
Total	\$ 31,831	\$ 25,090	\$ 36,316

The increase in cash SG&A expenses of \$6.6 million from the year ended December 31, 2009 to the year ended December 31, 2010 was primarily due to (1) an increase in performance incentive compensation of \$4.4 million resulting from the improvement in current year cash EBITDA, (2) \$0.8 million expense related to a long-term

incentive compensation plan implemented in 2010, (3) an increase of \$0.9 million in sales commissions as a result of higher revenues and (4) an increase of \$1.0 million in our allowance for doubtful accounts. These increases were partially offset by a decrease of \$0.5 million in various other expenses primarily related to severance and one-time costs associated with cost reduction measures.

The decrease in cash SG&A expenses of \$7.8 million from the year ended December 31, 2008 to the year ended December 31, 2009 was primarily due to (1) a decrease of \$4.1 million in personnel costs resulting from workforce reductions and reductions in base salaries and employee benefits implemented in 2009, (2) a decrease of \$1.1 million due to no performance incentive expense in 2009 because of lower cash resales resulting from the economic downturn, (3) a decrease of \$1.4 million in sales commissions as a result of lower revenues and (4) a decrease of \$2.6 million in various other expenses resulting primarily from cost cutting measures implemented in 2009, of which \$1.0 million resulted from savings in travel, marketing and entertainment costs. These decreases were partially offset by \$1.1 million of one-time costs incurred to implement cost reduction measures and additional reserves for bad debt in 2009 of \$0.3 million.

Non-cash equity compensation expense increased \$0.1 million in 2010 compared to 2009. The re-pricing of our outstanding stock options in May 2010 caused non-cash compensation expense to increase in 2010; this was partially offset by a reduction in expense related to stock options due to the use of graded vesting to amortize the compensation expense. The decrease in non-cash equity compensation expense of \$3.5 million between 2009 and 2008 was primarily due to a reduction in the expense related to stock options granted to certain employees and non-employee directors due to the expense being recognized using graded vesting.

The non-cash rent expense represents amortization of a favorable facility lease that was recorded as an intangible asset in connection with the Merger and is being amortized over its remaining lease term from the Merger date of 6.25 years.

#### **Other Income (Expense)**

Interest expense was \$41.1 million for the year ended December 31, 2010 and \$41.2 million for each of the years ended December 31, 2009 and 2008.

Interest income was \$0.6 million, \$0.5 million and \$1.2 million for the years ended December 31, 2010, 2009 and 2008, respectively. The decrease between 2008 and 2009 was mainly due to lower cash balances in 2009 resulting from lower cash resales as well as lower rates of return on our cash investments.

During the year ended December 31, 2010, we sold \$4.2 million of marketable securities through multiple transactions on an active international exchange. Total gains were equal to the proceeds received.

During the years ended December 31, 2010, 2009 and 2008, we reported foreign currency transaction gains (losses) on U.S. denominated transactions of our Canadian subsidiaries totaling \$0.4 million, \$1.0 million and \$(4.1) million, respectively.

#### **Income Taxes**

Tax benefit was \$4.0 million, \$3.0 million and \$3.5 million for the years ended December 31, 2010, 2009 and 2008, respectively. The 2010 benefit was comprised of (i) a benefit of \$3.7 million related to our Canadian operations, (ii) a benefit of \$0.4 million related to certain research and development tax credits received in Canada and (iii) an expense of \$0.1 million related to principal, penalties and interest on uncertain tax positions. The Federal tax benefit of \$18.1 million in 2010 resulting from our U.S. operations was offset by a valuation allowance because it was more likely than not that the deferred tax asset would not be realized.

The 2009 benefit was comprised of (i) a benefit of \$2.8 million related to our Canadian operations, (ii) a benefit of \$0.3 million related to certain research and development tax credits received in Canada, (iii) \$0.1 million of state tax benefit in the U.S. and (iv) an expense of \$0.2 million related to principal, penalties and interest on uncertain tax positions. The Federal tax benefit of \$30.8 million in 2009 resulting from our U.S. operations was offset by a valuation allowance because it was more likely than not that the deferred tax asset would not be realized.

The 2008 benefit was comprised of (i) a benefit of \$5.0 million related to our Canadian operations, (ii) an expense of \$1.3 million related to principal, penalties and interest on uncertain tax positions and (iii) \$0.2 million of Canadian withholding taxes. The Federal tax benefit of \$20.6 million resulting from our U.S. operations was offset by a valuation allowance because it was more likely than not that the deferred tax asset would not be realized.

### Liquidity and Capital Resources

As of December 31, 2010, we had \$90.0 million in consolidated cash, cash equivalents and short-term investments, including \$186,000 of restricted cash. Other sources of liquidity include our Canadian credit facility described below.

**U.S. Credit Facility:** On December 22, 2009, we entered into a secured credit agreement which provided the ability to borrow up to \$9.9 million until December 31, 2010. No borrowings were made on this facility; therefore, under its terms, the facility expired on December 31, 2010.

**Canadian Credit Facility:** Our wholly owned subsidiary, Olympic Seismic Ltd. ( Olympic ), has a revolving credit facility which allows it to borrow up to \$5.0 million (Canadian), subject to an availability formula, by way of prime-based loans or letters of credit. Available borrowings under the facility are equivalent to a maximum of \$5.0 million (Canadian), subject to a requirement that such borrowings may not exceed 75% of good accounts receivable (as defined in the agreement) of Olympic, less prior-ranking claims, if any, relating to inventory or accounts. As of December 31, 2010, no amounts were outstanding on this revolving line of credit and \$3.8 million (Canadian) was available.

**9.75% Senior Unsecured Notes:** On February 14, 2007, we issued in a private placement \$400.0 million aggregate principal amount of our 9.75% Senior Notes. The proceeds from the notes were used to partially fund the transactions in connection with the Merger. Interest on these senior notes is payable in cash, semi-annually in arrears on February 15 and August 15.

**11.75% Senior Unsecured Notes:** On July 2, 2004, we issued in a private placement \$193.0 million aggregate principal amount of our 11.75% Senior Notes. As of December 31, 2010, \$2.0 million of the 11.75% Senior Notes remain outstanding and mature on July 15, 2011. Interest on these senior notes is payable in cash, semi-annually in arrears on January 15 and July 15.

**Contractual Obligations.** As of December 31, 2010, we had outstanding debt and lease obligations, with aggregate contractual cash obligations, including principal and interest, summarized as follows (in thousands):

Contractual cash obligations	Total	Payments due by period			
		2011	2012-2014	2015-2016	2017 and thereafter
Debt obligations <sup>(1)(2)</sup>	\$ 538,909	\$ 41,307	\$ 497,602	\$	\$
Capital lease obligations <sup>(2)</sup>	4,830	373	1,222	824	2,411
Operating lease obligations	4,642	1,206	2,442	942	52
Total contractual cash obligations	\$ 548,381	\$ 42,886	\$ 501,266	\$ 1,766	\$ 2,463

(1) Debt obligations include the face amount of our 9.75% Senior Notes totaling \$400.0 million and our 11.75% Senior Notes totaling \$2.0 million.

(2) Amounts include interest related to debt and capital lease obligations.

**Cash Flows from Operating Activities:** Cash flows provided by operating activities were \$109.3 million, \$40.9 million, and \$88.8 million for the years ended December 31, 2010, 2009 and 2008, respectively. Operating cash flows for 2010 increased from 2009 primarily due to the higher level of our cash resales in 2010 and the related cash collections. Operating cash flows for the year ended December 31, 2009 decreased \$47.9 million from the year ended December 31, 2008 primarily due to the lower level of our cash resales in 2009 as a result of the economic downturn.

**Cash Flows from Investing Activities:** Cash flows used in investing activities were \$45.7 million, \$56.3 million, and \$92.1 million for the years ended December 31, 2010, 2009 and 2008, respectively. Cash expenditures for seismic data were \$49.5 million, \$55.9 million, and \$90.7 million for the years ended December 31, 2010, 2009 and 2008, respectively. The decrease in cash invested in seismic data for 2010 compared to 2009 was primarily due to the reduced activity in 2009 caused by the economic downturn which had a continuing effect into 2010. The decrease in cash invested in seismic data for 2009 compared to 2008 was primarily due to a decrease in cash paid for new data acquisition projects in both the U.S. and Canada because of our planned reduction in capital expenditures resulting from the poor industry conditions and economic uncertainty in 2009.



**Cash Flows from Financing Activities:** Cash flows used in financing activities were \$0.3 million, \$0.2 million and \$0.1 million for the years ended December 31, 2010, 2009 and 2008, respectively.

**Anticipated Liquidity:** Our ability to cover our operating and capital expenses, make required debt service payments on our 9.75% Senior Notes and 11.75% Senior Notes, incur additional indebtedness, and comply with our various debt covenants, will depend primarily on our ability to generate substantial operating cash flows. Our U.S. credit facility expired on December 31, 2010; however, over the next 12 months, we expect to obtain the funds necessary to pay our operating, capital and other expenses and principal and interest on our senior notes and our other indebtedness, from our operating cash flows, cash and cash equivalents on hand and, if required, from additional borrowings (to the extent available under our Canadian credit facility subject to the borrowing base). Our ability to satisfy our payment obligations depends substantially on our future operating and financial performance, which necessarily will be affected by, and subject to, industry, market, economic and other factors. If necessary, we could choose to reduce our spending on capital projects and operating expenses to ensure we operate within the cash flow generated from our operations. We will not be able to predict or control many of these factors, such as economic conditions in the markets where we operate and competitive pressures.

For a discussion of a number of factors that may impact our liquidity and the sufficiency of our capital resources, see - Overview and Item 1A. Risk Factors above.

### Deferred Taxes

As of December 31, 2010, we had a net deferred tax liability of \$2.1 million attributable to our Canadian operations. In the United States, we had a Federal deferred tax asset of \$107.5 million, all of which was fully offset by a valuation allowance. The recognition of the U.S. Federal deferred tax asset will not occur until such time that it is more likely than not that some portion or all of the Federal deferred tax asset will be realized. As of December 31, 2010, it was more likely than not that all of the U.S. Federal deferred tax asset will not be realized. Additionally, in the United States, we had a state deferred tax asset of \$0.3 million which was recognized as it is more likely than not that the state deferred tax asset will be realized.

### Off-Balance Sheet Transactions

Other than operating leases, we do not maintain any off-balance sheet transactions, arrangements, obligations or other relationships with unconsolidated entities or others that are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenue or expense, results of operations, liquidity, capital expenditures or capital resources.

### Capital Expenditures

During 2010, capital expenditures for seismic data and other property and equipment amounted to \$72.3 million. Our capital expenditures for 2011 are presently estimated to be \$172.0 million. Our 2010 actual and 2011 estimated capital expenditures are comprised of the following (in thousands):

	Year Ended Dec. 31, 2010	Estimate For Year Ending Dec. 31, 2011
New data acquisition	\$ 59,428	\$ 157,000
Cash purchases and data processing	1,767	7,000
Non-monetary exchanges	10,545	7,000
Property and equipment and other	527	1,000
<b>Total capital expenditures</b>	<b>72,267</b>	<b>172,000</b>
Less:		
Non-monetary exchanges	(10,545)	(7,000)
Changes in working capital	(11,730)	
<b>Cash investment per statement of cash flows</b>	<b>\$ 49,992</b>	<b>\$ 165,000</b>

Capital expenditures funded from operating cash flow are as follows (in thousands):

	Year Ended Dec. 31, 2010	Estimate For Year Ending Dec. 31, 2011
Total capital expenditures	\$ 72,267	\$ 172,000
Less:		
Non-cash additions	(10,545)	(7,000)
Cash underwriting	(37,823)	(95,000)
<b>Capital expenditures funded from operating cash flow</b>	<b>\$ 23,899</b>	<b>\$ 70,000</b>

As of March 10, 2011, we had capital expenditure commitments related to data acquisition projects of approximately \$103.3 million of which we have obtained approximately \$62.9 million of cash underwriting and \$1.1 million of underwriting from non-monetary exchanges.

### Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2009-13 on Topic 605, Revenue Recognition—Multiple Deliverable Revenue Arrangements—a consensus of the FASB Emerging Issues Task Force. The ASU provides guidance on accounting for products or services (deliverables) separately rather than as a combined unit utilizing a selling price hierarchy to determine the selling price of a deliverable. The selling price is based on vendor-specific evidence, third-party evidence or estimated selling price. We will be required to apply the standard prospectively to any contracts that may contain multiple-element arrangements entered into or materially modified on or after January 1, 2011; however, earlier application is permitted. We do not currently expect the adoption of this new accounting update to have a material impact on our consolidated financial statements.

In January 2010, the FASB issued ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements, which requires new disclosures regarding transfers in and out of Level 1 and 2 and activity within Level 3 fair value measurements and clarifies existing disclosures of inputs and valuation techniques for Level 2 and 3 fair value measurements. It will also require the presentation of purchases, sales, issuances and settlements within Level 3 on a gross basis rather than a net basis. This ASU was effective for annual and interim reporting periods beginning after December 15, 2009, except for the disclosure of activity within Level 3 fair value measurements, which is effective for fiscal years beginning after December 15, 2010, and for interim periods within those years. We have applied the new disclosure requirements as of January 1, 2010, except for the disclosures about purchases, sales, issuances and settlements in the Level 3 reconciliation, which will be applied effective January 1, 2011. The adoption of this guidance has not had and is not expected to have a material impact on our consolidated financial position, results of operations or cash flows.

In December 2010, the FASB issued ASU 2010-28, When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts—a consensus of the FASB Emerging Issues Task Force. This ASU updates ASC Topic 350, Intangibles—Goodwill and Other, to amend the criteria for performing Step 2 of the goodwill impairment test for reporting units with zero or negative carrying amounts and requires performing Step 2 if qualitative factors indicate that it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist. The qualitative factors are consistent with the existing guidance and examples, which require that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. Early adoption is not permitted. We do not expect the adoption of this guidance in 2011 to have a material impact on our consolidated financial statements.

**Reconciliation of Non-GAAP to GAAP Financial Measures**

The following table summarizes the percentage increases (decreases) between the periods indicated for cash resales and total revenue:

	2009 to 2010
Cash resales	179%
Total revenue	52%
Unconventional 3D data cash resales	261%
Unconventional 3D data total revenue	63%
Conventional 3D data cash resales	114%
Conventional 3D data total revenue	44%

  

	2008 to 2009
Cash resales	(58%)
Total revenue	(33%)
Core cash resales	(56%)
Core total revenue	(31%)
Non-core cash resales	(75%)
Non-core total revenue	(63%)

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to market risk, including adverse changes in interest rates and foreign currency exchange rates as discussed below.

