

UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
TEEKAY SHUTTLE TANKERS L.L.C.

Interim report for the three and nine months ended September 30, 2018

**INDEX TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
TO TEEKAY SHUTTLE TANKERS L.L.C.**

	<u>Page</u>
Introduction and Management's Discussion and Analysis	1
Responsibility Statement	3
Unaudited Consolidated Statements of Income (Loss)	4
Unaudited Consolidated Statements of Comprehensive Income (Loss)	5
Unaudited Consolidated Balance Sheets	6
Unaudited Statement of Cash Flows	7
Unaudited Consolidated Statement of Changes in Total Equity	8
Notes to the Unaudited Consolidated Financial Statements	9
Forward Looking Statements	19

Introduction

Teekay Shuttle Tankers L.L.C. is the world's largest owner and operator of shuttle tankers. Teekay Shuttle Tankers L.L.C. (*Teekay Shuttle Tankers* or the *Company*) and its subsidiaries (together with the Company, the *Group*) was formed in July 2017 by Teekay Offshore Holdings L.L.C. (*Offshore Holdings*), a 100% owned subsidiary of Teekay Offshore Partners L.P. (*Teekay Offshore* or the *Partnership*), a leading international midstream services provider to the offshore oil production industry, to expand its operations in the shuttle tanker shipping segment. Teekay Shuttle Tankers is an integral part to an oil company's value chain as the shuttle tankers move oil from the oil field to onshore terminals and refineries.

The Group was formed by Teekay Offshore in connection with a strategic transaction between its two sponsors, Teekay Corporation, a portfolio manager of marine services to the global oil and natural gas industries, and Brookfield Business Partners L.P., a business services and industrial company focused on owning and operating high-quality businesses that benefit from barriers to entry and/or low production costs, together with its institutional partners (collectively *Brookfield*). Following this strategic transaction, Brookfield owns approximately 60% and Teekay Corporation owns approximately 14% of Teekay Offshore's outstanding common units. As part of this strategic transaction, Teekay Offshore carved out its shuttle tanker business into a separate wholly owned subsidiary, Teekay Shuttle Tankers.

The Company acquired five wholly-owned subsidiaries and one 50% owned subsidiary from Offshore Holdings, which, at the time of acquisition, in aggregate controlled 35 shuttle tankers, including five shuttle tanker newbuildings and three in-chartered shuttle tankers, in exchange for \$765.9 million of equity in the Company. Included in the subsidiaries was cash of \$89.1 million.

Teekay Shuttle Tankers is a market leader for providing shuttle tanker services, whose customer base consists of primarily oil majors and producers and whose assets are operating under long-term, fixed-rate contracts of affreightment (or *CoA*), time-charter contracts, and bareboat contracts. The Company's core operating regions include the North Sea, Brazil and East Coast of Canada.

The Company's principal executive office is at 4th Floor, Belvedere Building, 69 Pitts Road, Hamilton, HM 08, Bermuda.

Management Discussion and Analysis

As at September 30, 2018, our fleet consisted of 27 shuttle tankers that operate under fixed-rate CoAs, time charters and bareboat charters, two vessels that are currently in lay-up, and six shuttle tanker newbuildings. Of these 35 shuttle tankers, five were owned through 50%-owned subsidiaries and two were chartered-in. The remaining vessels are owned 100% by us. The six shuttle tanker newbuildings are expected to be delivered in late-2019 through early-2021. All of our operating shuttle tankers, with the exception of two shuttle tankers that are currently trading as conventional tankers, provide transportation services to energy companies in the North Sea, Brazil, and the East Coast of Canada. Our shuttle tankers occasionally service the conventional spot tanker market. The strengthening or weakening of the U.S. Dollar relative to the Norwegian Kroner, Euro and Brazilian Real may result in significant decreases or increases, respectively, in our vessel operating expenses.

A shuttle tanker is a specialized ship designed to transport crude oil and condensates from offshore oil field installations to onshore terminals and refineries. Shuttle tankers are equipped with sophisticated loading systems and dynamic positioning (or *DP*) systems that allow the vessels to load cargo safely and reliably from oil field installations, even in harsh weather conditions. Shuttle tankers were developed in the North Sea as an alternative to pipelines.

Net Operating Results

Income from vessel operations. Income from vessel operations was \$50.2 million for the nine months ended September 30, 2018 which reflects the commencement of operations of the *Beothuk Spirit* newbuilding in late-2017 and the *Norse Spirit* and *Dorset Spirit* newbuildings during 2018 servicing the East Coast of Canada charter contracts, the dry docking of seven vessels, non-recurring repair and maintenance expenses for the *Nordic Rio* and *Nordic Brasilia* to allow the vessels to trade in the conventional tanker market, the redelivery of the *Nordic Spirit* in May 2018 and the redelivery and subsequent sale of the *Stena Spirit* in August 2018.

Gain on sale and (write-down) of vessels. Gain on sale of vessels for the nine months ended September 30, 2018 relates to a \$2.6 million gain on the sale of the *Navion Britannia* and a \$0.4 million gain on the sale of the *Stena Spirit*. Write-down of vessels was \$29.7 million for the nine months ended September 30, 2018 which consisted of a \$14.9 million write-down of the *Nordic Spirit* and a \$14.8 million write-down of the *Stena Spirit*, as a result of their charter contract expiration during 2018 and a change in operating plans for the vessels. The *Stena Spirit* is included in a 50%-owned subsidiary of the Company.

Other Operating Results

Interest Expense. Interest expense was \$56.1 million for the nine months ended September 30, 2018 which reflects the average debt balance outstanding for the period.

Income Tax Expense. Income tax expense was \$14.7 million for the nine months ended September 30, 2018, primarily due to an increase in our valuation allowance on certain Norwegian tax assets, due to changes in the assumptions of future taxable income.

Financial Condition and Liquidity

As at September 30, 2018, we had a working capital surplus of \$9.8 million. Our primary liquidity needs for the remainder of 2018 and 2019 are to pay existing, committed capital expenditures, to make scheduled repayments of debt, to pay debt service costs, to pay operating expenses and dry-docking expenditures and to fund general working capital requirements. As at September 30, 2018, our total future contractual obligations for vessel newbuildings were estimated to be \$795.1 million, consisting of \$27.3 million (remainder of 2018), \$377.4 million (2019), \$311.7 million (2020) and \$78.7 million (2021) related to six shuttle tanker newbuildings. We expect to secure long-term debt financing related to these shuttle tanker newbuildings.

During the nine months ended September 30, 2018, we refinanced our existing \$250.0 million debt facility secured by the three East Coast Canada shuttle tankers with a new five-year \$265.8 million debt facility and drew down on an additional \$30.0 million junior debt facility secured by the same vessels.

Strategy and Outlook

We expect to continue to generate strong cash flow during the remainder of 2018 and 2019. Our business strategy is primarily focused on implementing existing growth projects and pursuing strategic growth projects. We may enter into joint ventures and partnerships with companies that may provide increased access to charter opportunities. We seek to leverage the expertise, relationships and reputation of Teekay Offshore and Brookfield to pursue growth opportunities in the offshore sector.

