Aldeyra Therapeutics, Inc.
Form 10-K
March 30, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One)

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

For the fiscal year ended December 31, 2016

OR

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

For transition period from _____ to _____

Commission File Number 001-36332

ALDEYRA THERAPEUTICS, INC.

(Exact name of Registrant as specified in its charter)

Delaware	**20-1968197**
(State or other jurisdiction of incorporation)	**(IRS Employer Identification No.)**

131 Hartwell Avenue, Suite 320

Lexington, MA 02421

(Address of principal executive offices)

(781) 761-4904

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, $0.001 par value per share	**The NASDAQ Stock Market, LLC**
(Title of each class)	**(Name of each exchange on which registered)**

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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	(Do not check if a smaller reporting company)	Smaller reporting company	

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

As of June 30, 2016, the last business day of the registrant s last completed second quarter, the aggregate market value of the Common Stock held by non-affiliates of the registrant was approximately $59,217,833, based on the closing price of the registrant s Common Stock, as reported by the NASDAQ Capital Market. Shares of Common Stock held by each executive officer, director and stockholders known by the registrant to be affiliated with such individuals based on public filings and other information known to the registrant have been excluded since such persons may be deemed affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of March 30, 2017 there were 15,131,880 shares of the registrant s Common Stock issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Specified portions of the registrant s proxy statement with respect to the registrant s 2017 Annual Meeting of Stockholders, which is to be filed pursuant to Regulation 14A within 120 days after the end of the registrant s fiscal year ended December 31, 2016, are incorporated by reference into Part III of this Annual Report on Form 10-K.

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Aldeyra Therapeutics, Inc.

Annual Report on Form 10-K

For the Fiscal Year Ended December 31, 2016

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Various statements in this report are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve substantial risks and uncertainties. All statements, other than statements of historical facts, included in this report regarding our strategy, future operations, future financial position, future revenues, projected costs, prospects, plans and objectives of management are forward-looking statements. These statements are subject to risks and uncertainties and are based on information currently available to our management. Words such as, but not limited to, anticipate, believe, estimate, expect, int may, plan, contemplates, predict, project, target, likely, potential, continue, ongoing, design, would, should, could, or the negative of these terms and similar expressions or words, identify forward-looking statements. These statements reflect our current views with respect to future events and are based on assumptions and subject to risks and uncertainties. Given these uncertainties, you should not place undue reliance on these forward-looking statements. The events and circumstances reflected in our forward-looking statements may not occur and actual results could differ materially from those projected in our forward-looking statements. Meaningful factors which could cause actual results to differ include, but are not limited to:

- the timing of enrollment, commencement, and completion of our clinical trials;
- the timing and success of preclinical studies and clinical trials conducted by us and our development partners;
- the ability to obtain and maintain regulatory approval of our product candidates, and the labeling for any approved products;
- the scope, progress, expansion, and costs of developing and commercializing our product candidates;
- the size and growth of the potential markets and pricing for our product candidates and the ability to serve those markets;
- our expectations regarding our expenses and revenue, the sufficiency or use of our cash resources and needs for additional financing;
- the rate and degree of market acceptance of any of our product candidates;
- our expectations regarding competition;
- our anticipated growth strategies;

our ability to attract or retain key personnel;

our ability to establish and maintain development partnerships;

our expectations regarding federal, state and foreign regulatory requirements;

regulatory developments in the United States and foreign countries;

our ability to obtain and maintain intellectual property protection for our product candidates; and

the anticipated trends and challenges in our business and the market in which we operate.

All written and verbal forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We caution investors not to rely too heavily on the forward-looking statements we make or that are made on our behalf. We undertake no obligation, and specifically decline any obligation, to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosures we make on related subjects in any annual, quarterly or current reports that we may file with the Securities and Exchange Commission.

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We encourage you to read the discussion and analysis of our financial condition and our financial statements contained in this annual report on Form 10-K. We also encourage you to read Item 1A of Part 1 of this annual report on Form 10-K, entitled Risk Factors, which contains a more complete discussion of the risks and uncertainties associated with our business. In addition to the risks described above and in Item 1A of this report, other unknown or unpredictable factors also could affect our results. Therefore, the information in this report should be read together with other reports and documents that we file with the SEC from time to time, including Forms 10-Q, 8-K and 10-K, which may supplement, modify, supersede or update those risk factors. There can be no assurance that the actual results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, us. Therefore, no assurance can be given that the outcomes stated in such forward-looking statements and estimates will be achieved.

As used in this annual report on Form 10-K, the terms Aldeyra, Registrant, we, us, and our mean Aldeyra Therapeutics, Inc. unless the context indicates otherwise.

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INDUSTRY AND MARKET DATA

We obtained the industry, market and certain other data used throughout this annual report on Form 10-K from our own internal estimates and research, as well as from industry and general publications, in addition to research, surveys and studies conducted by third parties. Internal estimates are derived from publicly-available information released by industry analysts and third-party sources, our internal research and our industry experience, and are based on assumptions made by us based on such data and our knowledge of our industry and market, which we believe to be reasonable. In addition, while we believe the industry, market and other data included in this annual report on Form 10-K is reliable and is based on reasonable assumptions, such data involves risks and uncertainties and are subject to change based on various factors, including those discussed in Risk Factors. These and other factors could cause results to differ materially from those expressed in the estimates made by the independent parties and by us.

ITEM 1. *BUSINESS*

Overview

We are a biotechnology company focused primarily on the development of new products for inflammation, inborn errors of metabolism, and other diseases that are thought to be related to endogenously generated toxic and pro-inflammatory chemical species known as aldehydes. We are developing ADX-102 (formerly known as NS2), as well as other novel product candidates, including ADX-103 and ADX-104, that are designed specifically to sequester aldehydes for the treatment of:

- Noninfectious Anterior Uveitis, a rare but severe inflammatory eye disease that can lead to blindness;
- Allergic Conjunctivitis, a common disease that affects more than 20% of the population worldwide, and related rare allergic ocular diseases that are characterized by inflammation of the conjunctiva (a membrane covering part of the front of the eye), resulting in ocular itching, excessive tear production, swelling, and redness;
- Dry Eye Syndrome, a common inflammatory disease characterized by insufficient moisture and lubrication associated with the anterior surface of the eye, leading to ocular irritation, burning, stinging, and, in severe cases, loss of vision;
- Sjögren-Larsson Syndrome (SLS), a rare inborn error of metabolism caused by mutations in an enzyme that metabolizes fatty aldehydes, resulting in severe skin and neurological disorders; and
- Succinic Semi-Aldehyde Dehydrogenase Deficiency (SSADH), a rare inborn error of metabolism caused by genetic mutations in an aldehyde-metabolizing enzyme, leading to severe neurological disease.

In February 2016, we announced that the results of a randomized, parallel-group, double-masked, vehicle-controlled Phase 2a clinical trial of ADX-102 ophthalmic solution in patients with allergic conjunctivitis demonstrated

statistically and clinically significant activity of ADX-102 over vehicle in reducing ocular itching and tearing. In May 2016, we announced that the results of our randomized, parallel-group, investigator-masked, active-controlled Phase 2 clinical trial of ADX-102 ophthalmic solution in patients with noninfectious anterior uveitis demonstrated that ADX-102 reduced inflammatory cell count in the anterior chamber of the eye to a degree similar to that of standard-of-care corticosteroid therapy (which may lead to cataracts and glaucoma in some patients), but without the intraocular pressure elevations that were observed in subjects treated with corticosteroids. In August 2016, we announced that the results of a randomized, parallel-group, double-blind, vehicle-controlled clinical trial of a dermatologic formulation of ADX-102 for the treatment of the skin manifestations of SLS demonstrated clinically relevant activity of ADX-102 in diminishing the severity of ichthyosis, a serious dermatologic disease characteristic of SLS. In all clinical trials to date, ADX-102 was well tolerated, and no serious adverse events have been reported.

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In February 2017, we announced the enrollment of the first patient in a Phase 2b clinical trial of topical ocular ADX-102 for the treatment of allergic conjunctivitis. We expect to begin a planned Phase 3 clinical trial of topical ocular ADX-102 for the treatment of noninfectious anterior uveitis in the second quarter of 2017. We expect to begin a planned Phase 3 clinical trial of topical dermatologic ADX-102 for the treatment of the skin manifestations of SLS in the second half of 2017. We expect to begin a planned Phase 2a clinical trial of topical ocular ADX-102 for the treatment of Dry Eye Syndrome in the second quarter of 2017. Contingent on preclinical results, regulatory feedback, and other factors, we may also initiate a planned Phase 2a clinical trial of ADX-103 in Dry Eye Syndrome. We expect to begin a planned Phase 1 clinical trial of systemically administered ADX-102 or ADX-104 in the first half of 2018. We expect to begin systemically administered Phase 2a clinical trials in SLS and SSADH in the second half of 2018. All of our development timelines may be subject to adjustment depending on recruitment rate, regulatory review, preclinical and clinical results, and other factors that could delay the initiation or completion of clinical trials. Our clinical development pipeline is summarized in the figure below.

Clinical Development Pipeline

Since our incorporation, we have devoted substantially all of our resources to the preclinical and clinical development of our product candidates. Our ability to generate revenues largely depends upon our ability, alone or with others, to complete the development of our product candidates to obtain the regulatory approvals for and to manufacture, market and sell our products and product candidates. The results of our operations will vary significantly from year-to-year and quarter-to-quarter and depend on a number of factors, including risks related to our business and industry, risks relating to intellectual property and other legal matters, risks related to our common stock, and other risks that are detailed in the section of this annual report on Form 10-K entitled Risk Factors.

Business Strategy

We intend to develop ADX-102 and other novel aldehyde traps for the diseases described above as well as potentially other diseases where aldehydes may mediate pathology. We believe that aldehyde trapping is a novel approach with broad therapeutic potential in inflammatory diseases and inborn errors of aldehyde metabolism. Accordingly, we have patented and will continue to attempt to patent novel drug compositions, formulations, and methods that relate to aldehyde trapping. While we may continue to develop and eventually attempt to market aldehyde traps for certain diseases following regulatory approval, if any, we may also partner with larger companies to develop and commercialize products for other diseases where aldehyde toxicity is implicated, particularly diseases that afflict large populations worldwide.

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Specifically, our business strategy is to:

Continue the development of and pursue regulatory approval for ADX-102 and other aldehyde traps. We have initiated clinical trials of ADX-102 in several diseases, and we may initiate clinical trials of ADX-103, ADX-104, and other aldehyde traps. If sufficient safety and efficacy is demonstrated over multiple clinical trials as part of the standard drug development process, we intend to apply to the United States Food and Drug Administration (FDA) and comparable foreign agencies for marketing approval of our product candidates.

Aggressively develop new intellectual property and consider partnerships to accelerate development and maximize commercial potential. We have discovered and synthesized a variety of aldehyde traps that we intend to develop and patent for new indications. For some indications, especially those that afflict large populations worldwide, we will consider development and commercialization licensing opportunities with strategic partners that have significant financial resources, commercialization experience, and global infrastructure.

Explore building in-house capabilities to commercialize ADX-102, ADX-103, and ADX-104 in the United States and other geographies. As, and if, ADX-102 and our other product candidates progress through clinical programs, in addition to partnering opportunities that we may consider, we also intend to evaluate the development of our own specialty sales force and marketing capabilities to allow us to directly market our product candidates in the United States or in other geographies, if approved by FDA or analogous regulatory agencies outside the United States.

Consider in-licensing complementary drug programs. We may consider in-licensing additional product candidates or technology rights that are unrelated to aldehyde trapping but complementary to our current development programs.

The Markets for Our Product Candidates

Occurring generally as a result of a large number of metabolic processes, aldehydes are an endogenously generated chemical species that, among other things, promote inflammation. At high levels, aldehydes are toxic and are implicated as mediators of many inflammatory diseases. Other diseases thought to be related to aldehydes include inborn errors of metabolism, where genetic mutations lead to the incapacity to metabolize certain toxic aldehydes. We believe that the medical needs of the patients suffering from aldehyde-mediated diseases are not currently well addressed and that there is a large market potential for therapies that can lower aldehyde levels. In particular, current therapies for inflammatory diseases are often inadequate and may lead to toxicity, and there are no FDA-approved therapies specifically indicated for inborn errors of aldehyde metabolism.

Allergic Conjunctivitis

Allergic conjunctivitis is a common allergic disease that is thought to be mediated in part by pro-inflammatory aldehydes, and is characterized by inflammation of the conjunctiva, resulting in excessive ocular itching and tear production in addition to ocular swelling and redness. Allergic conjunctivitis has been estimated to affect more than 20% of the population worldwide. The mainstay of therapy for allergic conjunctivitis is anti-histamines, which may

lead to mydriasis (large pupils) and, in some patients, blurry vision. Further, approximately one million patients in the United States do not respond to anti-histamines, especially after the acute effects of the medication subside. Many anti-histamine refractory patients are treated with corticosteroids, which often lead to a variety of ocular toxicities that include glaucoma (a potentially blinding disease characterized by elevated intraocular pressure), cataracts (lens opacities that can lead to loss of vision), ocular infection, and ulceration. Other ocular diseases related to allergic conjunctivitis include atopic keratoconjunctivitis (AKC), a rare condition characterized by persistent allergic inflammation of the front of the eye. Treatment of AKC generally requires chronic corticosteroid administration, and physicians treating AKC patients must continuously balance the severity of the disease with the toxicity of corticosteroids.

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By trapping pro-inflammatory aldehydes, we believe ADX-102 may reduce inflammation in allergic conjunctivitis, AKC, and related diseases. ADX-102 may also reduce the burden of corticosteroid use in patients with persistent disease or in patients that do not respond adequately to anti-histamines. Given the toxicity of corticosteroids, we believe that there is a high demand for a novel topical anti-inflammatory agent to be used in conjunction with lower doses of, or in place of, corticosteroids.

Noninfectious Anterior Uveitis

Noninfectious anterior uveitis is an inflammatory ocular disease that is associated with elevated aldehyde levels and is characterized by severe pain, sensitivity to light, and loss of vision that can progress to blindness. The disease may occur with other autoimmune diseases. The annual incidence of noninfectious anterior uveitis in the United States is estimated to be 150,000 patients, and approximately one-third of these patients have one or more episodes per year. The disease is typically treated with topical corticosteroids, and many patients are at risk of developing glaucoma and cataracts as a result of corticosteroid treatment. Corticosteroids may also increase the incidence of infection and corneal ulceration.

By trapping pro-inflammatory aldehydes, we believe ADX-102 may diminish inflammation in noninfectious anterior uveitis and reduce the burden of corticosteroid use. Given the toxicity of corticosteroids, we believe that there is a high demand for a novel topical anti-inflammatory agent to be used in conjunction with lower doses of, or in place of, corticosteroids.

Dry Eye Syndrome

Dry Eye Syndrome is a common inflammatory disease that is estimated to affect five to ten percent of the population in the United States, and is characterized by insufficient moisture and lubrication of the anterior surface of the eye. Symptoms may include ocular irritation, burning, or stinging, and severe cases may lead to loss of vision. In patients with Dry Eye Syndrome, elevated ocular levels of pro-inflammatory aldehydes are correlated with disease severity and likely contribute to persistent inflammation. Since aldehydes covalently bind to lipids (fats) found in tears, the increased aldehyde load in Dry Eye Syndrome patients may also exacerbate insufficient ocular surface lubrication.

Until 2016, only one drug had been approved by the FDA for the treatment of Dry Eye Syndrome, and therapy for the disease is generally considered by patients and physicians to be inadequate. Patients with severe cases of Dry Eye Syndrome may require corticosteroids. Since lowering aldehyde levels may diminish ocular inflammation and preserve tear lubricating capacity in patients with Dry Eye Syndrome, ADX-102 and ADX-103 represent a potential novel, dual-acting therapeutic approach that could be used to augment the efficacy of currently available medications and, in severe cases, reduce or eliminate the need for corticosteroid therapy.

Sjögren-Larsson Syndrome

SLS is caused by genetic mutations of fatty aldehyde dehydrogenase (FALDH), an enzyme that converts long-chain aldehydes to fatty acids. FALDH dysfunction leads to fatty aldehyde accumulation, which is thought to result in a severe skin disorder called ichthyosis, which is characterized by thick, scaly, flaking, itchy and inflamed skin involving much of the body surface area, as well as mental delay, spasticity, and, in some patients, retinal disorders. SLS patients are generally diagnosed as neonates given the severe ichthyosis that presents at birth. The disease persists lifelong, and SLS patients have a shortened lifespan, often dying in the sixth decade of life. Some SLS patients are believed to inherit the disease, though most occurrences of SLS appear to be due to sporadic mutations. The disease occurs worldwide. To our knowledge, Sweden is currently the only country to have estimated the prevalence of the disease, at 1 per 250,000 people. Extrapolating from the Swedish estimate, it is generally assumed

that there are approximately 1,000 or fewer SLS patients in the United States and a larger number in Europe. The United States SLS prevalence estimate is supported by frequency analysis of FALDH missense mutations in the National Heart, Lung, and Blood Institute exome sequencing database. We believe that

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many older SLS patients may be undiagnosed, potentially due to the lack of available dermatologic and genetic medicine expertise available when those patients were younger. There is no FDA-approved treatment specifically indicated for SLS.

The primary day-to-day complaint of SLS patients and their caregivers is ichthyosis, a severe skin disease characterized in SLS patients by thick, scaly, dry, flaking, wrinkled, pigmented, pruritic (itchy), inflamed skin. SLS patients are consistently disturbed by pruritus and often excoriate skin by scratching. The scales that accumulate on the surface of the skin are subject to bacterial overgrowth, which results in an unpleasant odor that is associated with some SLS patients. The ichthyosis in SLS affects most of the body, generally sparing only the face, palms, and soles, and considerable social stigma and emotional burden is common, especially given scale odor, the flaking skin, and the misconception that patients suffer from diffuse cutaneous infectious disease. There is currently no specific therapy approved for the treatment of the dermatologic disease in SLS, though some patients and their caregivers apply non-specific topical creams, including keratinolytics (acids that soften skin), moisturizers, and retinoids. We believe that the effects of keratinolytic and moisturizing creams are minimal or non-existent in treating severe ichthyosis, and due to toxicity, retinoids are not suitable for chronic use.

The dermatologic disease in SLS is thought to be caused by aldehyde-mediated modification of lipids (fats) that are generated in the epidermis (the most superficial layer of skin) to form a moisture barrier that holds water in the skin. Moisture barrier compromise leads to water loss, which in turn leads to epidermal thickening characteristic of ichthyosis. We believe that by lowering levels of aldehydes and thereby preventing lipid modification and the ensuing moisture barrier dysfunction, ADX-102, when applied topically to the skin, has the potential to ameliorate the dermatologic symptoms of SLS. Further, by reducing aldehyde load throughout the body, we believe the systemic administration of ADX-102, ADX-104, or other aldehyde traps may be beneficial in the treatment of the neurological and ocular symptoms of SLS.

Succinic Semi-Aldehyde Dehydrogenase Deficiency

SSADH Deficiency is a neurological disease caused by mutations in succinic semi-aldehyde dehydrogenase that result in elevated levels of succinic semi-aldehyde, a toxic aldehyde that is converted into gamma-hydroxybutyrate (GHB) and other metabolites that lead to severe neurological dysfunction, including cognitive delay, seizures, and motor disease. Over 400 patients with SSADH Deficiency have been identified worldwide, though the precise prevalence of the disease is not known. GHB (also known as sodium oxybate, a drug marketed for psychiatric disorders) and possibly other succinic semi-aldehyde metabolites lead to depression of neurological function, and some patients with a diagnosis of autism have been found to have SSADH Deficiency.

There is currently no FDA-approved therapy specifically indicated for SSADH Deficiency, and most patients are treated supportively with anti-epileptic medications. While several therapeutic approaches have been attempted in clinical trials, and one medication is currently undergoing testing in a clinical trial run by the National Institute of Neurological Disorders and Stroke, to our knowledge, none have shown promise in addressing the core toxicity of succinic semi-aldehyde, and patients are generally poorly responsive to these approaches. By trapping succinic semi-aldehyde, ADX-102, ADX-104, or other systemically administered aldehyde traps may have the potential to reduce the direct toxicity of succinic semi-aldehyde as well as the formation of neurotoxic metabolites, and represent a novel approach with considerable therapeutic potential in a disease where there remains significant unmet medical need.

A New Therapeutic Approach for Inflammation and Inborn Errors of Aldehyde Metabolism: ADX-102, ADX-103, ADX-104, and Other Novel Aldehyde Traps

Aldehyde Toxicity and Sequestration

Aldehydes are generated through a variety of metabolic processes. At high levels, aldehydes are toxic, binding proteins, lipids, carbohydrates, and DNA, and may mediate inflammation in, and the progression of, many

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serious diseases through signaling cascades that lead to the activation of intracellular inflammatory factors, including NF-kB, an important protein in the inflammatory response. In addition, aldehyde binding to cellular constituents leads to the formation of adducts and aggregates that may lead to cellular dysfunction. Because of the inherent toxicity of aldehydes, most, if not all, living organisms contain enzymes such as aldehyde dehydrogenases that detoxify aldehydes. The toxicity of aldehydes is evidenced by human studies showing an increased rate of cognitive decline, cancer, and cardiovascular disease in populations with diminished aldehyde dehydrogenase capacity. Additionally, most inflammatory diseases, including autoimmune disease, neurodegenerative disease, and cardiovascular diseases, manifest elevated aldehyde levels that apparently overwhelm endogenous aldehyde catabolic capacity. To our knowledge, there has never been a concerted pharmaceutical effort to lower all free aldehyde levels. Thus, we believe that aldehyde sequestration represents a novel platform for the treatment of inflammatory conditions and inborn errors of aldehyde metabolism where genetic mutations prevent the normal degradation of aldehydes.

Aside from increasing levels of inflammation, there is no generally accepted biological role of high levels of aldehydes. Some physiologic molecules have aldehyde forms, including retinaldehyde (a form of Vitamin A) and pyridoxal and pyridoxal phosphate (forms of Vitamin B6), but these molecules are not free aldehydes in that they are tightly chaperoned and protected by proteins that prevent the aldehydes from reacting with other molecules, including aldehyde traps. Thus, pharmacotherapeutic aldehyde sequestration is expected *a priori* not to adversely affect normal physiologic processes. Consistent with the toxicity of free aldehydes and the lack of accessibility to chaperoned physiologic aldehydes, our most advanced aldehyde trap, ADX-102, which has been administered to over 100 subjects across four clinical trials, has been generally well tolerated and has not resulted in any serious adverse events.

Aldehyde Traps

We are currently developing ADX-102, a new chemical entity, for the treatment of inflammatory diseases and inborn errors of aldehyde metabolism. ADX-102 is a small molecule designed specifically to trap, and thereby allow for the degradation of, aldehydes. In *in vitro* and animal studies, ADX-102 appears to have minimal pharmacology, meaning that ADX-102 does not appear to affect most cellular components, including most receptors, enzymes, ion channels, or other proteins. ADX-102 has been shown to bind and trap aldehydes more rapidly than aldehydes bind any cellular constituent. Evidence suggests that ADX-102 covalently binds to aldehydes to form ADX-102-aldehyde adducts, which appear to be rapidly degraded in cellular environments, after which neither ADX-102 or free aldehydes are detectable. Outside of biological systems, ADX-102-aldehyde adducts are remarkably non-reactive and stable, suggesting that ADX-102-aldehyde binding is effectively irreversible; hence the notion of ADX-102 as an aldehyde trap. By essentially irreversibly binding aldehydes to form covalent adducts that are then degraded, ADX-102 and other aldehyde traps have the potential to substantially lower aldehyde levels.

We believe we have been the first to demonstrate the positive effects of lowering aldehyde levels with an aldehyde trap in a variety of animal models relating to inflammation, suggesting that aldehyde traps may have potent anti-inflammatory effects that persist hours after ADX-102 administration at a variety of different doses relevant to clinical testing. In addition, we believe we have also been the first to demonstrate the activity of ADX-102 in binding aldehydes in *in vitro* and preclinical models of inborn errors of aldehyde metabolism.

In mouse models of ocular inflammation and post-surgical healing, topically applied ADX-102 ophthalmic solution reduced ocular redness and inflammatory cytokines comparable to corticosteroid therapy and slowed the development of corneal haze (fibrosis). (Data presented at the Association for Research in Vision and Ophthalmology 2015 Annual Meeting)

In mice injected with a pro-inflammatory agent known as endotoxin, intraperitoneally administered ADX-102 statistically reduced a variety of inflammatory cytokines (protein inflammatory mediators), including IL-5, Il-1ß, IL-17, and TNF-a, while up-regulating the primary anti-inflammatory cytokine, IL-10. Additionally, in models of mouse contact dermatitis (induced by phorbol myristate acetate) and

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allergic contact dermatitis (induced by sensitivity to oxazolone), ADX-102 statistically reduced inflammation as measured by edema (swelling). (Data presented at the American Academy of Asthma Allergy and Immunology 2015 Annual Meeting)

In a model of radiation mucositis (oral inflammation) in hamsters, chronic subcutaneous administration of ADX-102 reduced healing time and decreased fibrosis (scarring). (Data presented at the Multinational Association of Supportive Care in Cancer International Society of Oral Oncology 2015 Annual Meeting)

In cells lacking FALDH (a model of SLS), ADX-102 prevented aldehydes from binding a lipid (fat) thought to be critical to the dermal moisture barrier. (Data presented at the Society for Inherited Metabolic Disorders 2015 Annual Meeting)

In a knock-out mouse model of SSADH Deficiency, ADX-102 trapped succinic semi-aldehyde in key tissues following intraperitoneal injection. (Data presented at the 2016 SSADH Symposium and at the 2015 American Society of Human Genetics Annual Meeting)

In two different mouse models of inflammatory pain, intraperitoneally administered ADX-102 dose-dependently reduced nociceptive behavior, suggesting that ADX-102 down-regulates pain signaling in inflammation. (Data presented at the 2016 International Conference on Pain Research and Management)

In rat cardiomyocyte culture, ADX-102 prevented fibrotic transformation, and inhibited NF-kB activation and IL-1ß release. (Data presented at the 2016 American Society for Cell Biology Annual Meeting)

Thus, we believe that aldehyde trapping with ADX-102 potentially has a variety of mechanisms of action lowering inflammation, reducing healing time, diminishing scarring, protecting a lipid important in tissue moisture barriers, and mitigating pain that may ameliorate aldehyde-mediated disease and deter aldehyde-mediated disease progression in different ways at the same time.

In addition to the development of ADX-102, we intend to continue the discovery and development of other novel aldehyde traps and we intend to continue to develop intellectual property around such molecules. We have identified, synthesized, and tested numerous molecules that may be more potent than ADX-102 in trapping aldehydes. We are currently screening novel traps for product candidates to address diseases where topical and systemic administration are applicable to reduce aldehyde-mediated pathology. We have nominated two new aldehyde traps, ADX-103 and ADX-104, for clinical development, which may begin 2018, depending on additional preclinical data, regulatory discussions, funding, and other factors.

Clinical Development

In order to assess the efficacy of aldehyde trapping in human disease, in 2015 we initiated a series of clinical trials in patients with ocular inflammatory disease and in patients with SLS, an inborn error of aldehyde metabolism. Our initial clinical trials in inflammation involved ocular testing, in part, due to the ability to non-invasively assess inflammation on the surface of and within the eye and the ability to treat the eye with topical administration of drug. Our initial clinical trial in inborn errors of aldehyde metabolism focused on SLS, in part, because the dermatologic aspects of the disease may respond to topical administration of drug, and assessment of dermatological response can

be performed with relatively non-invasive techniques and clinical examination. Most inflammatory diseases and inborn errors of aldehyde metabolism, involve at least some tissues that cannot be effectively treated topically, and thus we are developing systemic formulations of aldehyde traps, including ADX-102 and ADX-104. We plan to initiate Phase 1 clinical testing of a systemic formulation in the first half of 2018.

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Allergic Conjunctivitis

In September 2015, we initiated a randomized, parallel-group, double-masked, vehicle-controlled Phase 2a clinical trial of 0.5% ADX-102 ophthalmic solution in patients with allergic conjunctivitis. Using the conjunctival allergen provocation test (CAPT), one hundred healthy men and women with at least a two-year history of allergic conjunctivitis to grass, tree, or ragweed pollen were randomized in equal groups for treatment with topical ocular ADX-102 or vehicle, and ocular inflammation was induced by exposure to allergen. The clinical endpoints in the trial included patient assessment (on a 0 to 3 point scale) of ocular itching and tearing, two prominent inflammation-related symptoms of allergic conjunctivitis. In February 2016, we announced that the results demonstrated statistically significant activity of ADX-102 over vehicle in reducing ocular itching and tearing after a single dose (see figure below). Relative to baseline scores, ADX-102 demonstrated durable efficacy that persisted across substantially all time points over three hours following CAPT challenges. Despite a stronger than expected vehicle effect, peak changes in ocular itching and tearing scores were statistically superior to vehicle. The reductions from baseline scores were of the same magnitude previously observed in the CAPT model with existing therapies utilized in the treatment of allergic conjunctivitis. ADX-102 was generally well tolerated and there were no safety concerns during the trial. Transient and generally mild stinging was noted in the treatment arm. Two patients dropped out of the trial during treatment.

Allergic Conjunctivitis Phase 2a Clinical Trial Results for Ocular Itching and Tearing Following a Single Dose of ADX-102 vs. Vehicle

To our knowledge, the data from the allergic conjunctivitis Phase 2a clinical trial represent the first demonstration of the efficacy of aldehyde trapping in any human disease, and we believe that the results validate the potential of aldehyde traps as a novel anti-inflammatory therapy.

In February 2017, we announced the enrollment of the first patient in a Phase 2b allergic conjunctivitis clinical trial of topical ocular ADX-102. Given the unexpectedly large vehicle response observed in the Phase 2a clinical trial, we have reached agreement with the FDA that saline, instead of vehicle, will be the control in the Phase 2b clinical trial and subsequent clinical trials. The primary endpoint in Phase 2b will be difference from saline in patient-reported ocular itching following a single dose of ADX-102 in the Conjunctival Allergen Challenge (CAC) model, which has been used for the registration of other drugs for the treatment of allergic conjunctivitis. In addition to saline, two concentrations of ADX-102 topical ocular solution will be tested: 0.1% and 0.5%. Planned enrollment is 50 subjects in each of the three arms of the trial. Results from the trial are expected in the third quarter of 2017.

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Noninfectious Anterior Uveitis

In April 2015, we initiated a randomized, parallel-group, double-masked, comparator-controlled Phase 2 clinical trial of 0.5% ADX-102 ophthalmic solution in patients with noninfectious anterior uveitis, a rare but painful and potentially blinding ocular inflammatory disease. Forty-five subjects were randomized equally to receive six weeks of treatment with one of the following: ADX-102 0.5% four times daily; Pred Forte® 1% (a corticosteroid) four times daily (tapered); or ADX-102 0.5% four times daily and Pred Forte® 1% two times daily (tapered). In May 2016, we announced that the results of the trial demonstrated that the activity of ADX-102 was comparable to Pred Forte® in reducing anterior chamber inflammatory cell count (see figure below), which is the primary endpoint required for product registration. At the week 4 visit, grade 0 cell count (zero or one cells) was observed in 53% of ADX-102-treated patients versus 38% of corticosteroid-treated patients. Elevations of intraocular pressure observed in corticosteroid-treated patients were not observed in ADX-102-treated patients (see figure below). ADX-102 was generally well tolerated and there were no serious adverse events, consistent with previous Phase 1 and Phase 2 clinical trials.

Noninfectious Anterior Uveitis Phase 2 Clinical Trial Results for Anterior Chamber Cell Count Grade

Noninfectious Anterior Uveitis Phase 2 Clinical Trial Results for Intraocular Pressure (mmHg)

We expect to initiate, in the second quarter of 2017, a Phase 3 clinical trial of topical ocular 0.5% ADX-102 for the treatment of noninfectious anterior uveitis. We have reached agreement with the FDA that vehicle will be used as a control in the trial. The primary endpoint will be difference from control in time to cure (zero anterior chamber inflammatory cells). Up to 100 patients will be enrolled and randomized equally to receive either ADX-102 or vehicle for 4 weeks.

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Dry Eye Syndrome

In the second quarter of 2017, we expect to initiate enrollment of a Phase 2a clinical trial in Dry Eye Syndrome, a common ocular inflammatory disease characterized by pain, burning, and stinging. Approximately 45 patients will be equally randomized to 28 days of treatment with topical drops containing 0.1% ADX-102; 0.5% ADX-102 or 0.5% ADX-102 in a novel, lipid-based formulation. Endpoints will include assessment of tear quality (osmolarity and tear film breakup time), corneal integrity, and symptoms. Results from the trial are expected in the fourth quarter of 2017. Contingent on preclinical results, regulatory feedback, and other factors, we may also initiate a Phase 2a clinical trial of ADX-103 for the treatment of Dry Eye Syndrome.

Sjögren-Larsson Syndrome

In March 2015, we initiated a randomized, parallel-group, double-blinded, vehicle-controlled Phase 2 clinical trial of a dermatologic formulation of ADX-102 for the treatment of the skin manifestations of SLS. Twelve subjects with SLS and moderate to severe ichthyosis were randomized equally to receive ADX-102 1% dermatologic formulation or vehicle formulation administered once daily on a 4 x 10 inch area of skin for two months. Investigators and subjects were blinded to treatment group. Ichthyosis was graded by a blinded central review of digital photographs, as well as by clinical exam, using the Ichthyosis Severity Score, which is comprised of assessments of global impression, scaling, erythema (redness), lichenification (thickness) and excoriation (abrasion).

In August 2016, we reported that ADX-102 consistently produced clinically meaningful effects in reducing the severity of ichthyosis. As assessed by central review, five of six subjects (83%) treated with ADX-102 achieved a rating of almost clear or mild on global assessment. Six of six (100%) subjects treated with ADX-102 improved over the course of therapy as assessed by central review ($p < 0.05$, see figure below), and the improvement was greater than that observed with vehicle-treated patients ($p < 0.05$). For ADX-102-treated subjects, mean reductions in ichthyosis severity were greater after 8 weeks of therapy than after 4 weeks of therapy, suggesting a disease modifying effect of ADX-102. ADX-102 was observed to be generally well tolerated, and there were no significant adverse events, serious adverse events or discontinuations in the trial.

Sjögren-Larsson Syndrome Phase 2 Clinical Trial Results for Each ADX-102-Treated Patient as Assessed by Central Review

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In the second half of 2017, we expect to initiate a Phase 3 clinical trial of topical dermatologic ADX-102 for the treatment of the skin manifestations of SLS. Up to 30 patients will be treated with a 1% dermatologic formulation of ADX-102 for at least four months. The endpoint of the clinical trial is the severity of ichthyosis following treatment.

Intellectual Property and Proprietary Rights

Overview

We are building an intellectual property portfolio for ADX-102 and other aldehyde traps in the United States and abroad. We currently seek, and intend to continue to seek, patent protection in the United States and internationally for our product candidates, methods of use, and processes for manufacture, and for other technologies, where appropriate. Our current policy is to actively seek to protect our proprietary position by, among other things, filing patent applications in the United States and abroad relating to proprietary technologies that are important to the development of our business. We also rely on, and will continue to rely on, trade secrets, know-how, continuing technological innovation and in-licensing opportunities to develop and maintain our proprietary position. We cannot be sure that patents will be granted with respect to any of our pending patent applications or with respect to any patent applications filed by us in the future, nor can we be sure that any of our existing patents or any patents that may be granted to us in the future will be commercially useful in protecting our technology.

Our success will depend significantly on our ability to obtain and maintain patent and other proprietary protection for the technologies that we consider important to our business, our ability to defend our patents, and our ability to preserve the confidentiality of our trade secrets and operate our business without infringing the patents and proprietary rights of third parties.

Patent Portfolio

Our patent portfolio currently includes patents and patent applications covering the composition, formulation, and uses of ADX-102, ADX-103, ADX-104, and other novel aldehyde trapping compounds. As of December 31, 2016, we owned five United States patents and five pending United States non-provisional patent applications, as well as numerous foreign counterparts to these patents and patent applications. We expect the issued ADX-102 composition of matter patent in the United States, if the appropriate maintenance, renewal, annuity or other governmental fees are paid, to expire in 2028. It is possible that the term of the composition of matter patent in the United States may be extended up to five additional years under the provisions of the Hatch-Waxman Act. We expect the foreign ADX-102 composition of matter patents, if the appropriate maintenance, renewal, annuity or other governmental fees are paid, to expire in 2026. We expect other patent applications in the portfolio, if issued, and if the appropriate maintenance, renewal, annuity or other governmental fees are paid, to expire from 2026 to 2034. ADX-102 composition of matter patents have been issued in Australia, Canada, China, Europe (validated in approximately 14 member countries), Hong Kong, India, Japan, Mexico, Russia and South Korea. ADX-102 composition of matter patent claims are pending in Brazil.

Other Intellectual Property Rights

Our marks ALDEYRA THERAPEUTICS and our logo are registered with the United States Patent and Trademark Office.

Confidential Information and Inventions Assignment Agreements

We currently require and will continue to require each of our employees and consultants to execute confidentiality agreements upon the commencement of such individual s employment, consulting or collaborative relationships with us. These agreements provide that all confidential information developed or made known during the course of

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the relationship with us be kept confidential and not disclosed to third parties except in specific circumstances. In the case of employees, the agreements provide that all inventions resulting from such individual s work performed for us, utilizing our property or relating to our business and conceived or completed by the individual during employment shall be our exclusive property to the extent permitted by applicable law. Our consulting agreements also provide for assignment to us of any intellectual property resulting from services performed by a consultant for us.