**Interest Rate Risk**

We may enter into various financial instruments, such as interest rate swaps or interest rate lock agreements, to manage the impact of changes in interest rates. Currently, we have no open interest rate swap or interest rate lock agreements. Therefore, our exposure to changes in interest rates primarily results from our short-term and long-term debt with both fixed and floating interest rates. As of December 31, 2010 and 2009 we did not have any debt outstanding with floating interest rates. The following table presents principal or notional amounts (stated in thousands) and related average interest rates by year of maturity for our debt obligations and their indicated fair market value at December 31, 2010:

	2011	2012	2013	2014	2015	There-after	Total	Fair Value
Debt:								
Fixed Rate	\$ 2,059	\$ 66	\$ 29	\$ 400,000	\$	\$	\$ 402,154	\$ 386,077
Average Interest Rate	9.76%	9.75%	9.75%	9.75%			9.76%	

The following table presents principal or notional amounts (stated in thousands) and related average interest rates by year of maturity for our debt obligations and their indicated fair market value at December 31, 2009:

	2010	2011	2012	2013	2014	There-after	Total	Fair Value
Debt:								
Fixed Rate	\$ 54	\$ 2,059	\$ 66	\$ 29	\$ 400,000	\$	\$ 402,208	\$ 314,564
Average Interest Rate	9.76%	9.76%	9.75%	9.75%	9.75%		9.76%	

### **Foreign Currency Exchange Rate Risk**

Our Canadian subsidiaries conduct business in the Canadian dollar and are therefore subject to foreign currency exchange rate risk on cash flows related to sales, expenses, financing and investing transactions in currencies other than the U.S. dollar. Currently, we do not have any open forward exchange contracts.

### **Item 8. Financial Statements and Supplementary Data**

The financial statements and financial statement schedules required by this Item are set forth at the pages indicated in Item 15(a) (1) and (2) below.

### **Item 9. Change in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

### **Item 9A. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

As of December 31, 2010, our management carried out an evaluation, under the supervision and with the participation of our President and Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures, pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, our President and Chief Executive Officer along with our Chief Financial Officer concluded that our disclosure controls and procedures as of December 31, 2010 were designed to ensure, and were effective in ensuring, that our information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to our management, including our President and Chief Executive Officer and our Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

#### **Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining effective internal control over financial reporting (as defined in Rules 13a-15(f) or 15d-15(f) promulgated under the Exchange Act) for us. Even an effective internal control system, no matter how well designed, has inherent limitations, including the possibility of human error and circumvention or overriding of controls and therefore can provide only reasonable assurance with respect to reliable financial reporting. Furthermore, the effectiveness of a system of internal control over financial reporting in future periods can change as conditions change.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2010. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control - Integrated Framework*. Based on this assessment and such criteria, management believes that, as of December 31, 2010, our internal control over financial reporting was effective. Our assessment also appears on page F-1.

This annual report does not include an attestation report of our registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our registered public accounting firm pursuant to an exemption for non-accelerated filers set forth in the Dodd-Frank Wall Street Reform and Consumer Protection Act.

#### **Changes in Internal Controls Over Financial Reporting**

There have been no changes in our internal controls over financial reporting during the quarter ended December 31, 2010 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

### **Item 9B. Other Information**

None.

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**PART III**

**Item 10. *Directors, Executive Officers and Corporate Governance***

The information required by this Item is incorporated herein by reference from our Form 10-K/A to be filed within 120 days after December 31, 2010, under a similarly entitled caption.

**Item 11. *Executive Compensation***

The information required by this Item is incorporated herein by reference from our Form 10-K/A to be filed within 120 days after December 31, 2010, under a similarly entitled caption.

**Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters***

The information required by this Item is incorporated herein by reference from our Form 10-K/A to be filed within 120 days after December 31, 2010, under a similarly entitled caption.

**Item 13. *Certain Relationships and Related Transactions, and Director Independence***

The information required by this Item is incorporated herein by reference from our Form 10-K/A to be filed within 120 days after December 31, 2010, under a similarly entitled caption.

**Item 14. *Principal Accountant Fees and Services***

The information required by this Item is incorporated herein by reference from our Form 10-K/A to be filed within 120 days after December 31, 2010, under a similarly entitled caption.

**PART IV**

**Item 15. *Exhibits and Financial Statement Schedules***

- (a) Documents filed as part of this Report.

	Page
(1) Financial Statements	
<u>Management's Report on Internal Control Over Financial Reporting</u>	F-1
<u>Report of Independent Registered Public Accounting Firm</u>	F-2
<u>Consolidated Balance Sheets</u>	F-3
<u>Consolidated Statements of Operations</u>	F-5
<u>Consolidated Statements of Stockholder's Equity</u>	F-6
<u>Consolidated Statements of Cash Flows</u>	F-7
<u>Notes to Consolidated Financial Statements</u>	F-9



(3) Exhibits:

- 2.1 Agreement and Plan of Merger by and among Seitel Holdings, LLC (now known as Seitel Holdings, Inc.), Seitel Acquisition Corp. and Seitel, Inc., dated October 31, 2006 (incorporated by reference from Exhibit 2.1 to the Seitel, Inc. current report on Form 8-K, as filed with the SEC on November 2, 2006) (Seitel, Inc. agrees to furnish supplementally a copy of any omitted schedule to the SEC upon request).
- 3.1 Certificate of Incorporation of Seitel, Inc. (incorporated by reference from Exhibit 3.1 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 3.2 Bylaws of Seitel, Inc. (incorporated by reference from Exhibit 3.2 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 4.1 Indenture governing 11.75% Senior Subordinated Notes due 2011 by and among Seitel, Inc., the Guarantors named therein and LaSalle Bank National Association, as Trustee, dated July 2, 2004 (incorporated by reference from Exhibit 4.4 to the Seitel, Inc. Post Effective Amendment No. 1 to the Seitel, Inc. Registration Statement on Form S-1, No. 333-113446, as filed with the SEC on July 2, 2004).
- 4.2 Form of 11.75% Senior Subordinated Notes due 2011 (included in Exhibit 4.1).
- 4.3 Supplemental Indenture by and among Seitel, Inc., the Guarantors named therein and UBS Securities LLC and Jeffries & Company, Inc., as Initial Purchasers, dated July 2, 2004 (incorporated by reference from Exhibit 4.5 to the Seitel, Inc. Post Effective Amendment No. 1 to the Seitel, Inc. Registration Statement on Form S-1, No. 333-113446, as filed with the SEC on July 2, 2004).
- 4.4 Indenture governing 9.75% Senior Notes due 2014 by and among Seitel, Inc., the Guarantors named therein and LaSalle Bank National Association, as Trustee, dated February 14, 2007 (incorporated by reference from Exhibit 4.6 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 4.5 Form of 9.75% Senior Notes due 2014 (included in Exhibit 4.4) (incorporated by reference from Exhibit 4.7 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 4.6 Supplemental Indenture by and among Seitel, Inc., the Guarantors named therein and LaSalle Bank National Association, as Trustee, dated January 31, 2007 (incorporated by reference from Exhibit 4.1 to the Seitel, Inc. current report on Form 8-K, as filed with the SEC on February 2, 2007).
- 10.1 Support Agreement by and among Seitel, Inc., Seitel Holdings, Inc. and ValueAct Capital Master Fund, L.P., dated October 31, 2006 (incorporated by reference from Exhibit 2.2 to the Seitel, Inc. current report on Form 8-K, as filed with the SEC on November 2, 2006).
- 10.2 Credit Agreement dated as of December 22, 2009, by and among Seitel, Inc., as borrower, the lenders party thereto, and ValueAct Capital Management, L.P., as administrative agent (incorporated by reference from Exhibit 10.1 to the Seitel, Inc. current report on Form 8-K, as filed with the SEC on December 23, 2009).
- 10.3 Security Agreement dated as of December 22, 2009, made by Seitel, Inc. and the subsidiaries of Seitel, Inc. from time to time party thereto, in favor of ValueAct Capital Management, L.P., as collateral agent (incorporated by the reference from Exhibit 10.2 to the Seitel, Inc. current report on Form 8-K, as filed with the SEC on December 23, 2009).

- 10.4 Intellectual Property Security Agreement dated as of December 22, 2009, made by Seitel, Inc., in favor of ValueAct Capital Management, L.P., as collateral agent (incorporated by reference from Exhibit 10.3 to the Seitel, Inc. current report on Form 8-K, as filed with the SEC on December 23, 2009).
- 10.5 Amended and Restated Loan and Security Agreement by and among Seitel, Inc. and each of its subsidiaries named therein, as borrowers, and Wells Fargo Foothill, Inc., as lender, dated February 14, 2007 (incorporated by reference from Exhibit 10.2 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.6 First Amendment to Amended and Restated Loan and Security Agreement, dated as of December 24, 2008, by and between Seitel, Inc. and each of its subsidiaries named therein, as borrowers, and Wells Fargo Foothill, Inc., as lender (incorporated by reference from Exhibit 10.3 to the annual report on Form 10-K for the year ended December 31, 2008, as filed with the SEC on March 17, 2009).
- 10.7 Second Amendment to Amended and Restated Loan and Security Agreement, dated as of February 20, 2009, by and between Seitel, Inc. and each of its subsidiaries named therein, as borrowers, and Wells Fargo Foothill, Inc., as lender (incorporated by reference from Exhibit 10.4 to the annual report on Form 10-K for the year ended December 31, 2008, as filed with the SEC on March 17, 2009).
- 10.8 Advisory Agreement by and among Seitel Acquisition Corp. (now known as Seitel, Inc.), Seitel Holdings, LLC (now known as Seitel Holdings, Inc.) and ValueAct Capital Master Fund, L.P., dated January 30, 2007 (incorporated by reference from Exhibit 10.3 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.9 Securities Holders Agreement by and among Seitel Holdings LLC (now known as Seitel Holdings, Inc.), ValueAct Capital Master Fund, L.P. and the Management Investors named therein, dated January 8, 2007 (incorporated by reference from Exhibit 10.5 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.10 Registration Rights Agreement by and among Seitel Holdings LLC (now known as Seitel Holdings, Inc.), ValueAct Capital Master Fund, L.P. and the Management Investors named therein, dated January 8, 2007 (incorporated by reference from Exhibit 10.6 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.11 Joinder to Securities Holders Agreement and Registration Rights Agreement of Philip B. Livingston, dated February 16, 2007 (incorporated by reference from Exhibit 10.9 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.12 Joinder to Securities Holders Agreement and Registration Rights Agreement of Jay H. Golding, dated May 24, 2007 (incorporated by reference from Exhibit 10.10 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.13 Joinder to Securities Holders Agreement and Registration Rights Agreement of John E. Jackson, dated August 1, 2007 (incorporated by reference from Exhibit 10.12 to the annual report on Form 10-K for the year ended December 31, 2007, as filed with the SEC on March 31, 2008).

- 10.14 Seitel Holdings, Inc. 2007 Non-Qualified Stock Option Plan, effective February 14, 2007, as amended as of June 30, 2008 (incorporated by reference from Exhibit 10.3 to the quarterly report on Form 10-Q for the quarter ended June 30, 2008, as filed with the SEC on August 13, 2008).
- 10.15 Form of Stock Option Agreement (incorporated by reference from Exhibit 10.12 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.16 Form of Stock Option Agreement (incorporated by reference from Exhibit 10.1 to the quarterly report on Form 10-Q for the quarter ended June 30, 2010, as filed with the SEC on August 9, 2010).
- 10.17 Seitel Holdings, Inc. 2008 Restricted Stock and Restricted Stock Unit Plan, effective April 8, 2008 (incorporated by reference from Exhibit 10.1 to the quarterly report on Form 10-Q for the quarter ended June 30, 2008, as filed with the SEC on August 13, 2008).
- 10.18 Form of Seitel Holdings, Inc. Restricted Stock Unit Award Agreement (incorporated by reference from Exhibit 10.2 to the quarterly report on Form 10-Q for the quarter ended June 30, 2008, as filed with the SEC on August 13, 2008).
- 10.19 \* Summary of 2011 Long-Term Incentive Plan.
- 10.20 Employment Agreement by and between Seitel, Inc. and Robert D. Monson, dated January 30, 2007 (incorporated by reference from Exhibit 10.13 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.21 Employment Agreement by and between Seitel, Inc. and Kevin P. Callaghan, dated January 30, 2007 (incorporated by reference from Exhibit 10.15 to the Registration Statement on Form S-4, No. 333-144844, as filed with the SEC on July 25, 2007).
- 10.22 Form of Amendment to Employment Agreement (incorporated by reference from Exhibit 10.1 to the Seitel, Inc. current report on Form 8-K, as filed with the SEC on June 8, 2009).
- 10.23 Form of Second Amendment to Employment Agreement (incorporated by reference from Exhibit 10.1 to the current report on Form 8-K, as filed with the SEC on January 27, 2010).
- 21.1\* Subsidiaries of Seitel, Inc.
- 31.1\* Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 302 Of The Sarbanes-Oxley Act of 2002
- 31.2\* Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 302 Of The Sarbanes-Oxley Act of 2002
- 32.1\*\* Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 Of The Sarbanes-Oxley Act of 2002
- 32.2\*\* Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 Of The Sarbanes-Oxley Act of 2002

Management contract, compensation plan or arrangement.

\* Filed herewith.

\*\* Furnished, not filed, pursuant to Item 601(b)(32) of Regulation S-K.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Act of 1934, the Registrant has duly caused this report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized.

SEITEL, INC.

By: /s/ ROBERT D. MONSON  
**Robert D. Monson**  
**Chief Executive Officer and President**

Date: March 16, 2011

Pursuant to the requirements of the Securities Act of 1934, this Report on Form 10-K has been signed below by the following persons on behalf of the Registrant in the capacities and on the date indicated.