RESPONSIBILITY STATEMENT

I confirm that, to the best of my knowledge, the unaudited consolidated interim financial statements for the three and nine months ended September 30, 2018, which are prepared in accordance with the United States generally accepted accounting principles gives a true and fair view of the Company's consolidated assets, liabilities, financial position and results of operations and the MD&A includes a fair review of the development and performance of the business and the position of the issuer and the Company taken as a whole, together with a description of the principal risks and uncertainties that it face under Norwegian Securities Trading Act sections 5-6 fourth paragraph and contain relevant information on major related party transactions.

Hamilton, Bermuda
November 28, 2018

/s/ Edith Robinson
Edith Robinson
Sole Director

TEEKAY SHUTTLE TANKERS L.L.C.
UNAUDITED CONSOLIDATED STATEMENTS OF INCOME (LOSS)
(in thousands of U.S. dollars)

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018	Period from the date of incorporation July 5, 2017 to September 30, 2017
	\$	\$	\$
Revenues (notes 2, 4 and 6)	144,298	426,602	—
Voyage expenses (note 2)	(28,633)	(82,470)	—
Vessel operating expenses (notes 2 and 6)	(33,285)	(107,265)	—
Time-charter hire expenses	(9,469)	(27,361)	—
Depreciation and amortization (notes 1 and 2)	(37,403)	(118,006)	—
General and administrative (note 6)	(4,874)	(14,485)	—
Gain on sale and (write-down) of vessels (note 10)	350	(26,773)	—
Income from vessel operations	30,984	50,242	—
Interest expense (notes 5 and 7)	(19,111)	(56,137)	(2,686)
Interest income	437	925	—
Realized and unrealized gain on derivative instruments (note 7)	551	758	—
Foreign currency exchange gain	1,337	926	—
Other expense - net	(9)	(73)	—
Income (loss) before income tax expense	14,189	(3,359)	(2,686)
Income tax expense (note 8)	(443)	(14,698)	—
Net income (loss)	13,746	(18,057)	(2,686)
Non-controlling interests in net income (loss)	920	8,935	—
Net income (loss) attributable to member of Teekay Shuttle Tankers L.L.C.	14,666	(9,122)	(2,686)

Related party transactions (note 6)

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

TEEKAY SHUTTLE TANKERS L.L.C.
UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(in thousands of U.S. dollars)

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018	Period from the date of incorporation July 5, 2017 to September 30, 2017
	\$	\$	\$
Net income (loss)	13,746	(18,057)	(2,686)
Other comprehensive (loss) income:			
Other comprehensive (loss) income before reclassifications			
Unrealized gain on qualifying cash flow hedging instruments <i>(note 7)</i>	—	2,443	—
Accounts reclassified from accumulated other comprehensive income			
To interest expense:			
Realized gain on qualifying cash flow hedging instruments <i>(note 7)</i>	(58)	(6)	—
Other comprehensive (loss) income	(58)	2,437	—
Comprehensive income (loss)	13,688	(15,620)	(2,686)
Non-controlling interests in comprehensive income (loss)	920	8,935	—
Member's interest in comprehensive income (loss)	14,608	(6,685)	(2,686)

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

TEEKAY SHUTTLE TANKERS L.L.C.
UNAUDITED CONSOLIDATED BALANCE SHEETS
(in thousands of U.S. dollars)

	As at September 30, 2018	As at December 31, 2017
	\$	\$
ASSETS		
Current		
Cash and cash equivalents (notes 3a and 11)	90,481	96,314
Restricted cash (notes 3a and 11)	2,760	—
Accounts receivable, including non-trade of \$797 (December 31, 2017 - \$20,782) (note 2)	19,206	43,436
Current portion of derivative assets (note 7)	683	104
Net investment in direct financing lease - current (note 3b)	880	813
Prepaid expenses	16,008	18,011
Due from affiliates (note 6)	134,495	159,272
Other current assets (note 2)	5,506	—
Total current assets	270,019	317,950
Vessels and equipment		
At cost, less accumulated depreciation of \$731,551 (December 31, 2017 - \$716,254)	1,417,066	1,439,839
Advances on newbuilding contracts (note 9)	63,775	62,960
Net investment in direct finance lease (note 3b)	4,271	5,008
Derivative assets (note 7)	2,826	705
Deferred tax asset	—	13,920
Due from affiliates (note 6)	—	37,098
Other non-current assets (note 2)	30,840	14,142
Goodwill	127,113	127,113
Total assets	1,915,910	2,018,735
LIABILITIES AND EQUITY		
Current		
Accounts payable	5,338	29,681
Accrued liabilities (note 7)	24,906	55,621
Deferred revenues	9,027	14,727
Due to affiliates (note 6)	79,975	49,029
Current portion of derivative instruments (note 7)	527	883
Current portion of long-term debt (note 5)	141,808	159,012
Total current liabilities	261,581	308,953
Long-term debt (note 5)	1,064,669	1,064,809
Derivative instruments (note 7)	32	67
Due to affiliates (note 6)	77,292	109,669
Other long-term liabilities	19,808	2,353
Total liabilities	1,423,382	1,485,851
Commitments and contingencies (note 9)		
Equity		
Paid-in capital	483,879	483,879
Deficit	(36,350)	(5,492)
Accumulated other comprehensive income	2,878	441
Member's equity	450,407	478,828
Non-controlling interest	42,121	54,056
Total equity	492,528	532,884
Total liabilities and total equity	1,915,910	2,018,735
Subsequent events (note 12)		

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

Hamilton, Bermuda
November 28, 2018

/s/ Edith Robinson
Edith Robinson
Sole Director

TEEKAY SHUTTLE TANKERS L.L.C.
UNAUDITED CONSOLIDATED STATEMENT OF CASH FLOWS
(in thousands of U.S. dollars)

	Nine Months Ended September 30, 2018 \$	Period from the date of incorporation July 5, 2017 to September 30, 2017 \$
Cash and cash equivalents and restricted cash provided by (used for)		
OPERATING ACTIVITIES		
Net loss	(18,057)	(2,686)
Non-cash items:		
Unrealized gain on derivative instruments <i>(note 7)</i>	(597)	—
Depreciation and amortization	118,006	—
(Gain on sale) and write-down of vessels <i>(note 10)</i>	26,773	—
Deferred income tax expense <i>(note 8)</i>	13,920	—
Unrealized foreign currency exchange gain and other	(72)	—
Change in non-cash working capital items related to operating activities	48,684	92,709
Expenditures for dry docking	(17,560)	—
Net operating cash flow	171,097	90,023
FINANCING ACTIVITIES		
Proceeds from long-term debt <i>(note 5)</i>	103,884	—
Scheduled repayments of long-term debt <i>(note 5)</i>	(103,966)	—
Debt issuance costs <i>(note 5)</i>	(7,127)	—
Prepayments of long-term debt <i>(note 5)</i>	(15,330)	—
Cash distributions paid by the Company	(34,000)	—
Cash distributions paid by subsidiaries to non-controlling interests	(4,500)	—
Cash contribution paid from non-controlling interest to subsidiaries	1,500	—
Net financing cash flow	(59,539)	—
INVESTING ACTIVITIES		
Net payments for vessels and equipment, including advances on newbuilding contracts	(134,511)	—
Proceeds from sale of vessels and equipment <i>(note 10)</i>	19,210	—
Direct financing lease payments received	670	—
Net investing cash flow	(114,631)	—
(Decrease) increase in cash, cash equivalents and restricted cash	(3,073)	90,023
Cash, cash equivalents and restricted cash, beginning of the period	96,314	—
Cash, cash equivalents and restricted cash, end of the period	93,241	90,023