Sales and Marketing

We are currently seeking and will continue to seek to develop and commercialize ADX-102 or our other product candidates for certain diseases in the United States alone or with corporate partners. If approved by regulatory agencies for marketing, our current expectation is that ADX-102 or our other product candidates would initially be sold by us to small groups of physicians that specialize in rare disorders or severe disease. We may also plan to utilize strategic partners or contract sales forces to assist in the commercialization of ADX-102 or our other product candidates for common diseases, and with such partners, would seek to build awareness in the approved patient populations of the clinical utility of ADX-102 and our other product candidates.

Manufacturing

We do not own or operate manufacturing facilities for the production of ADX-102 or our other product candidates, nor do we have plans to develop our own manufacturing operations in the foreseeable future. We currently depend on third-party contract manufacturers for all of our required raw materials, drug substance and finished drug product for our preclinical research and clinical trials. We have no immediate plans to purchase, erect or otherwise create any manufacturing facilities to be owned by us for any of these purposes, and intend to continue to depend on third-party contract manufacturers for the foreseeable future. We do not have any current contractual relationships for the manufacture of commercial supplies of ADX-102 or our other product candidates. If ADX-102 or our other product candidates are approved by any regulatory agency, we intend to enter into agreements with third-party contract manufacturers for the commercial production at such time. We may utilize third-party consultants to manage our manufacturing contractors. We believe that the active pharmaceutical ingredient and other materials needed for the formulation of ADX-102, ADX-103, and ADX-104 are relatively easy to manufacture, and that multiple suppliers and formulators could be employed for this purpose. Further, the raw materials needed for manufacture of ADX-102, ADX-103 and ADX-104, as well as other components of our formulations, are generally readily available from multiple sources.

Employees

As of December 31, 2016, we had eleven full time employees and had engaged a number of consultants. We intend to increase our employee base in connection with the continuing clinical development of ADX-102, ADX-103, ADX-104, and other product candidates. We expect that a number of consultants previously engaged in development of our product candidates will participate in ongoing clinical and manufacturing activities. None of our employees is represented by a labor union. We have not experienced any work stoppages, and we consider our relations with our employees to be very good.

Competition

Aldehyde Modulation

Various academic groups have published on the idea of reducing aldehyde levels, primarily by using compounds with primary amines (certain nitrogen-containing compounds) that react with aldehydes through a well-known chemical

process known as the Schiff base reaction. The Schiff base reaction is reversible, and generally the substrates (precursors) and products of the reaction exist in equilibrium such that at any point in time, the aldehyde substrate may be bound or unbound. In this way, Schiff base reactions alone represent reversible and

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temporary aldehyde binding. Various aldehyde-binding amines have been described, particularly carnosine (a naturally occurring dipeptide), which has a variety of additional potential mechanisms of action unrelated to aldehydes. At least one group has published on the use of certain nitrogen-containing marketed products to temporarily, in a reversible manner, bind retinaldehyde as a potential therapy for retinal disease. We believe that ADX-102 and other novel aldehyde traps that we have discovered are differentiated from the above approaches in that the chemical structures are novel and the reaction with aldehydes is essentially irreversible *in vivo*, which we believe may result in a more effective means of diminishing aldehyde levels.

Other Pharmacotherapies

The pharmaceutical industry is characterized by intense competition and rapid innovation. Our potential competitors include large pharmaceutical and biotechnology companies, specialty pharmaceutical companies, academic institutions, government agencies and research institutions. We believe that the key competitive factors that will affect the development and lead to the commercial success of our product candidates are efficacy, safety, tolerability, and the ability to reduce the dependence on, or the dose of, more toxic products.

Many of our potential competitors have substantially greater financial, technical and human resources than we do and significantly greater experience in the discovery and development of product candidates, obtaining FDA and other regulatory approvals of products and the commercialization of those products. Accordingly, our competitors may be more successful than we may be in obtaining FDA approval for products and achieving widespread market acceptance. Our competitors products may be more effective, or more effectively marketed and sold, than any product that we may commercialize and may render our product candidates obsolete or non-competitive before we can recover the expenses of developing and commercializing any of our product candidates. We anticipate that we will face intense and increasing competition as new products enter the market and advanced technologies become available. In addition, the development of new treatment methods for the diseases we are targeting could render our products non-competitive or obsolete.

We expect that, if approved, ADX-102 and or our other product candidates, will compete with a variety of generic and proprietary pharmaceuticals, depending on the approved indication. Table 1 below summarizes competitive products by indication.

Table 1. Competitive Pharmaceuticals by Indication

Indication	Competitive Products
Allergic Conjunctivitis	Topical antihistamines and corticosteroids, nonsteroidal anti-inflammatory drugs (NSAIDs), mast cell stabilizers
Noninfectious Anterior Uveitis	Topical corticosteroids
Dry Eye Syndrome	Topical immunomodulators (cyclosporine, lifitegrast), topical corticosteroids, artificial tear solutions
Sjögren-Larsson Syndrome	Retinoids, keratinolytics, and moisturizers
Succinic Semi-Aldehyde Dehydrogenase Deficiency	Anti-epileptics

We believe that there is significant unmet medical need for the diseases that we intend to study. If ADX-102 or our other product candidates are proven to be safe and effective, we believe that ADX-102 and or our other product

candidates could be used in place of or in addition to current therapies, especially in instances where current therapies are toxic and reducing exposure to such therapies would be desirable. Topical corticosteroids for ocular inflammatory diseases are often associated with toxicity, including glaucoma, cataracts, ocular

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infection, and ulceration. There is no approved therapy for SLS. We believe that the current non-specific creams and medications for SLS are poorly effective, if effective at all. There is no approved therapy for SSADH Deficiency. We believe that anti-epileptics and other medications used in SSADH Deficiency are inadequate in controlling the symptoms of the disease. While ADX-102 and other novel aldehyde traps may manifest efficacy and safety advantages over currently available therapies, many such therapies are generic or may be priced considerably lower than the pricing we anticipate for our product candidates. Pricing factors may discourage the initial or prolonged use of ADX-102 or our other product candidates.

Many drugs are in development for allergic conjunctivitis and Dry Eye Syndrome. Novartis/Alcon (ESBA105, LME636) and EyeGate Pharmaceuticals, Inc. (EGP-437) have conducted or are conducting clinical trials in anterior uveitis. For the diseases we intend to study, there may be other developmental therapies of which we are not aware. We believe that there are no drugs in development specifically for SLS. The National Institute of Neurological Disorders and Stroke is conducting a clinical trial of a GABA receptor antagonist (SGS-742) for SSADH Deficiency.

A myriad of new treatments have been or are being developed to treat inflammatory diseases, and in theory could be used for the treatment of the diseases our products are intended to target. Immune-modulating products include cytokine inhibitors, immune cell receptor inhibitors, and Janus kinase inhibitors. Companies that currently market such therapies include Abbvie, Inc., Johnson & Johnson, UCB Inc. and UCB S.A., Amgen, Inc., Bristol-Myers Squibb Co., and Pfizer, Inc. As these products become used more commonly, they may begin to be used in the diseases that we intend to target, and such products may manifest efficacy and safety advantages over ADX-102 or our other product candidates.

Government Regulation

FDA Approval Process

In the United States, pharmaceutical products are subject to extensive regulation by the FDA. The Food Drug and Cosmetic Act (FDCA) and other federal and state statutes and regulations, govern, among other things, the research, development, testing, manufacture, storage, recordkeeping, approval, labeling, promotion and marketing, distribution, post-approval monitoring and reporting, sampling, and import and export of pharmaceutical products. Failure to comply with applicable FDA or other requirements may subject a company to a variety of administrative or judicial sanctions, such as the FDA s refusal to approve pending applications, a clinical hold, warning letters, recall or seizure of products, partial or total suspension of production, withdrawal of the product from the market, injunctions, fines, civil penalties or criminal prosecution.

FDA approval is required before any new drug, such as a new chemical entity, or a new dosage form, new use or new route of administration of a previously approved product, can be marketed in the United States. The process required by the FDA before a new drug product may be marketed in the United States generally involves:

- completion of preclinical laboratory and animal testing and formulation studies in compliance with the FDA s good laboratory practice (GLP) regulation;

- submission to the FDA of an IND for human clinical testing which must become effective before human clinical trials may begin in the United States;

approval by an independent institutional review board (IRB) at each site where a clinical trial will be performed before the trial may be initiated at that site;

performance of adequate and well-controlled human clinical trials in accordance with good clinical practices (GCP) to establish the safety and efficacy of the proposed product candidate for each intended use;

satisfactory completion of an FDA pre-approval inspection of the facility or facilities at which the product is manufactured to assess compliance with the FDA s cGMP regulations;

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submission to the FDA of a new drug application (NDA) which must be accepted for filing by the FDA;

satisfactory completion of an FDA advisory committee review, if applicable;

payment of user fees, if applicable; and

FDA review and approval of the NDA.

The preclinical and clinical testing and approval process requires substantial time, effort and financial resources. Preclinical tests include laboratory evaluation of product chemistry, formulation, manufacturing and control procedures and stability, as well as animal studies to assess the toxicity and other safety characteristics of the product. The results of preclinical tests, together with manufacturing information, analytical data and a proposed clinical trial protocol and other information, are submitted as part of an IND to the FDA. Some preclinical testing may continue even after the IND is submitted. The IND automatically becomes effective 30 days after receipt by the FDA, unless the FDA, within the 30-day time period, raises concerns or questions and places the clinical trial on a clinical hold. In such a case, the IND sponsor and the FDA must resolve any outstanding concerns before the clinical trial can begin. As a result, our submission of an IND may not result in FDA authorization to commence a clinical trial. A separate submission to an existing IND must also be made for each successive clinical trial conducted during product development. Even if the IND becomes effective and the trial proceeds without initial FDA objection, the FDA may stop the trial at a later time if it has concerns, such as if unacceptable safety risks arise.

Further, an independent IRB, covering each site proposing to conduct the clinical trial must review and approve the plan for any clinical trial and informed consent information for subjects before the trial commences at that site and it must monitor the study until completed. The FDA, the IRB, or the sponsor may suspend a clinical trial at any time on various grounds, including a finding that the subjects or patients are being exposed to an unacceptable health risk or for failure to comply with the IRB s requirements, or may impose other conditions.

If a Phase 2 clinical trial is the subject of discussion at an end-of-Phase 2 meeting with the FDA, a sponsor may be able to request a Special Protocol Assessment (SPA) the purpose of which is to reach agreement with the FDA on the design of the Phase 3 clinical trial protocol design and analysis that will form the primary basis of an efficacy claim. If such an agreement is reached, it will be documented and made part of the administrative record, and it will be binding on the FDA and may not be changed unless the sponsor fails to follow the agreed-upon protocol, data supporting the request are found to be false or incomplete, or the FDA determines that a substantial scientific issue essential to determining the safety or effectiveness of the drug was identified after the testing began. Even if an SPA is agreed to, approval of the NDA is not guaranteed because a final determination that an agreed-upon protocol satisfies a specific objective, such as the demonstration of efficacy, or supports an approval decision, will be based on a complete review of all the data in the NDA.

Clinical trials involve the administration of the investigational new product to human subjects under the supervision of qualified investigators in accordance with GCP requirements, which include the requirement that all research subjects provide their informed consent in writing for their participation in any clinical trial. Sponsors of clinical trials generally must register and report, at the NIH-maintained website ClinicalTrials.gov, key parameters of certain clinical trials. For purposes of an NDA submission and approval, human clinical trials are typically conducted in the following sequential phases, which may overlap or be combined:

Phase 1: The product is initially introduced into healthy human subjects or patients and tested for safety, dose tolerance, absorption, metabolism, distribution and excretion and, if possible, to gain an early indication of its effectiveness.

Phase 2: The product is administered to a limited patient population to identify possible adverse effects and safety risks, to preliminarily evaluate the efficacy of the product for specific targeted indications

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and to determine dose tolerance and optimal dosage. Multiple Phase 2 clinical trials may be conducted by the sponsor to obtain information prior to beginning larger and more extensive clinical trials.

Phase 3: These are commonly referred to as pivotal studies. When Phase 2 evaluations demonstrate that a dose range of the product appears to be effective and has an acceptable safety profile, trials are undertaken in large patient populations to further evaluate dosage, to obtain additional evidence of clinical efficacy and safety in an expanded patient population at multiple, geographically-dispersed clinical trial sites, to establish the overall risk-benefit relationship of the product and to provide adequate information for the labeling of the product.

Phase 4: In some cases, the FDA may condition approval of an NDA for a product candidate on the sponsor s agreement to conduct additional clinical trials to further assess the product s safety and effectiveness after NDA approval. Such post-approval trials are typically referred to as Phase 4 studies.

The results of product development, preclinical studies and clinical trials are submitted to the FDA as part of an NDA. NDAs must also contain extensive information relating to the product s pharmacology, chemistry, manufacturing and controls and proposed labeling, among other things.

Orphan Drug Designation

Under the Orphan Drug Act, the FDA may grant orphan drug designation to a drug intended to treat a rare disease or condition which is defined as one affecting fewer than 200,000 individuals in the United States or more than 200,000 individuals where there is no reasonable expectation that the product development cost will be recovered from product sales in the United States. Orphan drug designation must be requested before submitting an NDA and does not convey any advantage in, or shorten the duration of, the regulatory review and approval process.

If an orphan drug-designated product subsequently receives the first FDA approval for the disease for which it was designed, the product will be entitled to seven years of product exclusivity, which means that the FDA may not approve any other applications to market the same drug for the same indication, except in very limited circumstances, for seven years. If a competitor obtains approval of the same drug, as defined by the FDA, or if our product candidate is determined to be contained within the competitor s product for the same indication or disease, the competitor s exclusivity could block the approval of our product candidate in the designated orphan indication for seven years.

For some products, the FDA may require a risk evaluation and mitigation strategy (REMS) which could include measures imposed by the FDA such as prescribing restrictions, requirements for post-marketing studies or certain restrictions on distribution and use. Under federal law, the submission of most NDAs is additionally subject to a substantial application user fee, and the manufacturer and/or sponsor under an approved NDA are also subject to annual product and establishment user fees. The FDA has 60 days from its receipt of an NDA to determine whether the application will be accepted for filing based on the agency s threshold determination that it is sufficiently complete to permit substantive review. The FDA may request additional information rather than accept an NDA for filing. In this event, the NDA must be resubmitted with the additional information and is subject to payment of additional user fees. The resubmitted application is also subject to review before the FDA accepts it for filing.

Once the submission has been accepted for filing, the FDA begins an in-depth substantive review. Under the Prescription Drug User Fee Act (PDUFA), the FDA agrees to specific performance goals for NDA review time through a two-tiered classification system, Standard Review and Priority Review. Standard Review NDAs have a goal of being completed within a ten-month timeframe. A Priority Review designation is given to products that offer major

advances in treatment, or provide a treatment where no adequate therapy exists. The goal for completing a Priority Review is six months.

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It is likely that our product candidates will be granted a Standard Review. The review process may be extended by the FDA for three additional months to consider certain information or obtain clarification regarding information already provided in the submission. The FDA may refer applications for novel products or products which present difficult questions of safety or efficacy to an advisory committee for review, evaluation and recommendation as to whether the application should be approved and under what conditions. The FDA is not bound by the recommendation of an advisory committee, but it considers such recommendations carefully when making decisions. In addition, for combination products, the FDA s review may include the participation of both the FDA s Center for Drug Evaluation and Research and the FDA s Center for Devices and Radiological Health, which may complicate or prolong the review.

Before approving an NDA, the FDA may inspect the facility or facilities where the product is manufactured. The FDA will not approve an application unless it determines that the manufacturing processes and facilities are in compliance with cGMP.

After the FDA evaluates the NDA and, in some cases, the related manufacturing facilities, it may issue an approval letter or a Complete Response Letter (CRL) to indicate that the review cycle for an application is complete and that the application is not ready for approval. CRLs generally outline the deficiencies in the submission and may require substantial additional testing or information in order for the FDA to reconsider the application. Even with submission of this additional information, the FDA ultimately may decide that the application does not satisfy the regulatory criteria for approval. If and when the deficiencies have been addressed to the FDA s satisfaction, the FDA will typically issue an approval letter. An approval letter authorizes commercial marketing of the product with specific prescribing information for specific indications.

Once issued, the FDA may withdraw product approval if ongoing regulatory requirements are not met or if safety problems are identified after the product reaches the market. In addition, the FDA may require post-approval testing, including Phase 4 studies, and surveillance programs to monitor the effect of approved products which have been commercialized, and the FDA has the power to prevent or limit further marketing of a product based on the results of these post-marketing programs. Products may be marketed only for the approved indications and in accordance with the provisions of the approved label, and, even if the FDA approves a product, it may limit the approved indications for use for the product or impose other conditions, including labeling or distribution restrictions or other risk-management mechanisms, such as a Black Box Warning, which highlights a specific warning (typically life-threatening), or a REMS program. Further, if there are any modifications to the product, including changes in indications, labeling, or manufacturing processes or facilities, a company may be required to submit and obtain FDA approval of a new or supplemental NDA, which may require such company to develop additional data or conduct additional preclinical studies and clinical trials.

Post-Approval Requirements

Once an NDA is approved, a product will be subject to pervasive and continuing regulation by the FDA, including, among other things, requirements relating to product/device listing, recordkeeping, periodic reporting, product sampling and distribution, advertising and promotion and reporting of adverse experiences with the product.

In addition, drug manufacturers and other entities involved in the manufacture and distribution of approved drugs are required to register their establishments with the FDA and state agencies, and are subject to periodic unannounced inspections by the FDA and these state agencies for compliance with cGMP requirements. Changes to the manufacturing process are strictly regulated and generally require prior FDA approval before being implemented. FDA regulations also require investigation and correction of any deviations from cGMP and impose reporting and documentation requirements upon us and any third-party manufacturers that we may decide to use. Accordingly,

manufacturers must continue to expend time, money, and effort in the area of production and quality control to maintain cGMP compliance.

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Once an approval is granted, the FDA may withdraw the approval if compliance with regulatory requirements and standards is not maintained or if problems occur after the product reaches the market. Later discovery of previously unknown problems with a product, including adverse events of unanticipated severity or frequency, or with manufacturing processes, or failure to comply with regulatory requirements, may result in, among other things:

- restrictions on the marketing or manufacturing of the product, complete withdrawal of the product from the market or product recalls;
- fines, warning letters or holds on post-approval clinical trials;
- refusal of the FDA to approve pending applications or supplements to approved applications, or suspension or revocation of product license approvals;
- product seizure or detention, or refusal to permit the import or export of products; or
- injunctions or the imposition of civil or criminal penalties.

The FDA strictly regulates marketing, labeling, advertising and promotion of products that are placed on the market. While physicians may prescribe for off label uses, manufacturers may only promote for the approved indications and in accordance with the provisions of the approved label. The FDA and other agencies actively enforce the laws and regulations prohibiting the promotion of off label uses, and a company that is found to have improperly promoted off label uses may be subject to significant liability, both at the federal and state levels.

The Food and Drug Administration Amendments Act of 2007 gave the FDA the authority to require a Risk Evaluation and Mitigation Strategy, or REMS, from manufacturers to ensure that the benefits of a drug or biological product outweigh its risks. In determining whether a REMS is necessary, FDA must consider the size of the population likely to use the drug, the seriousness of the disease or condition to be treated, the expected benefit of the drug, the duration of treatment, the seriousness of known or potential adverse events, and whether the drug is a new molecular entity. If the FDA determines a REMS is necessary, the drug sponsor must agree to the REMS plan at the time of approval. A REMS may be required to include various elements, such as a medication guide or patient package insert, a communication plan to educate health care providers of the drug s risks, limitations on who may prescribe or dispense the drug, or other measures that the FDA deems necessary to assure the safe use of the drug. In addition, the REMS must include a timetable to assess the strategy at 18 months, three years, and seven years after the strategy s approval. The FDA may also impose a REMS requirement on a drug already on the market if the FDA determines, based on new safety information, that a REMS is necessary to ensure that the drug s benefits outweigh its risks.

Patent Term Restoration and Marketing Exclusivity

Depending upon the timing, duration and specifics of FDA approval of the use of our drug candidates, some of our United States patents may be eligible for limited patent term extension under the Drug Price Competition and Patent Term Restoration Act of 1984, referred to as the Hatch-Waxman Act. The Hatch-Waxman Act permits a patent restoration term of up to five years as compensation for patent term lost during product development and the FDA regulatory review process. However, patent term restoration cannot extend the remaining term of a patent beyond a

total of 14 years from the product s approval date. The patent term restoration period is generally one-half the time between the effective date of an IND, and the submission date of an NDA, plus the time between the submission date of an NDA and the approval of that application. Only one patent applicable to an approved drug is eligible for the extension and the application for extension must be made prior to expiration of the patent. The United States Patent and Trademark Office, in consultation with the FDA, reviews and approves the application for any patent term extension or restoration. In the future, we intend to apply for restorations of patent term for some of our currently owned or licensed patents to add patent life beyond their current expiration date, depending on the expected length of clinical trials and other factors involved in the submission of the relevant NDA.

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Market exclusivity provisions under the FDCA also can delay the submission or the approval of certain applications. The FDCA provides a five-year period of non-patent marketing exclusivity within the United States to the first applicant to gain approval of an NDA for a new chemical entity. A drug is a new chemical entity if the FDA has not previously approved any other new drug containing the same active moiety, which is the molecule or ion responsible for the action of the drug substance. During the exclusivity period, the FDA may not accept for review an abbreviated new drug application (ANDA) or a 505(b)(2) NDA submitted by another company for another version of such drug where the applicant does not own or have a legal right of reference to all the data required for approval. However, an application may be submitted after four years if it contains a certification of patent invalidity or non-infringement. The FDCA also provides three years of marketing exclusivity for an NDA, 505(b)(2) NDA or supplement to an approved NDA if new clinical investigations, other than bioavailability studies, that were conducted or sponsored by the applicant are deemed by the FDA to be essential to the approval of the application, for example, for new indications, dosages or strengths of an existing drug. This three-year exclusivity covers only the conditions associated with the new clinical investigations and does not prohibit the FDA from approving ANDAs for drugs containing the original active agent. Five-year and three-year exclusivity will not delay the submission or approval of a full NDA; however, an applicant submitting a full NDA would be required to conduct or obtain a right of reference to all of the preclinical studies and adequate and well-controlled clinical trials necessary to demonstrate safety and effectiveness.

Manufacturing Requirements

We and our third-party manufacturers must comply with applicable FDA regulations relating to FDA s cGMP regulations and, if applicable, quality system regulation requirements for medical devices. The cGMP regulations include requirements relating to, among other things, organization of personnel, buildings and facilities, equipment, control of components and drug product containers and closures, production and process controls, packaging and labeling controls, holding and distribution, laboratory controls, records and reports, and returned or salvaged products. The manufacturing facilities for our products must meet cGMP requirements to the satisfaction of the FDA pursuant to a pre-approval inspection before we can use them to manufacture our products. We and our third-party manufacturers are also subject to periodic unannounced inspections of facilities by the FDA and other authorities, including procedures and operations used in the testing and manufacture of our products to assess our compliance with applicable regulations. Failure to comply with statutory and regulatory requirements subjects a manufacturer to possible legal or regulatory action, including, among other things, warning letters, voluntary corrective action, the seizure of products, injunctions, consent decrees placing significant restrictions on or suspending manufacturing operations and civil and criminal penalties.

Other Regulatory Requirements

We are also subject to various laws and regulations regarding laboratory practices, the experimental use of animals, and the use and disposal of hazardous or potentially hazardous substances in connection with our research. In each of these areas, as above, the FDA has broad regulatory and enforcement powers, including, among other things, the ability to levy fines and civil penalties, suspend or delay issuance of approvals, seize or recall products, and withdraw approvals, any one or more of which could have an adverse effect on our ability to operate our business and generate revenues. Compliance with applicable environmental laws and regulations is expensive, and current or future environmental regulations may impair our research, development and production efforts, which could harm our business, operating results and financial condition.

Research and Development Expenses

Substantially all of our research and development expenses incurred to date have been related to the development of ADX-102 and our other product candidates. Our research and development expenses totaled $13.2 million for the year

ended December 31, 2016 and $7.6 million for the year ended December 31, 2015.

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We anticipate that we will incur additional research and development expenses in the future as we evaluate and possibly pursue the development of our product candidates for additional indications, or develop additional product candidates.

We recognize research and development expenses as they are incurred. Our research and development expenses consist primarily of:

- salaries and related expenses for personnel;
- fees paid to consultants and contract research organizations in conjunction with independently monitoring clinical trials and acquiring and evaluating data in conjunction with clinical trials, including all related fees such as investigator grants, patient screening, lab work and data compilation and statistical analysis;
- costs incurred with third parties related to the establishment of a commercially viable manufacturing process for our product candidates;
- costs related to production of clinical materials, including fees paid to contract manufacturers;
- costs related to upfront, milestone payments under in-licensing agreements as well as costs for unapproved inventory for which there is no future alternative use;
- costs related to compliance with FDA regulatory requirements;
- consulting fees paid to third-parties involved in research and development activities; and
- costs related to stock options or other stock-based compensation granted to personnel in development functions.

We expense both internal and external development costs as they are incurred.

We expect that a large percentage of our research and development expenses in the future will be incurred in support of our current and future non-clinical, preclinical and clinical development programs. These expenditures are subject to numerous uncertainties in terms of both their timing and total cost to completion. We expect to continue to develop stable formulations of our product candidates, test such formulations in preclinical studies for toxicology, safety and efficacy and to conduct clinical trials for each product candidate. We anticipate funding clinical trials for our product candidates ourselves, but we may engage collaboration partners at certain stages of clinical development. As we obtain results from clinical trials, we may elect to discontinue or delay clinical trials for certain product candidates or programs in order to focus our resources on more promising product candidates or programs. Completion of clinical trials by us or our future collaborators may take several years or more, the length of time generally varying with the type, complexity, novelty and intended use of a product candidate. The costs of clinical trials may vary significantly

over the life of a project owing to but not limited to the following:

- the number of sites included in the trials;
- the length of time required to enroll eligible patients;
- the number of patients that participate in the trials;
- the number of doses that patients receive;
- the drop-out or discontinuation rates of patients;
- the duration of patient follow-up;
- the phase of development the product candidate is in; and
- the efficacy and safety profile of the product candidate.

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Our expenses related to clinical trials are based on estimates of the services received and efforts expended pursuant to contracts with multiple research institutions and contract research organizations that conduct and manage clinical trials on our behalf. The financial terms of these agreements are subject to negotiation and vary from contract to contract and may result in uneven payment flows. Generally, these agreements set forth the scope of work to be performed at a fixed fee or unit price. Payments under the contracts depend on factors such as the successful enrollment of patients or the completion of clinical trial milestones. Expenses related to clinical trials generally are accrued based on contracted amounts applied to the level of patient enrollment and activity according to the protocol. If timelines or contracts are modified based upon changes in the clinical trial protocol or scope of work to be performed, we modify our estimates of accrued expenses accordingly on a prospective basis.

None of our product candidates have received FDA or foreign regulatory marketing approval. In order to grant marketing approval, a health authority such as the FDA or foreign regulatory agencies must conclude that clinical and preclinical data establish the safety and efficacy of our product candidates with an appropriate benefit to risk profile relevant to a particular indication, and that the product can be manufactured under cGMP in a reproducible manner to deliver the product s intended performance in terms of its stability, quality, purity and potency. Until our submission is reviewed by a health authority, there is no way to predict the outcome of their review. Even if the clinical studies meet their predetermined primary endpoints, and a registration dossier is accepted for filing, a health authority could still determine that an appropriate benefit to risk relationship does not exist for the indication that we are seeking.

We cannot forecast with any degree of certainty which of our product candidates will be subject to future collaborations or how such arrangements would affect our development plan or capital requirements.

As a result of the uncertainties discussed above, we are unable to determine the duration and completion costs of our development projects or when and to what extent we will receive cash inflows from the commercialization and sale of an approved product candidate.

Corporate Information

We were incorporated in the state of Delaware on August 13, 2004 as Neuron Systems, Inc. On December 20, 2012, we changed our name to Aldexa Therapeutics, Inc. and on March 17, 2014, we changed our name to Aldeyra Therapeutics, Inc. Our principal executive offices are located at 131 Hartwell Avenue, Suite 320, Lexington, Massachusetts 02421. Our telephone number is (781) 761-4904. Our website address is www.aldeyra.com. Information contained on our website is not incorporated by reference into this annual report on Form 10-K, and you should not consider information contained on our website to be part of this annual report on Form 10-K or in deciding whether to purchase shares of our common stock. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to reports filed or furnished pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended, are available free of charge on the Investors portion of our website at http://ir.aldeyra.com/ as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

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ITEM 1A. *RISK FACTORS*

Our business is subject to numerous risks. You should carefully consider the risks described below together with the other information set forth in this annual report on Form 10-K, which could materially affect our business, financial condition and future results. The risks described below are not the only risks facing our company. Risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, prospects, financial condition and operating results.

Risks Related to our Business

We have incurred significant operating losses since inception and we expect to incur significant losses for the foreseeable future. We may never become profitable or, if achieved, be able to sustain profitability.

We have incurred significant operating losses since we were founded in 2004 and expect to incur significant losses for the next several years as we continue our clinical trial and development programs for ADX-102 and our other product candidates. Net loss for the years ended December 31, 2016 and 2015 was approximately $18.7 million and $12.1 million, respectively. As of December 31, 2016, we had total stockholders equity of $21.6 million and an accumulated deficit of $77.3 million. Losses have resulted principally from costs incurred in our clinical trials, research and development programs and from our general and administrative expenses. In the future, we intend to continue to conduct research and development, clinical testing, regulatory compliance activities and, if ADX-102 or any of our other product candidates is approved, sales and marketing activities that, together with anticipated general and administrative expenses, will likely result in our incurring further significant losses for the next several years.

We currently generate no revenue from sales, and we may never be able to commercialize ADX-102 or our other product candidates. We do not currently have the required approvals to market any of our product candidates and we may never receive them. We may not be profitable even if we or any of our future development partners succeed in commercializing any of our product candidates. Because of the numerous risks and uncertainties associated with developing and commercializing our product candidates, we are unable to predict the extent of any future losses or when we will become profitable, if at all.

Our business is dependent in large part on the success of a single product candidate, ADX-102. We cannot be certain that we will be able to obtain regulatory approval for, or successfully commercialize, ADX-102.

Our product candidates are in the early stage of development and will require additional preclinical studies, substantial clinical development and testing, and regulatory approval prior to commercialization. We have not yet completed development of any product. We have only one product candidate that has been the focus of significant development: ADX-102, a novel small molecule chemical entity that is believed to trap and allow for the degradation of aldehydes, toxic chemical species suspected to cause and exacerbate numerous diseases in humans and animals. We are largely dependent on successful continued development and ultimate regulatory approval of this product candidate for our future business success. We have invested, and will continue to invest, a significant portion of our time and financial resources in the development of ADX-102. We will need to raise sufficient funds for, and successfully enroll and complete, our current and planned clinical trials of ADX-102. The future regulatory and commercial success of this product candidate is subject to a number of risks, including the following:

- we may not have sufficient financial and other resources to complete the necessary clinical trials for ADX-102 and our other product candidates;

we may not be able to provide evidence of safety and efficacy for ADX-102 and our other product candidates;

we may not be able to timely or adequately finalize the design or formulation of any product candidate or demonstrate that a formulation of our product candidate will be stable for commercially reasonable time periods;

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- the safety and efficacy results of our later phase or larger clinical trials may not confirm the results of our earlier trials;

- there may be variability in patients, adjustments to clinical trial procedures and inclusion of additional clinical trial sites;

- the results of our clinical trials may not meet the endpoints, or level of statistical or clinical significance required by the FDA, or comparable foreign regulatory bodies for marketing approval;

- patients in our clinical trials may suffer other adverse effects or die for reasons that may or may not be related to ADX-102 and our other product candidates;

- if approved for certain diseases, ADX-102 and our other product candidates will compete with well-established products already approved for marketing by the FDA, including corticosteroids and other agents that have demonstrated varying levels of efficacy in some of the diseases for which we may attempt to develop ADX-102 and our other product candidates;

- the effects of legislative or regulatory reform of the health care system in the U.S. or other jurisdictions in which we may do business; and

- we may not be able to obtain, maintain or enforce our patents and other intellectual property rights.

Of the large number of drugs in development in the pharmaceutical industry, only a small percentage result in the submission of a NDA to the FDA and even fewer are approved for commercialization. Furthermore, even if we do receive regulatory approval to market ADX-102 and our other product candidates, any such approval may be subject to limitations on the indicated uses for which we may market the product. Accordingly, even if we are able to obtain the requisite financing to continue to fund our development programs, we cannot assure you that ADX-102 and our other product candidates will be successfully developed or commercialized. If we or any of our future development partners are unable to develop, or obtain regulatory approval for or, if approved, successfully commercialize, ADX-102 and or our other product candidates, we may not be able to generate sufficient revenue to continue our business.

Because we have limited experience developing clinical-stage compounds, there is a limited amount of information about us upon which you can evaluate our product candidates and business prospects.

We commenced our first clinical trial in 2010, and we have limited experience developing clinical-stage compounds upon which you can evaluate our business and prospects. In addition, as an early-stage clinical development company, we have limited experience in conducting clinical trials, and we have never conducted clinical trials of a size required for regulatory approvals. Further, we have not yet demonstrated an ability to successfully overcome many of the risks and uncertainties frequently encountered by companies in new and rapidly evolving fields, particularly in the biopharmaceutical area. For example, to execute our business plan we will need to successfully:

execute our product candidate development activities, including successfully designing and completing our clinical trial programs and product design and formulation of future product candidates;

obtain required regulatory approvals for our product candidates;

manage our spending as costs and expenses increase due to the performance and completion of clinical trials, attempting to obtain regulatory approvals, manufacturing and commercialization;

secure substantial additional funding;

develop and maintain successful strategic relationships;

build and maintain a strong intellectual property portfolio;

build and maintain appropriate clinical, sales, distribution, and marketing capabilities on our own or through third parties; and

gain broad market acceptance for our product candidates.

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If we are unsuccessful in accomplishing these objectives, we may not be able to develop product candidates, raise capital, expand our business, or continue our operations.

The results of preclinical studies and early clinical trials are not always predictive of future results. Any product candidate we or any of our future development partners advance into clinical trials, including ADX-102, may not have favorable results in later clinical trials, if any, or receive regulatory approval.

Drug development has inherent risk. We or any of our future development partners will be required to demonstrate through adequate and well-controlled clinical trials that our product candidates are safe and effective, with a favorable benefit-risk profile, for use in their target indications before we can seek regulatory approvals for their commercial sale. Drug development is a long, expensive and uncertain process, and delay or failure can occur at any stage of development, including after commencement of any of our clinical trials. In addition, as product candidates proceed through development, the trial designs may often be different from phase to phase, the vehicles or controls may be modified from trial to trial and the product formulations or manufacturing process may differ due to the need to test product candidate samples that can be manufactured on a commercial scale. For instance, we plan to modify the control utilized in our expected Phase 2b allergic conjunctivitis trial from the control used in our prior Phase 2a trial. Success in early clinical trials does not mean that later clinical trials will be successful because product candidates in later-stage clinical trials may fail to demonstrate sufficient safety or efficacy despite having progressed through initial clinical testing. Furthermore, our clinical trials will need to demonstrate sufficient safety and efficacy for approval by regulatory authorities in larger patient populations. Companies frequently suffer significant setbacks in advanced clinical trials, even after earlier clinical trials have shown promising results. In addition, only a small percentage of drugs under development result in the submission of an NDA to the FDA and even fewer are approved for commercialization.

In addition, the presumed mechanisms of aldehyde-mediated inflammation are distinct from the presumed aldehyde-mediated pathology in inborn errors of metabolism, and the efficacy and safety of ADX-102 or our other product candidates in one indication does not predict the safety and efficacy of ADX-102 and our other product candidates in other indications.

Because we are developing novel product candidates for the treatment of diseases in a manner which there is little clinical drug development experience and, in some cases, are using new endpoints or methodologies, the regulatory pathways for approval are not well defined, and, as a result, there is greater risk that our clinical trials will not result in our desired outcomes.

Our clinical focus is on the development of new products for inflammation, inborn errors of metabolism, and other diseases that are thought to be related to naturally occurring toxic and pro-inflammatory chemical species known as aldehydes. Our planned Phase 3 vehicle-controlled clinical program in noninfectious anterior uveitis and our planned Phase 3 clinical program in SLS represent the first such clinical trials performed, and thus the comparative effects of vehicle and drug are unpredictable.

We could also face challenges in designing clinical trials and obtaining regulatory approval of aldehyde sequestering agents due to the small number of historical clinical trial experience for this novel class of therapeutics. Because no aldehyde sequestering agents have received regulatory approval anywhere in the world, it is difficult to determine whether regulatory agencies will be receptive to the approval of our product candidates and to predict the time and cost associated with obtaining regulatory approval. The clinical trial requirements of the FDA and other regulatory agencies and the criteria these regulators use to determine the safety and efficacy of a product candidate vary substantially according to the type, complexity, novelty and intended use and market of the potential products. The regulatory approval process for novel product candidates such as ours can be more expensive and take longer than for

other, better known or more extensively studied classes of product candidates. Any inability to design clinical trials with protocols and endpoints acceptable to applicable regulatory authorities, and to obtain regulatory approvals for our product candidates, would have an adverse impact on our business, prospects, financial condition and results of operations.