Signature	Title	Date
/s/ PETER H. KAMIN  <b>Peter H. Kamin</b>	Chairman of the Board of Directors	March 16, 2011
/s/ ROBERT D. MONSON  <b>Robert D. Monson</b>	Chief Executive Officer, President and Director  (Principal Executive Officer)	March 16, 2011
/s/ MARCIA H. KENDRICK  <b>Marcia H. Kendrick</b>	Chief Financial Officer  (Principal Financial Officer)	March 16, 2011
/s/ ALLISON A. BENNINGTON  <b>Allison A. Bennington</b>	Director	March 16, 2011
/s/ RYAN M. BIRTWELL  <b>Ryan M. Birtwell</b>	Director	March 16, 2011
/s/ KEVIN P. CALLAGHAN  <b>Kevin P. Callaghan</b>	Chief Operating Officer and Director	March 16, 2011
/s/ JAY H. GOLDING  <b>Jay H. Golding</b>	Director	March 16, 2011
/s/ JOHN E. JACKSON  <b>John E. Jackson</b>	Director	March 16, 2011
/s/ GREGORY P. SPIVY  <b>Gregory P. Spivy</b>	Director	March 16, 2011



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**MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

The accompanying consolidated financial statements of Seitel, Inc. and its subsidiaries (Seitel) were prepared by management, which is responsible for their integrity, objectivity and fair presentation. The consolidated financial statements have been prepared in conformity with generally accepted accounting principles in the United States of America and, accordingly, include some amounts that are based on the best estimates and judgments of management.

Seitel's management is also responsible for establishing and maintaining effective internal control over financial reporting. The system of internal control of Seitel is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles in the United States of America. This system consists of 1) entity level controls, including written policies and guidelines relating to the ethical conduct of business affairs, 2) general computer controls and 3) process controls over initiating, authorizing, recording, processing and reporting transactions. Even an effective internal control system, no matter how well designed, has inherent limitations, including the possibility of human error and circumvention or overriding of controls and therefore can provide only reasonable assurance with respect to reliable financial reporting. Furthermore, the effectiveness of an internal control system in future periods can change with conditions.

The adequacy of financial controls of Seitel and the accounting principles employed in financial reporting by Seitel are under the general oversight of the Audit Committee of the Board of Directors. No member of this committee is an officer or employee of Seitel. Seitel's independent registered public accounting firm has full, free, separate and direct access to the Audit Committee and meets with the committee from time to time to discuss accounting, auditing and financial reporting matters.

Seitel's management assessed the effectiveness of Seitel's internal control over financial reporting as of December 31, 2010. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control - Integrated Framework*. These criteria cover the control environment, risk assessment process, control activities, information and communication systems, and monitoring activities. Based on this assessment, management believes that, as of December 31, 2010, Seitel's internal control over financial reporting is effective based on those criteria.

/s/ ROBERT D. MONSON

**Robert D. Monson**

*Chief Executive Officer and President*

/s/ MARCIA H. KENDRICK

**Marcia H. Kendrick**

*Executive Vice President and Chief Financial Officer*

Houston, Texas

March 16, 2011

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Audit Committee, Board of Directors and Stockholder

Seitel, Inc.

Houston, Texas

We have audited the accompanying consolidated balance sheets of Seitel, Inc., as of December 31, 2010 and 2009, and the related consolidated statements of operations, stockholder's equity and cash flows for each of the years in the three year period ended December 31, 2010. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (PCAOB) (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, and we were not engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. Our audits also included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Seitel, Inc., as of December 31, 2010 and 2009, and the results of its operations and its cash flows for each of the years in the three year period ended December 31, 2010, in conformity with accounting principles generally accepted in the United States of America.

/s/ **BKD, LLP**

Houston, Texas

March 16, 2011

## SEITEL, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(In thousands)

	December 31,	
	2010	2009
<b>ASSETS</b>		
Cash and cash equivalents	\$ 89,971	\$ 26,270
Receivables		
Trade, less allowance for doubtful accounts of \$2,556 and \$1,108 at December 31, 2010 and 2009, respectively	34,404	29,498
Notes and other	84	286
Due from Seitel Holdings, Inc. (Note K)	156	147
Seismic data library (Note C)	728,134	646,426
Less: Accumulated amortization	(622,030)	(446,037)
Net seismic data library	106,104	200,389
Property and equipment	15,150	14,293
Less: Accumulated depreciation and amortization	(9,704)	(7,290)
Net property and equipment	5,446	7,003
Investment in marketable securities	3,102	3,173
Prepaid expenses, deferred charges and other	10,249	13,426
Intangible assets, net (Note D)	33,117	38,440
Goodwill (Note D)	208,050	203,060
Deferred income taxes (Note E)	326	327
<b>TOTAL ASSETS</b>	<b>\$ 491,009</b>	<b>\$ 522,019</b>

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

## SEITEL, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS-continued

(In thousands, except share and per share amounts)

	December 31,	
	2010	2009
<b>LIABILITIES AND STOCKHOLDER'S EQUITY</b>		
Accounts payable	\$ 21,013	\$ 10,016
Accrued liabilities	25,588	25,974
Employee compensation payable	6,569	1,087
Income taxes payable	8	9
Debt (Note F)		
Senior Notes	402,056	402,154
Notes payable	154	208
Obligations under capital leases (Note G)	3,394	3,370
Deferred revenue (Note B)	37,121	26,722
Deferred income taxes (Note E)	2,128	6,118
<b>TOTAL LIABILITIES</b>	<b>498,031</b>	<b>475,658</b>
<b>COMMITMENTS AND CONTINGENCIES (Note H)</b>		
<b>STOCKHOLDER'S EQUITY (DEFICIT)</b>		
Common stock, par value \$.001 per share; 100 shares authorized, issued and outstanding at December 31, 2010 and 2009		
Additional paid-in capital	277,488	274,331
Retained deficit	(311,401)	(247,984)
Accumulated other comprehensive income	26,891	20,014
<b>TOTAL STOCKHOLDER'S EQUITY (DEFICIT)</b>	<b>(7,022)</b>	<b>46,361</b>
<b>TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY (DEFICIT)</b>	<b>\$ 491,009</b>	<b>\$ 522,019</b>

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

## SEITEL, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands)

	Year Ended December 31,		
	2010	2009	2008
REVENUE	\$ 175,556	\$ 115,345	\$ 172,403
EXPENSES:			
Depreciation and amortization	175,592	150,199	168,629
Impairment of intangible asset			225
Cost of sales	97	290	462
Selling, general and administrative	31,831	25,090	36,316
Merger			357
	207,520	175,579	205,989
LOSS FROM OPERATIONS	(31,964)	(60,234)	(33,586)
Interest expense	(41,094)	(41,194)	(41,215)
Interest income	558	498	1,198
Foreign currency exchange gains (losses)	441	1,008	(4,059)
Gain on sale of marketable securities	4,188		
Other income	446	151	40
Loss before income taxes	(67,425)	(99,771)	(77,622)
Benefit for income taxes	(4,008)	(2,974)	(3,548)
NET LOSS	\$ (63,417)	\$ (96,797)	\$ (74,074)

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

## SEITEL, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(In thousands, except share amounts)

	Comprehensive Loss	Common Stock Shares	Stock Amount	Additional Paid-In Capital	Retained Deficit	Accumulated Other Comprehensive Income (Loss)
Balance, December 31, 2007		100	\$	\$ 264,805	\$ (77,113)	\$ 33,266
Issuance of restricted stock units				604		
Amortization of stock-based compensation costs				5,888		
Net loss	\$ (74,074)				(74,074)	
Foreign currency translation adjustments	(34,684)					(34,684)
Unrealized loss on marketable securities, net of tax	(2,907)					(2,907)
<b>Comprehensive loss</b>	<b>\$ (111,665)</b>					
Balance, December 31, 2008		100		271,297	(151,187)	(4,325)
Amortization of stock-based compensation costs				3,034		
Net loss	\$ (96,797)				(96,797)	
Foreign currency translation adjustments	22,483					22,483
Unrealized gain on marketable securities, net of tax	1,856					1,856
<b>Comprehensive loss</b>	<b>\$ (72,458)</b>					
Balance, December 31, 2009		100		274,331	(247,984)	20,014
Amortization of stock-based compensation costs				3,157		
Net loss	\$ (63,417)				(63,417)	
Foreign currency translation adjustments	6,948					6,948
Unrealized gain on securities held as available for sale, net of tax:						
Unrealized net holding gain arising during the period	4,117					4,117
Less: Reclassification adjustment for realized gains included in earnings	(4,188)					(4,188)
<b>Comprehensive loss</b>	<b>\$ (56,540)</b>					
Balance, December 31, 2010		100	\$	\$ 277,488	\$ (311,401)	\$ 26,891

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

## SEITEL, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Year Ended December 31,		
	2010	2009	2008
Cash flows from operating activities:			
Reconciliation of net loss to net cash provided by operating activities:			
Net loss	\$ (63,417)	\$ (96,797)	\$ (74,074)
Depreciation and amortization	175,592	150,199	168,629
Impairment of intangible asset			225
Deferred income tax benefit	(4,053)	(2,924)	(4,704)
Amortization of deferred financing costs	1,753	1,832	1,631
Amortization of debt premium	(98)	(93)	(86)
Amortization of stock-based compensation	3,157	3,034	5,888
Amortization of favorable lease facility	276	252	268
Allowance for collection of trade receivables	1,524	513	196
Reversal of allowance for notes receivable			(54)
Non-cash compensation expense			604
Non-cash other income	(124)		(24)
Non-cash revenue	(9,864)	(7,413)	(20,414)
Gain on sale of marketable securities	(4,188)		
Loss on sale of subsidiary		19	
(Increase) decrease in receivables	(7,285)	22,997	(12,219)
(Increase) decrease in other assets	(156)	1,180	(577)
Increase (decrease) in deferred revenue	12,811	(27,194)	20,933
Increase (decrease) in accounts payable and other liabilities	3,393	(4,751)	2,542
Net cash provided by operating activities	109,321	40,854	88,764
Cash flows from investing activities:			
Cash invested in seismic data	(49,465)	(55,865)	(90,688)
Cash paid to acquire property, equipment and other	(527)	(400)	(1,187)
Net proceeds from sale of marketable securities	4,188		
Cash paid for acquisition of company			(45)
Cash transferred upon sale of subsidiary		(22)	
Cash from sale of property, equipment and other	86	15	
Advances to Seitel Holdings, Inc.	(9)	(11)	(136)
Net cash used in investing activities	\$ (45,727)	\$ (56,283)	\$ (92,056)

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

## SEITEL, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS, continued

(In thousands)

	Year Ended December 31,		
	2010	2009	2008
<b>Cash flows from financing activities:</b>			
Principal payments on notes payable	\$ (54)	\$ (48)	\$ (44)
Principal payments on capital lease obligations	(146)	(124)	(128)
Borrowings on line of credit	10	401	286
Payments on line of credit	(10)	(401)	(286)
Payment of debt issue costs	(65)		
Payments on notes receivable from officers and employees			54
Net cash used in financing activities	(265)	(172)	(118)
Effect of exchange rate changes	372	(807)	2,645
Net increase (decrease) in cash and cash equivalents	63,701	(16,408)	(765)
Cash and cash equivalents at beginning of period	26,270	42,678	43,443
Cash and cash equivalents at end of period	\$ 89,971	\$ 26,270	\$ 42,678
<b>Supplemental disclosure of cash flow information:</b>			
Cash paid during the period for:			
Interest	\$ 39,440	\$ 39,455	\$ 39,669
Income taxes	\$ 15	\$ 292	\$ 874
<b>Supplemental disclosure of non-cash investing activities:</b>			
Additions to seismic data library	\$ 10,545	\$ 2,197	\$ 23,559

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

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**SEITEL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**NOTE A-ORGANIZATION**

On February 14, 2007, Seitel Acquisition Corp. ( Acquisition Corp. ) was merged with and into Seitel, Inc. (the Company ), pursuant to a merger agreement between the Company, Acquisition Corp. and Seitel Holdings, Inc. ( Holdings ) dated October 31, 2006 (the Merger ). Pursuant to the merger agreement, the Company continued as the surviving corporation and became a privately owned corporation and wholly-owned subsidiary of Holdings. Holdings is an investment entity controlled by ValueAct Capital Master Fund, L.P. ( ValueAct Capital ).

In connection with the Merger, Acquisition Corp. conducted a cash tender offer and consent solicitation for all of the \$189.0 million aggregate principal amount of the Company s 11.75% senior notes due 2011 (the 11.75% Senior Notes ). On February 14, 2007, the Company paid \$187.0 million aggregate principal amount for all of the notes tendered. In connection with the tender offer and consent solicitation, the Company entered into a supplemental indenture for the 11.75% Senior Notes. The supplemental indenture effected certain amendments to the original indenture, primarily to eliminate substantially all of the restrictive covenants and certain events of default triggered or implicated by the Merger. \$2.0 million aggregate principal amount of the 11.75% Senior Notes remain outstanding.

In addition, on February 14, 2007, the Company issued \$400.0 million aggregate principal amount of 9.75% senior notes due 2014 (the 9.75% Senior Notes ) pursuant to an indenture by and among the Company, certain subsidiary guarantors and Bank of America, N.A. (as successor by merger to LaSalle Bank National Association), as trustee. Effective September 21, 2009, Deutsche Bank Trust Company Americas became trustee.

The Company also entered into an Amended and Restated Loan and Security Agreement with Wells Fargo Foothill, Inc. which provided for the ability to borrow up to \$25.0 million, subject to certain borrowing base limitations. The Company terminated the facility effective August 28, 2009 in advance of its stated maturity.

Pursuant to the Merger, all of the Company s outstanding common stock (other than shares of the Company owned by ValueAct Capital and certain shares owned by management investors, which were contributed for ownership in Holdings) was exchanged for \$3.70 per share.

**NOTE B-BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations:** The Company owns an extensive library of proprietary onshore and offshore seismic data that it offers for license to oil and gas companies. The main geographic regions of the Company s focus include the U.S. Gulf Coast, including the Texas Gulf Coast, Eastern Texas, Southern Louisiana and Mississippi, as well as Western Canada, the Rocky Mountains and Northern Louisiana. The majority of the Company s seismic data covers onshore regions within North America with the remainder covering offshore United States. To support its seismic data licensing business and its clients, the Company maintains warehouse and electronic storage facilities in Houston, Texas and Calgary, Alberta, Canada and offers, through its Seitel Solutions business unit ( Solutions ), the ability to access and interact, via a standard web browser and the Internet, with the seismic data library owned and marketed by the Company.

**Basis of Presentation:** The accompanying consolidated financial statements include the accounts of the Company and the accounts of its wholly owned subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to the amounts in the prior year s financial statements to conform to the current year s presentation.

The Company presents its consolidated balance sheets on an unclassified basis. The portion of seismic data library costs to be amortized during the next year cannot be classified as a current asset due to Securities and Exchange Commission ( SEC ) guidance. Classification of all of these costs as noncurrent would be misleading to the reader because it would not indicate the level of assets expected to be converted into cash in the next year.