Supplemental cash flow disclosure *(note 11)*

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

TEEKAY SHUTTLE TANKERS L.L.C.
UNAUDITED CONSOLIDATED STATEMENT OF CHANGES IN TOTAL EQUITY
(in thousands of U.S. dollars)

	Paid-in Capital	Deficit	Accumulated Other Comprehensive Income	Non- Controlling Interest	Total
	\$	\$	\$	\$	\$
Balance as at December 31, 2017	483,879	(5,492)	441	54,056	532,884
Net loss	—	(9,122)	—	(8,935)	(18,057)
Cash distributions	—	(34,000)	—	—	(34,000)
Other comprehensive income <i>(note 7)</i>	—	—	2,437	—	2,437
Contribution of capital from Teekay Offshore	—	(531)	—	—	(531)
Distributions to non-controlling interests	—	—	—	(4,500)	(4,500)
Contribution from non-controlling interest	—	—	—	1,500	1,500
Change in accounting policy <i>(note 2)</i>	—	12,795	—	—	12,795
Balance as at September 30, 2018	483,879	(36,350)	2,878	42,121	492,528

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

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

1. Basis of Presentation

During July 2017, Teekay Offshore Holdings L.L.C. (*Teekay Offshore*), a 100% owned subsidiary of Teekay Offshore Partners L.P., formed Teekay Shuttle Tankers L.L.C., which is a company organized under the laws of the Republic of the Marshall Islands (the *Company*). On October 3, 2017, Teekay Offshore sold five wholly-owned subsidiaries and one 50% owned subsidiary (the *Subsidiaries*), which in aggregate controlled 35 shuttle tankers, including five shuttle tanker newbuildings and three chartered-in shuttle tankers, to the Company for total consideration of \$765.9 million, net of debt and working capital. The Subsidiaries consisted of Teekay Offshore Operating L.P., Teekay Shuttle Tanker Finance L.L.C., Lambada Spirit L.L.C., Samba Spirit L.L.C., Navion Bergen L.L.C. and a 50% interest in Navion Gothenburg L.L.C. Teekay Offshore Operating L.P. owned 23 100% owned subsidiaries and five 50% owned subsidiaries. Teekay Shuttle Tanker Finance L.L.C. owned two 100% owned subsidiaries. As the transaction was a related party transaction, assets and liabilities of the Subsidiaries acquired were originally recorded at the Subsidiaries' carrying value at the date of acquisition.

The Company accounted for the acquisition of the subsidiaries from Teekay Offshore as a transfer of net assets between entities under common control. The method of accounting for such transfers is similar to the pooling of interests method of accounting. Under this method, the carrying amount of net assets recognized in the balance sheets of each combining entity are carried forward to the balance sheet of the combined entity, and no other assets or liabilities are recognized as a result of the combination. The excess of Teekay Offshore's historical costs over the proceeds paid was accounted for as an equity contribution by Teekay Offshore.

The unaudited interim consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (or *GAAP*). The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Certain information and footnote disclosures required by GAAP for complete annual financial statements have been omitted and, therefore, these interim consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the period from the date of incorporation on July 5, 2017 to December 31, 2017, which are included in the Company's Annual Report, filed with the Oslo Bors on April 30, 2018. In the opinion of management, these interim unaudited consolidated financial statements reflect all adjustments, which are solely of a normal recurring nature, necessary to present fairly, in all material respects, the Company's consolidated financial position, results of operations, changes in total equity and cash flows for the interim periods presented. The results of operations for the interim periods presented are not necessarily indicative of those for a full fiscal year. Historically, the utilization of shuttle tankers in the North Sea is higher in the winter months as favorable weather conditions in the summer months provide opportunities for repairs and maintenance to the Company's vessels and the offshore oil platforms. Downtime for repairs and maintenance generally reduces oil production and, thus, transportation requirements. Intercompany balances and transactions have been eliminated upon consolidation.

The Company's shuttle tankers are comprised of two components: i) a conventional tanker (or the *tanker component*) and ii) specialized shuttle equipment (or the *shuttle component*). The Company differentiates these two components on the principle that a shuttle tanker can also operate as a conventional tanker without the use of the shuttle component. The economics of this alternate use depend on the supply and demand fundamentals in the two segments. Historically, the Company has assessed the useful life of the tanker component as being 25 years and the shuttle component as being 20 years. During the nine months ended September 30, 2018, the Company has considered challenges associated with shuttle tankers approaching 20 years of age in recent years and has reassessed the useful life of the tanker component to 20 years. This change in estimate, commencing January 1, 2018, increased depreciation and amortization expense and decreased net income or increased net loss by \$3.8 million and \$11.9 million, respectively, for the three and nine months ended September 30, 2018.

2. Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (or *FASB*) issued Accounting Standards Update 2014-09, *Revenue from Contracts with Customers* (or *ASU 2014-09*). ASU 2014-09 requires an entity to recognize revenue when it transfers promised goods or services to customers at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This update creates a five-step model that requires entities to exercise judgment when considering the terms of the contract(s) which include (i) identifying the contract(s) with the customer, (ii) identifying the separate performance obligations in the contract, (iii) determining the transaction price, (iv) allocating the transaction price to the separate performance obligations, and (v) recognizing revenue as each performance obligation is satisfied. ASU 2014-09 became effective for the Company on January 1, 2018, and has been applied, at the Company's option, retrospectively to each period presented or as a cumulative-effect adjustment as of the date of adoption. The Company has adopted ASU 2014-09 as a cumulative-effect adjustment as of this date. The Company has elected to apply ASU 2014-09 only to those contracts that are not completed as of January 1, 2018. The Company identified the following differences:

- Revenue from time-charter contracts with fixed annual increases in the daily hire rate during the firm period of the charter to compensate for expected inflationary cost increases will be recognized on a smoothed basis over the term of the time-charter, instead of recognized when due under the contract. These changes had the impact of increasing revenue by \$0.2 million and \$0.7 million, respectively, for the three and nine months ended September 30, 2018, as well as increasing other assets by \$1.7

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

million, and increasing equity by \$1.7 million as at September 30, 2018. The cumulative-effect adjustment on January 1, 2018 was an increase to equity of \$0.5 million.