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Because ADX-102 and our other product candidates are, to our knowledge, new chemical entities, it is difficult to predict the time and cost of development and our ability to successfully complete clinical development of these product candidates and obtain the necessary regulatory approvals for commercialization.

Our product candidates are, to our knowledge, new chemical entities, and unexpected problems related to such new technology may arise that can cause us to delay, suspend or terminate our development efforts. Although we have seen signs of efficacy and observed ADX-102 to be well tolerated in our clinical trials to date, because ADX-102 is a novel chemical entity with limited use in humans, short and long-term safety, as well as prospects for efficacy, are poorly understood and difficult to predict due to our and regulatory agencies lack of experience with them. Regulatory approval of new product candidates such as ADX-102 can be more expensive and take longer than approval for other more well-known or extensively studied pharmaceutical or biopharmaceutical product candidates.

Our dermatologic topical formulation of ADX-102 is unlikely to affect other clinical manifestations of Sjögren-Larsson Syndrome, which may decrease the likelihood of regulatory and commercial acceptance.

While the primary day-to-day complaint of SLS patients and their caregivers are symptoms associated with severe skin disease, SLS patients also manifest varying degrees of delay in mental development, spasticity, seizures and retinal disease. In August 2016, we announced that the results of our randomized, parallel-group, double-masked, vehicle-controlled clinical trial of a dermatologic formulation of ADX-102 for the treatment of the skin manifestations of SLS demonstrated clinically relevant activity of ADX-102 in diminishing the severity of ichthyosis, a serious dermatologic disease characteristic of SLS. There were no serious adverse events reported in any of these trials. However, due to expected low systemic exposure of ADX-102 when administered topically to the skin, it is unlikely that ADX-102 will significantly affect the non-dermatologic conditions of SLS. Lack of effect in neurologic and ocular manifestations of SLS may negatively impact regulatory discussions with the FDA and may also negatively impact reimbursement, pricing and commercial acceptance of ADX-102, if it is approved.

ADX-102 and our other product candidates are subject to extensive regulation, compliance with which is costly and time consuming, and such regulation may cause unanticipated delays, or prevent the receipt of the required approvals to commercialize our product candidates.

The clinical development, manufacturing, labeling, storage, record-keeping, advertising, promotion, import, export, marketing, and distribution of our product candidates are subject to extensive regulation by the FDA in the United States and by comparable authorities in foreign markets. In the United States, we are not permitted to market our product candidates until we receive regulatory approval from the FDA. The process of obtaining regulatory approval is expensive, often takes many years, and can vary substantially based upon the type, complexity, and novelty of the products involved, as well as the target indications, and patient population. Approval policies or regulations may change and the FDA has substantial discretion in the drug approval process, including the ability to delay, limit, or deny approval of a product candidate for many reasons. Despite the time and expense invested in clinical development of product candidates, regulatory approval is never guaranteed.

ADX-102 and our other product candidates and the activities associated with development and potential commercialization, including testing, manufacture, safety, efficacy, recordkeeping, labeling, storage, approval, advertising, promotion, sale and distribution, are subject to extensive regulation by the FDA and other regulatory agencies in the United States and by comparable authorities in other jurisdictions.

Our ongoing research and development activities and planned clinical development for our product candidates may be delayed, modified or ceased for a variety of reasons, including:

determining that a product candidate is ineffective or causes harmful side effects during preclinical studies or clinical trials;

difficulty establishing predictive preclinical models for demonstration of safety and efficacy of a product candidate in one or more potential therapeutic areas for clinical development;

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difficulties in manufacturing a product candidate, including the inability to manufacture a product candidate in a sufficient quantity, suitable form, or in a cost-effective manner, or under processes acceptable to the FDA for marketing approval;

the proprietary rights of third parties, which may preclude us from developing or commercializing a product candidate;

determining that a product candidate may be uneconomical to develop or commercialize, or may fail to achieve market acceptance or adequate reimbursement;

our inability to secure strategic partners which may be necessary for advancement of a product candidate into clinical development or commercialization; or

our prioritization of other product candidates for advancement.

The FDA or comparable foreign regulatory authorities can delay, limit, or deny approval of a product candidate for many reasons, including:

such authorities may disagree with the design or implementation of our or any of our future development partners clinical trials, including the endpoints of our clinical trials;

we or any of our future development partners may be unable to demonstrate to the satisfaction of the FDA or other regulatory authorities that a product candidate is safe and effective for any indication;

such authorities may not accept clinical data from trials which are conducted at clinical facilities or in countries where the standard of care is potentially different from the United States;

the results of clinical trials may not demonstrate the safety or efficacy required by such authorities for approval;

we or any of our future development partners may be unable to demonstrate that a product candidate s clinical and other benefits outweigh its safety risks;

such authorities may disagree with our interpretation of data from preclinical studies or clinical trials or the designs of such trials;

such authorities may find deficiencies in the manufacturing processes or facilities of third-party manufacturers with which we or any of our future development partners contract for clinical and commercial supplies; or

the approval policies or regulations of such authorities may significantly change in a manner rendering our or any of our future development partners clinical data insufficient for approval.

With respect to foreign markets, approval procedures vary among countries and, in addition to the aforementioned risks, can involve additional product testing, administrative review periods and agreements with pricing authorities. In addition, events raising questions about the safety of certain marketed pharmaceuticals may result in increased cautiousness by the FDA and comparable foreign regulatory authorities in reviewing new drugs based on safety, efficacy or other regulatory considerations and may result in significant delays in obtaining regulatory approvals. Any delay in obtaining, or inability to obtain, applicable regulatory approvals would prevent us or any of our future development partners from commercializing our product candidates. Moreover, we cannot predict healthcare reform initiatives, including potential reductions in federal funding, that may be adopted in the future and whether or not any such reforms would have an adverse effect on our business and our ability to obtain regulatory approval for our current or future product candidates.

Any termination or suspension of, or delays in the commencement or completion of, our clinical trials could result in increased costs to us, delay or limit our ability to generate revenue and adversely affect our commercial prospects.

Delays in the commencement or completion of our planned clinical trials for ADX-102 or other product candidates could significantly affect our product development costs. We do not know whether future trials will

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begin on time or be completed on schedule, if at all. The commencement and completion of clinical trials can be delayed for a number of reasons, including delays related to:

- the FDA failing to grant permission to proceed or placing the clinical trial on hold;
- subjects failing to enroll or remain in our clinical trials at the rate we expect;
- subjects choosing an alternative treatment for the indication for which we are developing ADX-102 or other product candidates, or participating in competing clinical trials;
- lack of adequate funding to continue the clinical trial;
- subjects experiencing severe or unexpected drug-related adverse effects;
- a facility manufacturing ADX-102, any of our other product candidates or any of their components being ordered by the FDA or other government or regulatory authorities, to temporarily or permanently shut down due to violations of current Good Manufacturing Practices, or cGMP, or other applicable requirements, or infections or cross-contaminations of product candidates in the manufacturing process;
- any changes to our manufacturing process that may be necessary or desired;
- inability to timely manufacture sufficient quantities of the applicable product candidate for the clinical trial or expiration of materials intended for use in the clinical trial;
- third-party clinical investigators losing the licenses or permits necessary to perform our clinical trials, not performing our clinical trials on our anticipated schedule or consistent with the clinical trial protocol, Good Clinical Practice or regulatory requirements, or other third parties not performing data collection or analysis in a timely or accurate manner;
- inspections of clinical trial sites by the FDA or the finding of regulatory violations by the FDA or an institutional review board, or IRB, that require us to undertake corrective action, result in suspension or termination of one or more sites or the imposition of a clinical hold on the entire trial, or that prohibit us from using some or all of the data in support of our marketing applications;
- third-party contractors becoming debarred or suspended or otherwise penalized by the FDA or other government or regulatory authorities for violations of regulatory requirements, in which case we may need to

find a substitute contractor, and we may not be able to use some or all of the data produced by such contractors in support of our marketing applications; or

one or more IRBs refusing to approve, suspending or terminating the trial at an investigational site, precluding enrollment of additional subjects, or withdrawing its approval of the trial.

Product development costs will increase if we have delays in testing or approval of ADX-102 and our other product candidates or if we need to perform more or larger clinical trials than planned. Additionally, changes in regulatory requirements and policies may occur and we may need to amend clinical trial protocols to reflect these changes. Amendments may require us to resubmit our clinical trial protocols to IRBs for reexamination, which may impact the costs, timing or successful completion of a clinical trial. If we experience delays in completion of or if we, the FDA or other regulatory authorities, the IRB, other reviewing entities, or any of our clinical trial sites suspend or terminate any of our clinical trials, the commercial prospects for a product candidate may be harmed and our ability to generate product revenues will be delayed. In addition, many of the factors that cause, or lead to, termination or suspension of, or a delay in the commencement or completion of, clinical trials may also ultimately lead to the denial of regulatory approval of a product candidate. Further, if one or more clinical trials are delayed, our competitors may be able to bring products to market before we do, and the commercial viability of ADX-102 or other product candidates could be significantly reduced.

We may find it difficult to enroll patients in our clinical trials or identify patients during commercialization (if our products are approved by regulatory agencies) for product candidates addressing orphan or rare diseases.

As part of our business strategy, we plan to evaluate the development and commercialization of product candidates for the treatment of orphan and other rare diseases. Given that we are in the early stages of clinical

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trials for ADX-102, we may not be able to initiate or continue clinical trials if we are unable to locate a sufficient number of eligible patients willing and able to participate in the clinical trials required by the FDA or other non-United States regulatory agencies. In addition, if others develop product candidates for the treatment of similar diseases, we would potentially compete with them for the enrollment in these rare patient populations, which may adversely impact the rate of patient enrollment in and the timely completion of our current and planned clinical trials. Additionally, insufficient patient enrollment, may be a function of many other factors, including the size and nature of the patient population, the nature of the protocol, the proximity of patients to clinical sites, the timing and magnitude of disease symptom presentation, the availability of effective treatments for the relevant disease, and the eligibility criteria for the clinical trial. Our inability to identify and enroll a sufficient number of eligible patients for any of our current or future clinical trials would result in significant delays or may require us to abandon one or more clinical trials altogether. Delays in patient enrollment in the future as a result of these and other factors may result in increased costs or may affect the timing or outcome of our clinical trials, which could prevent us from completing these trials and adversely affect our ability to advance the development of our product candidates. Further, if our products are approved by regulatory agencies, we may not be able to identify sufficient number of patients to generate significant revenues.

Any product candidate we or any of our future development partners advance into clinical trials may cause unacceptable adverse events or have other properties that may delay or prevent its regulatory approval or commercialization or limit its commercial potential.

Unacceptable adverse events caused by any of our product candidates that we advance into clinical trials could cause us or regulatory authorities to interrupt, delay, or halt clinical trials and could result in the denial of regulatory approval by the FDA or other regulatory authorities for any or all targeted indications and markets. This in turn could prevent us from completing development or commercializing the affected product candidate and generating revenue from its sale.

We have not yet completed testing of any of our product candidates in humans for the treatment of the indications for which we intend to seek approval, and we currently do not know the extent of adverse events, if any, that will be observed in patients who receive any of our product candidates. ADX-102, for example, has been observed to be toxic at high concentrations in *in vitro* human dermal tissue. In addition, there was transient and generally mild stinging noted in the ADX-102 treatment arm of our Phase 2a clinical trial in allergic conjunctivitis, with two patients out of the 50 patients in the treatment arm dropping out of the trial during treatment. There was an increased frequency of ocular stinging and burning in the ADX-102 treated arms of our Phase 2 clinical trial in noninfectious anterior uveitis, with one subject in the ADX-102 treatment arm and one subject in combination ADX-102 and Pred Forte® arm dropping out of the trial during treatment for an adverse event of stinging. However, there were no serious adverse events in this trial. In preparation for clinical testing of systemically administered ADX-102, we believe that we have identified a preliminary No Adverse Effect Level in pre-clinical toxicology studies where ADX-102 is administrated intravenously. If any of our product candidates cause unacceptable adverse events in clinical trials, which may be larger or longer than those previously conducted, we may not be able to obtain regulatory approval or commercialize such product candidate.

Final marketing approval for ADX-102 or our other product candidates by the FDA or other regulatory authorities for commercial use may be delayed, limited, or denied, any of which would adversely affect our ability to generate operating revenues.

After the completion of our clinical trials and, assuming the results of the trials are successful, the submission of an NDA, we cannot predict whether or when we will obtain regulatory approval to commercialize ADX-102 or our other product candidates and we cannot, therefore, predict the timing of any future revenue. We cannot commercialize

ADX-102 or our other product candidates until the appropriate regulatory authorities have reviewed and approved the applicable applications. We cannot assure you that the regulatory agencies will complete their review processes in a timely manner or that we will obtain regulatory approval for ADX-102 or

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our other product candidates. In addition, we may experience delays or rejections based upon additional government regulation from future legislation or administrative action or changes in FDA policy during the period of product development, clinical trials and FDA regulatory review. If marketing approval for ADX-102 or our other product candidates is delayed, limited or denied, our ability to market the product candidate, and our ability to generate product sales, would be adversely affected.

Even if we obtain marketing approval for ADX-102 or any other product candidate, it could be subject to restrictions or withdrawal from the market and we may be subject to penalties if we fail to comply with regulatory requirements or if we experience unanticipated problems with our product candidate, when and if any of them are approved.

Even if United States regulatory approval is obtained, the FDA may still impose significant restrictions on a product s indicated uses or marketing or impose ongoing requirements for potentially costly and time consuming post-approval studies, post-market surveillance or clinical trials. Following approval, if any, of ADX-102 or any other product candidates, such candidate will also be subject to ongoing FDA requirements governing the labeling, packaging, storage, distribution, safety surveillance, advertising, promotion, recordkeeping and reporting of safety and other post-market information. In addition, manufacturers of drug products and their facilities are subject to continual review and periodic inspections by the FDA and other regulatory authorities for compliance with cGMP requirements, including those relating to quality control, quality assurance and corresponding maintenance of records and documents. If we or a regulatory agency discovers previously unknown problems with a product, such as adverse events of unanticipated severity or frequency, or problems with the facility where the product is manufactured, a regulatory agency may impose restrictions on that product, the manufacturing facility or us, including requesting recall or withdrawal of the product from the market or suspension of manufacturing.

If we or the manufacturing facilities for ADX-102 or any other product candidate that may receive regulatory approval, if any, fail to comply with applicable regulatory requirements, a regulatory agency may:

- issue warning letters or untitled letters;
- seek an injunction or impose civil or criminal penalties or monetary fines;
- suspend or withdraw regulatory approval;
- suspend any ongoing clinical trials;
- refuse to approve pending applications or supplements or applications filed by us;
- suspend or impose restrictions on operations, including costly new manufacturing requirements; or

seize or detain products, refuse to permit the import or export of product, or request us to initiate a product recall.

The occurrence of any event or penalty described above may inhibit our ability to commercialize our product candidates and generate revenue.

The FDA has the authority to require a risk evaluation and mitigation strategy plan as part of a NDA or after approval, which may impose further requirements or restrictions on the distribution or use of an approved drug, such as limiting prescribing to certain physicians or medical centers that have undergone specialized training, limiting treatment to patients who meet certain safe-use criteria and requiring treated patients to enroll in a registry.

In addition, if ADX-102 or any of our other product candidates is approved, our product labeling, advertising and promotion would be subject to regulatory requirements and continuing regulatory review. The FDA strictly regulates the promotional claims that may be made about prescription products. In particular, a product may not be promoted for uses that are not approved by the FDA as reflected in the product s approved

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labeling. If we receive marketing approval for a product candidate, physicians may nevertheless prescribe it to their patients in a manner that is inconsistent with the approved label. If we are found to have promoted such off-label uses, we may become subject to significant liability. The FDA and other agencies actively enforce the laws and regulations prohibiting the promotion of off-label uses, and a company that is found to have improperly promoted off-label uses may be subject to significant sanctions. The federal government has levied large civil and criminal fines against companies for alleged improper promotion and has enjoined several companies from engaging in off-label promotion. The FDA has also requested that companies enter into consent decrees or permanent injunctions under which specified promotional conduct is changed or curtailed.

Even if we receive regulatory approval for ADX-102 or any other product candidate, we still may not be able to successfully commercialize it and the revenue that we generate from its sales, if any, could be limited.

Even if our product candidates receive regulatory approval, they may not gain market acceptance among physicians, patients, healthcare payors, and the medical community. Coverage and reimbursement of our product candidates by third-party payors, including government payors, is also generally necessary for commercial success. The degree of market acceptance of our product candidates will depend on a number of factors, including:

- demonstration of clinical efficacy and safety compared to other more-established products;
- the limitation of our targeted patient population and other limitations or warnings contained in any FDA-approved labeling;
- acceptance of a new formulation by health care providers and their patients;
- the prevalence and severity of any adverse effects;
- new procedures or methods of treatment that may be more effective in treating or may reduce the incidences of SLS or other conditions for which our products are intended to treat;
- pricing and cost-effectiveness;
- the effectiveness of our or any future collaborators sales and marketing strategies;
- our ability to obtain and maintain sufficient third-party coverage or reimbursement from government health care programs, including Medicare and Medicaid, private health insurers and other third-party payors;
- unfavorable publicity relating to the product candidate; and

the willingness of patients to pay out-of-pocket in the absence of third-party coverage.

Moreover, we cannot predict what healthcare reform initiatives may be adopted in the future. Further federal and state legislative and regulatory developments are likely, and we expect ongoing initiatives in the U.S. to increase pressure on drug pricing. Such reforms could have an adverse effect on anticipated revenues from our current or future product candidates for which we may obtain regulatory approval and may affect our overall financial condition and ability to develop drug candidates.

If any product candidate is approved but does not achieve an adequate level of acceptance by physicians, hospitals, healthcare payors or patients, we may not generate sufficient revenue from that product candidate and may not become or remain profitable. Our efforts to educate the medical community and third-party payors on the benefits of ADX-102 or any of our other product candidates may require significant resources and may never be successful. In addition, our ability to successfully commercialize our product candidate will depend on our ability to manufacture our products, differentiate our products from competing products and defend the intellectual property of our products.

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Reimbursement may be limited or unavailable in certain market segments for our product candidates, which could make it difficult for us to sell our product candidates profitably.

Market acceptance and sales of our product candidates will depend significantly on the availability of adequate insurance coverage and reimbursement from third-party payors for any of our product candidates and may be affected by existing and future health care reform measures. Government authorities and third-party payors, such as private health insurers and health maintenance organizations, decide which drugs they will pay for and establish reimbursement levels. As a result of negative trends in the general economy in the U.S. or other jurisdictions in which we may do business, these organizations may be unable to satisfy their reimbursement obligations or may delay payment. Reimbursement by a third-party payor may depend upon a number of factors including the third-party payor s determination that use of a product candidate is:

a covered benefit under its health plan;

safe, effective, and medically necessary;

appropriate for the specific patient;

cost-effective; and

neither experimental nor investigational.

Obtaining coverage and reimbursement approval for a product candidate from a government or other third-party payor is a time-consuming and costly process that could require us to provide supporting scientific, clinical and cost effectiveness data for the use of the applicable product candidate to the payor. We may not be able to provide data sufficient to gain acceptance with respect to coverage and reimbursement. We cannot be sure that coverage or adequate reimbursement will be available for any of our product candidates. Further, we cannot be sure that reimbursement amounts will not reduce the demand for, or the price of, our product candidates. If reimbursement is not available or is available only in limited levels, we may not be able to commercialize certain of our product candidates profitably, or at all, even if approved. In recent years, through legislative and regulatory actions, the federal government has made substantial changes to various payment systems under the Medicare program. Comprehensive reforms to the U.S. healthcare system were recently enacted, including changes to the methods for, and amounts of, Medicare reimbursement. The new presidential administration and Congress have indicated they may further reform the Medicare program and the U.S. healthcare system, but have not made any definitive proposals which allow us to gauge the impact of such potential reforms, if any, on our business and operations. These reforms could significantly reduce payments from Medicare and Medicaid over the next ten years. Reforms or other changes to these payment systems, including modifications to the conditions on qualification for payment, bundling of payments or the imposition of enrollment limitations on new providers, may change the availability, methods and rates of reimbursements from Medicare, private insurers and other third-party payers for our current and future product candidates, if any, for which we are able to obtain regulatory approval. Some of these changes and proposed changes could result in reduced reimbursement rates for such product candidates, if approved, which would adversely affect our business strategy, operations and financial results.

As a result of legislative proposals and the trend toward managed health care in the United States, third-party payors are increasingly attempting to contain health care costs by limiting both coverage and the level of reimbursement of new drugs. They may also refuse to provide coverage of approved product candidates for medical indications other than those for which the FDA has granted market approvals. As a result, significant uncertainty exists as to whether and how much third-party payors will reimburse patients for their use of newly approved drugs, which in turn will put pressure on the pricing of drugs. We expect to experience pricing pressures in connection with the sale of our product candidates due to the trend toward managed health care, the increasing influence of health maintenance organizations, and additional legislative proposals as well as country, regional or local healthcare budget limitations.

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If we fail to develop and commercialize other product candidates, we may be unable to grow our business.

As part of our growth strategy, we plan to evaluate the development and commercialization of other therapies related to immune-mediated, inflammatory, orphan and other diseases. We will evaluate internal opportunities from our compound libraries, and also may choose to in-license or acquire other product candidates as well as commercial products to treat patients suffering from immune-mediated or orphan or other disorders with high unmet medical needs and limited treatment options. These other product candidates will require additional, time-consuming development efforts prior to commercial sale, including preclinical studies, clinical trials and approval by the FDA and/or applicable foreign regulatory authorities. All product candidates are prone to the risks of failure that are inherent in pharmaceutical product development, including the possibility that the product candidate will not be shown to be sufficiently safe and/or effective for approval by regulatory authorities. In addition, we cannot assure you that any such products that are approved will be manufactured or produced economically, successfully commercialized or widely accepted in the marketplace or be more effective than other commercially available alternatives.

Orphan drug designation or Breakthrough Therapy Designation from the FDA may be difficult or not possible to obtain, and if we are unable to obtain one or both such designations for ADX-102 or our other product candidates, regulatory and commercial prospects may be negatively impacted.

The FDA designates orphan status to drugs that are intended to treat rare diseases with fewer than 200,000 patients in the United States or that affect more than 200,000 persons but are not expected to recover the costs of developing and marketing a treatment drug. Orphan status drugs do not require prescription drug user fees with a marketing application, may qualify the drug development sponsor for certain tax credits, and can be marketed without generic competition for seven years. We believe that ADX-102 will qualify as an orphan drug for SLS and noninfectious anterior uveitis, and possibly other diseases that we may test. However, we cannot guarantee that we will be able to receive orphan drug status from the FDA for ADX-102. If we are unable to secure orphan drug status or Breakthrough Therapy Designation for ADX-102 or our other product candidates, our regulatory and commercial prospects may be negatively impacted.

In addition, during challenging and uncertain economic times and in tight credit markets, there may be a disruption or delay in the performance of our third party contractors, suppliers or partners. If such third parties are unable to satisfy their commitments to us, our business and results of operations would be adversely affected.

We rely and will continue to rely on outsourcing arrangements for many of our activities, including clinical development and supply of ADX-102 and our other product candidates.

As of December 31, 2016, we had only eleven full-time employees and, as a result, we rely, and expect to continue to rely, on outsourcing arrangements for a significant portion of our activities, including clinical research, data collection and analysis, manufacturing, financial reporting and accounting and human resources, as well as for certain functions as a public company. We may have limited control over these third parties and we cannot guarantee that they will perform their obligations in an effective and timely manner.

We rely on third parties to conduct our clinical trials. If these third parties do not meet our deadlines or otherwise conduct the trials as required, our clinical development programs could be delayed or unsuccessful and we may not be able to obtain regulatory approval for or commercialize our product candidates when expected or at all.

We do not have the ability to conduct all aspects of our preclinical testing or clinical trials ourselves. We are dependent on third parties to conduct the clinical trials for ADX-102 and clinical trials for our other future product

candidates and, therefore, the timing of the initiation and completion of these trials is controlled by such third parties and may occur on substantially different timing from our estimates. Specifically, we use CROs to conduct our clinical trials and we also rely on medical institutions, clinical investigators and consultants to

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conduct our trials in accordance with our clinical protocols and regulatory requirements. Our CROs, investigators, and other third parties play a significant role in the conduct of these trials and subsequent collection and analysis of data.

There is no guarantee that any CROs, investigators, or other third parties on which we rely for administration and conduct of our clinical trials will devote adequate time and resources to such trials or perform as contractually required. If any of these third parties fails to meet expected deadlines, fails to adhere to our clinical protocols, or otherwise performs in a substandard manner, our clinical trials may be extended, delayed, or terminated. If any of our clinical trial sites terminates for any reason, we may experience the loss of follow-up information on subjects enrolled in our ongoing clinical trials unless we are able to transfer those subjects to another qualified clinical trial site. In addition, principal investigators for our clinical trials may serve as scientific advisors or consultants to us from time to time and may receive cash or equity compensation in connection with such services. If these relationships and any related compensation result in perceived or actual conflicts of interest, the integrity of the data generated at the applicable clinical trial site may be jeopardized.

We rely completely on third parties to supply drug substance and manufacture drug product for our clinical trials and preclinical studies. We intend to rely on other third parties to produce commercial supplies of product candidates, and our dependence on third parties could adversely impact our business.

We are completely dependent on third-party suppliers of the drug substance and drug product for our product candidates. If these third-party suppliers do not supply sufficient quantities of materials to us on a timely basis and in accordance with applicable specifications and other regulatory requirements, there could be a significant interruption of our supplies, which would adversely affect clinical development of the product candidate. Furthermore, if any of our contract manufacturers cannot successfully manufacture material that conforms to our specifications and within regulatory requirements, we will not be able to secure and/or maintain regulatory approval, if any, for our product candidates.

We will also rely on our contract manufacturers to purchase from third-party suppliers the materials necessary to produce our product candidates for our anticipated clinical trials. We do not have any control over the process or timing of the acquisition of raw materials by our contract manufacturers. Moreover, we currently do not have agreements in place for the commercial production of these raw materials. Any significant delay in the supply of a product candidate or the raw material components thereof for an ongoing clinical trial could considerably delay completion of that clinical trial, product candidate testing, and potential regulatory approval of that product candidate.

We do not expect to have the resources or capacity to commercially manufacture any of our proposed product candidates if approved, and will likely continue to be dependent on third-party manufacturers. Our dependence on third parties to manufacture and supply us with clinical trial materials and any approved product candidates may adversely affect our ability to develop and commercialize our product candidates on a timely basis.

We are subject to a multitude of manufacturing risks, any of which could substantially increase our costs and limit supply of our products.

The process of manufacturing our products is complex, highly regulated and subject to several risks, including:

- The manufacturing of compounds is extremely susceptible to product loss due to contamination, equipment failure, improper installation or operation of equipment, or vendor or operator error. Even minor deviations from normal manufacturing processes could result in reduced production yields, product defects and other

supply disruptions. If microbial, viral or other contaminations are discovered in our products or in the manufacturing facilities in which our products are made, such manufacturing facilities may need to be closed for an extended period of time to investigate and remedy the contamination.

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The manufacturing facilities in which our products are made could be adversely affected by equipment failures, labor shortages, natural disasters, power failures and numerous other factors.

We and our contract manufacturers must comply with the FDA s cGMP regulations and guidelines. We and our contract manufacturers may encounter difficulties in achieving quality control and quality assurance and may experience shortages in qualified personnel. We and our contract manufacturers are subject to inspections by the FDA and comparable agencies in other jurisdictions to confirm compliance with applicable regulatory requirements. Any failure to follow cGMP or other regulatory requirements or any delay, interruption or other issues that arise in the manufacture, fill-finish, packaging, or storage of our products as a result of a failure of our facilities or the facilities or operations of third parties to comply with regulatory requirements or pass any regulatory authority inspection could significantly impair our ability to develop and commercialize our products, including leading to significant delays in the availability of products for our clinical studies or the termination or hold on a clinical study, or the delay or prevention of a filing or approval of marketing applications for our product candidates. Significant noncompliance could also result in the imposition of sanctions, including fines, injunctions, civil penalties, failure of regulatory authorities to grant marketing approvals for our product candidates, delays, suspension or withdrawal of approvals, license revocation, seizures or recalls of products, operating restrictions and criminal prosecutions, any of which could damage our reputation. If we are not able to maintain regulatory compliance, we may not be permitted to market our products and/or may be subject to product recalls, seizures, injunctions, or criminal prosecution.

Any adverse developments affecting manufacturing operations for our products may result in shipment delays, inventory shortages, lot failures, product withdrawals or recalls, or other interruptions in the supply of our products. We may also have to take inventory write-offs and incur other charges and expenses for products that fail to meet specifications, undertake costly remediation efforts or seek more costly manufacturing alternatives.

We may not be successful in establishing and maintaining development or other strategic partnerships, which could adversely affect our ability to develop and commercialize product candidates.

We may choose to enter into development or other strategic partnerships in the future, including collaborations with major biotechnology or pharmaceutical companies. We face significant competition in seeking appropriate partners and the negotiation process is time consuming and complex. Moreover, we may not be successful in our efforts to establish a development partnership or other alternative arrangements for any of our other existing or future product candidates and programs because our research and development pipeline may be insufficient, our product candidates and programs may be deemed to be at too early a stage of development for collaborative effort and/or third parties may not view our product candidates and programs as having the requisite potential to demonstrate safety and efficacy. Even if we are successful in our efforts to establish development partnerships, the terms that we agree upon may not be favorable to us and we may not be able to maintain such development partnerships if, for example, development or approval of a product candidate is delayed or sales of an approved product candidate are disappointing. Any delay in entering into development partnership agreements related to our product candidates could delay the development and commercialization of our product candidates and reduce their competitiveness if they reach the market.

Moreover, if we fail to maintain development or other strategic partnerships related to our product candidates that we may choose to enter into:

the development of certain of our current or future product candidates may be terminated or delayed;

our cash expenditures related to development of certain of our current or future product candidates would increase significantly and we may need to seek additional financing;

we may be required to hire additional employees or otherwise develop expertise, such as sales and marketing expertise, for which we have not budgeted; and

we will bear all of the risk related to the development of any such product candidates.

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We may form strategic alliances in the future, and we may not realize the benefits of such alliances.

We may form strategic alliances, create joint ventures or collaborations or enter into licensing arrangements with third parties that we believe will complement or augment our existing business, including for the continued development or commercialization of ADX-102 or our other product candidates. These relationships or those like them may require us to incur non-recurring and other charges, increase our near- and long-term expenditures, issue securities that dilute our existing stockholders or disrupt our management and business. In addition, we face significant competition in seeking appropriate strategic partners and the negotiation process is time-consuming and complex. Moreover, we may not be successful in our efforts to establish a strategic partnership or other alternative arrangements for ADX-102 or our other product candidates because third parties may view the risk of success in our planned clinical trial as too significant or the commercial opportunity for our product candidate as too limited. We cannot be certain that, following a strategic transaction or license, we will achieve the revenues or specific net income that justifies such transaction.

If our competitors develop treatments for the target indications of our product candidates that are approved more quickly than ours, marketed more successfully or demonstrated to be safer or more effective than our product candidates, our commercial opportunity will be reduced or eliminated.

We operate in highly competitive segments of the biotechnology and biopharmaceutical markets. We face competition from many different sources, including commercial pharmaceutical and biotechnology enterprises, academic institutions, government agencies, and private and public research institutions. Our product candidates, if successfully developed and approved, will compete with established therapies as well as with new treatments that may be introduced by our competitors. With the exception of SLS and SSADH, there are a variety of drug candidates in development for the indications that we intend to test. Many of our competitors have significantly greater financial, product candidate development, manufacturing, and marketing resources than we do. Large pharmaceutical and biotechnology companies have extensive experience in clinical testing and obtaining regulatory approval for drugs. In addition, universities and private and public research institutes may be active in aldehyde research, and some could be in direct competition with us. We also may compete with these organizations to recruit management, scientists, and clinical development personnel. We will also face competition from these third parties in establishing clinical trial sites, registering subjects for clinical trials, and in identifying and in-licensing new product candidates. Smaller or early-stage companies may also prove to be significant competitors, particularly through collaborative arrangements with large and established companies.

New developments, including the development of other pharmaceutical technologies and methods of treating disease, occur in the pharmaceutical and life sciences industries at a rapid pace. Developments by competitors may render our product candidates obsolete or noncompetitive. There are methods that can potentially be employed to trap aldehydes that we have not conceived of or attempted to patent, and other parties may discover and patent aldehyde trapping approaches and compositions that are similar to or different from ours. Competition in drug development is intense. We anticipate that we will face intense and increasing competition as new treatments enter the market and advanced technologies become available.

Our future success depends on our ability to demonstrate and maintain a competitive advantage with respect to the design, development and commercialization of ADX-102 or our other product candidates. Noninfectious anterior uveitis and other inflammatory diseases may be treated with general immune suppressing therapies, including corticosteroids, some of which are generic. Our potential competitors in these diseases may be developing novel immune modulating therapies that may be safer or more effective than ADX-102 or our other product candidates.

We have no sales, marketing or distribution capabilities and we will have to invest significant resources to develop these capabilities.

We have no internal sales, marketing or distribution capabilities. If ADX-102 or any of our other product candidates ultimately receives regulatory approval, we may not be able to effectively market and distribute the

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product candidate. We will have to invest significant amounts of financial and management resources to develop internal sales, distribution and marketing capabilities, some of which will be committed prior to any confirmation that ADX-102 or any of our other product candidates will be approved. We may not be able to hire consultants or external service providers to assist us in sales, marketing and distribution functions on acceptable financial terms or at all. Even if we determine to perform sales, marketing and distribution functions ourselves, we could face a number of additional related risks, including:

- we may not be able to attract and build an effective marketing department or sales force;
- the cost of establishing a marketing department or sales force may exceed our available financial resources and the revenues generated by ADX-102 or any other product candidates that we may develop, in-license or acquire; and
- our direct sales and marketing efforts may not be successful.

We are highly dependent on the services of our employees and certain key consultants.

As a company with a limited number of personnel, we are highly dependent on the development, regulatory, commercial, and financial expertise of our senior management team composed of three individuals and certain other employees: Todd C. Brady, M.D., Ph.D., our President and Chief Executive Officer; Stephen J. Tulipano, our Chief Financial Officer; and David J. Clark, M.D., our Chief Medical Officer. In addition, we rely on the services of a number of key consultants, including IP, pharmacokinetic, chemistry, toxicology, dermatologic drug development and ocular drug development consultants. The loss of such individuals or the services of future members of our management team could delay or prevent the further development and potential commercialization of our product candidates and, if we are not successful in finding suitable replacements, could harm our business.

If we fail to attract and retain senior management and key commercial personnel, we may be unable to successfully develop or commercialize our product candidates.

We will need to expand and effectively manage our managerial, operational, financial, and other resources in order to successfully pursue our clinical development and commercialization efforts. Our success also depends on our continued ability to attract, retain, and motivate highly qualified management and scientific personnel and we may not be able to do so in the future due to intense competition among biotechnology and pharmaceutical companies, universities, and research organizations for qualified personnel. If we are unable to attract and retain the necessary personnel, we may experience significant impediments to our ability to implement our business strategy.

We expect to expand our management team. Our future performance will depend, in part, on our ability to successfully integrate newly hired executive officers into our management team and our ability to develop an effective working relationship among senior management. Our failure to integrate these individuals and create effective working relationships among them and other members of management could result in inefficiencies in the development and commercialization of our product candidates, harming future regulatory approvals, sales of our product candidates and our results of operations.

We may encounter difficulties in managing our growth and expanding our operations successfully.

Because, as of December 31, 2016, we only had eleven full-time employees, we will need to grow our organization to continue development and pursue the potential commercialization of ADX-102 and our other product candidates, as well as function as a public company. As we seek to advance ADX-102 and other product candidates, we will need to expand our financial, development, regulatory, manufacturing, marketing and sales capabilities or contract with third parties to provide these capabilities for us. As our operations expand, we expect that we will need to manage additional relationships with various strategic partners, suppliers and other third parties. Future growth will impose significant added responsibilities on members of management and require us

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to retain additional internal capabilities. Our future financial performance and our ability to commercialize our product candidates and to compete effectively will depend, in part, on our ability to manage any future growth effectively. To that end, we must be able to manage our development efforts and clinical trials effectively and hire, train and integrate additional management, clinical and regulatory, financial, administrative and sales and marketing personnel. We may not be able to accomplish these tasks, and our failure to so accomplish could prevent us from successfully growing our company.

Recently enacted and future legislation may increase the difficulty and cost for us to obtain marketing approval of and commercialize our product candidates and may affect the prices we may obtain.

In the United States and some foreign jurisdictions, there have been a number of legislative and regulatory changes and proposed changes regarding healthcare systems that could prevent or delay marketing approval for our product candidates, restrict or regulate post-approval activities and affect our ability to profitably sell our product candidates.

Legislative and regulatory proposals have been made to expand post-approval requirements and restrict sales and promotional activities for pharmaceutical products. We are not sure whether additional legislative changes will be enacted, or whether the FDA regulations, guidance or interpretations will be changed, or what the impact of such changes on the marketing approvals of our product candidates, if any, may be. In addition, increased scrutiny by the United States Congress of the FDA s approval process may significantly delay or prevent marketing approval, as well as subject us to more stringent product labeling and post-marketing testing and other requirements.