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**SEITEL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**    **Continued**

**Use of Estimates and Assumptions:** In preparing the Company's financial statements, a number of estimates and assumptions are made by management that affect the accounting for and recognition of assets, liabilities, revenues and expenses. These estimates and assumptions must be made because certain information that is used in the preparation of the Company's financial statements is dependent on future events, cannot be calculated with a high degree of precision from data available or is not otherwise capable of being readily calculated based on generally accepted methodologies. In some cases, these estimates are particularly difficult to determine and the Company must exercise significant judgment.

The most difficult, subjective and complex estimates and assumptions that deal with the greatest amount of uncertainty are related to the Company's accounting for its seismic data library and goodwill.

The Company's accounting for its seismic data library requires it to make significant subjective estimates and assumptions relative to future sales and cash flows from such library. These cash flows impact amortization rates, as well as potential impairment charges. Any changes in the Company's estimates or underlying assumptions will impact the Company's income from operations prospectively from the date changes are made. To the extent that such estimates, or the assumptions used to make those estimates, prove to be significantly different than actual results, the carrying value of the seismic data library may be subject to higher prospective amortization rates, additional straight-line amortization or impairment losses.

In a portion of its seismic data library activities, the Company engages in certain non-monetary exchanges and records a data library asset for the seismic data received and recognizes revenue on the transaction in accordance with its policy on revenue from data licenses or revenue from data acquisitions, as applicable. These transactions are valued at the fair value of the data received by the Company or licenses granted by the Company, whichever is more readily determinable. In addition, the Company obtains third-party concurrence on the portfolio of all non-monetary exchanges for data of \$750,000 or more in order to support its estimate of the fair value of the transactions. The Company's estimate of the value of these transactions is highly subjective and based, in large part, on data sales transactions between the Company and a limited number of customers over a limited time period, and appraisals of the value of such transactions based on a relatively small market of private transactions over a limited period of time.

For its estimates of the fair value of goodwill, the Company prepares discounted cash flow analysis, which requires significant judgments and estimates about the future performance of the Company. If these projected cash flows change materially, the Company may be required to record impairment losses relative to goodwill.

Actual results could differ materially from the estimates and assumptions that the Company uses in the preparation of its financial statements. To the extent management's estimates and assumptions change in the future, the effect on the Company's reported results could be significant to any particular reporting period.

**Revenue Recognition:**

***Revenue from Data Acquisition***

The Company generates revenue when it creates a new seismic survey that is initially licensed by one or more of its customers to use the resulting data. The initial licenses may provide the customer with a limited exclusivity period. The payments for the initial exclusive licenses are sometimes referred to as underwriting or prefunding. Customers make periodic payments throughout the creation period, which generally correspond to costs incurred and work performed. These payments are non-refundable. The Company considers the contracts signed up to the time the Company makes a firm commitment to create the new seismic survey as underwriting. Any subsequent licensing of the data while it is in progress is considered a resale license (see *Revenue from Non-Exclusive Data Licenses* ).

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**SEITEL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**    **Continued**

Underwriting revenue is recognized throughout the creation period using the proportional performance method based upon costs incurred and work performed to date as a percentage of total estimated costs and work required. Management believes that this method is the most reliable and representative measure of progress for its data creation projects. On average, the duration of the data creation process is approximately one year. Under these contracts, the Company creates new seismic data designed in conjunction with its customers and specifically suited to the geology of the area using the most appropriate technology available.

The Company outsources the substantial majority of the work required to complete data acquisition projects to third party contractors. The Company's payments to these third party contractors comprise the substantial majority of the total estimated costs of the project and are paid throughout the creation period. A typical survey includes specific activities required to complete the survey, each of which has value to the customers. Typical activities, that often occur concurrently, include:

    permitting for land access, mineral rights, and regulatory approval;

    surveying;

    drilling for the placement of energy sources;

    recording the data in the field; and

    processing the data.

The customers paying for the initial exclusive licenses receive legally enforceable rights to any resulting product of each activity described above. The customers also receive access to and use of the newly acquired, processed data.

The customers' access to and use of the results of the work performed and of the newly acquired, processed data is governed by a license agreement, which is a separate agreement from the acquisition contract. The Company's acquisition contracts require the customer either to have a license agreement in place or to execute one at the time the acquisition contract is signed. The Company maintains sole ownership of the newly acquired data, which is added to its library, and is free to license the data to other customers when any exclusivity period ends.

***Revenue from Non-Exclusive Data Licenses***

The Company recognizes a substantial portion of its revenue from data licenses sold after any exclusive license period. These are sometimes referred to as resale licensing revenue, post-acquisition license sales or shelf sales.

These sales fall under the following four basic forms of non-exclusive license contracts.

    Specific license contract - The customer licenses and selects data from the data library, including data currently in progress, at the time the contract is entered into and holds this license for a long-term period.

    Library card license contract - The customer initially receives only access to data. The customer may then select specific data, from the collection of data to which it has access, to hold long-term under its license agreement. The length of the selection periods under

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the library card contracts is limited in time and varies from customer to customer.

Review and possession license contract - The customer obtains the right to review a certain quantity of data for a limited period of time. During the review period, the customer may select specific data from that available for review to hold long-term under its license agreement. Any data not selected for long-term licensing must be returned to the Company at the end of the review period.

Review only license contract - The customer obtains rights to review a certain quantity of data for a limited period of time, but does not obtain the right to select specific data to hold long-term.

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**SEITEL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**    **Continued**

The Company's non-exclusive license contracts specify the following:

that all customers must also execute a master license agreement that governs the use of all data received under our non-exclusive license contracts;

the specific payment terms, generally ranging from 30 days to 12 months, and that such payments are non-cancelable and non-refundable;

the actual data that is accessible to the customer; and

that the data is licensed in its present form, where is and as is and the Company is under no obligation to make any enhancements, modifications or additions to the data unless specific terms to the contrary are included.

Revenue from the non-exclusive licensing of seismic data is recognized when the following criteria are met:

the Company has an arrangement with the customer that is validated by a signed contract;

the sales price is fixed and determinable;

collection is reasonably assured;

the customer has selected the specific data or the contract has expired without full selection;

the data is currently available for delivery; and

the license term has begun.

Copies of the data are available to the customer immediately upon request.

For licenses that have been invoiced for which payment is due or has been received, but have not met the aforementioned criteria, the revenue is deferred along with the related direct costs (primarily sales commissions). This normally occurs under the library card, review and possession or review only license contracts because the data selection may occur over time. Additionally, if the contract allows licensing of data that is not currently available or enhancements, modifications or additions to the data are required per the contract, revenue is deferred until such time that the data is available.

***Revenue from Non-Monetary Exchanges***

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In certain cases, the Company will take ownership of a customer's seismic data or revenue interest (collectively referred to as "data") in exchange for a non-exclusive license to selected seismic data from the Company's library. In connection with specific data acquisition contracts, the Company may choose to receive both cash and ownership of seismic data from the customer as consideration for the underwriting of new data acquisition. In addition, the Company may receive advanced data processing services on selected existing data in exchange for a non-exclusive license to selected data from the Company's library. These exchanges are referred to as non-monetary exchanges. A non-monetary exchange for data always complies with the following criteria:

the data license delivered is always distinct from the data received;

the customer forfeits ownership of its data; and

the Company retains ownership in its data.

In non-monetary exchange transactions, the Company records a data library asset for the seismic data received or processed at the time the contract is entered into or the data is completed, as applicable, and recognizes revenue on the transaction in equal value in accordance with its policy on revenue from data licenses, which is, when the data is selected by the customer, or revenue from data acquisition, as applicable. The data license to the customer is in the form of one of the four basic forms of contracts discussed above. These transactions are valued at the fair value of the data received or delivered, whichever is more readily determinable.

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**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** Continued

Fair value of the data exchanged is determined using a multi-step process as follows:

First, the Company considers the value of the data or services received from the customer. In determining the value of the data received, the Company considers the age, quality, current demand and future marketability of the data and, in the case of 3D seismic data, the cost that would be required to create the data. In addition, the Company applies a limitation on the value it assigns per square mile on the data received. In determining the value of the services received, the Company considers the cost of such similar services that it could obtain from a third party provider.

Second, the Company determines the value of the license granted to the customer. Typically, the range of cash transactions by the Company for licenses of similar data during the prior six months are evaluated. In evaluating the range of cash transactions, the Company does not consider transactions that are disproportionately high or low.

Third, the Company obtains concurrence from an independent third party on the portfolio of all non-monetary exchanges for data of \$750,000 or more in order to support the Company's valuation of the data received. The Company obtains this concurrence on an annual basis, usually in connection with the preparation of its annual financial statements.

Due to the Company's revenue recognition policies, revenue recognized on non-monetary exchange transactions may not occur at the same time the seismic data acquired is recorded as an asset. The activity related to non-monetary exchanges was as follows (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Seismic data library additions	\$ 10,545	\$ 2,197	\$ 23,559
Revenue recognized based on specific data licenses or selections of data	7,187	4,575	5,935
Revenue recognized related to acquisition contracts	2,677	2,838	14,479

***Revenue from Solutions***

Revenue from Solutions is recognized as the services for reproduction and delivery of seismic data are provided to customers.

**Trade Receivables:** The Company determines the adequacy of its allowance for doubtful accounts based on a periodic review of specific receivables for which revenue has been recognized.

In certain transactions, the Company may permit a customer to make payments on receivables over a period of time. If such payments extend beyond one year from the transaction date, the Company discounts such receivable and recognizes interest income over the term of the payments.

**Property and Equipment:** Property and equipment consists primarily of computer equipment, leasehold improvements and furniture and fixtures stated at historical cost through February 13, 2007, at which time the Company adjusted its property and equipment to fair value in accordance with purchase accounting. Subsequent additions are stated at historical cost. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the assets, the majority of which are three to five years. Leasehold improvements are amortized using the straight-line method over the shorter of their estimated useful lives or the term of the underlying lease. Depreciation expense for the years ended December 31, 2010, 2009 and 2008 was \$2.1 million, \$2.3 million, and \$2.3 million, respectively.

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SEITEL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

**Marketable Equity Securities:** Management determines the appropriate classification of marketable securities at the time of purchase and reevaluates such designation at each balance sheet date. The Company's marketable securities are categorized as available-for-sale and are carried at fair value, with unrealized holding gains and losses, net of taxes, reflected in accumulated other comprehensive income (loss) included in stockholder's equity until realized. For the purpose of computing realized gains and losses, cost is identified on a specific identification basis.

During 2010, the Company sold a portion of its marketable equity securities through a series of transactions. Proceeds from the sales were \$4.2 million. Total realized gains were equal to proceeds received. As of December 31, 2010 and 2009, total unrealized gains on marketable securities were \$3.1 million and \$3.2 million, respectively. The deferred tax expense of \$1.1 million on the net gains was not recognized at both December 31, 2010 and 2009, due to Company's deferred tax asset having a full valuation allowance.

**Debt Issue Costs:** Debt issue costs related to the Company's senior notes, secured credit facility and revolving line-of-credit are included in prepaid expenses, deferred charges and other assets in the consolidated balance sheets. Such costs are amortized over the scheduled maturities of the debt. As of December 31, 2010 and 2009, unamortized debt issue costs were \$6.8 million and \$8.6 million, respectively.

**Business Combinations:** The Company accounts for the assets acquired and liabilities assumed in a business combination based on fair value estimates as of the date of acquisition. These estimates are revised during the measurement period as necessary if, and when, information becomes available to further define and quantify assets acquired and liabilities assumed. The measurement period may not exceed one year. To the extent the fair value estimates are resolved or settled during the measurement period, such items are included in the revised allocation of the purchase price. After the measurement period, the effect of changes in the purchase price allocation is included in results of operations in the periods in which the adjustments are determined.

**Goodwill and Other Intangible Assets:** Goodwill is the excess of purchase price over the fair value of the net assets of acquired businesses. The Company does not amortize goodwill and indefinite-lived intangibles but, at least annually, evaluates whether goodwill and indefinite-lived intangibles are impaired. Goodwill is considered impaired if the carrying amount of the reporting unit exceeds its estimated fair value. In assessing the recoverability of goodwill, the Company reviews both quantitative as well as qualitative factors to support its assumptions with regard to fair value. The Company relies on discounted cash flow analysis, which requires significant judgments and estimates about future operations, to develop the Company's estimates of fair value. Additional impairment assessments may be performed on an interim basis if the Company encounters events or changes in circumstances that would indicate that, more likely than not, the carrying value of goodwill has been impaired.

The cost of intangible assets with determinable lives is amortized to reflect the pattern of economic benefits consumed, on a straight-line basis, over the estimated periods benefited, ranging from 1 to 10 years.

**Income Taxes:** The Company follows the asset and liability method of accounting for income taxes. Under this method, deferred income tax assets and liabilities are recorded for the future income consequences of temporary differences between the financial reporting and income tax bases of assets and liabilities, and are measured using enacted tax rates and laws.

The Company regularly evaluates valuation allowances established for deferred tax assets for which future realization is uncertain. In assessing the realizability of deferred tax assets at December 31, 2010 and 2009, the Company considered whether it was more likely than not that some portion or all of the deferred tax assets would not be realized. The Company considers the scheduled reversal of deferred tax liabilities and tax planning strategies in making this assessment.

The Company and all of its U.S. subsidiaries file a consolidated federal income tax return. The Company does not provide U.S. taxes on the undistributed earnings of its foreign subsidiaries whose earnings are intended to be permanently reinvested in foreign operations. At December 31, 2010, there were no accumulated net earnings of non-U.S. subsidiaries.

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**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued**

**Foreign Currency Translation:** For subsidiaries that have functional currency which is deemed to be other than the U.S. dollar, asset and liability accounts are translated at period-end exchange rates and revenue and expenses are translated at the current exchange rates as of the dates on which they are recognized. Resulting translation adjustments are included in accumulated other comprehensive income (loss) in stockholders' equity. Accumulated translation gains were \$23.8 million and \$16.8 million at December 31, 2010 and 2009, respectively. Any gains or losses realized on transactions or monetary assets or liabilities in currencies other than the functional currency are included in net income (loss) in the current period. Transaction gains (losses) totaled \$0.4 million, \$1.0 million and \$(4.1) million for the years ended December 31, 2010, 2009 and 2008, respectively.

**Use of Derivatives:** The Company may enter into various derivative instruments to manage foreign exchange risks. Derivatives are limited in use and are entered into for purposes of hedging cash flows and not for speculative purposes. The Company may enter into foreign exchange contracts to hedge certain foreign currency denominated assets or liabilities and currency commitments. As of December 31, 2010 and 2009, the Company did not have any derivative contracts.