- In certain cases, the Company will incur pre-operational costs that relate directly to a specific customer contract, that generate or enhance resources of the Company that will be used in satisfying performance obligations in the future, whereby such costs are expected to be recovered via the customer contract. Such costs will be deferred and amortized over the duration of the customer contract. The Company previously expensed such costs as incurred unless the costs were directly reimbursable by the contract or if they were related to the mobilization of offshore assets to an oil field. This change had the impact of decreasing (increasing) voyage expenses by nil and \$1.8 million, vessel operating expenses by (\$0.5) million and \$0.4 million, and depreciation and amortization by nil and \$1.1 million, respectively, for the three and nine months ended September 30, 2018, as well as increasing other assets by \$15.6 million and equity by \$15.6 million as at September 30, 2018. The cumulative increase to opening equity as at January 1, 2018 was \$12.4 million.
- Operating costs for the Company's Volatile Organic Compounds (or VOC) systems will be presented as vessel operating expenses and the reimbursement of such expenses will be presented as revenue instead of such amounts being presented on a net basis. This had the impact of increasing revenues and vessel operating expenses for the three and nine months ended September 30, 2018 by \$1.9 million and \$4.5 million, respectively. There was no cumulative impact to opening equity as at January 1, 2018.
- The Company previously presented all accrued revenue as a component of accounts receivable. The Company has determined that if the right to such consideration is conditional upon something other than the passage of time before payment of that consideration is due, such accrued revenue should be presented apart from accounts receivable. This had the impact of increasing other current assets and decreasing accounts receivable by \$7.2 million at September 30, 2018. There was no cumulative impact to opening equity as at January 1, 2018.

In November 2016, the FASB issued Accounting Standards Update 2016-18, *Statement of Cash Flows: Restricted Cash* (or ASU 2016-18). ASU 2016-18 requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Entities are also required to reconcile such total to amounts on the balance sheet and disclose the nature of the restrictions. ASU 2016-18 became effective for the Company on January 1, 2018. Adoption of ASU 2016-18 resulted in the Company including in its statement of cash flows changes in cash, cash equivalents and restricted cash.

In February 2016, the FASB issued Accounting Standards Update 2016-02, *Leases* (or ASU 2016-02). ASU 2016-02 establishes a right-of-use model that requires a lessee to record a right-of-use asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. For lessees, leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. ASU 2016-02 requires lessors to classify leases as a sales-type, direct financing, or operating lease. A lease is a sales-type lease if any one of five criteria are met, each of which indicate that the lease, in effect, transfers control of the underlying asset to the lessee. If none of those five criteria are met, but two additional criteria are both met, indicating that the lessor has transferred substantially all of the risks and benefits of the underlying asset to the lessee and a third party, the lease is a direct financing lease. All leases that are not sales-type leases or direct financing leases are operating leases. ASU 2016-02 is effective January 1, 2019, with early adoption permitted. FASB issued an additional accounting standards update in July 2018 that made further amendments to accounting for leases, including allowing the use of a transition approach whereby a cumulative effect adjustment is made as of the effective date, with no retrospective effect. The Company has elected to use this new optional transition approach. The Company will adopt ASU 2016-02 on January 1, 2019. To determine the cumulative effect adjustment, the Company will not reassess whether any expired or existing contracts are, or contain leases, will not reassess lease classification, and will not reassess initial direct costs for any existing leases. The adoption of ASU 2016-02 will result in a change in the accounting method for the lease portion of the daily charter hire for the Company's chartered-in vessels accounted for as operating leases with firm periods of greater than one year. Under ASU 2016-02, the Company will recognize a right-of-use asset and a lease liability on the balance sheet for these charters based on the present value of future minimum lease payments, whereas currently no right-of-use asset or lease liability is recognized. This will have the result of increasing the Company's assets and liabilities. The pattern of expense recognition of chartered-in vessels is expected to remain substantially unchanged, unless the right-of-use asset becomes impaired. In addition, direct financing lease payments received will be presented as an operating cash inflow instead of an investing cash inflow in the statement of cash flows. The Company expects to disclose in its consolidated financial statements for the year ended December 31, 2018 the quantitative impact of adopting ASU 2016-02.

In June 2016, the FASB issued Accounting Standards Update 2016-13, *Financial Instruments - Credit Losses: Measurement of Credit Losses on Financial Instruments* (or ASU 2016-13). ASU 2016-13 replaces the incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to prepare credit loss estimates. This update is effective for the Company January 1, 2020, with a modified-retrospective approach. The Company is currently evaluating the effect of adopting this new guidance.

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

3. Financial Instruments

a) Fair value measurements

For a description of how the Company estimates fair value and for a description of the fair value hierarchy levels, see note 4 in the Company's audited consolidated financial statements filed with its Annual Report for the period from the date of incorporation on July 5, 2017 to December 31, 2017. The following table includes the estimated fair value and carrying value of those assets and liabilities that are measured at fair value on a recurring basis as well as the estimated fair value of the Company's financial instruments that are not accounted for at fair value on a recurring basis.

	Fair Value Hierarchy Level	September 30, 2018		December 31, 2017	
		Carrying Amount Asset (Liability)	Fair Value Asset (Liability)	Carrying Amount Asset (Liability)	Fair Value Asset (Liability)
		\$	\$	\$	\$
Recurring:					
Cash, cash equivalents and restricted cash	Level 1	93,241	93,241	96,314	96,314
Derivative instruments (note 7)					
Interest rate swap agreements	Level 2	3,412	3,412	441	441
Foreign currency forward contracts	Level 2	(462)	(462)	(582)	(582)
Other:					
Long-term debt, including current portion - public (note 5)	Level 1	(247,222)	(247,545)	(246,687)	(252,138)
Long-term debt, including current portion - non-public (note 5)	Level 2	(959,255)	(983,230)	(977,134)	(1,006,408)

b) Financing Receivables

The following table contains a summary of the Company's financing receivables by type of borrower and the method by which the Company monitors the credit quality of its financing receivables on a quarterly basis:

	Credit Quality Indicator	Grade	September 30, 2018	December 31, 2017
			\$	\$
Direct financing leases	Payment activity	Performing	5,151	5,821

4. Revenues

The Company's primary source of revenues is chartering its shuttle tankers to its customers. The Company utilizes three primary forms of contracts, consisting of contracts of affreightment, time-charter contracts and bareboat charter contracts. During the nine months ended September 30, 2018, the Company also generated revenues from the operation of VOC systems on 13 of the Company's shuttle tankers.