In the United States, the Medical Modernization Act of 2003 (MMA) changed the way Medicare covers and pays for pharmaceutical products. The legislation expanded Medicare coverage for drug purchases by the elderly and introduced a new reimbursement methodology based on average sales prices for drugs. In addition, this legislation authorized Medicare Part D prescription drug plans to use formulas where they can limit the number of drugs that will be covered in any therapeutic class. As a result of this legislation and the expansion of federal coverage of drug products, we expect that there will be additional pressure to contain and reduce costs. These cost reduction initiatives and other provisions of this legislation could decrease the coverage and price that we receive for any approved products and could seriously harm our business. While the MMA applies only to drug benefits for Medicare beneficiaries, private payors often follow Medicare coverage policy and payment limitations in setting their own reimbursement rates, and any reduction in reimbursement that results from the MMA may result in a similar reduction in payments from private payors.

In early 2010, President Obama signed into law the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (together, PPACA), a sweeping law intended to broaden access to health insurance, reduce or constrain the growth of healthcare spending, enhance remedies against fraud and abuse, add new transparency requirements for healthcare and health insurance industries, impose new taxes and fees on the health industry and imposed additional health policy reforms. Effective October 1, 2010, the PPACA s definition of average manufacturer price was revised for reporting purposes, which could increase the amount of Medicaid drug rebates to states. Further, beginning in 2011, the PPACA imposes a significant annual fee on companies that manufacture or import branded prescription drug products. Substantial new provisions affecting compliance have also been enacted, which may require us to modify our business practices with healthcare practitioners. Although it is too early to determine the effect of the PPACA on our business, the new law appears likely to continue the pressure on pharmaceutical pricing, especially under Medicare, and may also increase our regulatory burdens and operating costs.

More recently, the new presidential administration and the U.S. Congress have indicated they may seek to replace PPACA and related legislation with new healthcare legislation. There is uncertainty with respect to the impact these potential changes may have, if any, and any changes will likely take time to unfold, and could have an impact on

coverage and reimbursement for healthcare items and services covered by plans that were

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authorized by PPACA. However, we cannot predict the ultimate content, timing or effect of any healthcare reform legislation or the impact of potential legislation on us.

We expect that additional state and federal healthcare reform measures will be adopted in the future, any of which could limit the amounts that federal and state governments will pay for healthcare products and services, which could result in reduced demand for our products once approved or additional pricing pressures, and may adversely affect our operating results.

The continuing efforts of the government, insurance companies, managed care organizations, and other payors of healthcare services to contain or reduce costs of health care may adversely affect:

- the demand for any product candidates for which we may obtain regulatory approval;
- our ability to set a price that we believe is fair for our product candidates;
- our ability to generate revenue and achieve or maintain profitability;
- the level of taxes that we are required to pay; and
- the availability of capital.

If we market products in a manner that violates healthcare fraud and abuse laws, or if we violate government price reporting laws, we may be subject to civil or criminal penalties.

In addition to FDA restrictions on the marketing of pharmaceutical products, several other types of state and federal healthcare fraud and abuse laws have been applied in recent years to restrict certain marketing practices in the pharmaceutical industry. These laws include false claims statutes and anti-kickback statutes. Because of the breadth of these laws and the narrowness of the safe harbors, it is possible that some of our business activities could be subject to challenge under one or more of these laws.

Federal false claims laws prohibit any person from knowingly presenting, or causing to be presented, a false claim for payment to the federal government or knowingly making, or causing to be made, a false statement to get a false claim paid. The federal healthcare program anti-kickback statute prohibits, among other things, knowingly and willfully offering, paying, soliciting or receiving remuneration to induce, or in return for, purchasing, leasing, ordering or arranging for the purchase, lease or order of any healthcare item or service reimbursable under Medicare, Medicaid or other federally financed healthcare programs. This statute has been interpreted to apply to arrangements between pharmaceutical manufacturers on the one hand and prescribers, purchasers and formula managers on the other. Although there are several statutory exemptions and regulatory safe harbors protecting certain common activities from prosecution, the exemptions and safe harbors are drawn narrowly, and practices that involve remuneration intended to induce prescribing, purchasing or recommending may be subject to scrutiny if they do not qualify for an exemption or safe harbor. Our practices may not in all cases meet all of the criteria for safe harbor protection from anti-kickback liability.

Over the past few years, several pharmaceutical and other healthcare companies have been prosecuted under these laws for a variety of alleged promotional and marketing activities, such as: allegedly providing free trips, free goods, sham consulting fees and grants and other monetary benefits to prescribers; reporting to pricing services inflated average wholesale prices that were then used by federal programs to set reimbursement rates; engaging in off-label promotion that caused claims to be submitted to Medicaid for non-covered, off-label uses; and submitting inflated best price information to the Medicaid Rebate Program to reduce liability for Medicaid rebates. Most states also have statutes or regulations similar to the federal anti-kickback law and false claims laws, which apply to items and services reimbursed under Medicaid and other state programs, or, in several states, apply regardless of the payor. Sanctions under these federal and state laws may include civil monetary penalties, exclusion of a manufacturer s products from reimbursement under government programs, criminal fines and imprisonment.

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Governments may impose price controls, which may adversely affect our future profitability.

We intend to seek approval to market our product candidates in both the United States and in foreign jurisdictions. If we obtain approval in one or more foreign jurisdictions, we will be subject to rules and regulations in those jurisdictions relating to our product candidates. In some foreign countries, particularly in the European Union, the pricing of prescription pharmaceuticals is subject to governmental control. In these countries, pricing negotiations with governmental authorities can take considerable time after the receipt of marketing approval for a product candidate. If reimbursement of our future products is unavailable or limited in scope or amount, or if pricing is set at unsatisfactory levels, we may be unable to achieve or sustain profitability.

Changes in government funding for the FDA and other government agencies could hinder their ability to hire and retain key leadership and other personnel, properly administer drug innovation, or prevent new products and services from being developed or commercialized by our life science tenants, which could negatively impact our business.

The ability of the FDA to review and approve new products can be affected by a variety of factors, including budget and funding levels, ability to hire and retain key personnel, and statutory, regulatory, and policy changes. Average review times at the agency have fluctuated in recent years as a result. In addition, government funding of other government agencies that fund research and development activities is subject to the political process, which is inherently fluid and unpredictable.

The ability of the FDA and other government agencies to properly administer their functions is highly dependent on the levels of government funding and the ability to fill key leadership appointments, among various factors. Currently, the FDA Commissioner position is vacant, pending the appointment of a new Commissioner by the new presidential administration. The confirmation process for a new commissioner may not occur efficiently. Delays in filling or replacing key positions could significantly impact the ability of the FDA and other agencies to fulfill their functions and could greatly impact healthcare and the biologics industry.

In December 2016, the 21st Century Cures Act was signed into law. This new legislation is designed to advance medical innovation and empower the FDA with the authority to directly hire positions related to drug and device development and review. In the past, the FDA was often unable to offer key leadership candidates (including scientists) competitive compensation packages as compared to those offered by private industry. The 21st Century Cures Act is designed to streamline the agency s hiring process and enable the FDA to compete for leadership talent by expanding the narrow ranges that are provided in the existing compensation structures.

In the first week of the new presidential administration, it issued executive orders to freeze government hiring of new employees with the exception of military, national security and public safety personnel. This hiring freeze could impede current or future operations at the FDA and other agencies. It is unknown at this time what the impact of the hiring freeze will have on the FDA and on programs such as the 21st Century Cures Act. Furthermore, future government proposals to reduce or eliminate budgetary deficits may include reduced allocations to the FDA and other related government agencies. These budgetary pressures may result in a reduced ability by the FDA to perform their respective roles; including the related impact to academic institutions and research laboratories whose funding is fully or partially dependent on both the level and timing of funding from government sources.

Disruptions at the FDA and other agencies may also slow the time necessary for new drugs, biologics and devices to be reviewed and/or approved by necessary government agencies and the healthcare and drug industries ability to deliver new products to the market in a timely manner, which would adversely affect our tenants operating results and business. Interruptions to the function of the FDA and other government agencies could adversely affect the demand

for office/laboratory space and significantly impact our operating results and our business.

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If product liability lawsuits are brought against us, we may incur substantial liabilities and may be required to limit commercialization of ADX-102 or our other product candidates.

We face an inherent risk of product liability as a result of the clinical testing of ADX-102 and our other product candidates and will face an even greater risk if we commercialize our product candidates. For example, we may be sued if ADX-102 or our other product candidates allegedly cause injury or are found to be otherwise unsuitable during product testing, manufacturing, marketing or sale. Any such product liability claims may include allegations of defects in manufacturing, defects in design, a failure to warn of dangers inherent in the product candidate, negligence, strict liability and a breach of warranties. Claims could also be asserted under state consumer protection acts.

If we cannot successfully defend ourselves against product liability claims, we may incur substantial liabilities or be required to limit commercialization of our product candidates. Even successful defense would require significant financial and management resources. Regardless of the merits or eventual outcome, liability claims may result in:

decreased demand for ADX-102 or our other product candidates;

injury to our reputation;

withdrawal of clinical trial participants;

costs to defend the related litigation;

a diversion of management s time and our resources;

substantial monetary awards to trial participants or patients;

product recalls, withdrawals or labeling, marketing or promotional restrictions;

loss of revenue;

the inability to commercialize ADX-102 or our other product candidates; and

a decline in our stock price.

We maintain product liability insurance with $3.0 million in coverage. Our inability to obtain and retain sufficient product liability insurance at an acceptable cost to protect against potential product liability claims could prevent or inhibit the commercialization of ADX-102 or our other product candidates. Although we will maintain such insurance, any claim that may be brought against us could result in a court judgment or settlement in an amount that is not

covered, in whole or in part, by our insurance or that is in excess of the limits of our insurance coverage. Our insurance policies will also have various exclusions, and we may be subject to a product liability claim for which we have no coverage. We may have to pay any amounts awarded by a court or negotiated in a settlement that exceed our coverage limitations or that are not covered by our insurance, and we may not have, or be able to obtain, sufficient capital to pay such amounts.

We and our development partners, third-party manufacturers and suppliers use biological materials and may use hazardous materials, and any claims relating to improper handling, storage, or disposal of these materials could be time consuming or costly.

We and our development partners, third-party manufacturers and suppliers may use hazardous materials, including chemicals and biological agents and compounds that could be dangerous to human health and safety or the environment. Our operations and the operations of our development partner, third-party manufacturers and suppliers also produce hazardous waste products. Federal, state, and local laws and regulations govern the use, generation, manufacture, storage, handling, and disposal of these materials and wastes. Compliance with applicable environmental laws and regulations may be expensive and current or future environmental laws and regulations may impair our product development efforts. In addition, we cannot entirely eliminate the risk of

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accidental injury or contamination from these materials or wastes. We do not carry specific biological or hazardous waste insurance coverage and our property, casualty, and general liability insurance policies specifically exclude coverage for damages and fines arising from biological or hazardous waste exposure or contamination. Accordingly, in the event of contamination or injury we could be held liable for damages or be penalized with fines in an amount exceeding our resources, and our clinical trials or regulatory approvals could be suspended.

We and any of our future development partners will be required to report to regulatory authorities if any of our approved products cause or contribute to adverse medical events, and any failure to do so would result in sanctions that would materially harm our business.

If we and any of our future development partners are successful in commercializing our products, the FDA and foreign regulatory authorities will require that we and any of our future development partners report certain information about adverse medical events if those products may have caused or contributed to those adverse events. The timing of our obligation to report would be triggered by the date we become aware of the adverse event as well as the nature of the event. We and any of our future development partners may fail to report adverse events we become aware of within the prescribed timeframe or to perform inadequate investigations of their causes. We and any of our future development partners may also fail to appreciate that we have become aware of a reportable adverse event, especially if it is not reported to us as an adverse event or if it is an adverse event that is unexpected or removed in time from the use of our products. If we and any of our future development partners fail to comply with our reporting obligations, the FDA or a foreign regulatory authority could take action including criminal prosecution, the imposition of civil monetary penalties, seizure of our products, or delay in approval or clearance of future products.

Our insurance policies are expensive and protect us only from some business risks, which leaves us exposed to significant uninsured liabilities.

We do not carry insurance for all categories of risk that our business may encounter. Some of the policies we currently maintain include general liability, product and clinical trial liability, workers compensation, and directors and officers insurance. We do not know, however, if we will be able to maintain existing insurance with adequate levels of coverage. Any significant, uninsured liability may require us to pay substantial amounts, which would adversely affect our working capital and results of operations.

If we engage in an acquisition, reorganization or business combination, we will incur a variety of risks that could adversely affect our business operations or our stockholders.

From time to time we have considered, and we will continue to consider in the future, strategic business initiatives intended to further the development of our business. These initiatives may include acquiring businesses, technologies or products or entering into a business combination with another company. If we do pursue such a strategy, we could, among other things:

- issue equity securities that would dilute our current stockholders percentage ownership;
- incur substantial debt that may place strains on our operations;

spend substantial operational, financial and management resources in integrating new businesses, technologies and products; and

assume substantial actual or contingent liabilities.

Our internal computer systems, or those of our development partners, third-party clinical research organizations or other contractors or consultants, may fail or suffer security breaches, which could result in a material disruption of our product development programs.

Despite the implementation of security measures, our internal computer systems and those of our current and any future CROs and other contractors, consultants and collaborators are vulnerable to damage from

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computer viruses, unauthorized access, natural disasters, terrorism, war and telecommunication and electrical failures. While we have not experienced any such material system failure, accident or security breach to date, if such an event were to occur and cause interruptions in our operations, it could result in a material disruption of our development programs and our business operations. For example, the loss of clinical trial data from completed or future clinical trials could result in delays in our regulatory approval efforts and significantly increase our costs to recover or reproduce the data. Likewise, we rely on third parties to manufacture our product candidates and conduct clinical trials, and similar events relating to their computer systems could also have a material adverse effect on our business. To the extent that any disruption or security breach were to result in a loss of, or damage to, our data or applications, or inappropriate disclosure of confidential or proprietary information, we could incur liability and the further development and commercialization of our product candidate could be delayed.

Business disruptions could seriously harm our future revenues and financial condition and increase our costs and expenses.

Our operations could be subject to earthquakes, power shortages, telecommunications failures, water shortages, floods, hurricanes, typhoons, fires, extreme weather conditions, medical epidemics and other natural or manmade disasters or business interruptions, for which we are predominantly self-insured. The occurrence of any of these business disruptions could seriously harm our operations and financial condition and increase our costs and expenses. We rely on third-party manufacturers to produce ADX-102 and our other product candidates. Our ability to obtain clinical supplies of ADX-102 or our other product candidates could be disrupted, if the operations of these suppliers are affected by a man-made or natural disaster or other business interruption.

Our employees may engage in misconduct or other improper activities including noncompliance with regulatory standards and requirements and insider trading.

We are exposed to the risk of employee fraud or other misconduct. Misconduct by employees could include intentional failures to comply with FDA regulations, provide accurate information to regulatory authorities, comply with manufacturing standards we have established, comply with federal and state health care fraud and abuse laws and regulations, report financial information or data accurately, or disclose unauthorized activities to us. In particular, sales, marketing, and business arrangements in the health care industry are subject to extensive laws and regulations intended to prevent fraud, kickbacks, self-dealing, and other abusive practices. These laws and regulations may restrict or prohibit a wide range of pricing, discounting, marketing and promotion, sales commission, customer incentive programs, and other business arrangements. Employee misconduct could also involve improper use of information obtained in the course of clinical trials, which could result in regulatory sanctions and serious harm to our reputation.

In addition, during the course of our operations our directors, executives, and employees may have access to material, nonpublic information regarding our business, our results of operations, or potential transactions we are considering. We may not be able to prevent a director, executive, or employee from trading in our common stock on the basis of, or while having access to, material, nonpublic information. If a director, executive, or employee was to be investigated or an action were to be brought against a director, executive, or employee for insider trading, it could have a negative impact on our reputation and our stock price. Such a claim, with or without merit, could also result in substantial expenditures of time and money, and divert attention of our management team from other tasks important to the success of our business.

Risks Relating to Our Intellectual Property

Our success depends on our ability to protect our intellectual property and our proprietary technologies.

Our commercial success depends in part on our ability to obtain and maintain patent protection and trade secret protection for our product candidates, proprietary technologies, and their uses as well as our ability to

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operate without infringing upon the proprietary rights of others. There can be no assurance that our patent applications or those of our licensors will result in additional patents being issued or that issued patents will afford sufficient protection against competitors with similar technology, nor can there be any assurance that the patents issued will not be infringed, designed around, or invalidated by third parties. Even issued patents may later be found unenforceable or may be modified or revoked in proceedings instituted by third parties before various patent offices or in courts. The degree of future protection for our proprietary rights is uncertain. Only limited protection may be available and may not adequately protect our rights or permit us to gain or keep any competitive advantage. This failure to properly protect the intellectual property rights relating to these product candidates could have a material adverse effect on our financial condition and results of operations.

Composition-of-matter patents on the biological or chemical active pharmaceutical ingredient are generally considered to be the strongest form of intellectual property protection for pharmaceutical products, as such patents provide protection without regard to any method of use. While we have issued composition-of-matter patents in the United States and other countries for ADX-102, we cannot be certain that the claims in our patent applications covering composition-of-matter of our other product candidates will be considered patentable by the United States Patent and Trademark Office (USPTO) and courts in the United States or by the patent offices and courts in foreign countries, nor can we be certain that the claims in our issued composition-of-matter patents will not be found invalid or unenforceable if challenged. Method-of-use patents protect the use of a product for the specified method. This type of patent does not prevent a competitor from making and marketing a product that is identical to our product for an indication that is outside the scope of the patented method. Moreover, even if competitors do not actively promote their product for our targeted indications, physicians may prescribe these products off-label. Although off-label prescriptions may infringe or contribute to the infringement of method-of-use patents, the practice is common and such infringement is difficult to prevent or prosecute. In addition, there are possibly methods that can be employed to trap aldehydes that we have not conceived of or attempted to patent, and other parties may discover and patent aldehyde trapping approaches and compositions that are similar to or different from ours.

The patent application process is subject to numerous risks and uncertainties, and there can be no assurance that we or any of our future development partners will be successful in protecting our product candidates by obtaining and defending patents. These risks and uncertainties include the following:

- the USPTO and various foreign governmental patent agencies require compliance with a number of procedural, documentary, fee payment and other provisions during the patent process. There are situations in which noncompliance can result in abandonment or lapse of a patent or patent application, resulting in partial or complete loss of patent rights in the relevant jurisdiction. In such an event, competitors might be able to enter the market earlier than would otherwise have been the case;

- patent applications may not result in any patents being issued;

- patents that may be issued or in-licensed may be challenged, invalidated, modified, revoked, circumvented, found to be unenforceable, or otherwise may not provide any competitive advantage;

- our competitors, many of whom have substantially greater resources than we do and many of whom have made significant investments in competing technologies, may seek or may have already obtained patents that

will limit, interfere with, or eliminate our ability to make, use, and sell our potential product candidates;

there may be significant pressure on the United States government and international governmental bodies to limit the scope of patent protection both inside and outside the United States for disease treatments that prove successful, as a matter of public policy regarding worldwide health concerns; and

countries other than the United States may have patent laws less favorable to patentees than those upheld by United States courts, allowing foreign competitors a better opportunity to create, develop, and market competing product candidates.

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In addition, we rely on the protection of our trade secrets and proprietary know-how. Although we have taken steps to protect our trade secrets and unpatented know-how, including entering into confidentiality agreements with third parties, and confidential information and inventions agreements with employees, consultants, and advisors, third parties may still obtain this information or may come upon this or similar information independently. If any of these events occurs or if we otherwise lose protection for our trade secrets or proprietary know-how, the value of this information may be greatly reduced.

Claims by third parties that we infringe their proprietary rights may result in liability for damages or prevent or delay our developmental and commercialization efforts.

The biotechnology industry has been characterized by frequent litigation regarding patent and other intellectual property rights. Because patent applications are maintained in secrecy until the application is published, we may be unaware of third party patents that may be infringed by commercialization of ADX-102 or our other product candidates. In addition, identification of third party patent rights that may be relevant to our technology is difficult because patent searching is imperfect due to differences in terminology among patents, incomplete databases and the difficulty in assessing the meaning of patent claims. Any claims of patent infringement asserted by third parties would be time consuming and could likely:

result in costly litigation;

divert the time and attention of our technical personnel and management;

cause development delays;

prevent us from commercializing ADX-102 or our other product candidates until the asserted patent expires or is held finally invalid or not infringed in a court of law;

require us to develop non-infringing technology; or

require us to enter into royalty or licensing agreements.

Although no third party has asserted a claim of patent infringement against us, others may hold proprietary rights that could prevent ADX-102 or our other product candidates from being marketed. Any patent-related legal action against us claiming damages and seeking to enjoin commercial activities relating to our product candidate or processes could subject us to potential liability for damages and require us to obtain a license to continue to manufacture or market ADX-102 or our other product candidates. We cannot predict whether we would prevail in any such actions or that any license required under any of these patents would be made available on commercially acceptable terms, if at all. In addition, we cannot be sure that we could redesign our product candidate or processes to avoid infringement, if necessary. Accordingly, an adverse determination in a judicial or administrative proceeding, or the failure to obtain necessary licenses, could prevent us from developing and commercializing ADX-102 or our other product candidates, which could harm our business, financial condition and operating results.

Any such claims against us could also be deemed to constitute an event of default under our loan and security agreement with Pacific Western. In the case of a continuing event of default under the loan, Pacific Western, the lender, could, among other remedies, elect to declare all amounts outstanding to be immediately due and payable and terminate all commitments to extend further credit. Although as of December 31, 2016, we had sufficient cash and cash equivalents to repay all obligations owed to Pacific Western if the debt was accelerated, in the event we do not or are not able to repay the obligations at the time a default occurred, Pacific Western may elect to commence and prosecute bankruptcy and/or other insolvency proceedings, or proceed against the collateral granted to Pacific Western under the loan, which includes our intellectual property.

Our issued patents could be found invalid or unenforceable if challenged in court.

If we or any of our future development partners were to initiate legal proceedings against a third party to enforce a patent covering one of our product candidates, or one of our future product candidates, the defendant

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could counterclaim that our patent is invalid and/or unenforceable. In patent litigation in the United States, defendant counterclaims alleging invalidity and/or unenforceability are commonplace. Grounds for a validity challenge could be an alleged failure to meet any of several statutory requirements, including lack of novelty, obviousness or non-enablement. Grounds for an unenforceability assertion could be an allegation that someone connected with prosecution of the patent withheld relevant information from the USPTO, or made a misleading statement during prosecution. Third parties may also raise similar claims before the USPTO, even outside the context of litigation. The outcome following legal assertions of invalidity and unenforceability is unpredictable. With respect to the validity question, for example, we cannot be certain that there is no invalidating prior art, of which we and the patent examiner were unaware during prosecution. If a defendant were to prevail on a legal assertion of invalidity and/or unenforceability, we would lose at least part, and perhaps all, of the patent protection on such product candidate. Such a loss of patent protection would have a material adverse impact on our business.

We may fail to comply with any of our obligations under existing or future agreements pursuant to which we license rights or technology, which could result in the loss of rights or technology that are material to our business.

We are a party to technology licenses and we may enter into additional licenses in the future. Such licenses do, and may in the future, impose commercial, contingent payment, royalty, insurance, indemnification, and other obligations on us. If we fail to comply with these obligations, the licensor may have the right to terminate the license, in which event we could lose valuable rights under our collaboration agreements and our ability to develop product candidates could be impaired. Additionally, should such a license agreement be terminated for any reason, there may be a limited number of licensors who would be suitable replacements and it may take a significant amount of time to transition to a replacement licensor.

We may be subject to claims that we have wrongfully hired an employee from a competitor or that we or our employees have wrongfully used or disclosed alleged confidential information or trade secrets of their former employers.

As is common in the biotechnology and pharmaceutical industry, we engage the services of consultants to assist us in the development of our product candidates. Many of these consultants were previously employed at, or may have previously provided or may be currently providing consulting services to, other biotechnology or pharmaceutical companies including our competitors or potential competitors. We may become subject to claims that our company or a consultant inadvertently or otherwise used or disclosed trade secrets or other information proprietary to their former employers or their former or current clients. Litigation may be necessary to defend against these claims. Even if we are successful in defending against these claims, litigation could result in substantial costs and be a distraction to our management team.

If we do not obtain protection under the Hatch-Waxman Amendments by extending the patent terms and obtaining data exclusivity for our product candidate, our business may be materially harmed.

Depending upon the timing, duration and specifics of FDA marketing approval of ADX-102 or other product candidates, one or more of our United States patents may be eligible for limited patent term restoration under the Drug Price Competition and Patent Term Restoration Act of 1984, referred to as the Hatch-Waxman Amendments. The Hatch-Waxman Amendments permit a patent restoration term of up to five years as compensation for patent term lost during product development and the FDA regulatory review process. However, we may not be granted an extension because of, for example, failing to apply within applicable deadlines, failing to apply prior to expiration of relevant patents or otherwise failing to satisfy applicable requirements. Moreover, the applicable time period or the scope of patent protection afforded could be less than we request. If we are unable to obtain patent term extension or restoration or the term of any such extension is less than we request, our competitors may obtain approval of competing products

following our patent expiration, and our revenue could be reduced, possibly materially.

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If our trademarks and trade names are not adequately protected, then we may not be able to build name recognition in our markets of interest and our business may be adversely affected.

If our trademarks and trade names are not adequately protected, then we may not be able to build name recognition in our markets of interest and our business may be adversely affected. Our registered or unregistered trademarks or trade names may be challenged, infringed, circumvented or declared generic or determined to be infringing on other marks. We may not be able to protect our rights to these trademarks and trade names, which we need to build name recognition among potential partners or customers in our markets of interest. At times, competitors may adopt trade names or trademarks similar to ours, thereby impeding our ability to build brand identity and possibly leading to market confusion. In addition, there could be potential trade name or trademark infringement claims brought by owners of other registered trademarks or trademarks that incorporate variations of our registered or unregistered trademarks or trade names. As of March 2014, we adopted a new brand, Aldeyra Therapeutics. Our marks ALDEYRA THERAPEUTICS and our logo are registered with the USPTO. Over the long term, if we are unable to establish name recognition based on our trademarks and trade names, then we may not be able to compete effectively and our business may be adversely affected. Our efforts to enforce or protect our proprietary rights related to trademarks, trade secrets, domain names, copyrights or other intellectual property may be ineffective and could result in substantial costs and diversion of resources and could adversely impact our financial condition or results of operations.

Changes in United States patent law could diminish the value of patents in general, thereby impairing our ability to protect our product candidates.

As is the case with other biopharmaceutical companies, our success is heavily dependent on intellectual property, particularly patents. Obtaining and enforcing patents in the biopharmaceutical industry involve technological and legal complexity. Therefore, obtaining and enforcing biopharmaceutical patents is costly, time consuming, and inherently uncertain. In addition, Congress may pass patent reform legislation. The Supreme Court has ruled on several patent cases in recent years, either narrowing the scope of patent protection available in certain circumstances or weakening the rights of patent owners in certain situations. In addition to increasing uncertainty with regard to our ability to obtain patents in the future, this combination of events has created uncertainty with respect to the value of patents, once obtained. Depending on decisions by the United States Congress, the federal courts, and the USPTO, the laws and regulations governing patents could change in unpredictable ways that would weaken our ability to obtain new patents or to enforce our existing patents and patents we might obtain in the future.

We may not be able to protect our intellectual property rights throughout the world.

While we have issued composition-of-matter patents covering ADX-102 in the United States and other countries, filing, prosecuting and defending patents on ADX-102 and our other product candidates in all countries throughout the world would be prohibitively expensive, and our intellectual property rights in some countries outside the United States can be less extensive than those in the United States. In addition, the laws of some foreign countries do not protect intellectual property rights to the same extent as federal and state laws in the United States. Consequently, we may not be able to prevent third parties from practicing our inventions in all countries outside the United States, or from selling or importing products made using our inventions in and into the United States or other jurisdictions. Competitors may use our technologies in jurisdictions where we have not obtained patent protection to develop their own products and further, may export otherwise infringing products to territories where we have patent protection, but enforcement is not as strong as that in the United States. These products may compete with our product candidates and our patents or other intellectual property rights may not be effective or sufficient to prevent them from competing.

Many companies have encountered significant problems in protecting and defending intellectual property rights in foreign jurisdictions. The legal systems of certain countries, particularly certain developing countries, do not favor the

enforcement of patents and other intellectual property protection, particularly those relating to biopharmaceuticals, which could make it difficult for us to stop the infringement of our patents or marketing of

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competing products in violation of our proprietary rights generally. Proceedings to enforce our patent rights in foreign jurisdictions could result in substantial costs and divert our efforts and attention from other aspects of our business, could put our patents at risk of being invalidated or interpreted narrowly and our patent applications at risk of not issuing and could provoke third parties to assert claims against us. We may not prevail in any lawsuits that we initiate and the damages or other remedies awarded, if any, may not be commercially meaningful. Accordingly, our efforts to enforce our intellectual property rights around the world may be inadequate to obtain a significant commercial advantage from the intellectual property that we develop or license.

Risks Related to Our Financial Position and Need for Capital

If we fail to obtain the capital necessary to fund our operations, we will be unable to successfully develop and commercialize ADX-102 and our other product candidates.

We will require substantial future capital in order to complete the remaining clinical development for ADX-102 and our other product candidates and to potentially commercialize these product candidates. We expect our spending levels to increase in connection with our clinical trials of ADX-102 and our other product candidates, as well as other corporate activities. The amount and timing of any expenditure needed to implement our development and commercialization programs will depend on numerous factors, including:

- the type, number, scope, progress, expansion costs, results of and timing of our planned clinical trials of ADX-102 or any our other product candidates which we are pursuing or may choose to pursue in the future;
- the need for, and the progress, costs and results of, any additional clinical trials of ADX-102 and our other product candidates we may initiate based on the results of our planned clinical trials or discussions with the FDA, including any additional trials the FDA or other regulatory agencies may require evaluating the safety of ADX-102 and our other product candidates;
- the costs of obtaining, maintaining and enforcing our patents and other intellectual property rights;
- the costs and timing of obtaining or maintaining manufacturing for ADX-102 and our other product candidates, including commercial manufacturing if any product candidate is approved;
- the costs and timing of establishing sales and marketing capabilities and enhanced internal controls over financial reporting;
- the terms and timing of establishing collaborations, license agreements and other partnerships on terms favorable to us;
- costs associated with any other product candidates that we may develop, in-license or acquire;

the effect of competing technological and market developments;

our ability to establish and maintain partnering arrangements for development; and

the costs associated with being a public company.

Some of these factors are outside of our control. We do not expect our existing capital resources to be sufficient to enable us to fund the completion of our clinical trials and remaining development program through commercial introduction. We expect that we will need to raise additional funds in the near future.

We have not sold any products, and we do not expect to sell or derive revenue from any product sales for the foreseeable future. We may seek additional funding through collaboration agreements and public or private financings, including debt financings. Uncertain economic conditions as to the general direction of the macroeconomic environment, are beyond our control and may make any necessary debt or equity financing more difficult, more costly, and more dilutive. Additional funding may not be available to us on acceptable terms or at all. In addition, the terms of any financing may adversely affect the holdings or the rights of our stockholders or

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be excessively dilutive. In addition, the issuance of additional shares by us, or the possibility of such issuance, may cause the market price of our shares to decline.

If we are unable to obtain funding on a timely basis, we will be unable to complete the planned clinical trials for ADX-102 and our other product candidates and we may be required to significantly curtail some or all of our activities. We also could be required to seek funds through arrangements with collaborative partners or otherwise that may require us to relinquish rights to our product candidates or some of our technologies or otherwise agree to terms unfavorable to us.

The terms of our secured debt facility require us to meet certain operating and financial covenants and place restrictions on our operating and financial flexibility. If we raise additional capital through debt financing, the terms of any new debt could further restrict our ability to operate our business.

We have a $5.0 million Credit Facility with Pacific Western that is secured by a lien covering all of our assets as of December 31, 2016. As of December 31, 2016 and December 31, 2015, the outstanding principal balance under the Credit Facility was approximately $1.4 million. The loan agreement contains customary affirmative and negative covenants and events of default. Affirmative covenants include, among others, covenants requiring us to maintain our legal existence and governmental approvals, deliver certain financial reports and maintain insurance coverage. Negative covenants include, among others, restrictions on transferring any part of our business or property, changing our business, including changing the composition of our executive team or board of directors, incurring additional indebtedness, engaging in mergers or acquisitions, paying dividends or making other distributions, making investments and creating other liens on our assets and other financial covenants, in each case subject to customary exceptions. If we default under the terms of the loan agreement, including failure to satisfy our operating covenants, the lender may accelerate all of our repayment obligations and take control of our pledged assets, potentially requiring us to renegotiate our agreement on terms less favorable to us or to immediately cease operations. Further, if we are liquidated, the lender s right to repayment would be senior to the rights of the holders of our common stock. The lender could declare a default upon the occurrence of any event that they interpret as a material adverse effect as defined under the loan agreement. Any declaration by the lender of an event of default could significantly harm our business and prospects and could cause the price of our common stock to decline. If we raise any additional debt financing, the terms of such additional debt could further restrict our operating and financial flexibility.

Our ability to use net operating loss carryforwards and tax credit carryforwards to offset future taxable income may be limited as a result of transactions involving our common stock.

In general, under Section 382 of the Internal Revenue Code of 1986, as amended (Code), a corporation that undergoes an ownership change is subject to limitations on its ability to utilize its pre-change net operating losses (NOLs) and certain other tax assets (tax attributes) to offset future taxable income. In general, an ownership change occurs if the aggregate stock ownership of certain stockholders increases by more than 50 percentage points over such stockholders lowest percentage ownership during the testing period (generally three years). Transactions involving our common stock, even those outside our control, such as purchases or sales by investors, within the testing period could result in an ownership change. A limitation on our ability to utilize some or all of our NOLs or credits could have a material adverse effect on our results of operations and cash flows. Prior to 2016, we underwent two ownership changes and it is possible that additional ownership changes have occurred since. However, our management believes that we have sufficient Built-In-Gain to offset the Section 382 of the Code limitation generated by such ownership changes. Any future ownership changes, including those resulting from our recent or future financing activities, may cause our existing tax attributes to have additional limitations.

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Risks Related to Our Common Stock

An active trading market for our common stock may not develop or be sustained and investors may not be able to resell their shares at or above the price at which they purchased them.

We have a limited history as a public company. An active trading market for our shares may never develop or be sustained. In the absence of an active trading market for our common stock, investors may not be able to sell their common stock at or above the price they paid or at the time that they would like to sell. In addition, an inactive market may impair our ability to raise capital by selling shares and may impair our ability to acquire other companies or technologies by using our shares as consideration, which, in turn, could harm our business.

The trading price of the shares of our common stock has been and is likely to continue to be highly volatile, and purchasers of our common stock could incur substantial losses.

Our stock price has been and will likely continue to be volatile for the foreseeable future. The stock market in general and the market for biotechnology companies in particular have experienced extreme volatility that has often been unrelated to the operating performance of particular companies. As a result of this volatility, investors may not be able to sell their common stock at or above the price they paid. The market price for our common stock may be influenced by many factors, including:

- our ability to enroll patients in our planned clinical trials;
- results of the clinical trials, and the results of trials of our competitors or those of other companies in our market sector;
- regulatory developments in the United States and foreign countries;
- variations in our financial results or those of companies that are perceived to be similar to us;
- changes in the structure of healthcare payment systems, especially in light of current reforms to the United States healthcare system;
- announcements by us or our competitors of significant acquisitions, strategic partnerships, joint ventures or capital commitments;
- market conditions in the pharmaceutical and biotechnology sectors and issuance of securities analysts reports or recommendations;
- sales of our stock by insiders and 5% stockholders;

trading volume of our common stock;

general economic, industry and market conditions other events or factors, many of which are beyond our control;

additions or departures of key personnel; and

intellectual property, product liability or other litigation against us.

In addition, in the past, stockholders have initiated class action lawsuits against biotechnology and pharmaceutical companies following periods of volatility in the market prices of these companies stock. Such litigation, if instituted against us, could cause us to incur substantial costs and divert management s attention and resources, which could have a material adverse effect on our business, financial condition and results of operations.

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Our quarterly operating results may fluctuate significantly.

We expect our operating results to be subject to quarterly fluctuations. Our net loss and other operating results will be affected by numerous factors, including:

- variations in the level of expenses related to our clinical trial and development programs;
- addition or termination of clinical trials;
- any intellectual property infringement lawsuit in which we may become involved;
- regulatory developments affecting ADX-102 and our other product candidates;
- our execution of any collaborative, licensing or similar arrangements, and the timing of payments we may make or receive under these arrangements;
- nature and terms of stock-based compensation grants; and
- derivative instruments recorded at fair value.

If our quarterly operating results fall below the expectations of investors or securities analysts, the price of our common stock could decline substantially. Furthermore, any quarterly fluctuations in our operating results may, in turn, cause the price of our stock to fluctuate substantially. We believe that quarterly comparisons of our financial results are not necessarily meaningful and should not be relied upon as an indication of our future performance.

Our failure to meet the continued listing requirements of The NASDAQ Capital Market could result in a delisting of our common stock.

If we fail to satisfy the continued listing requirements of The NASDAQ Capital Market, such as the corporate governance requirements or the minimum closing bid price requirement, NASDAQ may take steps to de-list our common stock. Such a delisting would likely have a negative effect on the price of our common stock and would impair your ability to sell or purchase our common stock when you wish to do so. In the event of a delisting, we would expect to take actions to restore our compliance with NASDAQ s listing requirements, but we can provide no assurance that any such action taken by us would allow our common stock to become listed again, stabilize the market price or improve the liquidity of our common stock, prevent our common stock from dropping below the NASDAQ minimum bid price requirement or prevent future non-compliance with NASDAQ s listing requirements.