**Stock-Based Compensation:** The Company measures the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award.

**Employee Benefit Plans:** The Company maintains savings plans in the United States and Canada that allow employees to contribute a portion of their compensation on a pre-tax and/or after-tax basis in accordance with specified guidelines. The Company matches a percentage of the employee contributions up to certain limits. Savings plan expense amounted to \$357,000, \$190,000 and \$583,000 for the years ended December 31, 2010, 2009 and 2008, respectively.

**Comprehensive Loss:** The Company has reported comprehensive loss in the consolidated statements of stockholders' equity for the years ended December 31, 2010, 2009 and 2008. Accumulated other comprehensive income (loss) for the Company consists of foreign currency translation adjustments and unrealized gains (losses) on marketable securities. Cumulative translation adjustments are not adjusted for income taxes as they relate to indefinite investments in non-U.S. subsidiaries.

**Recent Accounting Pronouncements:** In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2009-13 on Topic 605, Revenue Recognition—Multiple Deliverable Revenue Arrangements—a consensus of the FASB Emerging Issues Task Force. The ASU provides guidance on accounting for products or services (deliverables) separately rather than as a combined unit utilizing a selling price hierarchy to determine the selling price of a deliverable. The selling price is based on vendor-specific evidence, third-party evidence or estimated selling price. The Company will be required to apply the standard prospectively to any contracts that may contain multiple-element arrangements entered into or materially modified on or after January 1, 2011; however, earlier application is permitted. The Company does not currently expect the adoption of this new accounting update to have a material impact on its consolidated financial statements.

In January 2010, the FASB issued ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements, which requires new disclosures regarding transfers in and out of Level 1 and 2 and activity within Level 3 fair value measurements and clarifies existing disclosures of inputs and valuation techniques for Level 2 and 3 fair value measurements. It will also require the presentation of purchases, sales, issuances and settlements within Level 3 on a gross basis rather than a net basis. This ASU was effective for annual and interim reporting periods beginning after December 15, 2009, except for the disclosure of activity within Level 3 fair value measurements, which is effective for fiscal years beginning after December 15, 2010, and for interim periods within those years. The Company has applied the new disclosure requirements as of January 1, 2010, except for the disclosures about purchases, sales, issuances and settlements in the Level 3 reconciliation, which will be applied effective January 1, 2011. The adoption of this guidance has not had and is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In December 2010, the FASB issued ASU 2010-28, When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts—a consensus of the FASB Emerging Issues Task Force. This ASU updates ASC Topic 350, Intangibles—Goodwill and Other, to amend the criteria for performing

**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** Continued

Step 2 of the goodwill impairment test for reporting units with zero or negative carrying amounts and requires performing Step 2 if qualitative factors indicate that it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist. The qualitative factors are consistent with the existing guidance and examples, which require that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. Early adoption is not permitted. The Company does not expect the adoption of this guidance in 2011 to have a material impact on its consolidated financial statements.

**NOTE C-SEISMIC DATA LIBRARY**

The Company's seismic data library consists of seismic surveys that are offered for license to customers on a non-exclusive basis. Costs associated with creating, acquiring or purchasing the seismic data library are capitalized and amortized principally on the income forecast method subject to a straight-line amortization period of four years, applied on a quarterly basis at the individual survey level.

The following table sets forth a summary of the net book value of the Company's seismic data library (in thousands):

	As of December 31,	
	2010	2009
U.S. Onshore:		
Texas Gulf Coast and Eastern Texas 3D	\$ 61,274	\$ 87,433
Southern Louisiana/Mississippi 3D	9,374	39,629
Rocky Mountain 3D	1,538	4,704
Other U.S. 3D and U.S. 2D	1,506	11,253
Canadian 3D	30,081	42,624
Canadian 2D	1,304	9,129
U.S. Offshore	1,027	5,617
<b>Total</b>	<b>\$ 106,104</b>	<b>\$ 200,389</b>

At December 31, 2010 and 2009, approximately 25% and 6%, respectively, of the net book value of the seismic data library were projects in progress.

***Costs of Seismic Data Library***

For purchased seismic data, the Company capitalizes the purchase price of the acquired data.

For data received through a non-monetary exchange, the Company capitalizes an amount equal to the fair value of the data received by the Company or the fair value of the license granted to the customer, whichever is more readily determinable. See Note B for discussion of the process used to determine fair value.

For newly created data, the capitalized costs include costs paid to third parties for the acquisition of data and related permitting, surveying and other activities associated with the data creation activity. In addition, the Company capitalizes certain internal costs related to processing the created data. Such costs include salaries and benefits of the Company's processing personnel and certain other costs incurred for the benefit of the processing activity. The Company believes that the internal processing costs capitalized are not greater than, and generally are less than, those that would be incurred and capitalized if such activity were performed by a third party. Capitalized costs for internal data processing were \$1.6 million, \$1.5 million, and \$2.0 million for the years ended December 31, 2010, 2009 and 2008, respectively.



**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** Continued***Data Library Amortization***

The Company amortizes its seismic data library investment using the greater of the amortization that would result from the application of the income forecast method subject to a minimum amortization rate or a straight-line basis over the useful life of the data. With respect to each survey in the data library, the straight-line policy is applied from the time such survey is available for licensing to customers on a non-exclusive basis, since some data in the library may not be licensed until an exclusivity period has lapsed.

The Company applies the income forecast method by forecasting the ultimate revenue expected to be derived from a particular data library component over the estimated useful life of each survey comprising part of such component. This forecast is made by the Company annually and reviewed quarterly. If, during any such review, the Company determines that the ultimate revenue for a library component is expected to be significantly different than the original estimate of total revenue for such library component, the Company revises the amortization rate attributable to future revenue from each survey in such component. The lowest amortization rate the Company applies using the income forecast method is 70%. In addition, in connection with the forecast reviews and updates, the Company evaluates the recoverability of its seismic data library investment, and if required, records an impairment charge with respect to such investment. See discussion on Seismic Data Library Impairment below.

Amortization expense totaled \$167.8 million, \$142.5 million, and \$160.6 million for the years ended December 31, 2010, 2009 and 2008, respectively. The actual aggregate rate of amortization as a percentage of total seismic revenue was 98%, 129%, and 97% for the same periods, respectively. The actual aggregate rate of amortization depends on the specific seismic surveys licensed and selected by the Company's customers during the period and the amount of straight-line amortization recorded. The income forecast amortization rates can vary by component and, as of January 1, 2011, the amortization rate utilized under the income forecast method is 70% for all components. Additionally, certain seismic surveys have been fully amortized; consequently, no amortization expense is required on revenue recorded for these seismic surveys.

The greater of the income forecast or straight-line amortization policy is applied quarterly on a cumulative basis at the individual survey level. Under this policy, the Company first records amortization using the income forecast method. The cumulative amortization recorded for each survey is then compared with the cumulative straight-line amortization. If the cumulative straight-line amortization is higher for any specific survey, additional amortization expense is recorded, resulting in accumulated amortization being equal to the cumulative straight-line amortization for such survey. This requirement is applied regardless of future-year revenue estimates for the library component of which the survey is a part and does not consider the existence of deferred revenue with respect to the library component or to any survey.

***Seismic Data Library Impairment***

The Company evaluates its seismic data library investment by grouping individual surveys into components based on its operations and geological and geographical trends, resulting in the following data library segments for purposes of evaluating impairments: (I) North America 3D onshore comprised of the following components: (a) Texas Gulf Coast, (b) Eastern Texas, (c) Southern Louisiana/Mississippi, (d) Northern Louisiana, (e) Rocky Mountains, (f) other United States and (g) Canada; (II) United States 2D; (III) Canada 2D; (IV) Gulf of Mexico offshore; and (V) international data outside North America. The Company believes that these library components constitute the lowest levels of independently identifiable cash flows.

The Company evaluates its seismic data library investment for impairment whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. The Company considers the level of sales performance in each component compared to projected sales, as well as industry conditions, among others, to be key factors in determining when its seismic data investment should be evaluated for impairment. In evaluating sales performance of each component, the Company generally considers five consecutive quarters of actual performance below forecasted sales to be an indicator of potential impairment.

**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued**

The impairment evaluation is based first on a comparison of the undiscounted future cash flows over each component's remaining estimated useful life with the carrying value of each library component. If the undiscounted cash flows are equal to or greater than the carrying value of such component, no impairment is recorded. If undiscounted cash flows are less than the carrying value of any component, the forecast of future cash flows related to such component is discounted to fair value and compared with such component's carrying amount. The difference between the library component's carrying amount and the discounted future value of the expected revenue stream is recorded as an impairment charge.

For purposes of evaluating potential impairment losses, the Company estimates the future cash flows attributable to a library component by evaluating, among other factors, historical and recent revenue trends, oil and gas prospectivity in particular regions, general economic conditions affecting its customer base and expected changes in technology and other factors that the Company deems relevant. The cash flow estimates exclude expected future revenues attributable to non-monetary data exchanges and future data creation projects.

The estimation of future cash flows and fair value is highly subjective and inherently imprecise. Estimates can change materially from period to period based on many factors, including those described in the preceding paragraph. Accordingly, if conditions change in the future, the Company may record impairment losses relative to its seismic data library investment, which could be material to any particular reporting period.

The Company did not have any impairment charges during the three years ended December 31, 2010.

**NOTE D-GOODWILL AND OTHER INTANGIBLES**

The Company performs an annual assessment of the recoverability of goodwill and indefinite lived intangibles as of October 1 each year. Additionally, the Company assesses goodwill and indefinite lived intangibles for impairment whenever events or changes in circumstances indicate that such carrying values may not be recoverable. The Company incurred no impairment as a result of the annual tests in 2010, 2009 or 2008. Additionally, there were no events or changes in circumstances that indicated that an impairment was more likely than not during interim periods in 2010, 2009, or 2008. However, there can be no assurance that goodwill and indefinite lived intangibles will not be impaired at any time in the future.

Changes in the carrying amount of goodwill for the years ended December 31, 2010 and 2009 are as follows (in thousands):

	December 31,	
	2010	2009
Balance beginning of year	\$ 203,060	\$ 189,187
Translation adjustments	4,990	13,873
Balance end of year	\$ 208,050	\$ 203,060

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

The recorded carrying amount will change at each balance sheet date due to the impact of foreign currency fluctuations. The following is a summary of the Company's intangible assets other than goodwill (in thousands):

	Weighted Average Amortization Period	December 31, 2010	December 31, 2009
<b>Amortized intangible assets:</b>			
<b>Cost:</b>			
Favorable facility lease	6 years	\$ 1,792	\$ 1,703
Customer relationships	10 years	44,673	44,049
Covenants not to compete	1 year	180	180
Internally developed software	7 years	9,349	8,884
		55,994	54,816
<b>Accumulated Amortization:</b>			
Favorable facility lease	6 years	(1,111)	(783)
Customer relationships	10 years	(17,311)	(12,664)
Covenants not to compete	1 year	(180)	(180)
Internally developed software	7 years	(5,175)	(3,649)
		(23,777)	(17,276)
Net book value		32,217	37,540
<b>Indefinite-lived intangible assets:</b>			
Trade names		900	900
<b>Total intangible assets at net book value</b>		<b>\$ 33,117</b>	<b>\$ 38,440</b>

The Company's trade name assets have an indefinite life and are not amortized, but are reviewed annually and tested for impairment. The trade names were determined to have indefinite lives due to the length of time the trade names have been in place. The Company's current intentions are to maintain the trade names indefinitely. All other intangible assets are amortized on a straight-line basis over their expected useful lives. As of December 31, 2010, the weighted average amortization period for these intangible assets was 9.4 years.

Amortization expense for the Company's intangible assets was \$6.0 million, \$5.7 million, and \$6.0 million during the years ended December 31, 2010, 2009 and 2008, respectively. Estimated future amortization expense is as follows: fiscal year ending 2011 - \$6.1 million, fiscal year ending 2012 - \$6.1 million, fiscal year ending 2013 - \$5.9 million, fiscal year ending 2014 - \$4.6 million, fiscal year ending 2015 - \$4.5 million, and thereafter - \$5.0 million.

The Company evaluates the remaining useful life of these intangible assets on an annual basis. The Company also reviews for recoverability when events or changes in circumstances indicate the carrying values may not be recoverable.

During 2008, the Company recognized \$225,000 in impairment charges on the customer relationship intangible asset that resulted from the Company's acquisition of a small data fulfillment company in Canada in October 2007. The impairment was necessary as a result of the loss of significant customer business, current-period and projected operating losses associated with the customer relationship intangible asset. The impairment was calculated by comparing estimated future cash flows attributable to the customer relationship to the carrying value of the asset. The resulting impairment reduced the customer relationship intangible asset to \$0. Effective February 1, 2009, the Company sold the business that was related to the impaired customer relationship for a \$19,000 loss.