Contracts of affreightment (CoA)

Voyages performed pursuant to a CoA for the Company's shuttle tankers are price based on the pre-agreed terms in the CoA. The performance obligations within a voyage performed pursuant to a CoA, which will typically include the lease of the vessel to the charterer as well as the operation of the vessel, are satisfied as services are rendered over the duration of the voyage, as measured using the time that has elapsed from commencement of performance. In addition, any expenses that are unique to a particular voyage, including any bunker fuel expenses, port fees, cargo loading and unloading expenses, canal tolls, agency fees and commissions, are the responsibility of the vessel owner. Consideration for such voyages consists of a fixed daily hire rate for the duration of the voyage, the reimbursement of costs incurred from fuel consumed during the voyage, as well as fixed lump sum intended to compensate for time necessary for the vessel to return to the field following completion of the voyage. While such consideration is generally fixed, certain sources of variability exist, including variability in the duration of the voyage and the actual quantity of fuel consumed during the voyage. Payment for the voyage is not due until the voyage is completed. The duration of a single voyage will typically be less than two weeks. The Company does not engage in any specific tactics to minimize residual value risk due to the short-term nature of the contracts.

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

Time Charters

Pursuant to a time-charter contract, the Company charters a vessel to a customer for a fixed period of time, generally one year or more. The performance obligations within a time-charter contract, which will include the lease of the vessel to the charterer as well as the operation of the vessel, are satisfied as services are rendered over the duration of such contract, as measured using the time that has elapsed from commencement of performance. In addition, any expenses that are unique to a particular voyage, including any bunker fuel expenses, port fees, cargo loading and unloading expenses, canal tolls, agency fees and commissions, are the responsibility of the customer, as long as the vessel is not off-hire. Hire is typically invoiced monthly in advance for time-charter contracts, based on a fixed daily hire amount. In certain long-term time-charters, the fixed daily hire amount will increase on an annual basis by a fixed amount to offset expected increases in operating costs. As a result of the Company accounting for compensation from such charters on a straight-line basis over the duration of the charter, such fixed increases in rate will result in revenues being accrued in the first half of the charter and such accrual drawn down in the last half of the charter. Some time charters include variable consideration components in the form of expense adjustments or reimbursements, incentive compensation and penalties. For example, certain time charters contain provisions that allow the Company to be compensated for increases in the Company's costs during the term of the charter. Such provisions may be in the form of annual hire rate adjustments for changes in inflation indices or in the form of cost reimbursements for vessel operating expenditures or drydocking expenditures. During periods in which the vessels go off-hire or minimum speed and performance metrics are not met, penalties may be imposed. Variable consideration under the Company's contracts is typically recognized as incurred as either such revenues are allocated and accounted for under lease accounting requirements or alternatively such consideration is allocated to the distinct period in which such variable consideration is earned. The Company does not engage in any specific tactics to minimize residual value risk.

The time charters for the three shuttle tankers servicing the East Coast Canada project can be canceled upon two years' notice. The time charters for four shuttle tankers in Brazil can be extended by up to ten years, at the election of the charterer. The time charters for the vessels serving the Equinor ASA (or *Equinor*) (formerly Statoil ASA) North Sea requirements under the terms of a master agreement are one year in length and are renewed for subsequent one-year periods, however the number of vessels required under the terms of the master agreement may be adjusted annually based on the requirements of the fields serviced.

Bareboat Charters

Pursuant to a bareboat charter contract, the Company charters a vessel to a customer for a fixed period of time, generally one year or more, at rates that are generally fixed. However, the customer is responsible for operation and maintenance of the vessel with their own crew as well as any expenses that are unique to a particular voyage, including any bunker fuel expenses, port fees, cargo loading and unloading expenses, canal tolls, agency fees and commissions. If the vessel goes off-hire due to a mechanical issue or any other reason, the monthly hire received by the vessel owner is normally not impacted by such events. The performance obligations within a bareboat charter, which will include the lease of the vessel to the charterer, are satisfied over the duration of such contract, as measured using the time that has elapsed from commencement of the lease. The customer is typically invoiced monthly in advance for bareboat charters, based on a fixed daily hire amount.

Voyage Charters

Voyage charters are charters for a specific voyage. Voyage charters for the Company's shuttle tankers are priced on a current or "spot" market rate. The performance obligations within a voyage charter contract, which will typically include the lease of the vessel to the charterer as well as the operation of the vessel, are satisfied as services are rendered over the duration of the voyage, as measured using the time that has elapsed from commencement of performance. In addition, expenses that are unique to a particular voyage, including any bunker fuel expenses, port fees, cargo loading and unloading expenses, canal tolls, agency fees and commissions, are the responsibility of the vessel owner. The Company's voyage charters for shuttle tankers will normally contain a lease. Such determination involves judgment about the decision-making rights the charterer has within the contract. Consideration for such contracts is generally fixed, however certain sources of variability exist. Delays caused by the charterer result in additional consideration. Payment for the voyage is not due until the voyage is completed. The duration of a single voyage will typically be less than three months. The Company does not engage in any specific tactics to minimize residual value risk due to the short-term nature of the contracts.

Management Fees and Other

During the nine months ended September 30, 2018, the Company also generates revenues from the operation of VOC systems on 13 of the Company's shuttle tankers and the management of certain vessels on behalf of third parties who are the disponent owners or charterers of these assets. Such services include the arrangement of third party goods and services for the asset's disponent owners or charterers. The performance obligations within these contracts will typically consist of commercial management and administrative services. The performance obligations are satisfied concurrently and consecutively rendered over the duration of the management contract, as measured using the time that has elapsed from commencement of performance. Consideration for such contracts will generally consist of a fixed monthly management fee and all operational costs for the VOC systems. Management fees are typically invoiced monthly.

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

Revenue Table

The following table contains the Company's revenue for the three and nine months ended September 30, 2018 by contract type:

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
	\$	\$
Contracts of affreightment	51,977	140,155
Time charters	72,526	222,218
Bareboat charters	9,039	35,720
Voyage charters	7,924	21,032
Management fees and other ⁽¹⁾	2,832	7,477
Total	144,298	426,602

(1) Represents the Company's revenue from contracts that do not contain a lease element for the three and nine months ended September 30, 2018.

Contract Liabilities

Certain of the customer contracts that the Company enters into will result in situations where the customer will pay for consideration for performance to be provided in the following month or months. These receipts are a contract liability and will be presented as deferred revenue until performance is provided. In other cases, the Company will provide performance in the month or months prior to it being entitled to invoice for such performance. This will result in such receipts being reflected as a contract asset that is presented within other current assets. In addition to these short-term timing differences between the timing of revenue recognition and when the entity's right to consideration in exchange for goods or services is unconditional, the Company has long-term charter arrangements whereby it has received payments that are larger in the earlier periods of the arrangements. The following table presents the contract liabilities associated with these long-term charter arrangements from contracts with customers on the Company's consolidated balance sheet.

	September 30, 2018
	\$
Current	500
Non-Current	1,979
	2,479

During the three and nine months ended September 30, 2018, the Company recognized \$0.1 million and \$0.4 million, respectively, of revenue that was included in contract liabilities at the beginning of the period.