If our shares become subject to the penny stock rules, it would become more difficult to trade our shares.

The SEC has adopted rules that regulate broker-dealer practices in connection with transactions in penny stocks. Penny stocks are generally equity securities with a price of less than $5.00, other than securities registered on certain

national securities exchanges or authorized for quotation on certain automated quotation systems, provided that current price and volume information with respect to transactions in such securities is provided by the exchange or system. If we do not retain a listing on The NASDAQ Capital Market and if the price of our common stock is less than $5.00, our common stock will be deemed a penny stock. The penny stock rules require a broker-dealer, before a transaction in a penny stock not otherwise exempt from those rules, to deliver a standardized risk disclosure document containing specified information. In addition, the penny stock rules require that before effecting any transaction in a penny stock not otherwise exempt from those rules, a broker-dealer must make a special written determination that the penny stock is a suitable investment for the purchaser and receive (i) the purchaser s written acknowledgment of the receipt of a risk disclosure statement; (ii) a written agreement to transactions involving penny stocks; and (iii) a signed and dated copy of a written suitability statement. These disclosure requirements may have the effect of reducing the trading activity in the secondary market for our common stock, and therefore stockholders may have difficulty selling their shares.

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We may allocate our cash and cash equivalents in ways that you and other stockholders may not approve.

Our management has broad discretion in the application of our cash and cash equivalents. Because of the number and variability of factors that will determine our use of our cash and cash equivalents, their ultimate use may vary substantially from their currently intended use. Our management might not apply our cash and cash equivalents in ways that ultimately increase the value of your investment. We expect to use of our cash and cash equivalents to fund our planned clinical trials of ADX-102 and our other product candidates, development of other molecules that may relate to our aldehyde trapping platform, and the remainder for working capital and other general corporate purposes. The failure by our management to apply these funds effectively could harm our business. Pending their use, we may invest our cash and cash equivalents in short-term, investment-grade, interest-bearing securities. These investments may not yield a favorable return to our stockholders. If we do not invest or apply our cash and cash equivalents in ways that enhance stockholder value, we may fail to achieve expected financial results, which could cause our stock price to decline.

Because a small number of our existing stockholders own a majority of our voting stock, your ability to influence corporate matters will be limited.

As of December 31, 2016, our executive officers, directors and greater than 5% stockholders, in the aggregate, own approximately 67.0% of our outstanding common stock. As a result, such persons, acting together, will have the ability to control our management and business affairs and substantially all matters submitted to our stockholders for approval, including the election and removal of directors and approval of any significant transaction. This concentration of ownership may have the effect of delaying, deferring or preventing a change in control, impeding a merger, consolidation, takeover or other business combination involving us, or discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of our business, even if such a transaction would benefit other stockholders.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of us, which may be beneficial to our stockholders, more difficult and may prevent attempts by our stockholders to replace or remove our current management.

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws may delay or prevent an acquisition of us or a change in our management. These provisions include:

- authorizing the issuance of blank check preferred stock, the terms of which may be established and shares of which may be issued without stockholder approval;
- limiting the removal of directors by the stockholders;
- creating a staggered board of directors;
- prohibiting stockholder action by written consent, thereby requiring all stockholder actions to be taken at a meeting of our stockholders;

eliminating the ability of stockholders to call a special meeting of stockholders;

permitting our board of directors to accelerate the vesting of outstanding option grants upon certain transactions that result in a change of control; and

establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted upon at stockholder meetings.

In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which limits the ability of stockholders owning in excess of 15% of our outstanding voting stock to merge or combine with us. Although we believe these provisions collectively provide for an opportunity to obtain greater value for stockholders by requiring potential acquirors to negotiate with our board of directors, they would apply even if an offer rejected by our board were considered beneficial by some

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stockholders. In addition, these provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management.

We do not intend to pay dividends on our common stock and, consequently, your ability to achieve a return on your investment will depend on appreciation in the price of our common stock.

We have never declared or paid any cash dividend on our common stock and do not currently intend to do so for the foreseeable future. We currently anticipate that we will retain future earnings for the development, operation and expansion of our business and do not anticipate declaring or paying any cash dividends for the foreseeable future. In addition, our loan and security agreement with Pacific Western currently prohibits us from paying dividends on our equity securities, and any future debt financing arrangement may contain terms prohibiting or limiting the amount of dividends that may be declared or paid on our common stock. Any return to stockholders will therefore be limited to the appreciation of their stock. Therefore, the success of an investment in shares of our common stock will depend upon any future appreciation in their value. There is no guarantee that shares of our common stock will appreciate in value or even maintain the price at which our stockholders have purchased their shares.

A substantial number of shares of our common stock could be sold into the public market in the near future, which could depress our stock price.

Sales of substantial amounts of our common stock in the public market could reduce the prevailing market prices for our common stock. Substantially all of our outstanding common stock are eligible for sale as are common stock issuable under vested and exercisable stock options. If our existing stockholders sell a large number of shares of our common stock, or the public market perceives that existing stockholders might sell shares of common stock, the market price of our common stock could decline significantly. These sales might also make it more difficult for us to sell equity securities at a time and price that we deem appropriate.

We are an emerging growth company, and we cannot be certain if the reduced reporting requirements applicable to emerging growth companies will make our common stock less attractive to investors.

We are an emerging growth company, as defined in the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. For as long as we continue to be an emerging growth company, we may take advantage of exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies, including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding nonbinding advisory votes on executive compensation and stockholder approval of any golden parachute payments not previously approved. We could be an emerging growth company until December 31, 2019, although circumstances could cause us to lose that status earlier, including if we become a large accelerated filer, if we have total annual gross revenue of $1.0 billion or more during any fiscal year before that time, in which cases we would no longer be an emerging growth company as of the following December 31 or, if we issue more than $1.0 billion in non-convertible debt during any three year period before that time, we would cease to be an emerging growth company immediately. Even after we no longer qualify as an emerging growth company, we may still qualify as a smaller reporting company which would allow us to take advantage of many of the same exemptions from disclosure requirements including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act and reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements. We cannot predict if investors will find our common stock less attractive because we may rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price

may be more volatile.

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We are incurring significant increased costs and demands upon management as a result of operating as a public company.

As a public company, we are incurring significant legal, accounting and other expenses that we did not incur as a private company. We are subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act, which require, among other things, that we file with the Securities and Exchange Commission, or the SEC, annual, quarterly and current reports with respect to our business and financial condition. In addition, the Sarbanes-Oxley Act, as well as rules subsequently adopted by the SEC, and The NASDAQ Capital Market to implement provisions of the Sarbanes-Oxley Act, impose significant requirements on public companies, including requiring establishment and maintenance of effective disclosure and financial controls and changes in corporate governance practices. Further, in 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Dodd-Frank Act, was enacted. There are significant corporate governance and executive compensation related provisions in the Dodd-Frank Act that require the SEC to adopt additional rules and regulations in these areas such as say on pay and proxy access. Recent legislation permits smaller emerging growth companies to implement many of these requirements over a longer period and up to five years from our Initial Public Offering. We intend to continue to take advantage of this new legislation but cannot guarantee that we will not be required to implement these requirements sooner than budgeted or planned and thereby incur unexpected expenses. Stockholder activism, the current political environment and the current high level of government intervention and regulatory reform may lead to substantial new regulations and disclosure obligations, which may lead to additional compliance costs and impact the manner in which we operate our business in ways we cannot currently anticipate.

We expect the rules and regulations applicable to public companies to continue to substantially increase our legal and financial compliance costs and to make some activities more time-consuming and costly. If these requirements divert the attention of our management and personnel from other business concerns, they could have a material adverse effect on our business, financial condition and results of operations. The increased costs will decrease our net income or increase our net loss, and may require us to reduce costs in other areas of our business or increase the prices of our products or services. For example, these rules and regulations make it more difficult and more expensive for us to obtain director and officer liability insurance and we may be required to incur substantial costs to maintain the same or similar coverage. We cannot predict or estimate the amount or timing of additional costs we may incur to respond to these requirements. The impact of these requirements could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors, our board committees or as executive officers.

If we fail to maintain proper and effective internal control over financial reporting in the future, our ability to produce accurate and timely financial statements could be impaired, which could harm our operating results, investors views of us and, as a result, the value of our common stock.

Pursuant to Section 404 of the Sarbanes-Oxley Act, our management is required to report upon the effectiveness of our internal control over financial reporting. When and if we are a large accelerated filer or an accelerated filer and are no longer an emerging growth company, each as defined in the Exchange Act, our independent registered public accounting firm will be required to attest to the effectiveness of our internal control over financial reporting. However, for so long as we remain an emerging growth company, we intend to take advantage of certain exemptions from various reporting requirements that are applicable to public companies that are not emerging growth companies, including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404. Once we are no longer an emerging growth company or, if prior to such date, we opt to no longer take advantage of the applicable exemption, we will be required to include an opinion from our independent registered public accounting firm on the effectiveness of our internal controls over financial reporting. The rules governing the standards that must be met for management to assess our internal control over financial reporting are complex and require significant documentation, testing, and possible remediation. To comply with the requirements of being a reporting company

under the Exchange Act, we need to upgrade our systems including information technology; implement additional financial and management controls, reporting systems, and procedures; and hire additional accounting and finance staff.

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Historically, we have not had sufficient accounting and supervisory personnel with the appropriate level of technical accounting experience and training necessary or adequate formally documented accounting policies and procedures to support, effective internal controls. As we grow, we will hire additional personnel and engage in external temporary resources and may implement, document and modify policies and procedures to maintain effective internal controls. However, we may identify deficiencies and weaknesses or fail to remediate previously identified deficiencies in our internal controls. If material weaknesses or deficiencies in our internal controls exist and go undetected or unremediated, our financial statements could contain material misstatements that, when discovered in the future, could cause us to fail to meet our future reporting obligations and cause the price of our common stock to decline.

If securities or industry analysts do not publish research or reports or publish unfavorable research or reports about our business, our stock price and trading volume could decline.

The trading market for our common stock will depend in part on the research and reports that securities or industry analysts publish about us, our business, our market or our competitors. We currently have limited research coverage by securities and industry analysts. If other securities or industry analysts do not commence coverage of our company, the trading price for our stock could be negatively impacted. If one or more of the analysts who covers us downgrades our stock, our stock price would likely decline. If one or more of these analysts ceases to cover us or fails to regularly publish reports on us, interest in our stock could decrease, which could cause our stock price or trading volume to decline.

We could be subject to securities class action litigation.

In the past, securities class action litigation has often been brought against a company following a decline in the market price of its securities. This risk is especially relevant for us because pharmaceutical companies have experienced significant stock price volatility in recent years. If we face such litigation, it could result in substantial costs and a diversion of management s attention and resources, which could harm our business.

Our business could be negatively affected as a result of the actions of activist stockholders.

Proxy contests have been waged against many companies in the biopharmaceutical industry, over the last few years. We may be particularly vulnerable to these actions due to the highly concentrated ownership of our common stock. If faced with a proxy contest or other type of shareholder activism, we may not be able to respond successfully to the contest or dispute, which would be disruptive to our business. Even if we are successful, our business could be adversely affected by a proxy contest or shareholder dispute involving us or our partners because:

- responding to proxy contests and other actions by activist stockholders can be costly and time-consuming, disrupting operations and diverting the attention of management and employees;
- perceived uncertainties as to future direction may result in the loss of potential acquisitions, collaborations or in-licensing opportunities, and may make it more difficult to attract and retain qualified personnel and business partners; and
- if individuals are elected to a board of directors with a specific agenda, it may adversely affect our ability to effectively and timely implement our strategic plan and create additional value for our stockholders.

These actions could cause our stock price to experience periods of volatility.

ITEM 1B. ***UNRESOLVED STAFF COMMENTS***

Not applicable.

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ITEM 2. ***PROPERTIES***

Our offices are located in Lexington, Massachusetts. As of December 31, 2016, we had leased approximately 6,888 square feet of office space pursuant to leases that expire in 2017. Management believes that this office space is suitable and adequate to meet our anticipated near-term needs. We anticipate that following the expiration of the leases, additional or alternative space will be available at commercially reasonable terms.

ITEM 3. ***LEGAL PROCEEDINGS***

From time to time, we may become subject to legal proceedings, claims and litigation arising in the ordinary course of business. We currently are not a party to any threatened or pending material litigation and do not have contingency reserves established for any litigation liabilities. However, third parties might allege that we are infringing their patent rights or that we are otherwise violating their intellectual property rights, including trade names and trademarks. Such third parties may resort to litigation. We accrue contingent liabilities when it is probable that future expenditures will be made and such expenditures can be reasonably estimated.

ITEM 4. ***MINE SAFETY DISCLOSURES***

Not applicable.

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PART II

ITEM 5. *MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES*

Market Price of Our Common Stock

Our common stock has been trading on The NASDAQ Capital Market (NASDAQ) under the symbol ALDX since our IPO on May 1, 2014. Prior to that time, there was no established public trading market for our common stock. The following table sets forth, for the periods indicated, the range of high and low per share sale prices of our common stock as reported by NASDAQ.

Year Ended December 31, 2016	High	Low
First quarter	$ 6.76	$ 3.52
Second quarter	$ 6.50	$ 4.24
Third quarter	$ 7.82	$ 5.37
Fourth quarter	$ 7.51	$ 4.65
Year Ended December 31, 2015	**High**	**Low**
First quarter	$ 12.30	$ 6.90
Second quarter	$ 11.79	$ 6.64
Third quarter	$ 10.90	$ 5.35
Fourth quarter	$ 7.70	$ 4.84

Holders of Record

As of December 31, 2016, there were 16 holders of record of our common stock. The actual number of stockholders is greater than this number of record holders and includes stockholders who are beneficial owners but whose shares are held in street name by brokers and other nominees. This number of holders of record also does not include stockholders whose shares may be held in trust by other entities.

Dividends

We have not declared or paid any cash dividends on our common stock since our inception. We do not plan to pay dividends in the foreseeable future. Under our credit facility, we have agreed not to pay any dividends so long as it has any outstanding obligations thereunder. We currently intend to retain all available funds and any future earnings, if any, for use in the operation of our business. Any future determination to declare cash dividends will be made at the discretion of our board of directors, subject to applicable laws, and will depend on our financial condition, results of operations, capital requirements, general business conditions and other factors that our board of directors may deem relevant, and subject to the restrictions contained in our current or future financing instruments. Consequently, stockholders will need to sell shares of our common stock to realize a return on their investment, if any.

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Securities Authorized for Issuance under Equity Incentive Plans

The following table provides information as of December 31, 2016, with respect to shares of our common stock that may be issued, subject to certain vesting requirements, under our existing equity compensation plans, including our 2013 Equity Incentive Plan (2013 Plan), 2010 Employee, Director and Consultant Equity Incentive Plan (2010 Plan), 2004 Employee, Director and Consultant Stock Plan (2004 Plan) and our 2016 Employee Stock Purchase Plan (2016 ESPP).

Plan Category	A Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants, and Rights	B Weighted-Average Exercise Price of Outstanding Options, Warrants, and Rights	C Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (A))
Equity compensation plans approved by security holders	1,525,682(1)	$ 6.75(2)	966,568(3)
Equity compensation plans not approved by security holders			
Total	1,525,682	$ 6.75(2)	966,568(3)

(1) Of these shares, 27,096 were underlying then outstanding restricted stock unit awards and 984,786 were subject to options then outstanding under the 2013 Plan, 489,846 were subject to options then outstanding under the 2010 Plan and 23,954 were subject to options then outstanding under the 2004 Plan.

(2) Does not take into account restricted stock units, which have no exercise price.

(3) Represents 869,068 shares of common stock available for issuance under our 2013 Plan and 97,500 shares of common stock available for issuance under our 2016 ESPP. No shares are available for future issuance under the 2010 Plan or 2004 Plan. Our 2013 Plan provides for annual increases in the number of shares available for issuance thereunder on the first day of each fiscal year equal to the least of: (1) 1,000,000 shares of our common stock; (2) 7% of the shares of common stock outstanding at that time; and (3) such other amount as our board of directors may determine. Our 2016 ESPP provides for annual increases in the number of shares available for issuance thereunder on the first day of each fiscal year equal to the lesser of: (1) 1% of the shares of common stock outstanding at that time; and (2) such other amount as our board of directors may determine. On January 1, 2017, an additional 880,343 shares became available for future issuance under the 2013 Plan and an additional 125,763 shares became available for future issuance under the 2016 ESPP. The additional shares from the annual

increase on January 1, 2017 are not included in the table above.

ITEM 6. ***SELECTED FINANCIAL DATA***

As a smaller reporting company, we are not required to provide this information.

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ITEM 7. *MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS*

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes appearing at the end of this annual report on Form 10-K. Some of the information contained in this discussion and analysis, including information with respect to our plans and strategy for our business, includes forward-looking statements that involve risks, uncertainties and assumptions. You should read the Risk Factors and Special Note Regarding Forward-Looking Statements sections of this annual report on Form 10-K for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

Overview

We are a biotechnology company focused primarily on the development of new products for inflammation, inborn errors of metabolism and other diseases that are thought to be related to endogenously generated toxic and pro-inflammatory chemical species known as aldehydes. We are developing ADX-102 (formerly known as NS2), as well as other novel product candidates, including ADX-103 and ADX-104, that are designed specifically to sequester aldehydes for the treatment of:

- Noninfectious Anterior Uveitis, a rare but severe inflammatory eye disease that can lead to blindness;
- Allergic Conjunctivitis, a common disease that affects more than 20% of the population worldwide, and related rare allergic ocular diseases that are characterized by inflammation of the conjunctiva (a membrane covering part of the front of the eye), resulting in ocular itching, excessive tear production, swelling and redness;
- Dry Eye Syndrome, a common inflammatory disease characterized by insufficient moisture and lubrication associated with the anterior surface of the eye, leading to ocular irritation, burning, stinging, and, in severe cases, loss of vision;
- Sjögren-Larsson Syndrome (SLS), a rare inborn error of metabolism caused by mutations in an enzyme that metabolizes fatty aldehydes, resulting in severe skin and neurological disorders; and
- Succinic Semi-Aldehyde Dehydrogenase Deficiency (SSADH), a rare inborn error of metabolism caused by genetic mutations in an aldehyde-metabolizing enzyme, leading to severe neurological disease.

In 2015, we began clinical testing of ADX-102 in diseases where we believe aldehyde trapping may improve symptoms and slow or prevent disease progression. In February 2016, we announced that the results of a randomized, parallel-group, double-masked, vehicle-controlled Phase 2a clinical trial of ADX-102 ophthalmic solution in patients with allergic conjunctivitis demonstrated statistically and clinically significant activity of ADX-102 over vehicle in reducing ocular itching and tearing. In May 2016, we announced that the results of our randomized, parallel-group, investigator-masked, active-controlled Phase 2 clinical trial of ADX-102 ophthalmic solution in patients with noninfectious anterior uveitis demonstrated that ADX-102 reduced inflammatory cell count in the anterior chamber of

the eye to a degree similar to that of standard-of-care corticosteroid therapy (which may lead to cataracts and glaucoma in some patients), but without the intraocular pressure elevations that were observed in subjects treated with corticosteroids. In August 2016, we announced that the results of a randomized, parallel-group, double-blind, vehicle-controlled clinical trial of a dermatologic formulation of ADX-102 for the treatment of the skin manifestations of SLS demonstrated clinically relevant activity of ADX-102 in diminishing the severity of ichthyosis, a serious dermatologic disease characteristic of SLS. In all clinical trials to date, ADX-102 was well tolerated, and no serious adverse events have been reported.

In February 2017, we announced the enrollment of the first patient in a Phase 2b clinical trial of the topical ocular ADX-102 for the treatment of allergic conjunctivitis We expect to begin a planned Phase 3 clinical trial of

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topical ocular ADX-102 for the treatment of noninfectious anterior uveitis in the second quarter of 2017. We expect to begin a planned Phase 3 clinical trial of topical dermatologic ADX-102 for the treatment of the skin manifestations of SLS in the second half of 2017. We expect to begin a planned Phase 2a clinical trial of topical ocular ADX-102 for the treatment of Dry Eye Syndrome in the second quarter of 2017, and we may also subsequently initiate a planned Phase 2a clinical trial of ADX-103 in Dry Eye Syndrome. We expect to begin a planned Phase 1 clinical trial of systemically administered ADX-102 or ADX-104 in the first half of 2018. We expect to begin systemically administered Phase 2a clinical trials in SLS and SSADH in the second half of 2018. All of our development timelines could be subject to adjustment depending on recruitment rate, regulatory agency review, and other factors that could delay the initiation and completion of clinical trials.

We have no products approved for sale. We will not receive any revenue from any product candidates that we develop until we obtain regulatory approval and commercialize such products or until we potentially enter into agreements with third parties for the development and commercialization of product candidates. If our development efforts for any of our product candidates result in regulatory approval or we enter into collaboration agreements with third parties, we may generate revenue from product sales or from such third parties. We have primarily funded our operations through the sale of our convertible preferred stock, common stock, convertible promissory notes, warrants and borrowings under our loan and security agreements.

In January 2015, we received net proceeds of approximately $9.0 million, after placement agent fees and expenses from two private placements of common stock and warrants to purchase common stock. In addition, in May 2015, we raised approximately $19.5 million, after deducting underwriting discounts and commissions and other offering expenses through the issuance and sale of 2,822,500 shares of common stock in a follow-on public offering, including shares sold pursuant to the underwriters exercise of their option to purchase additional shares of common stock. In June 2016, we closed an underwritten public offering in which we sold, an aggregate of 2,760,000 shares of common stock, including 360,000 shares sold in connection with the exercise in full by the underwriter of its option to purchase additional shares. The net proceeds of the offering, including the full exercise of the option, were approximately $12.6 million, after deducting the underwriting discounts and commissions and the other offering expenses payable by us. In February 2017, we closed an underwritten public offering in which we sold, 2,555,555 shares of its common stock, including 333,333 shares sold in connection with the exercise in full by the underwriters of their option to purchase additional shares. The net proceeds of the offering, including the full exercise of the option, were approximately $10.5 million, after deducting the underwriting discounts and commissions and the other estimated offering expenses payable by Aldeyra.

We will need to raise additional capital in the form of debt or equity or through partnerships to fund additional development of ADX-102 and other aldehyde traps, and we may in-license, acquire or invest in complementary businesses or products. In addition, as capital resources permit, we may augment or otherwise modify the clinical development plan described herein.

Research and development expenses

We expense all of our research and development expenses as they are incurred. Research and development costs that are paid in advance of performance are capitalized as a prepaid expense until incurred. Research and development expenses primarily include:

non-clinical development, preclinical research, and clinical trial and regulatory-related costs;

expenses incurred under agreements with sites and consultants that conduct our clinical trials;

expenses related to generating, filing, and maintaining intellectual property; and

employee-related expenses, including salaries, benefits, travel and stock-based compensation expense.

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Substantially all of our research and development expenses to date have been incurred in connection with ADX-102. We expect our research and development expenses to increase for the foreseeable future as we advance ADX-102 and other compounds through preclinical and clinical development. The process of conducting clinical trials necessary to obtain regulatory approval is costly and time consuming. We are unable to estimate with any certainty the costs we will incur in the continued development of ADX-102 and our future product candidates. Clinical development timelines, the probability of success and development costs can differ materially from expectations. We may never succeed in achieving marketing approval for our product candidates.

The costs of clinical trials may vary significantly over the life of a project owing to, but not limited to, the following:

- per patient trial costs;
- the number of sites included in the trials;
- the countries in which the trials are conducted;
- the length of time required to enroll eligible patients;
- the number of patients that participate in the trials;
- the number of doses that patients receive;
- the cost of comparative agents used in trials;
- the drop-out or discontinuation rates of patients;
- potential additional safety monitoring or other studies requested by regulatory agencies;
- the duration of patient follow-up; and
- the efficacy and safety profile of the product candidate.

We do not expect ADX-102 and our other product candidates to be commercially available, if at all, for the next several years.

General and administrative expenses

General and administrative expenses consist primarily of salaries and related benefits, including stock-based compensation. Our general and administrative expenses consisted primarily of payroll expenses for our full-time employees during the years ended December 31, 2016 and 2015. Other general and administrative expenses include professional fees for auditing, tax, and legal services. We expect that general and administrative expenses will increase in the future as we expand our operating activities and continue to incur additional costs associated with being a publicly-traded company and maintaining compliance with exchange listing and SEC requirements. These increases will likely include higher consulting costs, legal fees, accounting fees, directors and officers liability insurance premiums and fees associated with investor relations.

Total other income (expense)

Total other income (expense) consists primarily of interest income we earn on interest-bearing accounts and interest expense incurred on our outstanding debt.

Comprehensive loss

Comprehensive loss is defined as the change in equity during a period from transactions and other events and/or circumstances from non-owner sources. For December 31, 2016, comprehensive loss is equal to our net loss of $18.7 million and an unrealized gain on marketable securities of $8,000. For December 31, 2015, comprehensive loss is equal to net loss of $12.1 million and an unrealized loss on marketable securities of $8,000.

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Critical Accounting Policies and Significant Judgments and Estimates

Our management s discussion and analysis of our financial condition and results of operations is based on our financial statements, which we have prepared in accordance with generally accepted accounting principles in the United States (US GAAP). The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the expenses during the reported periods. We evaluate these estimates and judgments on an ongoing basis. We base our estimates on historical experience and on various other factors that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Our actual results may differ materially from these estimates under different assumptions or conditions.

While our significant accounting policies are more fully described in Note 2 to our financial statements appearing elsewhere in this annual report on Form 10-K, we believe that the following accounting policies are the most critical for fully understanding and evaluating our financial condition and results of operations.

Accrued Research and Development Expenses

As part of the process of preparing financial statements, we are required to estimate and accrue research and development expenses. This process involves the following:

- communicating with our applicable personnel to identify services that have been performed on our behalf and estimating the level of service performed and the associated cost incurred for the service when we have not yet been invoiced or otherwise notified of actual cost;
- estimating and accruing expenses in our financial statements as of each balance sheet date based on facts and circumstances known to us at the time; and
- periodically confirming the accuracy of our estimates with selected service providers and making adjustments, if necessary.

Examples of estimated research and development expenses that we accrue include:

- fees paid to investigative sites in connection with clinical studies;
- fees paid to contract manufacturing organizations in connection with non-clinical development, preclinical research, and the production of clinical study materials; and
- professional service fees for consulting and related services.

We base our expense accruals related to non-clinical development, preclinical studies, and clinical trials on our estimates of the services received and efforts expended pursuant to contracts with organizations/consultants that

conduct and manage clinical studies on our behalf. The financial terms of these agreements vary from contract to contract and may result in uneven payment flows. Payments under some of these contracts may depend on many factors, such as the successful enrollment of patients, site initiation and the completion of clinical study milestones. Our service providers invoice us monthly in arrears for services performed. In accruing service fees, we estimate the time period over which services will be performed and the level of effort to be expended in each period. If we do not identify costs that we have begun to incur or if we underestimate or overestimate the level of services performed or the costs of these services, our actual expenses could differ from our estimates. To date, we have not experienced significant changes in our estimates of accrued research and development expenses after a reporting period. However, due to the nature of estimates, we cannot assure you that we will not make changes to our estimates in the future as we become aware of additional information about the status or conduct of our clinical studies and other research activities.

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Stock-Based Compensation

Stock-based compensation expense represents the grant date fair value of restricted stock awards and stock option grants, which are being recognized over the requisite service period of the awards (usually the vesting period) on a straight-line basis, net of estimated forfeitures. For stock option grants with performance-based milestones, the expense is recorded over the remaining service period after the point when the achievement of the milestone is probable or the performance condition has been achieved. We generally estimate the fair value of stock option grants using the Black-Scholes option pricing model. If vesting is based on market-based milestones, we perform Monte Carlo simulations to estimate the timing and number of shares that are most likely to vest and record the expense on a straight-line basis over the estimated period the milestone will be achieved. We account for stock options to non-employees using the fair value approach. Stock options to non-employees are subject to periodic revaluation over their vesting terms.

We generally estimate the fair value of our stock-based awards to employees and non-employees using the Black-Scholes option pricing model, which requires the input of highly subjective assumptions, including (a) the risk-free interest rate, (b) the expected volatility of our stock, (c) the expected term of the award and (d) the expected dividend yield. Due to the lack of sufficient historical public market trading activity, we have based our estimate of expected volatility on the historical volatility of a group of similar companies that are publicly traded. For these analyses, we have selected companies with comparable characteristics to ours including enterprise value, risk profiles, position within the industry, and with historical share price information sufficient to meet the expected life of the stock-based awards. We compute the historical volatility data using the daily closing prices for the selected companies shares over approximately the expected life of the options. The resulting volatility estimate was approximately 89%, and we have employed this value throughout our calculations. We have also computed the historical volatility of ALDX historical information regarding the volatility of our own stock price and have determined that a volatility estimate of 89% is reasonable. We have estimated the expected life of our employee stock options using the simplified method, whereby, the expected life equals the average of the vesting term and the original contractual term of the option for service-based awards. The risk-free interest rates for periods within the expected life of the option are based on the yields of zero-coupon United States Treasury securities.

The assumptions used in the Black-Scholes option pricing model to determine the fair value of employee stock option grants in 2016 and 2015 were as follows:

	December 31, 2016	December 31, 2015
Expected dividend yield	0%	0%
Anticipated volatility	88.57%	88.57%
Estimated stock price	$ 3.94 - $7.48	$ 7.19 - $8.37
Exercise price	$ 3.94 - $7.48	$ 7.19 - $8.37
Expected life (years)	5.50 - 6.25	5.50 - 6.25
Risk free interest rate	0.59% - 2.20%	0.27% - 1.91%

Other Information

Net Operating Loss Carryforwards

As of December 31, 2016, we have Federal and State income tax net operating loss (NOL) carryovers of approximately $42.8 million and $39.9 million, respectively, which will expire at various dates through 2036. As of December 31, 2016, we have Federal and State tax carryovers of credits for increasing research activities (R&D tax

credits) of approximately $1.2 million and $178,000, respectively, which will expire at various dates through 2036.

In general, under Section 382 of the Internal Revenue Code of 1986, as amended (Code), a corporation that undergoes an ownership change is subject to limitations on its ability to utilize its pre-change NOLs and

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certain other tax assets (tax attributes) to offset future taxable income. In general, an ownership change occurs if the aggregate stock ownership of certain stockholders increases by more than 50 percentage points over such stockholders lowest percentage ownership during the testing period (generally three years). Transactions involving our common stock, even those outside our control, such as purchases or sales by investors, within the testing period could result in an ownership change. A limitation on our ability to utilize some or all of our NOLs or credits could have a material adverse effect on our results of operations and cash flows. Prior to 2016, we underwent two ownership changes and it is possible that additional ownership changes have occurred since. However, our management believes that we have sufficient Built-In-Gain to offset the Section 382 of the Code limitation generated by such ownership changes. Any future ownership changes, including those resulting from our recent or future financing activities, may cause our existing tax attributes to have additional limitations.

Recent Accounting Pronouncements

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-15 (ASU 2016-15), Statement of Cash Flows. The standard is intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, with early adoption permitted. ASU 2016-15 may be adopted retrospectively or prospectively if it is impractical to apply the amendments retrospectively. The Company does not expect this standard to have a material impact on its financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instrument-Credit Losses (ASU 2016-13). ASU 2016-13 requires a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019. The Company does not expect this standard to have a material impact on its financial statements.

In March 2016, the FASB issued ASU No. 2016-09 Improvements to Employee Share-Based Payment Accounting (ASU 2016-09), to simplify the accounting for stock compensation. This update focuses on income tax accounting, award classification, estimating forfeitures, and cash flow presentation. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016. The Company does not expect this standard to have a material impact on its financial statements.

In February 2016, the FASB issued ASU No. 2016-02 (ASU 2016-02), Leases. ASU 2016-02 requires lessees to recognize on the balance sheet a right-of-use asset, representing its right to use the underlying asset for the lease term, and a lease liability for all leases with terms greater than 12 months. The guidance also requires qualitative and quantitative disclosures designed to assess the amount, timing, and uncertainty of cash flows arising from leases. The standard requires the use of a modified retrospective transition approach, which includes a number of optional practical expedients that entities may elect to apply. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018. The Company does not expect this standard to have a material impact on its financial statements.

In January 2016, the FASB issued ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities (ASU 2016-01). ASU 2016-01 amends the guidance on the classification and measurement of financial instruments. Although ASU 2016-01 retains many current requirements, it significantly revises accounting related to the classification and measurement of investments in equity securities and the presentation of certain fair value changes for financial liabilities measured at fair value. ASU 2016-01 also amends certain disclosure requirements associated with the fair value of financial instruments and is effective for fiscal years beginning after December 15, 2017. The Company does not expect this standard to have a material impact on its financial statements.

In November 2015, the FASB issued ASU No. 2015-17, Income Taxes (ASU 2015-17). ASU 2015-17 simplifies the presentation of deferred income taxes by requiring that deferred tax liabilities and assets be classified as

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noncurrent in a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in ASU 2015-17. ASU 2015-17 is effective for fiscal years beginning after December 15, 2016. The Company does not expect this standard to have a material impact on its financial statements.

In April 2015, the FASB issued ASU No. 2015-03, Simplifying the Presentation of Debt Issuance Costs (ASU 2015-03). The amendments in ASU 2015-03 require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 is effective for fiscal years beginning after December 15, 2016. The Company does not expect this standard to have a material impact on its financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes the revenue recognition requirements in ASC 605, Revenue Recognition. This ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. ASU 2014-09 is effective for fiscal years beginning after December 15, 2017. The Company does not expect this standard to have a material impact on its financial statements.

JOBS Act

We are an emerging growth company, as defined in the Jumpstart Our Business Startups Act of 2012, or the JOBS Act, and are eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies, including, but not limited to, only two years of audited financial statements in addition to any required unaudited interim financial statements with correspondingly reduced Management s Discussion and Analysis of Financial Condition and Results of Operations disclosure, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy or information statements, exemptions from the requirements of holding a non-binding advisory vote on executive compensation and seeking stockholder approval of any golden parachute payments not previously approved and not being required to adopt certain accounting standards until those standards would otherwise apply to private companies.

As an emerging growth company, we have irrevocably elected to not take advantage of the extended transition period afforded by the JOBS Act for the implementation of new or revised accounting standards and, as a result, will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies.

Results of Operations

We anticipate that our results of operations will fluctuate for the foreseeable future due to several factors, including the progress of our research and development efforts, the timing and outcome of clinical trials and regulatory requirements. Our limited operating history makes predictions of future operations difficult or impossible. Since our inception, we have incurred significant losses.

Comparison of Years Ended December 31, 2016 and 2015

Net loss. Net loss for the years ended December 31, 2016 and 2015 was approximately $18.7 million and $12.1 million, respectively. As of December 31, 2016, we had total stockholders equity of $21.6 million. Losses have resulted principally from costs incurred in our clinical trials, research and development programs and from our general and administrative expenses.

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Research and development expenses. Research and development expenses were $13.2 million for the year ended December 31, 2016 compared to $7.6 million for the same period in 2015. The increase of $5.6 million is primarily related to the increase in our external research and development expenditures, including manufacturing, preclinical and clinical costs and an increase in personnel costs.

General and administrative expenses. General and administrative expenses were $5.5 million for the year ended December 31, 2016, compared to $4.4 million for the year ended 2015. The increase of approximately $1.1 million is primarily related to an increase in legal costs, rent, consulting costs, and personnel costs.

Other income (expense). Total other income (expense) was approximately $(3,472) for the year ended December 31, 2016 and consisted of interest expense related to our credit facility partially offset by interest income. Total other income (expense) was $(101,180) for the same period in 2015 and primarily consisted of interest expense related to our credit facility partially offset by interest income. In 2016, there was twelve months of investment income as opposed to only one month in 2015.

Liquidity and Capital Resources

We have funded our operations primarily from the sale of equity securities and convertible equity securities and borrowings under our Credit Facility discussed below. We have incurred operating losses since inception and negative cash flows from operating activities in devoting substantially all of our efforts towards research and development. At December 31, 2016, we had total stockholders equity of approximately $21.6 million and cash, cash equivalents and marketable securities of $24.9 million. During the year ended December 31, 2016, we had net loss of approximately $18.7 million. We expect to generate operating losses for the foreseeable future.

We are a party to a loan and security agreement (the Credit Facility) with Pacific Western Bank (Pacific Western, formerly Square 1 Bank) which was originally entered into in April 2012 and has been subsequently amended. Pursuant to the Credit Facility, Pacific Western agreed to make term loans in a principal amount of up to $5.0 million available to us to fund expenses related to our clinical trials and general working capital purposes. The term loans are to be made available to us upon the following terms: (i) $2.0 million was made available in November 2014 (which was used in part to refinance then outstanding loans from Pacific Western); and (ii) $3.0 million (the Tranche B Loan) became available to the Company in 2016 following the satisfaction of certain conditions, including receipt of positive phase 2 data in noninfectious anterior uveitis. Any term loan made is payable as interest-only prior to November 2017 and thereafter is scheduled to be payable in monthly installments of principal plus accrued interest through the maturity date in October 2020. Each term loan accrues interest from its date of issue at a variable annual interest rate equal to the greater of 2.0% plus prime or 5.25% per annum. The annualized interest rate as of December 31, 2016 was 5.60%. The Credit Facility is collateralized by our assets, including our intellectual property. As of December 31, 2016, $1.4 million was outstanding under the Credit Facility. At December 31, 2016, the Credit Facility is shown net of a remaining debt discount of $79,663 which is being amortized using the effective interest method through the current maturity date of the Credit Facility, October 2020.