SEITEL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

NOTE E-INCOME TAXES

*Income Tax Expense (Benefit)*

Loss before income taxes is comprised of the following (in thousands):

	Year Ended December 31,		
	2010	2009	2008
U.S.	\$ (53,038)	\$ (88,535)	\$ (58,371)
Foreign	(14,387)	(11,236)	(19,251)
	\$ (67,425)	\$ (99,771)	\$ (77,622)

The provision (benefit) for income taxes is comprised of the following (in thousands):

	Year Ended December 31,		
	2010	2009	2008
<b>Current:</b>			
State	\$	\$ (2)	\$ 194
Foreign	45	(48)	962
	45	(50)	1,156
<b>Deferred:</b>			
Federal	(369)	98	106
State	1	(117)	(214)
Foreign	(3,685)	(2,905)	(4,596)
	(4,053)	(2,924)	(4,704)
<b>Tax provision (benefit):</b>			
Federal	(369)	98	106
State	1	(119)	(20)
Foreign	(3,640)	(2,953)	(3,634)
	\$ (4,008)	\$ (2,974)	\$ (3,548)

The differences between the U.S. Federal income taxes computed at the statutory rate (35%) and the Company's income taxes for financial reporting purposes are as follows (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Statutory Federal income tax	\$ (23,599)	\$ (34,920)	\$ (27,168)
Change in unrecognized tax benefits	83	334	1,286

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State income tax, less Federal benefit		1	(13)
Tax difference on foreign earnings	949	588	990
Change in foreign taxes	64	264	
Canadian withholding tax	45	(52)	190
Change in valuation allowance	18,050	30,774	20,456
Non-deductible expenses and other, net	400	37	711
Income tax benefit	\$ (4,008)	\$ (2,974)	\$ (3,548)

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## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

*Deferred Tax Asset/Liability*

The components of the net deferred income tax asset (liability) reflected in the Company's consolidated balance sheets at December 31, 2010 and 2009 were as follows (in thousands):

	Deferred Tax Assets (Liabilities)	
	December,	
	2010	2009
<b>Deferred tax assets:</b>		
Deferred revenue	\$ 1,035	\$ 1,882
Depreciation and amortization	21,402	23,695
Alternative minimum tax credit carryforward	1,782	1,782
Net operating loss carryforwards	86,827	69,399
Research and development tax credit carryforward	1,205	871
Accrued expenses and other	8,859	7,462
<b>Total deferred tax assets</b>	<b>121,110</b>	<b>105,091</b>
<b>Deferred tax liabilities:</b>		
Deferred revenue		(56)
Depreciation and amortization	(3,986)	(9,013)
Intangible assets	(10,174)	(11,837)
Unrealized gain on marketable securities	(1,086)	(1,111)
Deferred expenses and other	(176)	(171)
<b>Total deferred tax liabilities</b>	<b>(15,422)</b>	<b>(22,188)</b>
<b>Valuation allowance:</b>		
Beginning balance	(88,694)	(58,239)
Increase during the period	(18,796)	(30,455)
<b>Total valuation allowance</b>	<b>(107,490)</b>	<b>(88,694)</b>
<b>Net deferred tax liability</b>	<b>\$ (1,802)</b>	<b>\$ (5,791)</b>
<b>Deferred income taxes have been classified in the Consolidated Balance Sheet as:</b>		
Deferred income tax asset	\$ 326	\$ 327
Deferred income tax liability	(2,128)	(6,118)
<b>Net deferred income tax liability</b>	<b>\$ (1,802)</b>	<b>\$ (5,791)</b>

During 2010 and 2009, the Company's valuation allowance provided against its U.S. net deferred tax asset increased by \$18.8 million and \$30.5 million, respectively, primarily related to U.S. net operating losses incurred in 2010 and 2009 for which utilization is uncertain.

As of December 31, 2010, the Company has a U.S. Federal net operating loss ( NOL ) carryforward of approximately \$223.5 million which can be used to offset U.S. income taxes payable in future years. This U.S. NOL carryforward will expire in periods beginning 2025 through 2030. As of December 31, 2010, the Company has an alternative minimum tax (AMT) credit carryforward of approximately \$1.8 million which can be used to offset regular U.S. Federal income taxes payable in future years and which has an indefinite carryforward period. As of December 31,

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2010, the Company has Canadian NOL carryforwards of approximately \$10.2 million (Canadian) which can be used to offset Canadian income taxes payable in future years. These Canadian NOL carryforwards will expire in 2029.

In February 2006, Olympic Seismic Ltd. ( Olympic ), a wholly owned subsidiary of the Company, was notified by Canada Revenue Agency ( CRA ) that CRA was going to perform an audit of certain aspects of Olympic s tax returns for the years 2003 and 2004. In February 2009, CRA notified the Company that the current audit has been expanded to include years from 2005 through 2007. As of December 31, 2010, the audit has not been concluded. The Company has recorded liabilities associated with potential adjustments that may occur as a result of the audit.

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**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** Continued*Uncertain Tax Benefits*

The Company accounts for income taxes in accordance with ASC Topic 740, *Income Taxes*, which prescribes a minimum recognition threshold a tax position must meet before being recognized in the financial statements. A reconciliation of the beginning and ending gross unrecognized tax benefits is as follows (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Balance at beginning of year	\$ 5,545	\$ 4,859	\$ 2,339
Additions based on prior year tax positions	310	275	4,093
Reductions in tax positions due to a lapse in statute		(365)	(839)
Reductions based on prior year tax positions			(301)
Foreign currency translation	296	776	(433)
Balance at end of year	\$ 6,151	\$ 5,545	\$ 4,859

As of December 31, 2010, approximately \$6.2 million of the total unrecognized tax benefits would impact the effective income tax rate, if recognized in future periods.

Uncertain tax positions are reflected as income tax assets and liabilities. Income tax-related interest and penalty expenses are recorded as a component of income tax expense. As of December 31, 2010, we had \$0.3 million of accrued interest and \$1.0 million of accrued penalties. As of December 31, 2009, we had \$0.4 million of accrued interest and \$1.1 million of accrued penalties. Income tax expense (benefit) for the years ended December 31, 2010, 2009 and 2008 included (\$0.2) million, \$0.1 million and \$0.1 million, respectively, related to interest and penalties on unrecognized tax benefits.

The Company believes it is reasonably possible that, within the next 12 months, the amount of previously unrecognized tax benefits could decrease by approximately \$6.2 million primarily as a result of the resolution of tax audits.

With few exceptions, the Company is no longer subject to U.S. Federal, state and local, or non-U.S. income tax examinations by tax authorities for years prior to 2007, 2006 and 2003, respectively.

**NOTE F-DEBT**

The following is a summary of the Company's debt (in thousands):

	December 31,	
	2010	2009
9.75% Senior Notes	\$ 400,000	\$ 400,000
11.75% Senior Notes	2,000	2,000
U.S. Credit Facility		
Subsidiary revolving line of credit		
Note payable to former executive	154	208
	402,154	402,208
Plus: Premium on debt	56	154
	\$ 402,210	\$ 402,362



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**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** Continued

**9.75% Senior Unsecured Notes:** On February 14, 2007, the Company issued, in a private placement, \$400.0 million aggregate principal amount of 9.75% Senior Notes. The proceeds from the 9.75% Senior Notes were used to partially fund the transactions in connection with the Merger. As required by their terms, the 9.75% Senior Notes were exchanged for senior notes of like amounts and terms in a publicly registered exchange offer in August 2007. These notes mature on February 15, 2014. Interest is payable in cash, semi-annually in arrears on February 15 and August 15 of each year. As of December 31, 2010, accrued interest totaled \$14.6 million and was included in accrued liabilities on the Consolidated Balance Sheet. The 9.75% Senior Notes are unsecured and are guaranteed by substantially all of the Company's domestic subsidiaries on a senior basis. The 9.75% Senior Notes contain restrictive covenants which limit the Company's ability to, among other things, incur additional indebtedness, pay dividends and complete mergers, acquisitions and sales of assets.

Upon a change of control (as defined in the indenture), each holder of the 9.75% Senior Notes will have the right to require the Company to offer to purchase all of such holder's notes at a price equal to 101% of the principal amount, plus accrued and unpaid interest.

**11.75% Senior Unsecured Notes:** On July 2, 2004, the Company issued, in a private placement, \$193.0 million aggregate principal amount of 11.75% Senior Notes. As required by their terms, the 11.75% Senior Notes were exchanged for senior notes of like amounts and terms in a publicly registered exchange offer in February 2005. In connection with the 2004 excess cash flow offer in March 2005, \$4.0 million aggregate principal amount of these notes was tendered and accepted. In connection with the Merger and related transactions, \$187.0 million aggregate principal amount of these notes was tendered and accepted on February 14, 2007. The fair value of these notes was higher than the face value on the date of the Merger; consequently, a premium has been reflected in the financial statements related to these notes. Interest on the remaining notes is payable semi-annually in arrears on January 15 and July 15 of each year. As of December 31, 2010, accrued interest totaled \$0.1 million and was included in accrued liabilities on the Consolidated Balance Sheet. The remaining \$2.0 million of notes mature on July 15, 2011. The 11.75% Senior Notes are unsecured and are guaranteed by substantially all of the Company's U.S. subsidiaries on a senior basis.

As a result of the tender and consent offer, effective February 14, 2007, the 11.75% Senior Notes no longer contain any restrictive covenants, other than the requirement to make excess cash flow offers. Subject to certain conditions, if at the end of each fiscal year the Company has excess cash flow (as defined in the indenture) in excess of \$5.0 million, the Company is required to use 50% of the excess cash flow to fund an offer to repurchase the 11.75% Senior Notes on a pro rata basis at 100% of its principal amount, plus accrued and unpaid interest. If the Company has less than \$5.0 million in excess cash flow at the end of any fiscal year, such excess cash flow will be carried forward to succeeding years, and such repurchase offer is required to be made in the first year in which the cumulative excess cash flow for all years in which there has not been an offer is at least \$5.0 million.

Such repurchase offer is required only if there is no event of default under the Company's revolving credit facilities prior to and after giving effect to the repurchase payment. Upon a change of control (as defined in the indenture), each holder of the 11.75% Senior Notes will have the right to require the Company to offer to purchase all of such holder's notes at a price equal to 101% of the principal amount, plus accrued and unpaid interest.

**U.S. Credit Facility:** On December 22, 2009 the Company entered into a secured credit agreement with ValueAct Capital Management, L.P., as initial lender, and ValueAct Capital Management, L.P., as administrative agent. The credit facility provided the ability to borrow up to \$9.9 million until December 31, 2010. No borrowings were made on this facility; therefore, under its terms, the facility expired on December 31, 2010. The facility required the payment of an unused line fee of 0.5% per annum, payable in arrears, from the date of the agreement until December 31, 2010.

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

**Subsidiary Revolving Line of Credit:** Olympic has a revolving credit facility, which allows it to borrow up to \$5.0 million (Canadian) subject to an availability formula by way of prime-based loans or letters of credit. The interest rate applicable to borrowings is the bank's prime rate plus 0.75% per annum. Letter of credit fees are based on scheduled rates in effect at the time of issuance. The facility is secured by the assets of Olympic, but is not guaranteed by the Company or any of its other U.S. subsidiaries. Available borrowings under the facility are equivalent to a maximum of \$5.0 million (Canadian), subject to a requirement that such borrowings may not exceed 75% of good accounts receivable (as defined in the agreement) of Olympic, less prior-ranking claims, if any, relating to inventory or accounts. The facility is subject to repayment upon demand and is available from time to time at the bank's sole discretion.

**Note Payable to Former Executive:** In connection with the settlement of certain litigation, the Company entered into a note payable to a former executive with remaining payments of \$6,000 per month until May 2013. The note is non-interest bearing. The note is guaranteed by Olympic.

**Aggregate Maturities:** The aggregate maturities of the Company's debt over the next five years and thereafter are as follows: \$2,059,000 in 2011, \$66,000 in 2012, \$29,000 in 2013 and \$400,000,000 in 2014.

## NOTE G-LEASE OBLIGATIONS

Assets recorded under capital lease obligations of \$3.8 million and \$3.6 million at December 31, 2010 and 2009, respectively, are included in property and equipment. Accumulated depreciation related to such assets was \$1.0 million and \$0.7 million at December 31, 2010 and 2009, respectively. Depreciation on the assets recorded under capital leases is included in depreciation expense.

The Company leases office space under operating leases, some of which include renewal options. Rental expense for the years ended December 31, 2010, 2009 and 2008 was approximately \$1.7 million, \$1.6 million, and \$1.7 million, respectively. The Company received income from subleases of approximately \$319,000, \$271,000 and \$249,000 for the years ended December 31, 2010, 2009 and 2008, respectively.

Future minimum lease payments for the five years subsequent to December 31, 2010, thereafter and in the aggregate are as follows (in thousands):

	Capital Leases	Operating Leases
2011	\$ 373	\$ 1,206
2012	398	1,206
2013	412	765
2014	412	471
2015	412	471
Thereafter	2,823	523
<b>Total minimum lease payments</b>	<b>4,830</b>	<b>\$ 4,642</b>
Less amount representing interest	(1,436)	
<b>Present value of net minimum lease payments</b>	<b>\$ 3,394</b>	

On April 30, 2002, Olympic entered into a sale leaseback agreement on a building and land located in Calgary, Alberta, Canada. Proceeds of the sale were \$3.6 million (Canadian dollars). The term of the lease is a 20-year capital lease with remaining lease payments of: \$370,860 (Canadian dollars) in years 6-10; \$409,500 (Canadian dollars) in years 11-15; and \$452,340 (Canadian dollars) in years 16-20. The transaction resulted in a gain on the sale of \$737,000, which, prior to the Merger, was deferred and recognized into income over the term of the lease. In connection with the Merger, the deferred gain was eliminated.



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**SEITEL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**    **Continued**

**NOTE H-COMMITMENTS AND CONTINGENCIES**

*Litigation*

The Company is involved from time to time in ordinary, routine claims and lawsuits incidental to its business. In the opinion of management, uninsured losses, if any, resulting from the ultimate resolutions of these matters should not be material to the Company's financial position or results of operations. However, it is not possible to predict or determine the outcomes of the legal actions brought against it or by it, or to provide an estimate of all additional losses, if any, that may arise. At December 31, 2010, the Company did not have any amounts accrued related to litigation and claims.

**NOTE I-STOCK-BASED COMPENSATION**

In connection with the Merger, Holdings, the Company's parent, adopted a stock-based compensation plan (the 2007 Non-Qualified Stock Option Plan) for the benefit of the Company's key employees and non-employee directors. In April 2008, Holdings adopted the 2008 Restricted Stock and Restricted Stock Unit Plan which is designed to provide incentives to present and future employees of the Company through the grant of restricted stock and restricted stock unit awards.

Total stock-based compensation cost recognized and included in selling, general and administrative expenses was \$3.2 million, \$3.0 million and \$6.5 million for the years ended December 31, 2010, 2009 and 2008, respectively. The Company has not recognized any tax benefits related to stock based compensation for the three years ended December 31, 2010.

*Restricted Stock Units*

The 2008 Restricted Stock and Restricted Stock Unit Plan, which is administered by the board of directors of Holdings, authorizes the issuance of up to 25,000 shares of Holdings' common stock pursuant to such grants. In April 2008, 2,341 restricted stock units with a fair value of \$604,000 were granted. The fair value was measured using a weighted calculation of two valuation techniques (price to net asset value adjustment method and an option hedging strategy). The restricted stock units vested immediately; thus, the Company recognized the entire compensation expense on the date of issuance. The restricted stock units are convertible into common shares of Holdings within 30 days of one of the following events: termination of employment, death, disability or upon a change in control of the Company. During 2010, 241 restricted stock units were converted into shares of Holdings. During 2009, no restricted stock units were converted into shares of Holdings. A total of 22,659 restricted shares were available for grant at December 31, 2010.

*Stock Options*

In connection with the Merger, Holdings, adopted the 2007 Non-Qualified Stock Option Plan in order to provide an equity component to management compensation following the Merger. The 2007 Non-Qualified Stock Option Plan became effective February 14, 2007. The board of directors of Holdings, which administers the 2007 Non-Qualified Stock Option Plan, may issue options to purchase up to 105,200 shares of Holdings' common stock to employees, directors and other service providers of Holdings and its subsidiaries, including the Company, under the 2007 Non-Qualified Stock Option Plan.