Contract Costs

In certain cases, the Company incurs pre-operational costs that relate directly to a specific customer contract, that generate or enhance resources of the Company that will be used in satisfying performance obligations in the future, whereby such costs are expected to be recovered via the customer contract. Those costs will primarily include costs incurred to reposition a vessel to a location where a charterer will take delivery of the vessel. In certain cases, the Company will need to make judgements about whether costs relate directly to a specific customer contract or whether costs were factored into the pricing of a customer contract and thus expected to be recovered. Such deferred costs are amortized over the duration of the customer contract. Amortization of such costs for the three and nine months ended September 30, 2018 were \$0.5 million and \$1.2 million, respectively.

At September 30, 2018, the balance of assets recognized from the costs to fulfill a contract with a customer totaled \$15.6 million, is categorized as vessel repositioning costs and included within other non-current assets in the consolidated balance sheet.

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

5. Long-Term Debt

	September 30, 2018	December 31, 2017
	\$	\$
Revolving Credit Facility due through 2022	500,000	575,000
Term Loan due through 2021	58,255	85,574
Term Loans due through 2030	288,417	191,916
Non-Public Bonds due 2024	131,104	140,697
Public Bonds due 2022	250,000	250,000
Total principal	1,227,776	1,243,187
Less debt issuance costs and other	(21,299)	(19,366)
Total debt	1,206,477	1,223,821
Less current portion	(141,808)	(159,012)
Long-term portion	1,064,669	1,064,809

As at September 30, 2018, the Company had one revolving credit facility (December 31, 2017 - one), which, as at such date, provided for total borrowings of up to \$500 million, which was fully drawn (December 31, 2017 - fully drawn). The total amount available under the revolving credit facility reduces by \$25.0 million (remainder of 2018), \$100.0 million (2019), \$100.0 million (2020), \$100.0 million (2021), and \$175.0 million (2022). The revolving credit facility is guaranteed by the Company for all outstanding amounts and is collateralized by first-priority mortgages granted on 17 of the Company's vessels, together with other related security.

As at September 30, 2018, two of the Company's 50%-owned subsidiaries (December 31, 2017 - three) had one outstanding term loan (December 31, 2017 - two), which totaled \$58.3 million (December 31, 2017 - \$85.6 million). The term loan reduces over time with quarterly payments and matures in 2021. The term loan is collateralized by first-priority mortgages on the two shuttle tankers to which the loan relates, together with other related security. As at September 30, 2018, a subsidiary of the Company guaranteed \$29.1 million of the term loan, which represents its 50% share of the outstanding term loan, and the other owner had guaranteed the remaining \$29.1 million of the term loan.

As at September 30, 2018, the Company had two term loans (December 31, 2017 - one) outstanding for three shuttle tankers. During the nine months ended September 30, 2018, one term loan was re-financed with a five-year \$265.8 million debt facility and an additional \$30.0 million junior debt facility was secured by the same three shuttle tankers. As at September 30, 2018, the carrying value of the term loans was \$288.4 million (December 31, 2017 - \$191.9 million) and one facility reduces over time with semi-annual payments. These term loans have varying maturities through 2030 and are collateralized by first-priority mortgages on the vessels to which the term loans relate, together with other related security. As at September 30, 2018, the Company had guaranteed both term loans.

Interest payments on the revolving credit facility and the term loans are based on LIBOR plus margins. At September 30, 2018, the margins ranged between 1.85% and 4.30% (December 31, 2017 - 2.40% and 3.50%). The weighted-average interest rate on the Company's variable rate long-term debt as at September 30, 2018 was 5.2% (December 31, 2017 - 4.7%). This rate does not include the effect of the Company's interest rate swaps (see note 7) or fixed rate facilities.

In September 2013 and November 2013, one of the Company's subsidiaries issued, in a U.S. private placement, a total of \$174.2 million of ten-year senior bonds that mature in January 2024 to finance the *Bossa Nova Spirit* and *Sertanejo Spirit* shuttle tankers. The bonds accrue interest at a fixed combined rate of 4.96%. The bonds are collateralized by first-priority mortgages on the two vessels to which the bonds relate, together with other related security. The subsidiary makes semi-annual repayments on the bonds and as at September 30, 2018, the carrying amount of the bonds was \$131.1 million (December 31, 2017 - \$140.7 million).

In August 2017, the Company entered into an agreement to issue \$250.0 million in senior unsecured bonds in the Norwegian bond market that mature in August 2022. In October 2017, the Company completed the issuance of these bonds when the conditions precedent were met which included the sale of the Subsidiaries by Teekay Offshore to the Company. These bonds are listed on the Oslo Stock Exchange. As at September 30, 2018, the carrying amount of the bonds was \$250.0 million. The interest payments on the bonds are fixed at a rate of 7.125%.

The aggregate annual long-term debt principal repayments required to be made subsequent to September 30, 2018 are \$40.3 million (remainder of 2018), \$143.0 million (2019), \$141.9 million (2020), \$162.0 million (2021), \$443.5 million (2022), and \$297.0 million (thereafter).

The Company's revolving credit facility, term loans and bonds contain covenants, debt-service coverage ratio (or *DSCR*) requirements and other restrictions typical of debt financing secured by vessels that restrict the ship-owning subsidiaries from incurring or guaranteeing indebtedness; changing ownership or structure, including mergers, consolidations, liquidations and dissolutions; making dividends or distributions if the Company is in default or do not meet minimum *DSCR* requirements; making capital expenditures in excess of specified levels; making certain negative pledges and granting certain liens; selling, transferring, assigning or conveying assets; making certain loans and investments; or entering into a new line of business. Obligations under the Company's credit facilities are secured by certain vessels, and if the Company is unable to repay debt under the credit facilities, the lenders could seek to foreclose on those

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

assets. The Company has one revolving credit facility and three term loans that require the Company to maintain vessel values to drawn principal balance ratios of a minimum range of 100% to 125%. Such requirement is assessed either on a semi-annual or annual basis, with reference to vessel valuations compiled by one or more agreed upon third parties. Should the ratio drop below the required amount, the lender may request the Company to either prepay a portion of the loan in the amount of the shortfall or provide additional collateral in the amount of the shortfall, at the Company's option. As at September 30, 2018, these ratios were estimated to range from 120% to 200% and the Company was in compliance with the minimum ratios required. The vessel values used in calculating these ratios are the appraised values provided by third parties where available, or prepared by the Company based on second-hand sale and purchase market data. Changes in the shuttle tanker market could negatively affect these ratios.

Certain loan agreements require that (a) the Company maintain a minimum liquidity (cash, cash equivalents and undrawn committed revolving credit lines with at least six months to maturity) in an amount equal to the greater of \$35.0 million and 5.0% of the Company's total consolidated debt, (b) the Company to maintain a net debt to total capitalization ratio no greater than 75.0%, and (c) a minimum ratio of 12 months' historical EBITDA relative to total interest expense and installments of 1.20 times. As at September 30, 2018, the Company was in compliance with all covenants related to the credit facilities and consolidated long-term debt.