On May 7, 2014, we closed our Initial Public Offering, in which 1,500,000 shares of common stock were sold at a price to the public of $8.00 per share for an aggregate offering price of $12.0 million. The offer and sale of all of the shares in the Initial Public Offering were registered under the Securities Act of the 1933, as amended, pursuant to a registration statement on Form S-1 (File No. 333-193204), which was declared effective by the SEC on May 1, 2014. We raised approximately $10.0 million in net proceeds after deducting underwriting discounts and commissions of $0.8 million, $1.0 million in prepaid offering and printing costs and other offering costs of $0.2 million.

On January 15, 2015, we sold, in a private placement, an aggregate of approximately 1.1 million shares of common stock at a price of $7.00 per share. Investors received warrants to purchase up to approximately 1.1 million shares of common stock at an exercise price of $9.50. The warrants will expire 3 years from the date

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of issuance. The warrants do not include a net-exercise feature. The warrants may be redeemed by us at a price of $0.001 per share upon notice to the holders in the event that the closing bid for Aldeyra s common stock for each of the fifteen consecutive trading days prior to such redemption is at least $20.00 per share and the average trading volume of Aldeyra s common stock during such period is 50,000 shares per day. Following Aldeyra s notification to the warrant holders of its exercise of the redemption right under the warrants, each warrant holder will have the option to exercise their warrants prior to the redemption date rather than having them redeemed. We raised approximately $7.1 million in net proceeds in the private placement of common stock and warrants.

On January 22, 2015, in a subsequent private placement, we sold an aggregate of 211,528 shares of common stock at a price of $9.33 per share and a warrant to purchase up to 211,528 shares of common stock at a price of $0.125 per share subject to the warrant. The exercise price of the warrant is $9.50 per share. The warrant will expire 3 years from the date of issuance. The warrant does not include a net-exercise feature. The warrant may be redeemed by us at a price of $0.001 per share upon notice to the holder thereof in the event that the closing bid for Aldeyra s common stock for each of the fifteen consecutive trading days prior to such redemption is at least $20.00 per share and the average trading volume of Aldeyra s common stock during such period is 50,000 shares per day. Following Aldeyra s notification to the warrant holder of its exercise of the redemption right under the warrant, the warrant holder will have the option to exercise the warrant prior to the redemption date rather than having it redeemed. We raised approximately $1.9 million in net proceeds in the private placement of common stock and a warrant to purchase common stock.

We raised approximately $19.5 million, after deducting underwriting discounts and commissions and other offering expenses, which closed on May 22, 2015, through the issuance and sale of 2,822,500 shares of common stock in a follow-on public offering, including shares sold pursuant to the underwriters exercise of their option to purchase additional shares of common stock.

In June 2016, we closed an underwritten public offering in which we sold, an aggregate of 2,760,000 shares of common stock, including 360,000 shares sold in connection with the exercise in full by the underwriter of its option to purchase additional shares. The net proceeds of the offering, including the full exercise of the option, were approximately $12.6 million, after deducting the underwriting discounts and commissions and the other offering expenses payable by us.

In February 2017, we closed an underwritten public offering in which we sold, 2,555,555 shares of its common stock, including 333,333 shares sold in connection with the exercise in full by the underwriters of their option to purchase additional shares. The net proceeds of the offering, including the full exercise of the option, were approximately $10.5 million, after deducting the underwriting discounts and commissions and the other estimated offering expenses payable by Aldeyra.

We believe that our cash, cash equivalents and marketable securities as of December 31, 2016, together with the proceeds from the February 2017 public offering and the amounts available under the Credit Facility, will be adequate to fund operations into approximately the third quarter of 2018 based on our current business plan. However, these amounts will not be sufficient for us to commercialize our product candidates or conduct any substantial, additional development requirements requested by the FDA. At this time, due to the risks inherent in the drug development process, we are unable to estimate with any certainty the costs we will incur in the continued clinical development of ADX-102 and our other product candidates. Subsequent trials initiated at a later date will cost considerably more, depending on the results of our prior clinical trials, and feedback from the FDA or other third parties. Accordingly, we will continue to require substantial additional capital to continue our clinical development and potential commercialization activities. The amount and timing of our future funding requirements will depend on many factors, including but not limited to:

the progress, costs, results of and timing of our clinical development program for ADX-102 and our other product candidates, including our current and planned clinical trials;

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- the need for, and the progress, costs and results of, any additional clinical trials of ADX-102, including systemic formulations, we may initiate based on the results of our planned clinical trials or discussions with the FDA, including any additional trials the FDA or other regulatory agencies may require evaluating the safety of ADX-102 and our other product candidates;

- the outcome, costs and timing of seeking and obtaining regulatory approvals from the FDA, and any similar regulatory agencies;

- the timing and costs associated with manufacturing ADX-102 and our other product candidates for clinical trials and other studies and, if approved, for commercial sale;

- our need and ability to hire additional management, development and scientific personnel;

- the cost to maintain, expand and defend the scope of our intellectual property portfolio, including the amount and timing of any payments we may be required to make, or that we may receive, in connection with licensing, filing, prosecuting, defending and enforcing of any patents or other intellectual property rights;

- the timing and costs associated with establishing sales and marketing capabilities;

- market acceptance of ADX-102 and our other product candidates;

- the costs of acquiring, licensing or investing in additional businesses, products, product candidates and technologies; and

- our need to remediate any material weaknesses and implement additional internal systems and infrastructure, including financial and reporting systems.

We may need or desire to obtain additional capital to finance our operations through debt, equity or alternative financing arrangements. We may also seek capital through collaborations or partnerships with other companies. The issuance of debt could require us to grant additional liens on certain of our assets that may limit our flexibility. If we raise additional capital by issuing equity securities, the terms and prices for these financings may be much more favorable to the new investors than the terms obtained by our existing stockholders. These financings also may significantly dilute the ownership of our existing stockholders. If we are unable to obtain additional financing, we may be required to reduce the scope of our future activities which could harm our business, financial condition and operating results. There can be no assurance that any additional financing required in the future will be available on acceptable terms, if at all.

We will continue to incur costs as a public company including, but not limited to, costs and expenses for directors fees; increased directors and officers insurance; investor relations fees; expenses for compliance with the Sarbanes-Oxley Act of 2002 and rules implemented by the SEC and NASDAQ, on which our common stock is listed; and various other costs. The Sarbanes-Oxley Act of 2002 requires that we maintain effective disclosure controls and

procedures and internal controls. The following table summarizes our cash flows:

	Years ended December 31,	
	2016	2015
Net cash used in operating activities	$ (15,147,512)	$ (9,311,753)
Net cash used in investing activities	(225,234)	(13,036,256)
Net cash provided by financing activities	12,738,941	28,469,571
Net (decrease) increase in cash and cash equivalents	$ (2,633,805)	$ 6,121,562

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Operating Activities. Net cash used in operating activities was $15.1 million in 2016 compared to net cash used in operating activities of $9.3 million in 2015. The primary use of cash was to fund our operations. The increase in the amount of cash used in operating activities for 2016 as compared to 2015 was due to an increase in both research and development and general and administrative expenses.

Investing Activities. Net cash used in investing activities in 2016 were $(225,234) related primarily to the purchase of marketable securities partially offset by sales and maturities of marketable securities compared to net cash used in investing activities in 2015 of $13.0 million related primarily to the purchase of marketable securities.

Financing Activities. Net cash provided by financing activities was $12.7 million for the year ended December 31, 2016 related to our public placement offering, compared to net cash provided by financing activities of $28.5 million for year ended 2015 which was related to our private and public offerings.

Off-Balance Sheet Arrangements

Through December 31, 2016, we have not entered into and did not have any relationships with unconsolidated entities or financial collaborations, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purpose.

Contractual Obligations and Commitments

During the year ended December 31, 2014, we entered into a lease agreement for a certain commercial office space. The thirty-seven month lease which began in September 2014 provides us with approximately 3,700 square feet of space in Lexington, Massachusetts. Base annual rent is initially set at $5,604 per month. Total base rent payable over the lease period is approximately $205,000. In March 2016, we entered into a sublease for approximately 3,188 additional square feet of office space to expand our headquarters in Lexington, Massachusetts. The sublease expires in September 2017. The sublease provides for the payment of annual base rent in the amount of $67,000 payable in monthly installments and the requirement to pay certain operating expenses, taxes and other fees in accordance with the terms of the master lease.

Our long-term debt obligation consists of amounts we are obligated to repay under our Credit Facility with Pacific Western, of which $1.4 million was outstanding as of December 31, 2016. We entered into the Credit Facility in April 2012 and it has been subsequently amended to make term loans in a principal amount of up to $5,000,000 available to us with proceeds to be used first to refinance outstanding loans from Pacific Western, second to fund expenses related to our clinical trials, and the remainder for general working capital purposes. The term loans are to be made available to us upon the following terms: (i) $2,000,000 was made available on November 10, 2014; and (ii) $3.0 million (the Tranche B Loan) which was made available to the Company in May 2016 following the satisfaction of certain conditions, including receipt of positive phase 2 data in noninfectious anterior uveitis. Each term loan accrues interest from its date of issue at a variable annual interest rate equal to the greater of 2.0% plus prime or 5.25% per annum. In November 2016, we amended our Credit Facility such that any term loan we draw is payable as interest-only prior to November 2017 and thereafter is payable in monthly installments of principal plus accrued interest over 36 months. The following table summarizes our contractual obligations at December 31, 2016.

The following table summarizes our contractual obligations at December 31, 2016:

	Total	Less than 1 Year	Years 1 - 3	Years 3 - 5	More than 5 Years
Credit Facility	$ 1,395,833	$ 77,546	$ 1,318,287	$	$
Operating lease obligations	$ 107,195	$ 107,195	$	$	$
Total	$ 1,503,028	$ 184,741	$ 1,318,287	$	$

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The table above detailing contractual commitments and obligations does not include severance pay obligations to certain of our executive officers in the event of a not-for-cause termination under existing employment contracts and any contingent obligations under licensing agreements. The cash amount for which we might be liable upon any such termination, based on current executive pay and bonus levels, could be up to approximately $1.0 million.

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ITEM 7A. ***QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK***

Interest rates

Our exposure to market risk is currently confined to our cash and cash equivalents and our Credit Facility. We have not used derivative financial instruments for speculation or trading purposes. Because of the short-term maturities of our cash and cash equivalents, we do not believe that an increase in market rates would have any significant impact on the realized value of our investments. Our Credit Facility accrues interest from its date of issue at a variable annual interest rate equal to the greater of 2.0% plus prime or 5.25% per annum. The annualized interest rate as of December 31, 2016 was 5.60%.

Effects of inflation

Inflation has not had a material impact on our results of operations.

ITEM 8. ***FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA***

The information required by this Item 8 is contained on pages 73 through 93 of this annual report on Form 10-K and is incorporated herein by reference.

ITEM 9. ***CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE***

None.

ITEM 9A. ***CONTROLS AND PROCEDURES***

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

As of the end of the period covered by this annual report on Form 10-K, we carried out an evaluation under the supervision and with the participation of our Disclosure Committee and our management, including our Chief Executive Officer and President and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rules 13a-15(e) and 15d-15(e). Disclosure controls are procedures that are designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, or the Exchange Act, such as this annual report on Form 10-K, is recorded, processed, summarized and reported within the time periods specified by the U.S. Securities and Exchange Commission. Disclosure controls are also designed to ensure that such information is accumulated and communicated to our management, including our Chief Executive Officer and President and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Our quarterly evaluation of disclosure controls includes an evaluation of some components of our internal control over financial reporting. We also perform a separate annual evaluation of internal control over financial reporting for the purpose of providing the management report below.

The evaluation of our disclosure controls included a review of their objectives and design, our implementation of the controls and the effect of the controls on the information generated for use in this annual report on Form 10-K. In the course of the controls evaluation, we reviewed data errors or control problems identified and sought to confirm that

appropriate corrective actions, including process improvements, were being undertaken. This type of evaluation is performed on a quarterly basis so that the conclusions of management, including our Chief Executive Officer and President and our Chief Financial Officer, concerning the effectiveness of the disclosure controls can be reported in our periodic reports on Form 10-Q and Form 10-K. The overall goals of our evaluation activities are to monitor our disclosure controls and to modify them as necessary. We intend to maintain our disclosure controls as dynamic processes and procedures that we adjust as circumstances merit.

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Based on our management s evaluation (with the participation of our Chief Executive Officer and President and our Chief Financial Officer), as of the end of the period covered by this report, our Chief Executive Officer and President and our Chief Financial Officer have concluded that our disclosure controls and procedures were effective.

Management s Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management utilized the criteria established in the Internal Control Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) to conduct an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2016. Based on the assessment, our management has concluded that, as of December 31, 2016, our internal control over financial reporting was effective.

Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during the fourth quarter of 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. ***OTHER INFORMATION***

On March 28, 2017, the Compensation Committee of our Board of Directors approved and established the Aldeyra Therapeutics, Inc. Change in Control Plan (the CIC Plan), which provides for the accelerated vesting for outstanding unvested equity awards held by our eligible employees are subject to a qualifying employment termination in connection with a change in control, including our named executive officers. The CIC Plan provides for acceleration of 100% of the unvested equity held by our executive officers in the event the officer s employment is terminated without cause, or the officer resigns for good reason, in each case within 3 months before or 12 months of a change of control.

For the purpose of the CIC Plan, the following terms have the definitions set forth below:

A termination for cause means termination by us of the executive officer s employment by reason of the occurrence of any one or more of the following: (i) an act or acts of personal dishonesty taken by the executive officer and intended to result in substantial personal enrichment of the executive officer at the expense of the Company; (ii) repeated violations by the executive officer of the executive officer s duties and obligations (other than as a result of incapacity due to physical or mental illness) which are demonstrably willful and deliberate on the executive officer s part, which are committed in bad faith or without reasonable belief that such violations are in the Company s best interests and which are not remedied in a reasonable period of time after receipt of written notice from the Company; (iii) indictment or plea of nolo contendere of the executive officer of a felony involving moral turpitude; or (iv) the material breach of the executive s proprietary information and inventions agreement.

Change in Control means the occurrence of any of the following: (i) any person (as such term is used in Sections 13(d) and 14(d) of the Exchange Act) becomes the beneficial owner (as defined in Rule 13d-3 of the

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Exchange Act), directly or indirectly, of securities of the Company representing more than fifty percent (50%) of the total voting power represented by the Company s then-outstanding voting securities; (ii) the consummation of the sale or disposition by the Company of all or substantially all of the Company s assets; (iii) the consummation of a merger or consolidation of the Company with or into any other entity, other than a merger or consolidation which would result in the voting securities of the Company outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity or its parent) more than fifty percent (50%) of the total voting power represented by the voting securities of the Company or such surviving entity or its parent outstanding immediately after such merger or consolidation; or individuals who are members of the Board (the Incumbent Board) cease for any reason to constitute at least a majority of the members of the Board over a period of 12 months; provided, however, that if the appointment or election (or nomination for election) of any new Board member was approved or recommended by a majority vote of the members of the Incumbent Board then still in office, such new member shall, for purposes of this Plan, be considered as a member of the Incumbent Board. A transaction shall not constitute a Change in Control if its sole purpose is to change the state of the Company s incorporation or to create a holding company that will be owned in substantially the same proportions by the persons who held the Company s securities immediately before such transaction.

Good reason means (i) a material diminution in the executive officer s base compensation or target bonus by more than 10%, except in connection with company-wide cost reduction; (ii) a material diminution in the executive officer s authority, duties or responsibilities with respect to the Company or any successor or acquiring entity, including, without limitation, any requirement that an officer who is the Chief Executive Officer report to anyone other than to the Board of Directors of the ultimate parent entity of the Company (the Ultimate Parent) or that the executive officer (other than the Chief Executive Officer) report to anyone other than the Chief Executive Officer of the Ultimate Parent; (iii) a breach of a material provision of the executive officer s employment or other written agreement governing employment with the Company (it being understand that a change in title without the executive officer s consent shall be a material breach); or (iv) a relocation of the executive officer s principal workplace by more than 50 miles from where the executive officer performed services prior to the relocation, without the executive officer s prior consent. However, good reason shall not exist unless (i) the executive officer has given written notice to us within 90 days of the initial existence of the good reason event or condition(s) giving specific details regarding the event or condition; (ii) we have failed to cure such event or condition within 30-days of receiving such notice, and (iii) the executive officer resigns within 30 days of the expiration of the 30-day cure period provided for in clause (ii) provided that we have not cured the event or condition.

This summary of the CIC Plan is qualified in its entirety by reference to the text of the CIC Plan, which is included as Exhibit 10.25 hereto and incorporated herein by reference.

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PART III

ITEM 10. Directors, Executive Officers and Corporate Governance

Except as set forth below, the information required by this item will be contained in our definitive proxy statement to be filed with the SEC in connection with the Annual Meeting of Stockholders within 120 days after the conclusion of our fiscal year ended December 31, 2016 (the Proxy Statement), and is incorporated in this annual report on Form 10-K by reference.

Code of Conduct

Our board of directors adopted a code of ethics and business conduct that applies to each of our directors, officers and employees. The full text of our code of business conduct is posted on the Investors portion of our website at http://ir.aldeyra.com. Any waiver of the code of ethics and business conduct for an executive officer or director may be granted only by our board of directors or a committee thereof and must be timely disclosed as required by applicable law. We have implemented whistleblower procedures that establish format protocols for receiving and handling complaints from employees. Any concerns regarding accounting or auditing matters reported under these procedures will be communicated promptly to the audit committee.

ITEM 11. Executive Compensation

Other than with respect to the Securities Authorized for Issuance under Equity Incentive Plans contained in Part II, Item 5 of this annual report, the information required by this item will be contained in the Proxy Statement and is incorporated in this annual report on Form 10-K by reference.

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

The information required by this item will be contained in the Proxy Statement and is incorporated in this annual report on Form 10-K by reference.

ITEM 13. Certain Relationships and Related Party Transactions, and Director Independence

The information required by this item will be contained in the Proxy Statement and is incorporated in this annual report on Form 10-K by reference.

ITEM 14. Principal Accounting Fees and Services

The information required by this item will be contained in the Proxy Statement and is incorporated in this annual report on Form 10-K by reference.

PART IV

ITEM 15. Exhibits and Financial Statements Schedules

The financial statements filed as part of this annual report on Form 10-K are listed and indexed at page 73. Certain schedules are omitted because they are not applicable, or not required, or because the required information is included in the financial statements or notes thereto.

The Exhibits listed in the Exhibit Index immediately preceding the Exhibits are filed as part of this annual report on Form 10-K.

ITEM 16. Form 10-K Summary

None.

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Signatures

Pursuant to the requirements of Section 13 and 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this annual report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, in the Commonwealth of Massachusetts, on March 30, 2017.

ALDEYRA THERAPEUTICS, INC.

By: /s/ Todd Brady, M.D., Ph.D.
Todd Brady, M.D., Ph.D.
President and Chief Executive Officer

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

Signature	Title	Date
/s/ Todd C. Brady, M.D., Ph.D.	Chief Executive Officer and Director	March 30, 2017
Todd C. Brady, M.D., Ph.D.	(principal executive officer)	
/s/ Stephen J. Tulipano	Chief Financial Officer	March 30, 2017
Stephen J. Tulipano	(principal financial and accounting officer)	
/s/ C. Boyd Clarke	Chairman of the Board of Directors	March 30, 2017
C. Boyd Clarke		
/s/ Ben Bronstein, M.D.	Director	March 30, 2017
Ben Bronstein, M.D.		
/s/ Richard H. Douglas, Ph.D.	Director	March 30, 2017
Richard H. Douglas, Ph.D.		
/s/ Martin J. Joyce	Director	March 30, 2017
Martin J. Joyce		
/s/ Gary Phillips, M.D.	Director	March 30, 2017
Gary Phillips, M.D.		

/s/ Jesse Treu, Ph.D. Jesse Treu, Ph.D.	Director	March 30, 2017
/s/ Neal Walker, D.O. Neal Walker, D.O.	Director	March 30, 2017

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ALDEYRA THERAPEUTICS, INC.

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Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders

Aldeyra Therapeutics, Inc.

Lexington, Massachusetts

We have audited the accompanying balance sheets of Aldeyra Therapeutics, Inc. (the Company) as of December 31, 2016 and 2015 and the related statements of operations, comprehensive loss, and stockholders equity, and cash flows for each of the two years in the period ended December 31, 2016. 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 (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, nor were we 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. An audit also includes 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, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Aldeyra Therapeutics, Inc. at December 31, 2016 and 2015, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America.

/s/ BDO USA, LLP

Boston, Massachusetts

March 30, 2017

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ALDEYRA THERAPEUTICS, INC.

BALANCE SHEETS

	December 31, 2016	December 31, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	$ 12,015,061	$ 14,648,866
Marketable securities	12,897,584	12,941,776
Prepaid expenses and other current assets	218,682	497,552
Total current assets	25,131,327	28,088,194
Deferred offering costs		36,236
Fixed assets, net	56,352	80,334
Total assets	$ 25,187,679	$ 28,204,764
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 275,441	$ 851,160
Accrued expenses	1,946,251	1,186,429
Current portion of credit facility	77,546	77,546
Total current liabilities	2,299,238	2,115,135
Credit facility, net of current portion and debt discount	1,238,624	1,211,310
Total liabilities	3,537,862	3,326,445
Commitments and contingencies (Note 11)		
Stockholders equity:		
Preferred stock, $0.001 par value, 15,000,000 shares authorized, none issued and outstanding		
Common stock, voting, $0.001 par value; 150,000,000 authorized and 12,576,325 and 9,712,521 shares issued and outstanding, respectively	12,576	9,713
Additional paid-in capital	98,938,446	83,478,851
Accumulated other comprehensive income (loss)	129	(8,361)
Accumulated deficit	(77,301,334)	(58,601,884)
Total stockholders equity	21,649,817	24,878,319
Total liabilities and stockholders equity	$ 25,187,679	$ 28,204,764

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

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ALDEYRA THERAPEUTICS, INC.

STATEMENTS OF OPERATIONS

	Years ended December 31, 2016	2015
Operating expenses:		
Research and development	$ 13,175,670	$ 7,574,398
General and administrative	5,520,308	4,414,709
Loss from operations	(18,695,978)	(11,989,107)
Other income (expense):		
Interest income	102,037	11,126
Interest expense	(105,509)	(112,306)
Total other expense, net	(3,472)	(101,180)
Net loss	$ (18,699,450)	$ (12,090,287)
Net loss per share basic and diluted	$ (1.65)	$ (1.40)
Weighted average common shares outstanding basic and diluted	11,352,230	8,633,897

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

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ALDEYRA THERAPEUTICS, INC.

STATEMENTS OF COMPREHENSIVE LOSS

	Years ended December 31,	
	2016	**2015**
Net loss	$ (18,699,450)	$ (12,090,287)
Other comprehensive income/(loss):		
Unrealized gain/(loss) on marketable securities	8,490	(8,361)
Total other comprehensive income/(loss)	$ 8,490	$ (8,361)
Comprehensive loss	$ (18,690,960)	$ (12,098,648)

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

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ALDEYRA THERAPEUTICS, INC.

STATEMENTS OF STOCKHOLDERS EQUITY

	Stockholders Equity					
	Common Voting Stock			Accumulated Other		
	Shares	Amount	Additional Paid-in Capital	Comprehensive Income/(Loss), net of tax	Accumulated Deficit	Total Stockholders Equity
Balance, December 31, 2014	5,565,415	$ 5,565	$ 52,790,090	$	$ (46,511,597)	$ 6,284,058
Stock-based compensation			2,187,102			2,187,102
Issuance of common stock, net of issuance costs	4,147,106	4,148	28,501,659			28,505,807
Other comprehensive loss				(8,361)		(8,361)
Net loss					(12,090,287)	(12,090,287)
Balance, December 31, 2015	9,712,521	9,713	83,478,851	(8,361)	(58,601,884)	24,878,319
Stock-based compensation			2,759,753			2,759,753
Issuance of common stock, net of issuance costs of $240,000	2,760,000	2,760	12,610,863			12,613,623
Issuance of common stock, upon exercise of stock options	103,804	103	88,979			89,082
Other comprehensive loss				8,490		8,490
Net loss					(18,699,450)	(18,699,450)
Balance, December 31, 2016	12,576,325	$ 12,576	$ 98,938,446	$ 129	$ (77,301,334)	$ 21,649,817

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

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ALDEYRA THERAPEUTICS, INC.

STATEMENTS OF CASH FLOWS

	Years ended December 31,	
	2016	**2015**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (18,699,450)	$ (12,090,287)
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock-based compensation	2,759,753	2,187,102
Amortization of debt discount non-cash interest expense	27,314	35,829
Net amortization of premium on debt securities available for sale	266,106	
Depreciation	35,792	18,778
Change in assets and liabilities:		
Prepaid expenses and other current assets	278,870	(264,984)
Accounts payable	(575,719)	509,866
Accrued expenses	759,822	291,943
Net cash used in operating activities	(15,147,512)	(9,311,753)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisitions of property and equipment	(11,810)	(86,119)
Purchases of marketable securities	(16,048,424)	(12,950,137)
Sales of marketable securities	15,835,000	
Net cash used in investing activities	(225,234)	(13,036,256)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock and exercise of options	12,738,941	28,505,807
Deferred offering costs paid in cash		(36,236)
Net cash provided by financing activities	12,738,941	28,469,571
NET (DECREASE)/INCREASE IN CASH	(2,633,805)	6,121,562
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	14,648,866	8,527,304
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 12,015,061	$ 14,648,866
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	$ 78,128	$ 74,299

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

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ALDEYRA THERAPEUTICS, INC.

NOTES TO THE FINANCIAL STATEMENTS

1. NATURE OF BUSINESS

Aldeyra Therapeutics, Inc. (the Company or Aldeyra) was incorporated in the state of Delaware on August 13, 2004 as Neuron Systems, Inc. On December 20, 2012, the Company changed its name to Aldexa Therapeutics, Inc. and, on March 17, 2014, the Company changed its name to Aldeyra Therapeutics, Inc. The Company is a biotechnology company focused primarily on the development of new products for inflammation, inborn errors of metabolism and other diseases that are thought to be related to endogenously generated toxic and pro-inflammatory chemical species known as aldehydes. The ongoing research and development activities will be subject to extensive regulation by numerous governmental authorities in the United States. Prior to marketing in the United States, any drug developed by the Company must undergo rigorous preclinical and clinical testing and an extensive regulatory approval process implemented by the United States Food and Drug Administration (FDA) under the Food, Drug and Cosmetic Act. The Company has limited experience in conducting and managing the preclinical and clinical testing necessary to obtain regulatory approval. There can be no assurance that the Company will not encounter problems in the clinical trials that will cause the Company or the FDA to delay or suspend clinical trials.

The Company s success will depend in part on its ability to obtain patents and product license rights, maintain trade secrets, and operate without infringing on the property rights of others, both in the United States and other countries. There can be no assurance that patents issued to or licensed by the Company will not be challenged, invalidated, circumvented, or that the rights granted thereunder will provide proprietary protection or competitive advantages to the Company.

The Company s principal activities to date include raising capital and research and development activities.

2. BASIS OF PRESENTATION

Basis of Presentation and Management s Plans The accompanying financial statements were prepared in conformity with accounting principles generally accepted in the United States of America (US GAAP).

Liquidity and Management s Plans At December 31, 2016, the Company had an accumulated deficit of approximately $77.3 million and cash and cash equivalents and marketable securities of approximately $24.9 million.

On May 7, 2014, the Company closed its Initial Public Offering, in which 1,500,000 shares of common stock were sold at a price to the public of $8.00 per share for an aggregate offering price of $12.0 million. The offer and sale of all of the shares in the Initial Public Offering were registered under the Securities Act of the 1933, as amended, pursuant to a registration statement on Form S-1 (File No. 333-193204), which was declared effective by the SEC on May 1, 2014. The Company raised approximately $10.0 million in net proceeds after deducting underwriting discounts and commissions of $0.8 million, $1.0 million in prepaid offering and printing costs and other offering costs of $0.2 million.

On January 15, 2015, the Company sold, in a private placement, an aggregate of approximately 1.1 million shares of common stock at a price of $7.00 per share. Investors received warrants to purchase up to approximately 1.1 million shares of common stock at an exercise price of $9.50. The warrants will expire 3 years from the date of issuance. The

warrants do not include a net-exercise feature. The warrants may be redeemed by the Company at a price of $0.001 per share upon notice to the holders in the event that the closing bid for Aldeyra s common stock for each of the fifteen consecutive trading days prior to such redemption is at least $20.00 per share and the average trading volume of Aldeyra s common stock during such period is 50,000 shares per day. Following Aldeyra s notification to the warrant holders of its exercise of the redemption right under the warrants, each warrant holder will have the option to exercise their warrants prior to the redemption date rather than having them redeemed. The Company raised approximately $7.1 million in net proceeds in the private placement of common stock and warrants.

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On January 22, 2015, in a subsequent private placement, the Company sold an aggregate of 211,528 shares of common stock at a price of $9.33 per share and a warrant to purchase up to 211,528 shares of common stock at a price of $0.125 per share subject to the warrant. The exercise price of the warrant is $9.50 per share. The warrant will expire 3 years from the date of issuance. The warrant does not include a net-exercise feature. The warrant may be redeemed by the Company at a price of $0.001 per share upon notice to the holder thereof in the event that the closing bid for Aldeyra s common stock for each of the fifteen consecutive trading days prior to such redemption is at least $20.00 per share and the average trading volume of Aldeyra s common stock during such period is 50,000 shares per day. Following Aldeyra s notification to the warrant holder of its exercise of the redemption right under the warrant, the warrant holder will have the option to exercise the warrant prior to the redemption date rather than having it redeemed. The Company raised approximately $1.9 million in net proceeds in the private placement of common stock and a warrant to purchase common stock.

On May 22, 2015, the Company raised approximately $19.5 million, after deducting underwriting discounts and commissions and other offering expenses, through the issuance and sale of 2,822,500 shares of common stock in a follow-on public offering, including shares sold pursuant to the underwriters exercise of their option to purchase additional shares of common stock.

In June 2016, the Company closed an underwritten public offering in which the Company sold, an aggregate of 2,760,000 shares of common stock, including 360,000 shares sold in connection with the exercise in full by the underwriter of its option to purchase additional shares. The net proceeds of the offering, including the full exercise of the option, were approximately $12.6 million, after deducting the underwriting discounts and commissions and the other offering expenses payable by the Company.

In February 2017, the Company closed an underwritten public offering in which we sold, 2,555,555 shares of its common stock, including 333,333 shares sold in connection with the exercise in full by the underwriters of their option to purchase additional shares. The net proceeds of the offering, including the full exercise of the option, were approximately $10.5 million, after deducting the underwriting discounts and commissions and the other estimated offering expenses payable by Aldeyra.

In addition, as discussed in Note 7, the Company entered into its credit facility (the Credit Facility) in April 2012 and it has been subsequently amended to make term loans in a principal amount of up to $5,000,000 available to the Company with proceeds to be used first to refinance outstanding loans from Pacific Western, second to fund expenses related to the Company s clinical trials, and the remainder for general working capital purposes. The term loans are to be made available to the Company upon the following terms: (i) $2,000,000 was made available on November 10, 2014; and (ii) $3.0 million (the Tranche B Loan) which was made available to the Company in May 2016 following the satisfaction of certain conditions, including receipt of positive phase 2 data in noninfectious anterior uveitis. Each term loan accrues interest from its date of issue at a variable annual interest rate equal to the greater of 2.0% plus prime or 5.25% per annum. In November 2016, the Company amended its Credit Facility such that any term loan the Company may draw is payable as interest-only prior to November 2017 and thereafter is payable in monthly installments of principal plus accrued interest over 36 months. The Credit Facility is collateralized by the Company s assets, including its intellectual property.

The Company s management believes that its currently available resources, including the funds from the February 2017 public offering and amounts available under the Credit Facility, will provide sufficient funds to enable the Company to meet its obligations into at least the third quarter of 2018 based on its current business plan. The Company will need to raise additional capital to implement its near-term business plan. Additional funding may not be available to the Company on acceptable terms, or at all. If the Company is unable to secure additional capital, or meet financial covenants that could be implemented under the Company s term loans in certain circumstances, it will be

required to significantly decrease the amount of planned expenditures, and may be required to cease operations.

Curtailment of operations would cause significant delays in the Company s efforts to introduce its products to market, which is critical to the realization of its business plan and the future operations of the Company.

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Use of Estimates The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. The Company evaluates its estimates and assumptions on an ongoing basis. The most significant estimates in the Company s financial statements relate to accruals, including research and development costs, accounting for income taxes and the related valuation allowance and accounting for stock based compensation and the related fair value. Although these estimates are based on the Company s knowledge of current events and actions it may undertake in the future, actual results may ultimately materially differ from these estimates and assumptions.

Segment Information Operating segments are defined as components of an enterprise about which separate discrete information is available for evaluation by the chief operating decision maker, or decision-making group, in deciding how to allocate resources and in assessing performance. The Company views its operations and manages its business in one segment, which is the identification and development of a treatment for diseases related to high levels of aldehydes.

Cash and Cash Equivalents The Company classifies all highly liquid investments with original maturities of three months or less as cash equivalents and all highly liquid investments with original maturities of greater than three months but less than 12 months as current marketable securities. The Company has a policy of making investments only with commercial institutions that have at least an investment grade credit rating. The Company invests its cash primarily in reverse repurchase agreements (RRAs), government securities and obligations, and money market funds.

RRAs are collateralized by deposits in the form of Government Securities and Obligations for an amount not less than 102% of their value. The Company does not record an asset or liability related to the collateral as the Company is not permitted to sell or repledge the associated collateral. The Company has a policy that the collateral has at least an A (or equivalent) credit rating. The Company utilizes a third party custodian to manage the exchange of funds and ensure that collateral received is maintained at 102% of the value of the RRAs on a daily basis. RRAs with original maturities of greater than three months are classified as marketable securities.

Marketable Securities Marketable securities consist of government securities and obligations with original maturities of more than 90 days. Investments are classified as available-for-sale and are recorded on the balance sheet at fair value with unrealized gains or losses reported as a separate component of other comprehensive income/(loss). Management determines the appropriate classification of its investments at the time of purchase and re-evaluates such determination at each balance sheet date.

Fair Value of Financial Instruments Financial instruments including cash equivalents and accounts payable are carried in the financial statements at amounts that approximate their fair value based on the short maturities of those instruments. The carrying amount of the Company s term loans under its credit facility approximates market rates currently available to the Company. Marketable securities are carried at fair value and are more fully described in Note 5.

Concentration of Credit Risk Financial instruments that potentially subject us to significant concentrations of credit risk principally consist of cash, cash equivalents and marketable securities. We place our cash and cash equivalents and marketable securities with financial institutions with high credit ratings. As part of our cash and investment management processes, we perform periodic evaluations of the credit standing of the financial institutions with whom we maintain deposits, and have not recorded any credit losses to-date.

Intellectual Property The legal and professional costs incurred by the Company to acquire its patent rights are expensed as incurred and included in operating expenses. At December 31, 2016 and 2015, the Company has

determined that these expenses have not met the criteria to be capitalized. Intellectual property related expenses for the years ended December 31, 2016 and 2015 were $553,871 and $473,878, respectively.

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Income Taxes The Company follows the provisions of FASB ASC 740, *Income Taxes*, in reporting deferred income taxes. ASC 740 requires a company to recognize deferred tax liabilities and assets for expected future income tax consequences of events that have been recognized in the Company s financial statements. Under this method, deferred tax assets and liabilities are determined based on temporary differences between financial statement carrying amounts and the tax basis of assets and liabilities using enacted tax rates in the years in which the temporary differences are expected to reverse. Valuation allowances are provided if based on the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

The Company accounts for uncertain tax positions pursuant to ASC 740 which prescribes a recognition threshold and measurement process for financial statement recognition of uncertain tax positions taken or expected to be taken in a tax return. If the tax position meets this threshold, the benefit to be recognized is measured as the tax benefit having the highest likelihood of being realized upon ultimate settlement with the taxing authority. The Company recognizes interest accrued related to unrecognized tax benefits and penalties in the provision for income taxes. Management is not aware of any uncertain tax positions.

Research and Development Costs Research and development costs are charged to expense as incurred. Research and development expenses include consulting expenses, preclinical studies, clinical trials, clinical trial materials, regulatory and clinical consultants, lab supplies, lab services, lab equipment maintenance, non-refundable license fees and small equipment purchased to support the research laboratory. Research and development costs that are paid in advance of performance are capitalized as a prepaid expense until incurred.

Stock-Based Compensation Stock-based payments are accounted for in accordance with the provisions of ASC 718, *Compensation Stock Compensation*. For options, the fair value of stock-based payments is estimated, on the date of grant, using the Black-Scholes option pricing model. For restricted stock, fair value is based on the fair value of the stock on the date of grant. The resulting fair value for restricted stock and options expected to vest is recognized on a straight-line basis over the requisite service period, which is generally the vesting period of the applicable restricted stock or option.

Equity instruments issued to nonemployees are accounted for under the provisions of ASC 718 and ASC 505-50, *Equity Equity-Based Payments to Non-Employees*. Accordingly, the estimated fair value of the equity instrument is recorded on the earlier of the performance commitment date or the date the services are completed and are marked to market through the date of vesting.

From time to time the Company may grant awards with performance conditions necessary to be achieved in order to vest in the award. The Company records compensation expense for those awards over the vesting period of the award to the extent the performance conditions are deemed probable of achievement.