The options contain only service condition requirements and vest 25 percent on each of the first, second, third and fourth anniversaries of each grant date; however, the options provide for accelerated vesting after a change in control. The Company recognizes compensation expense for these options on a straight-line basis over the requisite service period for each separate vesting portion of the option as if the option was, in substance, multiple options (graded vesting). The options expire 10 years after the date of grant. Upon exercise of the options, shares will be issued from authorized but unissued shares of Holdings. A total of 12,859 shares of Holdings common stock were available for grant as options at December 31, 2010.

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

The fair value of the options was estimated on each grant date in 2010 and 2008 using the Black-Scholes option pricing method. No options were granted in 2009. The assumptions used in the model are outlined in the following table:

	Year Ended December 31, 2010	Year Ended December 31, 2008
Weighted average grant date fair value per share	\$ 47.15	\$ 197.51
Weighted average assumptions used:		
Expected volatility	45%	45%
Expected life (in years)	6.63	6.25
Risk free interest rate	3.23%	2.9 - 3.7%
Expected dividend yield	0.0%	0.0%

In May 2010, the Company cancelled and reissued all of its then outstanding stock options in order to reduce the exercise price of the options to \$193.13. The vesting conditions and the expiration dates were not changed from the original grant of each option. The modification affected 16 employees and 2 non-employee directors who had a total of 86,135 options outstanding as of the modification date. The incremental compensation cost as a result of the modified exercise price was \$1.3 million, of which \$0.9 million was expensed immediately for vested options at the date of modification. The remaining \$0.4 million incremental cost along with the remaining unrecognized compensation cost prior to the modification is being recognized using the graded vesting attribution method over the remaining vesting periods of the stock options. The incremental compensation cost as a result of the re-pricing was calculated as the difference in the fair value of the stock options immediately before the re-pricing and the fair value of the stock options at the new exercise price. The fair value was estimated using the Black-Scholes option pricing method. The assumptions used in the model are outlined in the following table:

	Prior to Re-pricing	After Re-pricing
Weighted average grant date fair value per share	\$ 21.43	\$ 36.74
Weighted average assumptions used:		
Expected volatility	45%	45%
Expected life (in years)	5.97	4.97
Risk free interest rate	3.01%	2.60%
Expected dividend yield	0.0%	0.0%

The computation of the expected volatility assumptions used in the Black-Scholes calculations was based on historical volatilities and implied volatilities of peer companies. The Company utilized the volatilities of peer companies due to its lack of extensive history. When establishing its expected life assumptions, the Company used the simplified method prescribed in SEC Staff Accounting Bulletin (SAB) No. 107, Shared-Based Payment, as amended by SAB 110, for companies that do not have adequate historical data.

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

The following table summarizes stock option activity during the years ended December 31, 2010, 2009 and 2008 (shares in thousands):

	Year Ended December 31, 2010		Year Ended December 31, 2009		Year Ended December 31, 2008	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding at beginning of period	92	\$ 392.07	103	\$ 391.79	94	\$ 389.42
Granted	91	\$ 193.13		\$	14	\$ 406.69
Exercised		\$		\$	(1)	\$ 389.42
Cancelled	(91)	\$ 392.09		\$		\$
Forfeited	(1)	\$ 389.42	(11)	\$ 389.42	(4)	\$ 389.42
Outstanding at end of period <sup>(1)</sup>	91	\$ 193.13	92	\$ 392.07	103	\$ 391.79
Options exercisable at end of period <sup>(2)</sup>	62	\$ 193.13	48	\$ 390.69	22	\$ 389.42
Available for grant at end of period	13		12		1	

<sup>(1)</sup> Stock options outstanding at December 31, 2010 have a weighted average remaining contractual term of 6.4 years.

<sup>(2)</sup> Exercisable stock options at December 31, 2010 have a weighted average remaining contractual term of 6.2 years.

As of December 31, 2010, the total future compensation cost related to non-vested options not yet recognized in the Consolidated Statement of Operations was \$0.5 million and will be recognized using graded vesting over a weighted average period of 5.4 months. The Company did not receive any cash from option exercises during the three years ended December 31, 2010.

## NOTE J-FAIR VALUE MEASUREMENTS

Authoritative guidance on fair value measurements provides a framework for measuring fair value and establishes a fair value hierarchy that prioritizes the inputs used to measure fair value, giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).

The Company uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. In measuring the fair value of the Company's assets and liabilities, market data or assumptions are used that the Company believes market participants would use in pricing an asset or liability, including assumptions about risk when appropriate. As of December 31, 2010 and 2009, the Company's assets that are measured at fair value on a recurring basis include the following (in thousands):

	Total	Fair Value Measurements Using	
		Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2) Unobservable Inputs (Level 3)
<b>At December 31, 2010:</b>			
Cash equivalents	\$ 89,581	\$ 89,581	\$
Investment in equity securities	2,232	2,232	

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Investment in stock options related to equity securities	870		870
<b>At December 31, 2009:</b>			
Cash equivalents	\$ 26,099	\$ 26,099	\$ \$
Investment in equity securities	2,873	2,873	
Investment in stock options related to equity securities	300		300

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**SEITEL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**    **Continued**

The Company had no transfers of assets between any of the above levels during the years ended December 31, 2010 or 2009.

Cash equivalents include treasury bills and money market funds that invest in United States government obligations and a Canadian dollar investment account, all with original maturities of three months or less. The original costs of these assets approximates fair value due to their short-term maturity.

Investment in equity securities are measured at fair value using closing stock prices from an active international market and are classified within Level 1 of the valuation hierarchy. Investment in stock options related to equity securities are measured at fair value using the Black-Scholes option pricing model based on observable market inputs such as stock prices, interest rates and expected volatility assumptions. Based on these inputs, these assets are classified within Level 2 of the valuation hierarchy.

During the year ended December 31, 2010, the Company sold a portion of its investment in equity securities for proceeds totaling \$4.2 million. Total realized gains were equal to proceeds received.

**Other Financial Instruments:**

**Debt**    Based upon the rates available to the Company, the fair value of the 9.75% Senior Notes, the 11.75% Senior Notes and the note payable to a former executive approximated \$386.1 million as of December 31, 2010, compared to the book value of \$402.2 million. The quoted market price of the 9.75% Senior Notes was \$384.0 million at December 31, 2010. The fair value of the 9.75% Senior Notes, the 11.75% Senior Notes and the note payable to a former executive approximated \$314.6 million as of December 31, 2009, compared to the book value of \$402.4 million. The quoted market price of the 9.75% Senior Notes was \$312.6 million at December 31, 2009.

**Accounts Receivable and Accounts Payable**    The fair values of accounts receivable and accounts payable approximated carrying value due to the short-term maturity of these instruments.

**NOTE K-RELATED PARTY TRANSACTIONS**

Holdings does not maintain a cash account. Consequently, the Company makes payments, as needed, on Holdings' behalf for corporate expenditures such as taxes and share repurchases for employees that have left the Company and who held equity instruments in Holdings. In 2010 and 2009, the Company made payments of approximately \$9,000 and \$11,000, respectively on behalf of Holdings. The balance due from Holdings as of December 31, 2010 and 2009 was \$156,000 and \$147,000, respectively.

On December 22, 2009, the Company entered into a secured credit agreement with ValueAct Capital Management, L.P., an affiliate of ValueAct Capital, which provided the Company the ability to borrow up to \$9.9 million until December 31, 2010. No borrowings were made on this facility; therefore, under its terms, the facility expired on December 31, 2010.

The Company owns 20% of Wandoo Energy LLC ( Wandoo ), a privately owned oil and gas prospecting company. The Company's Chief Operating Officer serves as the Company's representative on the board of directors of Wandoo. The Company received \$40,000 and \$107,000 in 2010 and 2009, respectively, in tax distribution payments from Wandoo. Additionally, Wandoo reimbursed the Company in 2010 for \$133,000 in geophysical consulting services previously paid to Wandoo's president in 2005 and 2006.

**NOTE L-MAJOR CUSTOMERS**

No single customer accounted for 10% or more of revenue for the years ended December 31, 2010 and 2009. One customer accounted for 10% or more of the Company's revenue for the year ended December 31, 2008.



**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** Continued

The Company extends credit to various companies in the oil and gas industry for the purchase of their seismic data, which results in a concentration of credit risk. This concentration of credit risk may be affected by changes in economic or other conditions and may accordingly impact the Company's overall credit risk. However, management believes that the risk is mitigated by the number, size, reputation, and diversified nature of the companies to which they extend credit. Historical credit losses incurred on receivables by the Company have not been significant relative to sales.

**NOTE M-STATEMENT OF CASH FLOW INFORMATION**

Cash and cash equivalents at December 31, 2010 and 2009 included \$186,000 and \$113,000, respectively of restricted cash related to collateral on seismic operations bonds.

For purposes of the statement of cash flows, the Company considers all highly liquid investments or debt instruments with an original maturity of three months or less to be cash equivalents. The Company maintains its day-to-day operating cash and temporary excess cash with various banking institutions that, in turn, invest in time deposits and U.S. Treasury bills.

Significant non-cash investing and financing activities are as follows:

The Company had non-cash additions to its seismic data library comprised of the following (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Non-monetary exchanges related to resale licensing revenue	\$ 4,000	\$ 1,764	\$ 9,804
Non-monetary exchanges from underwriting of new data acquisition	3,222	(1,291)	14,476
Other non-monetary additions	124		24
Completion of data in progress from prior non-monetary exchanges	3,199	1,724	1,855
Less: Non-monetary exchanges for data in progress			(2,600)
Total non-cash additions to seismic data library	\$ 10,545	\$ 2,197	\$ 23,559

During the year ended December 31, 2009, the Company reversed a non-monetary exchange valued at \$1.3 million that was originally entered into in 2008. The Company was notified that the client was unable to provide clear title to one of the seismic surveys included in the original contract resulting in the negative amount of non-monetary exchanges from underwriting of new acquisition in the 2009 period. This portion of non-cash underwriting was subsequently satisfied with a cash payment.

Non-cash revenue consisted of the following (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Acquisition revenue on underwriting from non-monetary exchange contracts	\$ 2,677	\$ 2,838	\$ 14,479
Licensing revenue from specific data licenses and selections on non-monetary exchange contracts	7,187	4,575	5,935
Total non-cash revenue	\$ 9,864	\$ 7,413	\$ 20,414

**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** Continued**NOTE N-INDUSTRY SEGMENTS**

The Company operates in one business segment, which is made up of seismic data acquisition, seismic data licensing, seismic data processing and seismic reproduction service.

Geographic information for the periods presented is as follows (in thousands):

	United States	Canada	Other Foreign Countries	Total
<i>Year ended December 31, 2010</i>				
Revenue	\$ 129,888	45,668	\$	\$ 175,556
Assets	316,248	174,761		491,009
<i>Year ended December 31, 2009</i>				
Revenue	\$ 78,792	\$ 36,529	\$ 24	\$ 115,345
Assets	339,431	182,588		522,019
<i>Year ended December 31, 2008</i>				
Revenue	\$ 113,333	\$ 58,697	\$ 373	\$ 172,403
Assets	446,180	197,645		643,825

The Company's revenues may be divided into two major categories, (i) acquisition and licensing of seismic data and (ii) reproduction and delivery of seismic data and other services. Revenue by type of service for the periods presented is as follows (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Acquisition and licensing of seismic data	\$ 171,778	\$ 110,821	\$ 165,860
Reproduction and delivery of seismic data and other services	3,778	4,524	6,543
	\$ 175,556	\$ 115,345	\$ 172,403

**NOTE O-SUPPLEMENTAL GUARANTORS CONSOLIDATING CONDENSED FINANCIAL INFORMATION**

On February 14, 2007, the Company completed a private placement of 9.75% Senior Notes in the aggregate principal amount of \$400.0 million. The Company's payment obligations under the 9.75% Senior Notes are jointly and severally guaranteed by certain of its 100% owned U.S. subsidiaries (Guarantor Subsidiaries). All subsidiaries of the Company that do not guarantee the 9.75% Senior Notes are referred to as Non-Guarantor Subsidiaries.

The consolidating condensed financial statements are presented below and should be read in connection with the Consolidated Financial Statements of the Company. Separate financial statements of the Guarantor Subsidiaries are not presented because (i) the Guarantor Subsidiaries are wholly-owned and have fully and unconditionally guaranteed the 9.75% Senior Notes on a joint and several basis, and (ii) the Company's management has determined such separate financial statements are not material to investors.

The following consolidating condensed financial information presents the consolidating condensed balance sheets as of December 31, 2010 and 2009 and the consolidating condensed statements of operations and statements of cash flows for the years ended December 31, 2010, 2009 and 2008 of (a) the Company; (b) the Guarantor Subsidiaries; (c) the Non-Guarantor Subsidiaries; (d) elimination entries; and (e) the Company, the Guarantor Subsidiaries and the Non-Guarantor Subsidiaries on a consolidated basis.

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Investments in subsidiaries are accounted for on the equity method. The principal elimination entries eliminate investments in subsidiaries, intercompany balances, intercompany transactions and intercompany sales.