6. Related Party Transactions

- a) During the three months ended September 30, 2018, two shuttle tankers of the Company were employed on long-term time-charter-out contracts with subsidiaries of Teekay Corporation. During the nine months ended September 30, 2018, three shuttle tankers of the Company were employed on long-term time-charter-out contracts with subsidiaries of Teekay Corporation. Teekay Corporation, a portfolio manager of marine services to the global oil and natural gas industries, owns approximately 14% of Teekay Offshore Partners L.P.'s outstanding common units.
- b) Teekay Offshore Partners L.P. and its wholly-owned subsidiaries provided substantially all of the Company's commercial, technical, crew training, strategic, business development and administrative service needs. Such related party transactions were as follows for the periods indicated:

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
	\$	\$
Revenues ⁽¹⁾	11,759	35,810
Vessel operating expenses ⁽²⁾	(804)	(10,539)
General and administrative ⁽³⁾	(6,109)	(11,678)

(1) Includes revenues from time-charter-out contracts with subsidiaries or affiliates of Teekay Corporation and management fees charged by one of the Company's subsidiaries to Teekay Corporation and its subsidiaries.

(2) Includes ship management and crew training services provided by Teekay Offshore Partners L.P. and its subsidiaries.

(3) Includes commercial, technical, strategic, business development and administrative management fees charged by Teekay Corporation and its subsidiaries or affiliates and Teekay Offshore Partner L.P. and its subsidiaries or affiliates.

- c) At September 30, 2018, the carrying value of due from affiliates totaled \$134.5 million and of due to affiliates totaled \$157.3 million. Amounts due to and from affiliates are non-interest bearing and unsecured, and all current due to and from affiliates balances are expected to be settled within the next 12 months in the normal course of operations or from financings. Affiliates includes Teekay Corporation and certain of its wholly owned subsidiaries and Teekay Offshore Partners L.P. and certain of its subsidiaries.

7. Derivative Instruments and Hedging Activities

The Company uses derivatives to manage certain risks in accordance with its overall risk management policies.

Foreign Exchange Risk

The Company economically hedges portions of its forecasted expenditures denominated in foreign currencies with foreign currency forward contracts. The Company has not designated, for accounting purposes, any of the foreign currency forward contracts held during the three or nine months ended September 30, 2018 as cash flow hedges.

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

As at September 30, 2018, the Company was committed to the following foreign currency forward contracts:

	Contract Amount in Foreign Currency (thousands)	Fair Value / Carrying Amount of Asset (Liability) (in thousands of U.S. Dollars)	Average Forward Rate ⁽¹⁾	Expected Maturity	
				2018	2019
(in thousands of U.S. Dollars)					
Norwegian Kroner	230,000	(462)	7.96	7,587	21,312

(1) Average forward rate represents the contracted amount of foreign currency one U.S. Dollar will buy.

Interest Rate Risk

The Company enters into interest rate swaps, which exchange a receipt of floating interest for a payment of fixed interest, to reduce the Company's exposure to interest rate variability on its outstanding floating-rate debt. During the three months ended September 30, 2018, the Company de-designated, for accounting purposes, its interest rate swap. As at September 30, 2018, the Company was committed to the following interest rate swap agreement:

	Interest Rate Index	Notional Amount \$	Fair Value / Carrying Amount of Assets (Liabilities) \$	Weighted - Average Remaining Term (years)	Fixed Interest Rate (%) ⁽¹⁾
U.S. Dollar-denominated interest rate swap	LIBOR	100,000	3,412	4.0	2.1%

(1) Excludes the margin the Company pays on its variable-rate debt, which at September 30, 2018, ranged from 1.85% to 4.30%.

For the period indicated, the following table presents the effective and ineffective portion of the gain on interest rate swap agreements designated and qualifying as cash flow hedges.

Three Months Ended September 30, 2018			
Effective Portion Recognized in AOCI ⁽¹⁾	Effective Portion Reclassified from AOCI ⁽²⁾	Ineffective Portion ⁽³⁾	
—	58	—	Interest expense
—	58	—	

Nine Months Ended September 30, 2018			
Effective Portion Recognized in AOCI ⁽¹⁾	Effective Portion Reclassified from AOCI ⁽²⁾	Ineffective Portion ⁽³⁾	
(2,495)	6	—	Interest expense
(2,495)	6	—	

(1) Effective portion of designated and qualifying cash flow hedges recognized in accumulated other comprehensive income (or AOCI).

(2) Effective portion of designated and qualifying cash flow hedges recorded in AOCI during the term of the hedging relationship and reclassified to earnings.

(3) Ineffective portion of designated and qualifying cash flow hedges.

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

Tabular disclosure

The following table presents the location and fair value amounts of derivative instruments, segregated by type of contract, on the Company's consolidated balance sheets.

	Current portion of derivative assets	Other non- current assets	Accrued liabilities	Current portion of derivative liabilities	Derivative liabilities
	\$	\$	\$	\$	\$
As at September 30, 2018					
Foreign currency contracts	56	41	—	(527)	(32)
Interest rate swap	627	2,785	—	—	—
	<u>683</u>	<u>2,826</u>	<u>—</u>	<u>(527)</u>	<u>(32)</u>
As at December 31, 2017					
Foreign currency contracts	104	28	—	(647)	(67)
Interest rate swap	—	677	(2)	(236)	—
	<u>104</u>	<u>705</u>	<u>(2)</u>	<u>(883)</u>	<u>(67)</u>

Total realized and unrealized gain on interest rate swap and foreign currency forward contracts that are not designated for accounting purposes as cash flow hedges are recognized in earnings and reported in realized and unrealized gain on derivative instruments in the consolidated statements of income (loss). The effect of the gain on these derivatives in the consolidated statements of income (loss) for the three and nine months ended September 30, 2018 is as follows:

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
	\$	\$
Realized (loss) gain on derivative instruments		
Interest rate swaps	61	61
Foreign currency forward contracts	(202)	100
	<u>(141)</u>	<u>161</u>
Unrealized gain on derivative instruments		
Interest rate swaps	477	477
Foreign currency forward contracts	215	120
	<u>692</u>	<u>597</u>
Total realized and unrealized gain on derivative instruments	<u>551</u>	<u>758</u>

The Company is exposed to credit loss in the event of non-performance by the counterparties, all of which are financial institutions, to the foreign currency forward contracts and the interest rate swap agreements.