From time to time the Company may grant awards with a market condition necessary to be achieved in order to vest in the award. The Company records compensation expense for those awards over the vesting period of the award on a straight-line basis utilizing Monte Carlo simulations to estimate the timing and number of shares that are most likely to vest.

Comprehensive Loss Comprehensive loss is defined as the change in equity during a period from transactions and other events and/or circumstances from non-owner sources. For December 31, 2016, comprehensive loss is equal to the Company s net loss of $18.7 million and an unrealized gain on marketable securities of $8,490. For December 31, 2015, comprehensive loss is equal to net loss of $12.1 million and an unrealized loss on marketable securities of $(8,361).

Net Loss Per Share

Basic net loss per share available to common stockholders is calculated by dividing the net loss available to common stockholders by the weighted-average number of common shares outstanding during the period, without consideration for common stock equivalents. Diluted net loss per share available to common

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stockholders is computed by dividing the net loss available to common stockholders by the weighted-average number of common share equivalents outstanding for the period determined using the treasury-stock method. For purposes of this calculation, stock options, restricted stock units and common stock warrants are considered to be common stock equivalents and are only included in the calculation of diluted net loss per share available to common stockholders when their effect is dilutive.

Recent Accounting Pronouncements

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-15 (ASU 2016-15), Statement of Cash Flows. The standard is intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, with early adoption permitted. ASU 2016-15 may be adopted retrospectively or prospectively if it is impractical to apply the amendments retrospectively. The Company does not expect this standard to have a material impact on its financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instrument-Credit Losses (ASU 2016-13). ASU 2016-13 requires a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019. The Company does not expect this standard to have a material impact on its financial statements.

In March 2016, the FASB issued ASU No. 2016-09 Improvements to Employee Share-Based Payment Accounting (ASU 2016-09), to simplify the accounting for stock compensation. This update focuses on income tax accounting, award classification, estimating forfeitures, and cash flow presentation. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016. The Company does not expect this standard to have a material impact on its financial statements.

In February 2016, the FASB issued ASU No. 2016-02 (ASU 2016-02), Leases. ASU 2016-02 requires lessees to recognize on the balance sheet a right-of-use asset, representing its right to use the underlying asset for the lease term, and a lease liability for all leases with terms greater than 12 months. The guidance also requires qualitative and quantitative disclosures designed to assess the amount, timing, and uncertainty of cash flows arising from leases. The standard requires the use of a modified retrospective transition approach, which includes a number of optional practical expedients that entities may elect to apply. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018. The Company does not expect this standard to have a material impact on its financial statements.

In January 2016, the FASB issued ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities (ASU 2016-01). ASU 2016-01 amends the guidance on the classification and measurement of financial instruments. Although ASU 2016-01 retains many current requirements, it significantly revises accounting related to the classification and measurement of investments in equity securities and the presentation of certain fair value changes for financial liabilities measured at fair value. ASU 2016-01 also amends certain disclosure requirements associated with the fair value of financial instruments and is effective for fiscal years beginning after December 15, 2017. The Company does not expect this standard to have a material impact on its financial statements.

In November 2015, the FASB issued ASU No. 2015-17, Income Taxes (ASU 2015-17). ASU 2015-17 simplifies the presentation of deferred income taxes by requiring that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in

ASU 2015-17. ASU 2015-17 is effective for fiscal years beginning after December 15, 2016. The Company does not expect this standard to have a material impact on its financial statements.

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In April 2015, the FASB issued ASU No. 2015-03, Simplifying the Presentation of Debt Issuance Costs (ASU 2015-03). The amendments in ASU 2015-03 require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 is effective for fiscal years beginning after December 15, 2016. The Company does not expect this standard to have a material impact on its financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes the revenue recognition requirements in ASC 605, Revenue Recognition. This ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. ASU 2014-09 is effective for fiscal years beginning after December 15, 2017. The Company does not expect this standard to have a material impact on its financial statements.

3. NET LOSS PER SHARE

The following table summarizes the computation of basic and diluted net loss per share:

	Years ended December 31,	
	2016	2015
Net loss basic and diluted	$ (18,699,450)	$ (12,090,287)
Weighted-average number of common shares basic and diluted	11,352,230	8,633,897
Net loss per share basic and diluted	$ (1.65)	$ (1.40)

The following potentially dilutive securities outstanding, prior to use of the treasury stock method, have been excluded from the computation of diluted weighted-average shares outstanding, because such securities had an antidilutive impact:

	Years ended December 31,	
	2016	2015
Options to purchase common stock	1,498,585	1,077,330
Warrants to purchase common stock	1,384,608	1,384,608
Restricted stock units	27,096	
Total of common stock equivalents	2,910,289	2,461,938

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4. CASH, CASH EQUIVALENTS AND MARKETABLE SECURITIES

At December 31, 2016, cash, cash equivalents and marketable securities were comprised of:

	Carrying Amount	Unrecognized Gain	Unrecognized Loss	Estimated Fair Value	Cash Equivalents	Current Marketable Securities
Cash	$ 394,849	$	$	$ 394,849	$ 394,849	$
Money market funds	70,212			70,212	70,212	
U.S. reverse repurchase agreements	11,550,000			11,550,000	11,550,000	
U.S. government agency securities	12,897,455	1,396	(1,267)	12,897,584		12,897,584
Available for Sale(1)	24,447,455	1,396	(1,267)	24,447,584	11,550,000	12,897,584
Total Cash, cash equivalents and current marketable securities					$ 12,015,061	$ 12,897,584

(1) Available for sale securities are reported at fair value with unrealized gains and losses reported net of taxes in other comprehensive income.

Fair value of government securities and obligations and corporate debt securities were estimated using quoted broker prices and significant other observable inputs.

The contractual maturities of all available for sale securities are less than one year at December 31, 2016.

5. FAIR VALUE MEASUREMENTS

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value are performed in a manner to maximize the use of observable inputs and minimize the use of unobservable inputs. ASC 820, *Fair Value Measurements*, establishes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value, which are the following:

Level 1 Quoted prices in active markets that are accessible at the market date for identical unrestricted assets or liabilities.

Level 2 Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs for which all significant inputs are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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There were no liabilities measured at fair value at December 31, 2016 or 2015, respectively.

	December 31, 2016			
	Level 1	Level 2	Level 3	Total
Assets:				
Money market funds	$ 70,212	$	$	$ 70,212
U.S. reverse repurchase agreements		11,550,000		11,550,000
U.S. government agency securities		12,897,584		12,897,584
Total assets at fair value	$ 70,212	$ 24,447,584	$	$ 24,517,796

	December 31, 2015			
	Level 1	Level 2	Level 3	Total
Assets:				
Money market funds	$ 35,886	$	$	$ 35,886
U.S. reverse repurchase agreements		12,950,000		12,950,000
U.S. government agency securities		12,941,776		12,941,776
Total assets at fair value	$ 35,886	$ 25,891,776	$	$ 25,927,662

Financial instruments including cash equivalents and accounts payable are carried in the financial statements at amounts that approximate their fair value based on the short maturities of those instruments. The carrying amount of the Company s term loans under its credit facility approximates market rates currently available to the Company. Marketable securities are carried at fair value.

6. ACCRUED EXPENSES

Accrued expenses at December 31, 2016 and 2015 were:

	2016	2015
Accrued compensation	$ 983,449	$ 413,172
Accrued research and development	913,838	574,742
Accrued general & administrative	48,964	198,515
Accrued expenses	$ 1,946,251	$ 1,186,429

7. CREDIT FACILITY

The Company s long-term debt obligation consists of amounts the Company is obligated to repay under its Credit Facility with Pacific Western, of which $1.4 million was outstanding as of December 31, 2016. The Company entered

into the Credit Facility in April 2012 and it has been subsequently amended to make term loans in a principal amount of up to $5,000,000 available to the Company with proceeds to be used first to refinance outstanding loans from Pacific Western, second to fund expenses related to its clinical trials, and the remainder for general working capital purposes. The term loans are to be made available upon the following terms: (i) $2,000,000 was made available on November 10, 2014; and (ii) $3.0 million (the Tranche B Loan) which was made available to the Company in May 2016 following the satisfaction of certain conditions, including receipt of positive phase 2 data in noninfectious anterior uveitis. Each term loan accrues interest from its date of issue at a variable annual interest rate equal to the greater of 2.0% plus prime or 5.25% per annum. In November 2016, we amended our Credit Facility such that any term loan the Company draws is payable as interest-only prior to November 2017 and thereafter is payable in monthly installments of principal plus accrued interest over 36 months.

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The Credit Facility is collateralized by the Company s assets, including its intellectual property. As of December 31, 2016, $1.4 million was outstanding under the Credit Facility. Future maturities of the existing term loans under the Credit Facility as of December 31, 2016 are as follows:

2017	$ 77,546
2018	465,278
2019	465,278
2020	387,731
Total	$ 1,395,833

In conjunction with obtaining the November 2013 amended credit facility, the Company issued a warrant exercisable for 9,692 shares of Series B Preferred Stock with an exercise price of $5.16 per share and a term of seven years (Note 12). The warrant was valued at $178,000 and, together with the fair value of the warrant issued in connection with the April 12, 2012 Credit Facility ($88,000), was recorded as a discount on the Credit Facility. These discounts are being amortized using the effective interest method through the current maturity date of the Credit Facility in November 2018. All amendments to the credit facility were determined to be modifications in accordance with ASC 470, *Debt* and did not result in extinguishment.

At December 31, 2016 and 2015, the Credit Facility is shown net of a remaining debt discount of $80,000 and $107,000, respectively.

8. INCOME TAXES

No provision for federal and state taxes has been recorded as the Company has incurred losses since inception for tax purposes. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

In assessing the realizability of net deferred taxes in accordance with ASC 740, *Income Taxes*, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Based on the weight of available evidence, primarily the incurrence of net losses since inception, anticipated net losses in the near future, reversals of existing temporary differences and expiration of various federal and state attributes, the Company does not consider it more likely than not that some or all of the net deferred taxes will be realized. Accordingly, a 100% valuation allowance has been applied against net deferred taxes.

As of December 31, 2016, the Company had Federal and State income tax net operating loss (NOL) carryforwards of approximately $42.8 million and $39.9 million, respectively, which will expire at various dates through 2036. As of December 31, 2016, the Company had Federal and State research and development tax credit carryforwards of approximately $1.2 million and $178,000, respectively, which will expire at various dates through 2036.

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Significant components of the Company s deferred tax assets and liabilities at December 31, 2016 and 2015 are as follows:

	12/31/2016	12/31/2015
Deferred Tax Assets		
Federal & State NOL carryforward	$ 16,669,295	$ 10,115,458
Federal & State R&D credit carryforward	1,271,891	667,688
Intangibles net	700,215	932,060
Accounts payable and accrued expenses	772,841	591,843
Stock options	2,399,666	2,152,854
Fixed assets net	3,861	213
Gross deferred tax assets	21,817,769	14,460,116
Valuation Allowance US	(21,786,477)	(14,418,095)
Net Deferred Tax Assets	31,292	42,021
Deferred Tax Liabilities		
Note Discounts	(31,292)	(42,021)
Gross deferred tax liabilities	(31,292)	(42,021)
TOTAL	$	$

The change in valuation allowance of $7.4 million from December 31, 2015 to December 31, 2016 is driven by no tax benefit being recorded on the current year loss from operations.

Under Section 382 of the Internal Revenue Code of 1986, as amended (Code), a corporation that undergoes an ownership change is subject to limitations on its ability to utilize its pre-change net operating losses (NOLs) and certain other tax assets (tax attributes) to offset future taxable income. In general, an ownership change occurs if the aggregate stock ownership of certain stockholders increases by more than 50 percentage points over such stockholders lowest percentage ownership during the testing period (generally three years). Transactions involving the Company s common stock, even those outside the Company s control, such as purchases or sales by investors, within the testing period could result in an ownership change. A limitation on the Company s ability to utilize some or all of its NOLs or credits could have a material adverse effect on the Company s results of operations and cash flows. Prior to 2016, Aldeyra underwent two ownership changes and it is possible that additional ownership changes have occurred since. However, the Company s management believes that it has sufficient Built-In-Gain to offset the Section 382 of the Code limitation generated by such ownership changes. Any future ownership changes, including those resulting from the Company s recent or future financing activities, may cause the Company s existing tax attributes to have additional limitations.

All tax years are open for examination by the taxing authorities for both federal and state purposes.

A reconciliation of the federal statutory tax rate of 34% to the Company s effective income tax rates are as follows:

	Years ended December 31,	
	2016	2015
Statutory tax rate	34.00%	34.00%
State taxes, net of federal benefits	5.24%	5.22%
Federal research and development credits	2.84%	1.92%
Change in valuation allowance	(39.42)%	(40.10)%
Stock-based compensation	(2.63)%	0.00%
Other	(0.03)%	(1.04)%
Effective tax rate	0.00%	0.00%

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The Company accounts for uncertain tax positions pursuant to ASC 740 which prescribes a recognition threshold and measurement process for financial statement recognition of uncertain tax positions taken or expected to be taken in a tax return. If the tax position meets this threshold, the benefit to be recognized is measured as the tax benefit having the highest likelihood of being realized upon ultimate settlement with the taxing authority. The Company recognizes interest accrued related to unrecognized tax benefits and penalties in the provision for income taxes. Management is not aware of any uncertain tax positions.

9. STOCK INCENTIVE PLAN

The Company has three incentive plans. One was adopted in 2004 (2004 Plan) and provided for the granting of stock options and restricted stock awards and generally prescribed a contractual term of seven years. The 2004 Plan terminated in August 2010. However, grants made under the 2004 Plan are still governed by that plan. As of December 31, 2016, options to purchase 23,954 shares of common stock at a weighted average exercise price of $3.24 per share remained outstanding under the 2004 Plan.

The Company approved the 2010 Employee, Director and Consultant Equity Incentive Plan (2010 Plan) in September 2010 to replace the 2004 Plan. The 2010 Plan provided for the granting of stock options and restricted stock awards. The 2010 Plan terminated upon the Initial Public Offering. However, grants made under the 2010 Plan are still governed by that plan. As of December 31, 2016, options to purchase 489,846 shares of common stock at a weighted average exercise price of $1.58 per share remained outstanding under the 2010 Plan.

The Company approved the 2013 Equity Incentive Plan (2013 Plan) in October 2013. The 2013 Plan became effective immediately on adoption although no awards were to be made under it until the effective date of the Registration Statement for the Initial Public Offering. The 2013 Plan provides for the granting of stock options, restricted stock, stock appreciation rights, stock units, and performance cash awards to certain employees, members of the board of directors and consultants of the Company. As of December 31, 2015, the number of shares of common stock authorized for issuance in connection with the 2013 Plan was 847,614. On January 1 of each year the aggregate number of common shares that may be issued under the Plan shall automatically increase. As of January 1, 2016, the number of shares of common stock that may be issued under the 2013 Plan was automatically increased by 333,333 shares. In June 2016, the 2013 Plan was amended to provide an increase of 700,000 shares of common stock authorized for issuance increasing the number of shares of common stock available for issuance under the 2013 Plan to 1,880,950 shares and that the annual increase would equal a number of shares equal to the least of (a) 7% of the total number of common shares outstanding on the last calendar day of the prior fiscal year, (b) subject to adjustment for certain corporate transactions, 1,000,000 common shares, or (c) a number of common shares determined by the Company s board of directors. As of December 31, 2016, options to purchase 984,786 shares of common stock at a weighted average exercise price of $6.18 per share and restricted stock units of 27,096 remained outstanding under the 2013 Plan. As of December 31, 2016, there were 869,068 shares of common stock available for grant under the 2013 Plan. As of January 1, 2017, the number of shares of common stock that may be issued under the 2013 Plan was automatically increased by 880,343 shares, increasing the number of shares of common stock available for issuance under the 2013 Plan to 2,761,293.

Terms of stock award agreements, including vesting requirements, are determined by the board of directors, subject to the provisions of the respective plan they were granted. Options granted by the Company typically vest over a four year period. Certain of the options are subject to acceleration of vesting in the event of certain change of control transactions. The options may be granted for a term of up to ten years from the date of grant. The exercise price for options granted under the 2013 Plan must be at a price no less than 100% of the fair market value of a common share on the date of grant.

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The Company recognizes stock-based compensation expense over the requisite service period. The Company s share-based awards are accounted for as equity instruments. The amounts included in the consolidated statements of operations relating to stock-based compensation are as follows:

	Year ended December 31,	
	2016	2015
Research and development expenses	$ 1,167,142	$ 841,289
General and administrative expenses	1,592,611	1,345,813
Total stock-based compensation expense	$ 2,759,753	$ 2,187,102

The following table summarizes option activity under the incentive plans for the years ended December 31, 2016 and 2015:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Contractual Term	Aggregate Intrinsic Value(a)
Outstanding at December 31, 2015	1,077,330	$ 3.98		
Granted	759,314	5.43		
Cancelled	(63,096)	4.85		
Forfeited	(171,159)	6.30		
Exercised	(103,804)	0.88		463,604
Outstanding at December 31, 2016	1,498,585	$ 4.63	7.86	$ 2,185,696
Exercisable at December 31, 2016	802,532	$ 2.34	7.10	$ 1,874,659

(a) The aggregate intrinsic value in this table was calculated on the positive difference, if any, between the closing market value of our common stock on December 31, 2016 of $5.35 and the price of the underlying options.

The Company records stock-based compensation related to stock options granted at fair value. During the years ended December 31, 2016 and 2015, the Company used the Black-Scholes option-pricing model to estimate the fair value of stock option grants and to determine the related compensation expense. The assumptions used in calculating the fair value of stock-based payment awards represent management s best estimates. The weighted-average fair value of options granted was $ 5.43 and $7.78 for the years ended December 31, 2016 and 2015, respectively. The assumptions used in determining fair value of the employee stock options for the years ended December 2016 and 2015, are as follows:

	December 31, 2016	December 31, 2015

Expected dividend yield	0%	0%
Anticipated volatility	88.57%	88.57%
Estimated stock price	$ 3.94 - $7.48	$ 7.19 - $8.37
Exercise price	$ 3.94 - $7.48	$ 7.19 - $8.37
Expected life (years)	5.50 - 6.25	5.50 - 6.25
Risk free interest rate	0.59% - 2.20%	0.27% - 1.91%

The dividend yield of zero is based on the fact that the Company has never paid cash dividends and have no present intention to pay cash dividends. Expected volatility is based on the historical volatility of a group of similar companies. The Company has also computed the historical volatility of the Company s historical information regarding the volatility of its stock price and has determined that a volatility estimate of 89% is reasonable. The Company has estimated the expected life of our employee stock options using the simplified method, whereby, the expected life equals the average of the vesting term and the original contractual term of the option for service-based awards since the Company doesn t have sufficient historical

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or implied data of its own. The risk-free interest rates for periods within the expected life of the option are based on the yields of zero-coupon United States Treasury securities.

At December 31, 2016, there is approximately $3.2 million of unrecognized compensation cost relating to stock options outstanding, which the Company expects to recognize over a weighted average period 2.11 years. Total unrecognized compensation cost will be adjusted for future forfeitures, if necessary.

Restricted Stock Units

Restricted stock units are not included in issued and outstanding common stock until the shares are vested and released. During the year ended December 31, 2016, the Company granted a restricted stock unit award for 27,096 underlying shares of common stock with a weighted-average grant date fair value of $6.33 per share. As of December 31, 2016, the outstanding restricted stock units had unamortized stock-based compensation of $134,281 with a weighted-average remaining recognition period of 3.33 years and no aggregate intrinsic value.

Employee Stock Purchase Plan

In March 2016, the Company s Board of Directors approved the 2016 Employee Stock Purchase Plan (2016 ESPP), which became effective in June 2016 following the approval of the Company s stockholders. The 2016 ESPP authorizes the initial issuance of up to a total of 97,500 shares of the Company s common stock to participating employees. The number of shares reserved for issuance under the 2016 ESPP automatically increases on the first business day of each fiscal year, commencing in 2017, by a number equal to the lesser of (i) 1% of the shares of common stock outstanding on the last business day of the prior fiscal year; or (ii) the number of shares determined by the Company s Board of Directors. Unless otherwise determined by the administrator of the 2016 ESPP, two offering periods of six months duration will begin each year on January 1 and July 1. As of December 31, 2016, there was no activity under the 2016 ESPP. On January 1, 2017, the number of shares available for issuance under the 2016 ESPP was automatically increased by 125,763 shares, increasing the number of shares of common stock available for issuance under the 2016 ESPP to 223,263.

10. STOCK PURCHASE WARRANTS

On January 14, 2015, the Company sold, in a private placement, an aggregate of approximately 1.1 million shares of common stock at a price of $7.00 per share. Investors received warrants to purchase up to approximately 1.1 million shares of common stock at an exercise price of $9.50. The Company raised approximately $7.1 million in net proceeds in the private placement of common stock and warrants. Additionally, on January 21, 2015, in a subsequent private placement, the Company sold an aggregate of 211,528 shares of common stock at a price of $9.33 per share and a warrant to purchase up to 211,528 shares of common stock at a price of $0.125 per share subject to the warrant. The Company raised approximately $1.9 million in net proceeds in the private placement of common stock and a warrant to purchase common stock. In both transactions, the exercise price of the warrants is $9.50 per share. The warrants will expire 3 years from their respective date of issuance. The warrants do not include a net-exercise feature. The warrants may be redeemed by the Company at a price of $0.001 per share upon notice to the holders thereof in the event that the closing bid for Aldeyra s common stock for each of the fifteen consecutive trading days prior to such redemption is at least $20.00 per share and the average trading volume of Aldeyra s common stock during such period is at least 50,000 shares per day. Following Aldeyra s notification to the warrant holders of its exercise of the redemption right under the warrants, the warrant holders will have the option to exercise the warrants prior to the redemption date rather than having them redeemed.

In connection with the Initial Public Offering, the Company issued the underwriters of the offering warrants to purchase up to 60,000 shares of common stock. The warrants are exercisable beginning on May 1, 2015 for cash or on a cashless basis at a per share price of $10.00. The warrants will expire on May 1, 2019.

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All of the warrants above were outstanding at December 31, 2016.

11. COMMITMENTS AND CONTINGENCIES

Guarantees and Indemnifications As permitted under Delaware law, the Company indemnifies its officers and directors for certain events or occurrences while the officer or director is, or was, serving at the Company s request in such capacity. The term of the indemnification is for the officer s or director s lifetime. Through December 31, 2016, the Company had not experienced any losses related to these indemnification obligations and no material claims were outstanding. The Company does not expect significant claims related to these indemnification obligations, and consequently, concluded that the fair value of these obligations is negligible, and no related reserves were established.

Other Contractual Arrangements During the year ended December 31, 2014, the Company entered into a lease agreement for a certain commercial office space. The thirty-seven month lease which began in September 2014 provides the Company with approximately 3,700 square feet of space in Lexington, Massachusetts. Base annual rent is initially set at $5,604 per month. Total base rent payable over the lease period is approximately $205,000. In March 2016, the Company entered into a sublease for approximately 3,188 additional square feet of office space to expand its headquarters in Lexington, Massachusetts. The sublease expires in September 2017. The sublease provides for the payment of annual base rent in the amount of $67,000 payable in monthly installments and the requirement to pay certain operating expenses, taxes and other fees in accordance with the terms of the master lease.

The Company s gross future minimum payments under all non-cancelable operating leases as of December 31, 2016, are $107,195 for the year ending December 31, 2017.

12. SUBSEQUENT EVENT

In February 2017, the Company closed an underwritten public offering in which it sold, 2,555,555 shares of its common stock, including 333,333 shares sold in connection with the exercise in full by the underwriters of their option to purchase additional shares. The net proceeds of the offering, including the full exercise of the option, were approximately $10.5 million, after deducting the underwriting discounts and commissions and the other estimated offering expenses payable by Aldeyra.

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EXHIBIT INDEX

Exhibit Number	Exhibit Title
3.1	Restated Certificate of Incorporation of Registrant, (filed as Exhibit 3.1 to the Registrant s Current Report on Form 8-K as filed on May 7, 2014, and incorporated herein by reference)
3.2	Amended and Restated Bylaws of the Registrant (filed as Exhibit 3.1 to the Registrant s Current Report on Form 8-K as filed on May 7, 2014, and incorporated herein by reference)
4.1	Specimen stock certificate evidencing the shares of common stock (filed as Exhibit 4.1 to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)
4.2	Investor Rights Agreement dated as of December 20, 2012 (filed as Exhibit 4.2 to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)
4.3	Form of Representative s Warrant Agreement (filed as Exhibit 4.3 to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)
4.4	Form of Warrant to Purchase Common Stock of Aldeyra Therapeutics, Inc. (filed as Exhibit 4.4 to the Registrant s Current Report on Form 8-K as filed on January 15, 2015, and incorporated herein by reference)
4.5	Form of Warrant to Purchase Common Stock of Aldeyra Therapeutics, Inc. (filed as Exhibit 4.5 to the Registrant s Current Report on Form 8-K as filed on January 22, 2015, and incorporated herein by reference)
10.1	Form of Indemnity Agreement for Directors and Officers (filed as Exhibit 10.1 to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)
10.2	Offer Letter, effective as of August 1, 2013, between the Registrant and Todd C. Brady, M.D., Ph.D. (filed as Exhibit 10.2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on January 7, 2014, and incorporated herein by reference)
10.4	Offer Letter, effective November 29, 2013 between the Registrant and Todd C. Brady, M.D., Ph.D. (filed as Exhibit 10.4 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on January 7, 2014, and incorporated herein by reference)
10.4(a)	Offer Letter Amendment, effective February 19, 2014 between the Registrant and Todd C. Brady, M.D., Ph.D. (filed as Exhibit 10.4(a) to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)
10.6	2004 Employee, Director and Consultant Stock Plan, as amended, and form of option agreement thereunder (filed as Exhibit 10.6 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on January 7, 2014, and incorporated herein by reference)
10.7	

	2010 Employee, Director and Consultant Equity Incentive Plan, as amended, and form of option agreement thereunder (filed as Exhibit 10.7 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on January 7, 2014, and incorporated herein by reference)
10.8	2013 Equity Incentive Plan and form of option agreement thereunder (filed as Exhibit 10.8 to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)

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Exhibit Number	Exhibit Title
10.8.(a)	Form Notice of Stock Option Grant under the 2013 Equity Incentive Plan (filed as Exhibit 10.8(a) to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)
10.8(b)	Form Notice of Stock Unit Award under the 2013 Equity Incentive Plan (filed as Exhibit 10.8(b) to Amendment No. 2 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on March 17, 2014, and incorporated herein by reference)
10.9	Loan and Security Agreement, dated as of April 12, 2012, between Square 1 Bank and the Registrant (filed as Exhibit 10.11 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on January 7, 2014, and incorporated herein by reference)
10.10	Amendment No. 1 to Loan and Security Agreement, date as of November 20, 2013 between Square 1 Bank and the Registrant (filed as Exhibit 10.12 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on January 7, 2014, and incorporated herein by reference)
10.11	Amendment No. 1 to Loan and Security Agreement, date as of November 20, 2013 between Square 1 Bank and the Registrant (filed as Exhibit 10.13 to the Registrant s Registration Statement on Form S-1 (SEC File No. 333-193204), as filed on January 7, 2014, and incorporated herein by reference)
10.12	Offer Letter dated June 13, 2014 between the Registrant and Stephen Tulipano (filed as Exhibit 10.14 to the Registrant s Quarterly Report on Form 10-Q for the quarter ended June 30, 2014 (as filed on August 7, 2014, and incorporated herein by reference))
10.13	Sublease dated August 18, 2014 between the Registrant and MacLean Power L.L.C. (filed as Exhibit 10.15 to the Registrant s Quarterly Report on Form 10-Q for the quarter ended September 30, 2014 (as filed on November 12, 2014, and incorporated herein by reference))
10.14	Second Amendment to Loan and Security Agreement, dated as of November 7, 2014, between Square 1 Bank and the Registrant (filed as Exhibit 10.2 to the Registrant s Current Report on Form 8-K as filed on November 7, 2014, and incorporated herein by reference)
10.15	Form of Purchase Agreement dated January 12, 2015 (filed as Exhibit 10.42 to the Registrant s Current Report on Form 8-K as filed on January 13, 2015, and incorporated herein by reference)
10.16	Form of Registration Rights Agreement, dated as of January 14, 2015 (filed as Exhibit 10.43 to the Registrant s Current Report on Form 8-K as filed on January 15, 2015, and incorporated herein by reference)
10.17	Form of Purchase Agreement dated January 20, 2015 (filed as Exhibit 10.44 to the Registrant s Current Report on Form 8-K as filed on January 20, 2015, and incorporated herein by reference)
10.18	Form of Registration Rights Agreement, dated as of January 21, 2015 (filed as Exhibit 10.45 to the Registrant s Current Report on Form 8-K as filed on January 22, 2015, and incorporated herein by reference)
10.19	Third Amendment to Loan and Security Agreement, dated as of March 18, 2015, between Pacific Western Bank and the Registrant. (filed as Exhibit 10.21 to the Registrant s Quarterly Report on Form 10-Q for the quarter ended March 31, 2015 (as filed on May 14, 2015, and incorporated herein by reference))
10.20	Fourth Amendment to Loan and Security Agreement, dated as of November 9, 2015, between Pacific Western Bank and the Registrant. (filed as Exhibit 10.21 to the Registrant s Quarterly Report on Form

10-Q for the quarter ended September 30, 2015 (as filed on November 13, 2015, and incorporated herein by reference))

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Exhibit Number	Exhibit Title
10.21*	Fifth Amendment to Loan and Security Agreement, dated as of December 1, 2016, between Pacific Western Bank and the Registrant
10.22	Offer Letter between the Registrant and David J. Clark, M.D. dated December 15, 2015 (filed as Exhibit 10.23 to the Registrant s Annual Report on Form 10-K for the fiscal year ended December 31, 2015 (as filed on March 30, 2016, and incorporated herein by reference))
10.23	Sublease dated as of March 7, 2016 between Planck, LLC and the Registrant and Master Lease dated June 3, 2014 between WLC Three VI, L.L.C. and Plank, LLC (filed as Exhibit 10.23 to the Registrant s Annual Report on Form 10-K for the fiscal year ended December 31, 2015 (as filed on March 30, 2016, and incorporated herein by reference))
10.24	Aldeyra Management Cash Incentive Plan (filed as Exhibit 10.25 to the Registrant s Current Report on Form 8-K as filed on March 18, 2016, and incorporated herein by reference)
10.25 *	Aldeyra Therapeutics, Inc. Change in Control Plan
23.1*	Consent of BDO USA, LLP, independent registered public accounting firm
31.1*	Certification of the Chief Executive Officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	Certification of the Chief Financial Officer as required by Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certifications of the Chief Executive Officer and Chief Financial Officer as required by 18 U.S.C. 1350
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

Compensation Arrangement.
Confidential treatment has been granted with respect to certain portions of this document.
* Filed herewith.

Additionally, we own a large oceangoing pushboat, the Argos I, and two container feeder vessels, the M.V. Asturiano and the M.V. Argentino. Our current ocean fleet has an aggregate cargo carrying capacity of near 110,000 dwt and an average age of approximately 14 years.

We have pursued the expansion of our ocean fleet by participating in the container feeder service. Through the acquisition of the M.V. Asturiano and M.V. Argentino during 2010, we began operating in such a market. The first vessel to commence service was the M.V. Asturiano, on May 21, 2010, while the M.V. Argentino commenced its operation in Argentina in February 2011. Both vessels serve the regional container transportation requirements between the Argentinean coastal ports south of Buenos Aires and those on the south of Uruguay from mainline large container vessels.

Our four Product Tankers, Miranda I, Alejandrina, Austral and Amadeo are currently employed under time charters with major oil companies serving regional trades in Argentina and Brazil.

Ultrapetrol Fleet Summary (1)

River Fleet	Number of Vessels	Capacity	Description
Alianza G2	1	35,000 tons	Storage and Transshipment Station
Pushboat Fleet	33	127,273 BHP	Various Sizes and Horse Power Carry
Tank Barges	77	183,762 m3	Liquid Cargo (Petroleum Products, Vegetable Oil)
Dry Barges	570	993,270 tons	Carry Dry Cargo (Soy, Iron Ore, other products)
Total (1)	647	N/A	

Offshore Supply Fleet	Year Built	Capacity (DWT)	Deck Area (m2)
In Operation			
UP Esmeralda	2005	4,200	840
UP Safira	2005	4,200	840
UP Agua-Marinha	2006	4,200	840
UP Topazio	2006	4,200	840
UP Diamante	2007	4,200	840
UP Rubi	2009	4,200	840
UP Turquoise	2010	4,900	1,020
UP Jasper	2011	4,900	1,020

Offshore Supply Fleet	Delivery Date (2)	Capacity (DWT)	Deck Area (m2)
Under Construction			
UP Jade (India, V-381)	2012	4,200	840
UP Amber (India,V-382)	2012	4,200	840
UP Pearl (India, V-386)	2012	4,200	840
UP Onyx (India, V-387)	2013	4,200	840
Total		51,800	

Ocean Fleet	Year Built	Capacity (DWT/TEUs)	Description
Parana Petrol (Ex-Al.G3)	1993 (3)	43,164	Inland Tank Barge
Miranda I (5)	1995	6,575	Product / Chemical Tanker
Amadeo (5)	1996	39,530	Oil / Product Tanker
Alejandrina	2006	9,219	Product Tanker
Austral (6)	2006	11,299	Product / Chemical Tanker
Argos I (Ex -Al. Campana)	1975	N/A	Oceangoing Pushboat
M.V. Asturiano	2003	1,118 (4)	Container Feeder Vessel
M.V. Argentino	2002	1,050 (4)	Container Feeder Vessel
Total		110,000 (7)	

(1) As of December 31, 2011.
(2) Expected build or delivery date, as applicable, as advised by the shipyard.
(3) Originally built in 1982, converted in 1993 to product tank barge.

(4) Twenty Foot-Equivalent Units, or TEUs.
(5) Our Miranda I and Amadeo were both converted to double hull in 2007.
(6) Bareboat chartered.
(7) Only DWT capacity added – excludes TEUs.

Chartering Strategy

We continually monitor developments in the shipping industry and make charter-related decisions based on an individual vessel and segment basis, as well as on our view of overall market conditions.

In our River Business, we have contracted a substantial portion of our fleet's barge capacity on a one - to five-year basis to major clients. These contracts typically provide for fixed pricing, minimum volume requirements and fuel price adjustment formulas and we intend to develop new customers and cargoes as we grow our fleet capacity.

In our Offshore Supply Business, we plan to continue chartering our PSV fleet in Brazil and in the North Sea for time charter employment (up to four years). Currently there is no significant spot market in Brazil for PSVs. In the future, we may also decide to employ our PSVs in the North Sea spot market (short duration, one day or more) combined with longer-term charters or in Brazil, either with cabotage privileges or as foreign flagged vessels.

We have historically operated our cabotage Ocean Business tanker vessels under period time charters and will try to continue to do so.

The future minimum revenues, before deduction for brokerage commissions, expected to be received on time charter agreements of our eight PSVs in our Offshore Supply Business (seven chartered in South America and one in the North Sea), which terms are longer than one year were as follows:

Year ending December 31,	(Dollars in thousands)
2012	$ 73,012
2013	22,076
2014	10,623
2015	1,942
2016	--
Total	$ 107,653

The future minimum revenues, before deduction for brokerage commissions of four product tanker vessels (one of them leased) in our Ocean Business chartered in South America, expected to be received on time charter agreements, which original terms are longer than one year were as follows:

Year ending December 31,	(Dollars in thousands)
2012	$ 21,152
2013	13,591
2014	4,965
Total	$ 39,708

Revenues from a time charter are generally not received when a vessel is off-hire, which includes time required for normal periodic maintenance of the vessel including drydock. In arriving at the minimum future charter revenues, an estimated off-hire time to perform periodic maintenance on each vessel has been deducted, although there is no assurance that such estimate will be reflective of the actual off-hire in the future. The scheduled future minimum revenues should not be construed to reflect total shipping revenues for any of the periods.

Our Fleet Management

We conduct the day-to-day management and administration of our operations in-house.

Our subsidiary, Ravenscroft undertakes part of the technical and marine related management for our offshore and ocean vessels including dry docks, repairs and maintenance, the purchasing of supplies, spare parts and husbandry items, crewing, superintendence and preparation and payment of a portion of the related accounts on our behalf through its related offices in Coral Gables, Aberdeen, Buenos Aires and Rio de Janeiro. Ravenscroft is certified for ISM and is also ISO 9001:2008 certified. It holds Documents of Compliance for the management and operation of tankers, PSVs, general cargo vessels and container ships.

Ravenscroft seeks to manage vessels for and on behalf of vessel owners who are not related to us and will actively pursue new business opportunities through Ship Management and Commercial Services Ltd., or SMS, which is our subsidiary dealing with third party ship management.

Competition

River Business

We maintain a leading market share in our River Business. We own the largest fleet of pushboats and barges in the Hidrovia Region. We believe that we have more than twice the number of barges and dwt capacity than our nearest competitor. We compete based on reliability, efficiency and price. Key competitors include Navios South American Logistics, Interbarge and Fluvioalba. In addition, some of our customers, including Archer Daniels Midland, Cargill, Louis Dreyfus and Vale have some of their own dedicated barge capacity, which they can use to transport cargo in lieu of hiring a third party. Our River Business also indirectly competes with other forms of land-based transportation such as truck and rail.