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## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED BALANCE SHEET

As of December 31, 2010

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
<b>ASSETS</b>					
Cash and cash equivalents	\$	\$ 75,068	\$ 14,903	\$	\$ 89,971
Receivables					
Trade, net		23,269	11,135		34,404
Notes and other		70	14		84
Due from Seitel Holdings, Inc.		156			156
Intercompany receivables (payables)	128,299	(124,507)	(3,792)		
Investment in subsidiaries	246,883	414,476	1,262	(662,621)	
Net seismic data library		74,719	31,385		106,104
Net property and equipment		1,402	4,044		5,446
Investment in marketable securities		3,102			3,102
Prepaid expenses, deferred charges and other	6,948	2,912	389		10,249
Intangible assets, net	900	19,674	12,543		33,117
Goodwill		107,688	100,362		208,050
Deferred income taxes		326			326
<b>TOTAL ASSETS</b>	<b>\$ 383,030</b>	<b>\$ 598,355</b>	<b>\$ 172,245</b>	<b>\$ (662,621)</b>	<b>\$ 491,009</b>
<b>LIABILITIES AND STOCKHOLDER'S EQUITY (DEFICIT)</b>					
Accounts payable and accrued liabilities	\$ 14,731	\$ 18,410	\$ 20,029	\$	\$ 53,170
Income taxes payable	2		6		8
Senior Notes	402,056				402,056
Notes payable	154				154
Obligations under capital leases			3,394		3,394
Deferred revenue		31,140	5,981		37,121
Deferred income taxes			2,128		2,128
<b>TOTAL LIABILITIES</b>	<b>416,943</b>	<b>49,550</b>	<b>31,538</b>		<b>498,031</b>
<b>STOCKHOLDER'S EQUITY (DEFICIT)</b>					
Common stock					
Additional paid-in capital	277,488				277,488
Parent investment		764,752	156,908	(921,660)	
Retained deficit	(311,401)	(219,050)	(39,989)	259,039	(311,401)
Accumulated other comprehensive income		3,103	23,788		26,891
<b>TOTAL STOCKHOLDER'S EQUITY (DEFICIT)</b>	<b>(33,913)</b>	<b>548,805</b>	<b>140,707</b>	<b>(662,621)</b>	<b>(7,022)</b>
<b>TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY (DEFICIT)</b>	<b>\$ 383,030</b>	<b>\$ 598,355</b>	<b>\$ 172,245</b>	<b>\$ (662,621)</b>	<b>\$ 491,009</b>



## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED BALANCE SHEET

As of December 31, 2009

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
<b>ASSETS</b>					
Cash and cash equivalents	\$	\$ 24,221	\$ 2,049	\$	\$ 26,270
Receivables					
Trade, net		15,652	13,846		29,498
Notes and other	40	87	159		286
Due from Seitel Holdings, Inc.		147			147
Intercompany receivables (payables)	147,022	(145,814)	(1,208)		
Investment in subsidiaries	287,245	428,995	876	(717,116)	
Net seismic data library		148,636	51,753		200,389
Net property and equipment		2,238	4,765		7,003
Investment in marketable securities		3,173			3,173
Prepaid expenses, deferred charges and other	8,610	4,368	448		13,426
Intangible assets, net	900	22,886	14,654		38,440
Goodwill		107,688	95,372		203,060
Deferred income taxes		327			327
<b>TOTAL ASSETS</b>	<b>\$ 443,817</b>	<b>\$ 612,604</b>	<b>\$ 182,714</b>	<b>\$ (717,116)</b>	<b>\$ 522,019</b>
<b>LIABILITIES AND STOCKHOLDER'S EQUITY (DEFICIT)</b>					
Accounts payable and accrued liabilities	\$ 15,099	\$ 5,456	\$ 16,522	\$	\$ 37,077
Income taxes payable	9				9
Senior Notes	402,154				402,154
Notes payable	208				208
Obligations under capital leases			3,370		3,370
Deferred revenue		18,188	8,534		26,722
Deferred income taxes			6,118		6,118
<b>TOTAL LIABILITIES</b>	<b>417,470</b>	<b>23,644</b>	<b>34,544</b>		<b>475,658</b>
<b>STOCKHOLDER'S EQUITY (DEFICIT)</b>					
Common stock					
Additional paid-in capital	274,331				274,331
Parent investment		764,752	161,422	(926,174)	
Retained deficit	(247,984)	(178,965)	(30,093)	209,058	(247,984)
Accumulated other comprehensive income		3,173	16,841		20,014
<b>TOTAL STOCKHOLDER'S EQUITY (DEFICIT)</b>	<b>26,347</b>	<b>588,960</b>	<b>148,170</b>	<b>(717,116)</b>	<b>46,361</b>
<b>TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY (DEFICIT)</b>	<b>\$ 443,817</b>	<b>\$ 612,604</b>	<b>\$ 182,714</b>	<b>\$ (717,116)</b>	<b>\$ 522,019</b>

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## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

For the Year Ended December 31, 2010

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
REVENUE	\$	\$ 131,417	\$ 47,892	\$ (3,753)	\$ 175,556
EXPENSES:					
Depreciation and amortization		126,593	48,999		175,592
Cost of sales		87	10		97
Selling, general and administrative	3,219	19,612	12,753	(3,753)	31,831
	3,219	146,292	61,762	(3,753)	207,520
LOSS FROM OPERATIONS	(3,219)	(14,875)	(13,870)		(31,964)
Interest expense, net	(20,115)	(20,173)	(248)		(40,536)
Foreign currency exchange gains		24	417		441
Gain on sale of marketable securities		4,188			4,188
Other income	2	319	125		446
Loss before income taxes and equity in loss of subsidiaries	(23,332)	(30,517)	(13,576)		(67,425)
Benefit for income taxes		(328)	(3,680)		(4,008)
Equity in loss of subsidiaries	(40,085)	(9,896)		49,981	
NET LOSS	\$ (63,417)	\$ (40,085)	\$ (9,896)	\$ 49,981	\$ (63,417)

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

For the Year Ended December 31, 2009

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
REVENUE	\$	\$ 80,400	\$ 38,090	\$ (3,145)	\$ 115,345
EXPENSES:					
Depreciation and amortization		111,476	38,723		150,199
Cost of sales		282	8		290
Selling, general and administrative	3,051	14,343	10,841	(3,145)	25,090
	3,051	126,101	49,572	(3,145)	175,579
LOSS FROM OPERATIONS	(3,051)	(45,701)	(11,482)		(60,234)
Interest expense, net	(17,139)	(23,403)	(154)		(40,696)
Foreign currency exchange gains		2	1,006		1,008
Other income (loss)	1	168	(18)		151
Loss before income taxes and equity in loss of subsidiaries	(20,189)	(68,934)	(10,648)		(99,771)
Benefit for income taxes		(73)	(2,901)		(2,974)
Equity in loss of subsidiaries	(76,608)	(7,747)		84,355	
NET LOSS	\$ (96,797)	\$ (76,608)	\$ (7,747)	\$ 84,355	\$ (96,797)

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

For the Year Ended December 31, 2008

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
REVENUE	\$	\$ 117,058	\$ 60,319	\$ (4,974)	\$ 172,403
EXPENSES:					
Depreciation and amortization	23	111,458	57,148		168,629
Impairment of intangible asset			225		225
Cost of sales		351	111		462
Selling, general and administrative	6,475	17,916	16,899	(4,974)	36,316
Merger		357			357
	6,498	130,082	74,383	(4,974)	205,989
LOSS FROM OPERATIONS	(6,498)	(13,024)	(14,064)		(33,586)
Interest expense, net	(17,947)	(21,192)	(878)		(40,017)
Foreign currency exchange losses		(121)	(3,938)		(4,059)
Other income		15	25		40
Loss before income taxes and equity in loss of subsidiaries	(24,445)	(34,322)	(18,855)		(77,622)
Provision (benefit) for income taxes		274	(3,822)		(3,548)
Equity in loss of subsidiaries	(49,629)	(15,033)		64,662	
NET LOSS	\$ (74,074)	\$ (49,629)	\$ (15,033)	\$ 64,662	\$ (74,074)

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## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2010

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
Cash flows from operating activities:					
Net cash provided by (used in) operating activities	\$ (39,719)	\$ 115,585	\$ 33,455	\$	\$ 109,321
Cash flows from investing activities:					
Cash invested in seismic data		(33,287)	(16,178)		(49,465)
Cash paid to acquire property, equipment and other		(380)	(147)		(527)
Net proceeds from sale of marketable securities		4,188			4,188
Cash from sale of property, equipment and other		86			86
Advances to Seitel Holdings, Inc.		(9)			(9)
Return of capital from subsidiary		4,501	(4,501)		
Net cash used in investing activities		(24,901)	(20,826)		(45,727)
Cash flows from financing activities:					
Principal payments on notes payable	(54)				(54)
Principal payments on capital lease obligations			(146)		(146)
Borrowings on line of credit			10		10
Payments on line of credit			(10)		(10)
Payment of debt issue costs	(65)				(65)
Intercompany transfers	39,838	(39,838)			
Net cash provided by (used in) financing activities	39,719	(39,838)	(146)		(265)
Effect of exchange rate changes		1	371		372
Net increase in cash and cash equivalents		50,847	12,854		63,701
Cash and cash equivalents at beginning of period		24,221	2,049		26,270
Cash and cash equivalents at end of period	\$	\$ 75,068	\$ 14,903	\$	\$ 89,971

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2009

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
Cash flows from operating activities:					
Net cash provided by (used in) operating activities	\$ (38,969)	\$ 51,051	\$ 28,772	\$	\$ 40,854
Cash flows from investing activities:					
Cash invested in seismic data		(45,972)	(9,893)		(55,865)
Cash paid to acquire property, equipment and other		(284)	(116)		(400)
Cash transferred upon sale of subsidiary			(22)		(22)
Cash from disposal of property and equipment		15			15
Advances to Seitel Holdings, Inc.		(11)			(11)
Return of capital from subsidiary		11,150	(11,150)		
Net cash used in investing activities		(35,102)	(21,181)		(56,283)
Cash flows from financing activities:					
Principal payments on notes payable	(48)				(48)
Principal payments on capital lease obligations			(124)		(124)
Borrowings on line of credit			401		401
Payments on line of credit			(401)		(401)
Intercompany transfers	39,017	(24,762)	(14,255)		
Net cash provided by (used in) financing activities	38,969	(24,762)	(14,379)		(172)
Effect of exchange rate changes			(807)		(807)
Net decrease in cash and cash equivalents		(8,813)	(7,595)		(16,408)
Cash and cash equivalents at beginning of period		33,034	9,644		42,678
Cash and cash equivalents at end of period	\$	\$ 24,221	\$ 2,049	\$	\$ 26,270

## SEITEL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

## CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2008

(In thousands)

	Parent	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Consolidating Eliminations	Consolidated Total
Cash flows from operating activities:					
Net cash provided by (used in) operating activities	\$ (40,292)	\$ 88,896	\$ 40,160	\$	\$ 88,764
Cash flows from investing activities:					
Cash invested in seismic data		(56,814)	(33,874)		(90,688)
Cash paid to acquire property, equipment and other		(552)	(635)		(1,187)
Cash paid for acquisition of company			(45)		(45)
Advances to Seitel Holdings, Inc.		(136)			(136)
Net cash used in investing activities		(57,502)	(34,554)		(92,056)
Cash flows from financing activities:					
Principal payments on notes payable	(44)				(44)
Principal payments on capital lease obligations			(128)		(128)
Borrowings on line of credit			286		286
Payments on line of credit			(286)		(286)
Payments on notes receivable from officers and employees		54			54
Intercompany transfers	40,336	(35,371)	(4,965)		
Net cash provided by (used in) financing activities	40,292	(35,317)	(5,093)		(118)
Effect of exchange rate changes			2,645		2,645
Net increase (decrease) in cash and cash equivalents		(3,923)	3,158		(765)
Cash and cash equivalents at beginning of period		36,957	6,486		43,443
Cash and cash equivalents at end of period	\$	\$ 33,034	\$ 9,644	\$	\$ 42,678

**SEITEL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued****NOTE P-QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)**

The following is a summary of the unaudited quarterly results of operations for the years ended December 31, 2010 and 2009:

	March 31	Quarter Ended June 30      Sept. 30 (In thousands)		Dec. 31
<i>2010</i>				
Revenue	\$ 32,376	\$ 32,962	\$ 46,140	\$ 64,078
Operating income (loss )	(12,833)	(13,557)	(7,407)	1,833
Net loss	(22,242)	(22,586)	(15,917)	(2,672)

	March 31	Quarter Ended June 30      Sept. 30 (In thousands)		Dec. 31
<i>2009</i>				
Revenue	\$ 34,722	\$ 22,446	\$ 19,504	\$ 38,673
Operating loss	(12,726)	(20,143)	(19,438)	(7,927)
Net loss	(22,492)	(28,039)	(27,969)	(18,297)

**Report of Independent Registered Public Accounting**

**Firm on Financial Statement Schedule**

Audit Committee, Board of Directors

and Stockholder

Seitel, Inc.

Houston, Texas

In connection with our audits of the consolidated financial statements of Seitel, Inc., for the years ended December 31, 2010, 2009 and 2008, we have also audited the financial statement schedule. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement schedule, based on our audits of the basic consolidated financial statements. The financial statement schedule is presented for purposes of complying with the Securities and Exchange Commission's rules and regulations, and is not a required part of the consolidated financial statements.

In our opinion, the 2010, 2009 and 2008 financial statement schedule referred to above, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information required to be included therein.

/s/ **BKD, LLP**

Houston, Texas

March 16, 2011

**SCHEDULE II: VALUATION AND QUALIFYING ACCOUNTS****For the Years Ended December 31, 2010, 2009 and 2008****(Amounts in thousands)**

	Balance at beginning of period	Charged to expense	Deductions from reserves	Balance at end of period
<b>Year ended December 31, 2010:</b>				
Reserves deducted from assets to which they apply:				
Allowance for doubtful accounts	\$ 1,108	\$ 1,524	\$ (76)	\$ 2,556
Valuation allowance on deferred tax asset	88,694	18,796		107,490
<b>Total</b>	<b>\$ 89,802</b>	<b>\$ 20,320</b>	<b>\$ (76)</b>	<b>\$ 110,046</b>
<b>Year ended December 31, 2009:</b>				
Reserves deducted from assets to which they apply:				
Allowance for doubtful accounts	\$ 845	\$ 513	\$ (250)	\$ 1,108
Allowance for notes receivable	225		(225)	
Valuation allowance on deferred tax asset	58,239	30,455		88,694
<b>Total</b>	<b>\$ 59,309</b>	<b>\$ 30,968</b>	<b>\$ (475)</b>	<b>\$ 89,802</b>
<b>Year ended December 31, 2008:</b>				
Reserves deducted from assets to which they apply:				
Allowance for former employee advances and receivables	\$ 3,164	\$	\$ (3,164)	\$
Allowance for doubtful accounts	688	196	(39)	845
Allowance for notes receivable	238		(13)	225
Allowance for stock notes receivable from former employees	493	(54)	(439)	
Valuation allowance on deferred tax asset	31,799	26,440		58,239
<b>Total</b>	<b>\$ 36,382</b>	<b>\$ 26,582</b>	<b>\$ (3,655)</b>	<b>\$ 59,309</b>

EXHIBIT

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Exhibit	Title
10.19	Summary of 2011 Long-Term Incentive Plan.
21.1	Subsidiaries of Seitel, Inc.
31.1	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 302 Of The Sarbanes-Oxley Act of 2002
31.2	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 302 Of The Sarbanes-Oxley Act of 2002
32.1**	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
32.2**	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.

Management contract, compensation plan or arrangement.

\*\* Furnished, not filed, pursuant to Item 601(b)(32) of Regulation S-K.