8. Income Taxes

The components of the provision for income taxes are as follows:

	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2018
	\$	\$
Current	443	778
Deferred	—	13,920
Income tax expense	<u>443</u>	<u>14,698</u>

TEEKAY SHUTTLE TANKERS L.L.C.
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(all tabular amounts stated in thousands of U.S. dollars, except unit and per unit data or unless otherwise indicated)

9. Commitments and Contingencies

In 2017, certain subsidiaries of the Company entered into shipbuilding contracts with Samsung Heavy Industries Co., Ltd. to construct four Suezmax DP2 shuttle tanker newbuildings, for an aggregate fully built-up cost of approximately \$601 million. These newbuilding vessels are being constructed based on the Company's new *Shuttle Spirit* design which incorporates technologies intended to increase fuel efficiency and reduce emissions, including liquefied natural gas (or LNG) propulsion technology. Upon expected delivery in late-2019 through 2020, these vessels are to provide shuttle tanker services in the North Sea, with two to operate under the Company's existing master agreement with Equinor, and two to operate directly within the North Sea CoA fleet, which will add vessel capacity to service the Company's CoA portfolio in the North Sea. As at September 30, 2018, payments made towards these commitments were \$63.3 million and the remaining payments required to be made are estimated to be \$26.7 million (remainder of 2018), \$321.5 million (2019) and \$189.0 million (2020). The Company expects to secure long-term debt financing related to these shuttle tanker newbuildings.

In July 2018, certain subsidiaries of the Company entered into shipbuilding contracts with Samsung Heavy Industries Co. Ltd., to construct two Aframax DP2 shuttle tanker newbuildings, for an estimated aggregate fully built-up cost of \$270 million. These newbuildings will be constructed based on the Company's new *Shuttle Spirit* design. Upon delivery in late-2020 through early-2021, these vessels will join the Company's CoA portfolio in the North Sea. As at September 30, 2018, payments made towards these commitments were \$11.9 million and the remaining payments required to be made are estimated to be \$0.6 million (remainder of 2018), \$55.9 million (2019), \$122.7 million (2020) and \$78.7 million (2021).

10. Gain on sale and (write-down) of vessels

During the three and nine months ended September 30, 2018, the Company sold the 2001-built shuttle tanker, the *Stena Spirit*, for net proceeds of \$8.8 million. The consolidated statement of income (loss) for the three and nine months ended September 30, 2018 includes a \$0.4 million gain related to the sale of this vessel, which is included in a 50%-owned subsidiary of the Company.

During the nine months ended September 30, 2018, the Company sold a 1998-built shuttle tanker, the *Navion Britannia*, for net proceeds of \$10.4 million. The Company's consolidated statements of income (loss) for the nine months ended September 30, 2018 includes a \$2.6 million gain related to the sale of this vessel.

During the nine months ended September 30, 2018, the carrying value of the *Nordic Spirit* and *Stena Spirit* shuttle tankers were written down to their estimated fair values, using appraised values, due to the redelivery of these vessels from their charterer after completing their bareboat charter contracts in May 2018 and the resulting change in the expectations for the future opportunities for the vessels. The Company's consolidated statement of income (loss) for the nine months ended September 30, 2018 includes a \$29.7 million write-down related to these vessels, of which \$14.8 million is included in a 50%-owned subsidiary of the Company.

11. Supplemental Cash Flow Information

The following is a tabular reconciliation of the Company's cash, cash equivalents and restricted cash balances for the periods presented in these consolidated financial statements:

	As at September 30, 2018	As at December 31, 2017	As at September 30, 2017
	\$	\$	\$
Cash and cash equivalents	90,481	96,314	90,023
Restricted cash ⁽¹⁾	2,760	—	—
	93,241	96,314	90,023

(1) Restricted cash as at September 30, 2018 includes amounts held in escrow for certain future dry-dock costs.

12. Subsequent Events

In October 2018, the Company sold the 1998-built shuttle tanker, the *Stena Alexita*, which had a carrying value of \$7.5 million, to a subsidiary of Teekay Offshore Partners L.P. for gross proceeds of \$8.5 million. The vessel was included in a 50%-owned subsidiary of the Company.

In November 2018, the Company sold the 1998-built shuttle tanker, the *Navion Scandia*, which had a carrying value of \$8.6 million, for gross proceeds of \$10.3 million.

FORWARD-LOOKING STATEMENTS

This quarterly report contains certain forward-looking statements concerning future events and our operations, performance and financial condition, including, in particular, statements regarding:

- our future growth prospects, business strategy and other plans and objectives for future operations;
- future capital expenditures and availability of capital resources to fund capital expenditures;
- our liquidity needs and sufficiency of cash flows;
- the expected lifespan and residual value of our vessels;
- our ability to leverage the expertise, relationships and reputation of Teekay Offshore and Brookfield;
- certainty of completion, estimated delivery and completion dates, commencement of charter, intended financing and estimated costs for newbuildings and acquisitions, including the shuttle tanker newbuildings;
- the expected employment of the newbuilding shuttle tankers under our existing master agreement with Equinor and the expected required capacity in our CoA fleet in the North Sea;
- expected employment and trading of older shuttle tankers;
- our entering into joint ventures and partnerships with companies;
- our ability to maximize the use of our vessels, including the re-deployment or disposition of vessels no longer under long-term time charter contracts;
- our position as the leading provider of CoA shuttle tanker services in the North Sea;
- timing of settlement of amounts due to and from affiliates;
- the potential impact and timing of adoption of new accounting policies;
- the future valuation of goodwill and potential impairment;
- our compliance with covenants under our credit facilities;
- the ability of the counterparties for our derivative contracts to fulfill their contractual obligations;
- our hedging activities relating to foreign exchange and interest rate risks;
- our exposure to foreign currency fluctuations, particularly in Norwegian Kroner;
- the passage of climate control legislation or other regulatory initiatives that restrict emissions of greenhouse gases;
- our expected use of proceeds from debt issuances; and
- increasing the efficiency of our business and redeploying vessels as charters expire or terminate.

Forward-looking statements include, without limitation, any statement that may predict, forecast, indicate or imply future results, performance or achievements, and may contain the words "believe", "anticipate", "expect", "estimate", "project", "will be", "will continue", "will likely result", "plan", "intend" or words or phrases of similar meanings. These statements involve known and unknown risks and are based upon a number of assumptions and estimates that are inherently subject to significant uncertainties and contingencies, many of which are beyond our control. Actual results may differ materially from those expressed or implied by such forward-looking statements. Important factors that could cause actual results to differ materially include, but are not limited to: changes in the demand for offshore oil transportation; greater or less than anticipated levels of vessel newbuilding orders or greater or less than anticipated rates of vessel recycling; changes in trading patterns; changes in our expenses; the timing of implementation of new laws and regulations; potential inability to implement our growth strategy; competitive factors in the markets in which we operate; potential for early termination of long-term contracts and our potential inability to renew or replace long-term contracts; loss of any customer, time charter or vessel; shipyard production or vessel delivery delays; failure to raise financing to refinance debt maturities, fund existing projects or purchase additional vessels; levels of cash reserves required by any financing agreements; our exposure interest rate and currency exchange rate fluctuations; changes to the amount or proportion of revenues and expenses denominated in foreign currencies; delays in the start-up of offshore oil fields related to the CoA contracts or the actual vessel equivalent requirements of new CoAs; and other risk factors detailed from time to time in our periodic reports filed with the Oslo Bors, including our Annual Report for the year ended December 31, 2017. We do not intend to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with respect thereto or any change in events, conditions or circumstances on which any such statement is based.