Offshore Supply Business

In our Offshore Supply Business, our main competitors in Brazil are the local offshore companies that own and operate modern PSVs. The largest of these companies are CBO, Wilson Sons and Chouest who currently own a substantial number of modern PSVs and are in the process of building additional units. Also, some of the international offshore companies that own and operate PSVs, such as Tidewater and Maersk, have built Brazilian-flagged PSVs. In the North Sea market, where three of our PSVs operated during 2008 and 2009 and where our UP Jasper is operating today, we actively compete with other large, well established owners and operators such as Gulfmark Offshore, Bourbon and DOF Farstad.

Ocean Business

We face competition in the transportation of crude oil and petroleum products as well as other bulk commodities from other independent ship owners and from vessel operators who primarily charter-in vessels to meet their cargo carrying needs. The charter markets in which our vessels operate are highly competitive. Competition is primarily based on prevailing market charter rates, vessel location and the vessel manager's reputation. Our competitor in crude oil and petroleum products transportation within Argentina and between Argentina and other South American countries, is Antares Naviera S.A. and its affiliated companies. The other major participant in the Argentina / Brazil trade is Transpetro. Transpetro is a subsidiary of Petrobras, our primary customer in Brazil. Navios South American Logistics, who is a competitor in our River operation, also competes in the Argentinean Coastal Tanker market. In other South American trades our main competitors are Naviera Sur Petrolera S.A., Naviera Elcano (through their various subsidiaries) and Sonacol S.A. These companies and other smaller entities are regular competitors of ours in our

primary tanker trading areas.

We operate two container vessels in the Argentinean market to supply the domestic trade between different ports and operate as a feeder service for mainline carriers such as Maersk Line, Evergreen, MOL, MSC, Hamburg Sud, CMA-CGM, PIL and Login for import and export cargoes. Our main competitor in this sector is a local company called Maruba, which currently operates chartered vessels of similar characteristic as ours and that offer a similar service in the market. Our Container Business also indirectly competes with other forms of land-based transportation such as trucks.

Seasonality

Each of our businesses has seasonal aspects, which affect their revenues on a quarterly basis. The high season for our River Business is generally between the months of March and September, in connection with the South American harvest and higher river levels. However, growth in the soy pellet manufacturing, minerals and forest industries may help offset some of this seasonality. The Offshore Supply Business operates year-round, particularly off the coast of Brazil, although weather conditions in the North Sea may reduce activity from December to February. In the Ocean Business, we employ our Product Tankers on time charters so there is no seasonality effect, while our container feeder service experiences a somewhat slower season during the first quarter due to the congestion at the main discharge terminal in Patagonia in connection with the cruise tourist season.

Industry Conditions

River Industry

Key factors driving cargo movements in the Hidrovia Region are agricultural production and exports, particularly soybeans, from Argentina, Brazil and Paraguay, exports of Brazilian iron ore, regional demand and Paraguayan imports of petroleum products. A significant portion of the cargos transported in the Hidrovia Region are export or import-related cargoes and the applicable freights are paid in U.S. Dollars.

The Parana / Paraguay, the High Parana and the Uruguay rivers consist of over 2,200 miles of a natural interconnected navigable river system serving five countries namely Argentina, Bolivia, Brazil, Paraguay and Uruguay. The extension of this river system is comparable to that of the Mississippi river in the United States.

Dry Bulk Cargo

Soybeans. Argentina, Bolivia, Brazil, Paraguay and Uruguay produced in aggregate about 41.5 million tons, or mt, of soybeans in 1995 and an estimated 136.0 mt in 2011, a 16-year compound annual growth rate, or CAGR, of 7.7% from 1995. These countries account for an estimated 51% of world soybean production in 2011, up from only 30% in 1995.

Of the above-mentioned countries of the Hidrovia Region, the area harvested of soybeans has increased from approximately 18.9 Mha (million hectares, 1 hectare = 2.47 acres) in 1995 to an estimated 47.1 Mha in 2011, a 16-year CAGR of 5.9%. Further, with advances in technology, productivity of farmland has also improved.

The growth in soybean production has not occurred at the expense of other key cereal grains. Production of corn (maize) in Argentina, Bolivia, Brazil, Paraguay and Uruguay combined grew from 50.3 mt in 1995 to 84.3 mt in 2011, a 16-year CAGR of 3.3%. Production of wheat in these countries grew from 14.4 mt in 1995 to 24.9 mt in 2011, a 16-year CAGR of 3.5%.

Iron Ore. In the Corumba area in Brazil reached by the High Paraguay River, there are three large iron ore mines, two of which are owned by the Brazilian mining company Vale (following the 2009 acquisition of Rio Tinto's assets in the region) while the third one is owned by MMX Mineração & Metálicos S.A. (MMX). Their combined production of iron ore, which is entirely transported by river barge, has grown from about 1.1 million mt, or mmt, since 1999 to 6.0 mmt in 2010, a CAGR of 16.7%. Estimated production for 2011 is 7.2 mmt (based on reported nine months 2011 production for Vale and MMX annualized on a pro rata basis) which would provide an annual increase of 20%. Iron ore prices have on average increased 30% from December 2009 to December 2011. Continued high iron ore prices during 2012 and 2013 should support continued growth in production of iron ore.

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In addition to the above, Jindal Steel & Power Limited, through one of its subsidiaries, Jindal Steel Bolivia S.A., has acquired the development rights for 20.0 billon tonnes of El Mutun iron ore reserves located in Bolivia. This mine is expected to progressively scale up production reaching up to 3.0 mmt of iron ore, which will be exported through the Parana and Paraguay rivers of the Hidrovia.

Oil transportation

Paraguay has no known indigenous sources of petroleum. Barges using the rivers in the Hidrovia Region are currently the preferred method of supplying Paraguay with crude and petroleum products, according to industry sources totaling between 1.1 million cubic meters to 1.3 million cubic meters per year in each of the last 7 years.

Most petroleum products travel north to destinations in Northern Argentina, Paraguay and Bolivia, creating synergies with dry cargo volumes that mostly travel south.

Mode Comparison

Along with growth in production of commodities transported by barge in the Hidrovia Region, cost, safety and environmental incentives exist to shift commodity transport to barges.

Inland barge transportation is generally the most cost efficient, safest and cleanest means of transporting bulk commodities as compared with railroads and trucks.

According to a 2007 Texas Transport Institute study commissioned by the U.S. government, one Mississippi River-type barge (1,500 dwt) has the carrying capacity of about 15 railcars or 58 tractor-trailer trucks and is able to move 576 ton-miles per gallon of fuel compared to 413 ton-miles per gallon of fuel for rail transportation or 155 ton-miles per gallon of fuel for tractor-trailer transportation. In the case of Jumbo barges (2,500 dwt) as are many of UABL's existing barges or the ones Ultrapetrol builds in its yard, these efficiencies are even larger. The study also shows barge transportation is the safest mode of cargo transportation, based on the percentage of fatalities or injuries and the number of hazardous materials incidents. Inland barge transportation predominantly operates away from population centers, which generally reduces both the number and impact of waterway incidents. According to industry sources, in terms of unit transportation cost for most dry bulk cargos, barge is cheapest, rail is second cheapest and truck is third cheapest. There are clear and significant incentives to build port infrastructure and switch from truck to barge to reduce transportation costs.

Offshore Supply Industry

The market for offshore supply vessels, or OSVs, both on a worldwide basis and within Brazil, is driven by a variety of factors. On the demand side, the driver is the growth in offshore oil development / production activity, which in the long term is driven by the price of oil and the cost of developing the particular offshore reserves. Demand for OSVs is further driven by the location of the reserves, with fields located further offshore and in deeper waters generally requiring more vessels per field and larger, more technologically advanced vessels. The supply side is driven by the availability of the vessel type needed (i.e., appropriate size and technology), which in turn is driven by historical newbuilding patterns and scrapping rates as well as the current employment of vessels in the worldwide fleet (i.e., whether under long-term charter) and the rollover schedule for those charters. Technological developments also play an important role on the supply side, with technology such as dynamic positioning better able to meet certain support requirements.

Both demand for and supply of OSVs are heavily influenced by cabotage laws (such as the U.S. Jones Act). Since most offshore supply activities occur within the jurisdiction of a country, they fall within that country's cabotage laws. This distinguishes the OSV sector from most other types of shipping. Cabotage laws may restrict the supply of tonnage, give special preferences to locally flagged ships or require that any vessel working in that country's waters be owned, flagged, crewed and, in some cases, constructed in that country.

OSVs generally support oil exploration, production, construction and maintenance activities on the continental shelf and have a high degree of cargo flexibility relative to other offshore vessel types. They utilize space above and below deck to transport dry and liquid cargo, including heavy equipment, pipe, drilling fluids, provisions, fuel, dry bulk cement and drilling mud.

The OSV sector includes conventional supply vessels, or SVs, and platform supply vessels, or PSVs. PSVs are large and often sophisticated vessels constructed to allow for economic operation in environments requiring some combination of deepwater operations, long distance support, economies of scale and demanding operating conditions. PSVs serve drilling and production facilities and support offshore construction and maintenance work for clusters of offshore locations and/or relatively distant deepwater locations. They have larger deck space and larger and more varied cargo handling capabilities relative to other offshore support vessels to provide more economic service to distant installations or several locations. Some vessels have dynamic positioning, which allows close station keeping while underway. PSVs can be designed with certain characteristics required for specific offshore trades such as the North Sea or deepwater Brazilian service.

Brazilian Offshore Industry

Driven by Brazil's policy of becoming energy self-sufficient as well as by oil price and cost considerations, offshore exploration, development and production activities within Brazil have grown significantly. Brazil is becoming a major exporter of oil. Since most Brazilian reserves are located far offshore in deep waters, Brazil has become a world leader in deep drilling technology.

The primary customer for PSVs in Brazil is Petrobras, the Brazilian national oil company. The Brazilian government has also allowed foreign companies to participate in offshore oil and gas exploration and production since 1999. Other companies active in Brazil in offshore oil and gas exploration and production industry include Total, Shell, BP, OGX, Repsol YPF and ChevronTexaco. The deepwater Campos Basin, an area located about 80 miles offshore, has been the leading area for offshore activity. Activities have been extended to the deepwater Santos and Espirito Santo Basins located far off the coast while additionally requiring resources to develop pre salt areas of water depths of over 9,000 feet. During 2008, 2009 and 2010, several significant discoveries have been made, which could possibly more than double Brazilian oil reserves when confirmed.

Petrobras has announced that it will increase the use of supply and special vessels from the current 254 vessels to 465 vessels by 2013. The Brazilian market has seen an increasing demand for PSVs since 2006 (prior to 2006 large PSVs in excess of 4000 DWT were unusual in Brazilian waters) and now according to Petrobras, the demand for this type of vessel will grow significantly in the next three years.

Deepwater service favors large modern vessels that can provide a full range of flexible services including dynamic positioning systems while providing economies of scale to installations distant from shore. Cabotage laws favor employment of Brazilian flag vessels. However, according to industry sources, many of the Brazilian flag PSVs and supply vessels are smaller and older than now required, with approximately 23% of the national fleet at least 20 years of age. Temporary authority is granted for foreign vessels to operate only if no Brazilian flag vessels are available.

The North Sea Market

The North Sea is a similarly demanding offshore market due to difficult weather and sea conditions, significant water depths, long distances to be traveled and sophisticated technical requirements.

In 2000 and 2001, increases in oil prices led to increased North Sea exploration activity and higher OSV demand. Oil prices fell in early 2002, leading to questions regarding the sustainability of the higher oil prices and reduced exploration and development activity. Even with recovery in the West Texas Intermediate, or WTI, price to an average of about $31 per barrel in 2003, North Sea exploration and development activity remained low. Low oil prices and availability of more attractive opportunities elsewhere resulted in a shift of activities by oil majors towards other regions. Oil prices continued their increase, with average WTI crude prices of about $42 per barrel in 2004, $57 per barrel in 2005, $66 per barrel in 2006, $72 per barrel in 2007 and $100 in 2008. Exploration and development activities increased. Major oil companies returned to the North Sea while the independents remained and increased their activities. WTI crude oil prices decreased from an average of $77 per barrel in October 2008 to an average of $45 during January-April 2009, then recovered to an average $70 per barrel for the remainder of 2009 and reached an average $79 per barrel in 2010 and $95 per barrel in 2011. After the decrease in 2009 exploration and development activities versus 2008, activity increased in 2010 leading to improved vessel earnings during the summer, with weaker earnings later in 2010 as the winter season approached continuing through February 2011.

Ocean Industry

Regional Cabotage Trades

Voyages between two Argentine ports are regulated by the Argentine government as "cabotage" and require the use of an Argentine flag vessel or a vessel operated under special permit by an Argentine company. Cabotage is used to mean both voyages between two national ports and laws that reserve such voyages for nationally operated vessels. Argentine registry requires that vessels be built in an Argentine shipyard or that import duty be paid, which increases the cost of new vessels versus foreign construction. The special permit described above allows younger foreign-built vessels to enter cabotage trades while retaining the Argentine nationality requirement for operations.

Access to the Argentine coastal cabotage market is thus controlled by legal requirements, which limit its access to those companies with a legitimate operating presence in Argentina with vessels registered or holding a special permit in Argentina.

Regional tanker and container shipping market factors, including local demand factors and vessel supply information, are described below, reflecting market conditions in the primary area of employment for these vessels.

The Regional Tanker Market

Regional Oil Demand

Argentina's oil demand was estimated at about 580,000 barrels per day, or bpd, in 2009, up from about 511,000 bpd in 2000, resulting in a 2000-2009 CAGR of 1.4%.

Argentina's refining capacity is largely located in the Plate River estuary near Buenos Aires. Crude oil from oil fields in southern Argentina is shipped to refineries near Buenos Aires by tankers. Coastal cities in Southern Argentina receive petroleum products by tankers from these refineries. Cabotage tankers are also used for lightering of international tankers (discharge of cargo to reduce draft) and for short voyages within the Plate Estuary and Parana River. Vessels with IMO chemical classification (see below) are also used for Argentine or other regional voyages carrying petroleum products and chemicals such as styrene monomer.

The Regional Patagonian Container Shipping Trades

Regional Container Shipping Demand

Coastal container shipping provides important north-south links between Buenos Aires and coastal ports in southern Argentina. Buenos Aires city and province have about 46% of Argentina's population and is the centre of much economic activity. However, Argentine economic development programs encourage manufacturing in the southern Argentine region of Tierra del Fuego. Finished goods from the manufacturing are transported north from the port of Ushuaia to Buenos Aires for distribution. Most of the cargo in this service initiates as containers transported by the major international lines containing components for manufacturing that are carried from China and other foreign ports of origin to Buenos Aires with transshipment to Ushuaia under feeder agreements with the major international lines. Cargo is also carried to and from other southern Argentine ports, such as Puerto Madryn, as demand requires.

Throughout this Industry Section, all figures related to harvested area and production of soybean, corn and wheat for South America and specifically for Argentina, Bolivia, Brazil, Paraguay and Uruguay are obtained through the USDA Foreign Agricultural Service website some time prior to filing this 20-F.

Figures related to Iron Ore production in the Corumba Region from Vale, MMX, Rio Tinto and Jindal Steel & Power were extracted from each of the respective companies' public records (including Earnings Presentation, 20-Fs and Annual Reports). Iron Ore price trends were extracted from Indexmundi's website whose source in the International Monetary Fund.

Data included in the Brazilian offshore section has been extracted from public information presented by both Petrobras and ANTAQ, as well as industry sources, while both current North Sea activities and crude oil prices have been retrieved from industry sources.

Oil demand figures were extracted from Indexmundi's website whose source is the International Monetary Fund.

All other data and information included in this Industry Section not expressly addressed above have been included in an unchanged manner from the Industry Section of our 20-F for the Fiscal Year ending December 31, 2010, which was prepared in all respect by Doll Shipping Consultancy.

Environmental and Government Regulation

Government regulations significantly affect our operations, including the ownership and operation of our vessels. Our operations are subject to international conventions, national, state and local laws and regulations in force in international waters and the jurisdictional waters of the countries in which our vessels may operate or are registered, including OPA, the Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, the U.S. Port and Tanker Safety Act, the IMO International Convention for the Prevention of Pollution from Ships, or MARPOL, other regulations adopted by the IMO and the European Union, various volatile organic compound emission requirements, the IMO / U.S. Coast Guard pollution regulations and various SOLAS amendments, as well as other regulations. Compliance with these requirements entails significant expense, including vessel modifications and implementation of certain operating procedures.

A variety of governmental and private entities, each of which may have unique requirements, subject our vessels to both scheduled and unscheduled inspections. These entities include the local port authorities (U.S. Coast Guard, harbour master or equivalent), port state controls, classification societies, flag state administration (country of registry) and charterers, particularly terminal operators. Certain of these entities require us to obtain permits, licenses, certificates or approvals for the operation of our vessels. Failure to maintain necessary permits, licenses, certificates or approvals could require us to incur substantial costs or temporarily suspend operation of one or more of our vessels.

We believe that the heightened level of environmental and quality concerns among insurance underwriters, regulators and charterers will lead to greater inspection and safety requirements on all vessels and may accelerate the scrapping of older vessels throughout the industry. Increasing environmental concerns have created a demand for vessels that conform to the stricter environmental standards. We are required to maintain operating standards for all of our ocean-going vessels for operational safety, quality maintenance, continuous training of our officers and crews and compliance with U.S. and international regulations. We believe that the operation of our vessels is in substantial compliance with applicable environmental laws and regulations. However, such laws and regulations may change and impose stricter requirements, such as in response to the 2010 Deepwater Horizon oil spill or future serious marine incidents. Future requirements may limit our ability to do business, increase our operating costs, force the early retirement of our vessels and / or affect their resale value, all of which could have a material adverse effect on our financial condition and results of operations.

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International Maritime Organization

The United Nations' International Maritime Organization , or IMO, has adopted the International Convention for the Prevention of Marine Pollution from Ships, 1973, as modified by the Protocol of 1978 relating thereto (collectively referred to as MARPOL 73/78 and herein as "MARPOL"). MARPOL entered into force on October 2, 1983. It has been adopted by over 150 nations, including many of the jurisdictions in which our vessels operate. MARPOL sets forth pollution-prevention requirements applicable to drybulk carriers, among other vessels, and is broken into six Annexes, each of which regulates a different source of pollution. Annex I relates to oil leakage or spilling; Annexes II and III relate to harmful substances carried, in bulk, in liquid or packaged form, respectively; Annexes IV and V relate to sewage and garbage management, respectively; and Annex VI, lastly, relates to air emissions. Annex VI was separately adopted by the IMO in September of 1997.

Air Emissions

In September of 1997, the IMO adopted Annex VI to MARPOL to address air pollution. Effective May 2005, Annex VI sets limits on nitrogen oxide emissions from ships whose diesel engines were constructed (or underwent major conversions) on or after January 1, 2000. It also prohibits "deliberate emissions" of "ozone depleting substances," defined to include certain halons and chlorofluorocarbons. "Deliberate emissions" are not limited to times when the ship is at sea; they can for example include discharges occurring in the course of the ship's repair and maintenance. Emissions of "volatile organic compounds" from certain tankers, and the shipboard incineration (from incinerators installed after January 1, 2000) of certain substances (such as polychlorinated biphenyls (PCBs)) are also prohibited. Annex VI also includes a global cap on the sulfur content of fuel oil (see below).

The IMO's Maritime Environment Protection Committee, or MEPC, adopted amendments to Annex VI on October 10, 2008, which amendments were entered into force on July 1, 2010. The amended Annex VI seeks to further reduce air pollution by, among other things, implementing a progressive reduction of the amount of sulphur contained in any fuel oil used on board ships. By January 1, 2012, the amended Annex VI requires that fuel oil contain no more than 3.50% sulfur (from the current cap of 4.50%). By January 1, 2020, sulfur content must not exceed 0.50%, subject to a feasibility review to be completed no later than 2018.

Sulfur content standards are even stricter within certain "Emission Control Areas" or ECAs. By July 1, 2010, ships operating within an ECA may not use fuel with sulfur content in excess of 1.0% (from 1.50%), which is further reduced to 0.10% on January 1, 2015. Amended Annex VI establishes procedures for designating new ECAs. Currently, the Baltic Sea and the North Sea have been so designated. Effective August 1, 2012, certain coastal areas of North America will also be designated ECAs, as will (effective January 1, 2014), the United States Caribbean Sea. Ocean-going vessels in these areas will be subject to stringent emissions controls and may cause us to incur additional costs. If other ECAs are approved by the IMO or other new or more stringent requirements relating to emissions from marine diesel engines or port operations by vessels are adopted by the EPA or the states where we operate, compliance with these regulations could entail significant capital expenditures or otherwise increase the costs of our operations.

Amended Annex VI also establishes new tiers of stringent nitrogen oxide emissions standards for new marine engines, depending on their date of installation. The U.S. Environmental Protection Agency promulgated equivalent (and in some senses stricter) emissions standards in late 2009.

The North America ECA entered into force on July 15, 2011, however this had a one year exemption for enforcement and will be enforced as of 1st August 2012. This will require vessels to use fuel oils of sulfur content below 1% in US / Canada coastal waters including Hawaii with further reduction to 0.1% sulfur as of January 1, 2015. A new ECA has also been designated for the Puerto Rico and US Virgin Islands (actually designated "United State Caribbean Sea") which will come into force on January 1, 2013, and enforced with a 1 year grace period. ECA designations subject

ocean-going vessels within the designated area to stringent emissions controls, which might cause vessels to require segregated bunker tanks and cylinder oil tanks to use different fuels in coastal waters and open seas, which threatens to add an additional cost burden to shipowners.

Safety Management System Requirements

The IMO also adopted the International Convention for the Safety of Life at Sea, or SOLAS, and the International Convention on Load Lines, or the LL Convention, which impose a variety of standards that regulate the design and operational features of ships. The IMO periodically revises the SOLAS and LL Convention standards.

The operation of our ships is also affected by the requirements set forth in Chapter IX of SOLAS, which sets forth the IMO's International Management Code for the Safe Operation of Ships and Pollution Prevention, or the ISM Code. The ISM Code requires ship owners and bareboat charterers to develop and maintain an extensive "Safety Management System" that includes the adoption of a safety and environmental protection policy setting forth instructions and procedures for safe operation and describing procedures for dealing with emergencies. The failure of a ship owner or bareboat charterer to comply with the ISM Code may subject such party to increased liability, may decrease available insurance coverage for the affected ships and may result in a denial of access to, or detention in, certain ports. Currently, each of the ships in our fleet is ISM code-certified. However, there can be no assurance that such certification will be maintained indefinitely.

The ISM Code requires that ship operators obtain a safety management certificate, or SMC, for each ship they operate. This certificate evidences compliance by a ship's operators with the ISM Code requirements for a safety management system, or SMS. No ship can obtain an SMC under the ISM Code unless its manager has been awarded a document of compliance, or DOC, issued in most instances by the ship's flag state.

Pollution Control and Liability Requirements

The IMO has negotiated international conventions that impose liability for pollution in international waters and the territorial waters of the signatories to such conventions. For example, the IMO has adopted the International Convention on Civil Liability for Oil Pollution Damage of 1969, as amended by different Protocol in 1976, 1984, and 1992, and amended in 2000, or the CLC. Under the CLC and depending on whether the country in which the damage results is a party to the 1992 Protocol to the CLC, a vessel's registered owner is strictly liable for pollution damage caused in the territorial waters of a contracting state by discharge of persistent oil, subject to certain exceptions. The 1992 Protocol changed certain limits on liability, expressed using the International Monetary Fund currency unit of Special Drawing Rights. The right to limit liability is forfeited under the CLC where the spill is caused by the shipowner's actual fault and under the 1992 Protocol where the spill is caused by the shipowner's intentional or reckless act or omission where the shipowner knew pollution damage would probably result. The CLC requires ships covered by it to maintain insurance covering the liability of the owner in a sum equivalent to an owner's liability for a single incident. We believe that our insurance will cover the liability under the plan adopted by the IMO.

The IMO adopted the International Convention on Civil Liability for Bunker Oil Pollution Damage, or the Bunker Convention, to impose strict liability on ship owners for pollution damage in jurisdictional waters of ratifying states caused by discharges of bunker fuel. The Bunker Convention requires registered owners of ships over 1,000 gross tons to maintain insurance for pollution damage in an amount equal to the limits of liability under the applicable national or international limitation regime (but not exceeding the amount calculated in accordance with the Convention on Limitation of Liability for Maritime Claims of 1976, as amended). With respect to non-ratifying states, liability for spills or releases of oil carried as fuel in ship's bunkers typically is determined by the national or other domestic laws in the jurisdiction where the events or damages occur.

In March 2006, the IMO amended Annex I to MARPOL, including a new regulation relating to oil fuel tank protection, which became effective August 1, 2007. The new regulation applies to various ships delivered on or after August 1, 2010. It includes requirements for the protected location of the fuel tanks, performance standards for accidental oil fuel outflow, a tank capacity limit and certain other maintenance, inspection and engineering standards.

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IMO regulations also require owners and operators of certain vessels to adopt Ship Oil Pollution Emergency Plans. Periodic training and drills for response personnel and for vessels and their crews are required.

The IMO adopted the International Convention for the Control and Management of Ships' Ballast Water and Sediments, or the BWM Convention, in February 2004. The BWM Convention's implementing regulations call for a phased introduction of mandatory ballast water exchange requirements, to be replaced in time with mandatory concentration limits. The BWM Convention will not enter into force until 12 months after it has been adopted by 30 states, the combined merchant fleets of which represent not less than 35% of the gross tonnage of the world's merchant shipping tonnage. To date, there has not been sufficient adoption of this standard for it to take force. However, Panama may adopt this standard in the relatively near future, which would be sufficient for it to take force. Upon entry into force of the BWM Convention, mid-ocean ballast exchange would be mandatory for our vessels. In addition, our vessels would be required to be equipped with a ballast water treatment system that meets mandatory concentration limits not later than the first intermediate or renewal survey, whichever occurs first, after the anniversary date of delivery of the vessel in 2014, for vessels with ballast water capacity of 1500-5000 cubic meters, or after such date in 2016, for vessels with ballast water capacity of greater than 5000 cubic meters. If mid-ocean ballast exchange or ballast water treatment requirements become mandatory, the cost of compliance could increase for ocean carriers. Although we do not believe that the costs of compliance with a mandatory mid-ocean ballast exchange would be material, it is difficult to predict the overall impact of such a requirement on our operations.

The MEPC has also adopted revised guidelines on implementation of effluent standards and performance tests for sewage treatment plants installed on vessels after January 1, 2010. The maximum discharge rate of untreated sewage beyond the 12 mile limit from land has also been revised.

The U.S. Oil Pollution Act of 1990 and Comprehensive Environmental Response, Compensation and Liability Act

OPA established an extensive regulatory and liability regime for the protection and cleanup of the environment from oil spills. OPA affects all "owners and operators" whose vessels trade with the United States, its territories and possessions or whose vessels operate in United States waters, which includes the United States' territorial sea and its 200 nautical mile exclusive economic zone around the United States. The United States has also enacted the Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, which applies to the discharge of hazardous substances other than oil, whether on land or at sea. OPA and CERCLA both define "owner and operator" in the case of a vessel as any person owning, operating or chartering by demise, the vessel. Both OPA and CERCLA impact our operations.

Under OPA, vessel owners and operators are "responsible parties" and are jointly, severally and strictly liable (unless the spill results solely from the act or omission of a third party, an act of God or an act of war) for all containment and clean-up costs and other damages arising from discharges or threatened discharges of oil from their vessels.

OPA contains statutory caps on liability and damages; such caps do not apply to direct cleanup costs. OPA limits the liability of responsible parties with respect to single-hull tankers over 3,000 gross tons to the greater of $3,200 per gross ton or $23,496,000 million; but for all other tankers over 3,000 gross tons, liability is limited to the greater of $2,000 per gross ton or $17.088 million. For non-tank vessels (e.g. drybulk), liability is limited to the greater of $1,000 per gross ton or $854,400 (subject to periodic adjustment for inflation). These limits of liability do not apply if an incident was proximately caused by the violation of an applicable U.S. federal safety, construction or operating regulation by a responsible party (or its agent, employee or a person acting pursuant to a contractual relationship), or a responsible party's gross negligence or willful misconduct. The limitation on liability similarly does not apply if the responsible party fails or refuses to (i) report the incident where the responsibility party knows or has reason to know of the incident; (ii) reasonably cooperate and assist as requested in connection with oil removal activities; or (iii) without sufficient cause, comply with an order issued under the Federal Water Pollution Act (Section

311 (c), (e)) or the Intervention on the High Seas Act.

CERCLA contains a similar liability regime whereby owners and operators of vessels are liable for cleanup, removal and remedial costs, as well as damage for injury to, or destruction or loss of, natural resources, including the reasonable costs associated with assessing same, and health assessments or health effects studies. There is no liability if the discharge of a hazardous substance results solely from the act or omission of a third party, an act of God or an act of war. Liability under CERCLA is limited to the greater of $300 per gross ton or $5.0 million for vessels carrying a hazardous substance as cargo and the greater of $300 per gross ton or $500,000 for any other vessel. These limits do not apply (rendering the responsible person liable for the total cost of response and damages) if the release or threat of release of a hazardous substance resulted from willful misconduct or negligence, or the primary cause of the release was a violation of applicable safety, construction or operating standards or regulations. The limitation on liability also does not apply if the responsible person fails or refused to provide all reasonable cooperation and assistance as requested in connection with response activities where the vessel is subject to OPA.

OPA and CERCLA both require owners and operators of vessels to establish and maintain with the U.S. Coast Guard evidence of financial responsibility sufficient to meet the maximum amount of liability to which the particular responsible person may be subject. Vessel owners and operators may satisfy their financial responsibility obligations by providing a proof of insurance, a surety bond, qualification as a self-insurer or a guarantee.

We currently maintain, for each of our vessels, pollution liability coverage insurance in the amount of $1 billion per incident. If the damages from a catastrophic spill exceeded our insurance coverage, it could have a material adverse effect on our business and the results of operations.

Under OPA, with certain limited exceptions, all newly-built or converted vessels operating in U.S. waters must be built with double-hulls, and existing vessels that do not comply with the double-hull requirement are prohibited from trading in U.S. waters as of dates ranging over a 25-year period (1990-2015) based on size, age and place of discharge, unless retrofitted with double-hulls. Notwithstanding the prohibition to trade schedule, the act currently permits existing single-hull and double-sided tankers to operate until the year 2015 if their operations within U.S. waters are limited to discharging at the Louisiana Offshore Oil Port or off-loading by lightering within authorized lightering zones more than 60 miles off-shore. Lightering is the process by which vessels at sea off-load their cargo to smaller vessels for ultimate delivery to the discharge port.

We believe we are in substantial compliance with OPA, CERCLA and all applicable state regulations in the ports where our vessels call or are likely to call.

The U.S. Clean Water Act

The U.S. Clean Water Act, or CWA, prohibits the discharge of oil, hazardous substances and ballast water in U.S. navigable waters unless authorized by a duly-issued permit or exemption, and imposes strict liability in the form of penalties for any unauthorized discharges. The CWA also imposes substantial liability for the costs of removal, remediation and damages and complements the remedies available under OPA and CERCLA. Furthermore, many U.S. states that border a navigable waterway have enacted environmental pollution laws that impose strict liability on a person for removal costs and damages resulting from a discharge of oil or a release of a hazardous substance. These laws may be more stringent than U.S. federal law.

The EPA regulates the discharge of ballast water and other substances in U.S. waters under the CWA. EPA regulations require vessels 79 feet in length or longer (other than commercial fishing and recreational vessels) to comply with a Vessel General Permit authorizing ballast water discharges and other discharges incidental to the operation of vessels. The Vessel General Permit imposes technology and water-quality based effluent limits for certain types of discharges and establishes specific inspection, monitoring, recordkeeping and reporting requirements to ensure the effluent limits are met. The EPA has proposed a draft 2013 Vessel General Permit to replace the current Vessel General Permit upon its expiration on December 19, 2013, authorizing discharges incidental to operations of commercial vessels. The draft permit also contains numeric ballast water discharge limits for most vessels to reduce the risk of invasive species in US waters, more stringent requirements for exhaust gas scrubbers and the use of environmentally acceptable lubricants.

U.S. Coast Guard regulations adopted under the U.S. National Invasive Species Act, or NISA, also impose mandatory ballast water management practices for all vessels equipped with ballast water tanks entering or operating in U.S. waters. In 2009 the Coast Guard proposed new ballast water management standards and practices, including limits regarding ballast water releases. As of November 2011, the Office of Management and Budget continues to review this proposed rule. Compliance with the EPA and the U.S. Coast Guard regulations could require the installation of equipment on our vessels to treat ballast water before it is discharged or the implementation of other port facility disposal arrangements or procedures at potentially substantial cost, and/or otherwise restrict our vessels from entering

U.S. waters.

As of January 1, 2007, vessels operating in coastal waters of the state of California were required to comply with the State's Marine Vessel Rules concerning emissions from auxiliary diesel engines. These rules impose emission limits on vessels operating in 24 nautical miles coastal area from the California baseline. They additionally require certain emission requirements compliance based on the fleet size and frequency of port calls and alternatively requires use of shore power or payment of fees for non compliance. They are codified at California Code of Regulations (CCR), Title 13, 2299.1 and CCR Title 17, 93118. Currently, however, the rules are not being enforced. On February 27, 2008, the United States Court of Appeals for the Ninth Circuit, in Pacific Merchant Shipping Association v. Goldstene, 517 F.3d 1108 (No. 07-16695), held that the rules were preempted by the United States Clean Air Act and issued an injunction preventing their enforcement.

The U.S. Clean Air Act

The U.S. Clean Air Act of 1970 (including its amendments of 1977 and 1990), or the CAA, requires the EPA to promulgate standards applicable to emissions of volatile organic compounds and other air contaminants. Our vessels are subject to vapor control and recovery requirements for certain cargoes when loading, unloading, ballasting, cleaning and conducting other operations in regulated port areas. Our vessels that operate in such port areas with restricted cargoes are equipped with vapor recovery systems that satisfy these requirements. The CAA also requires states to draft State Implementation Plans, or SIPs, designed to attain national health-based air quality standards in each state. Although state-specific, SIPs may include regulations concerning emissions resulting from vessel loading and unloading operations by requiring the installation of vapor control equipment. As indicated above, our vessels operating in covered port areas are already equipped with vapor recovery systems that satisfy these existing requirements.

The state of California has proposed more stringent regulations of air emissions from ocean-going vessels. On July 24, 2008, the California Air Resources Board of the State of California, or CARB, approved clean-fuel regulations applicable to all vessels sailing within 24 miles of the California coastline. The new CARB regulations require such vessels to use low sulfur marine fuels rather than bunker fuel. By July 1, 2009, such vessels are required to switch either to marine gas oil with a sulfur content of no more than 1.5% or marine diesel oil with a sulfur content of no more than 0.5%. By August 1, 2012, only marine gas oil with a sulfur content of no more than 1% or marine diesel oil with a sulfur content of no more than .5% will be allowed. By January 1, 2014, only marine gas oil and marine diesel oil fuels with 0.1% sulfur will be allowed. These new regulations may require significant expenditures on low-sulfur fuel and would increase our operating costs.

Our operations occasionally generate and require the transportation, treatment and disposal of both hazardous and non-hazardous solid wastes that are subject to the requirements of the U.S. Resource Conservation and Recovery Act, or RCRA, or comparable state, local or foreign requirements. The RCRA imposes significant recordkeeping and reporting requirements on transporters of hazardous waste In addition, from time to time we arrange for the disposal of hazardous waste or hazardous substances at offsite disposal facilities. If such materials are improperly disposed of by third parties, we may still be held liable for cleanup costs under applicable laws.

European Union Regulations

In October 2009, the European Union amended a directive to impose criminal sanctions for illicit ship-source discharges of polluting substances, including minor discharges, if committed with intent, recklessly or with serious negligence and the discharges individually or in the aggregate result in deterioration of the quality of water. Aiding and abetting the discharge of a polluting substance may also lead to criminal penalties. Member States were required to enact laws or regulations to comply with the directive by the end of 2010. Criminal liability for pollution may result in substantial penalties or fines and increased civil liability claims. The directive applies to all types of vessels, irrespective of their flag, but certain exceptions apply to warships or where human safety or that of the ship is in

danger.

China

As China becomes more aware of the impact of pollution and with increased sea going traffic in its coastal waters, they are beginning to impose new regulations for vessels entering Chinese coastal waters. As of January 1, 2012, China Marine Safety Agency, or MSA, requires certain vessels entering Chinese coastal waters to have a contract in place with a qualified ship pollution response company in the region. These vessels are required to notify the contracted Pollution Response company of the vessel's movements as per China MSA rules.

Greenhouse Gas Regulation

Currently, the emissions of greenhouse gases from international shipping are not subject to the Kyoto Protocol to the United Nations Framework Convention on Climate Change, which entered into force in 2005 and pursuant to which adopting countries have been required to implement national programs to reduce greenhouse gas emissions. However, in July 2011 the MEPC adopted two new sets of mandatory requirements to address greenhouse gas emissions from ships that will enter into force in January 2013. Currently operating ships will be required to develop Ship Energy Efficiency Management Plans, and minimum energy efficiency levels per capacity mile will apply to new ships. These requirements could cause us to incur additional compliance costs. The IMO is also considering the development of market-based mechanisms to reduce greenhouse gas emissions from ships. The European Union has indicated that it intends to propose an expansion of the existing European Union emissions trading scheme to include emissions of greenhouse gases from marine vessels, and in January 2012 the European Commission launched a public consultation on possible measures to reduce greenhouse gas emissions from ships. In the United States, the EPA has issued a finding that greenhouse gases endanger the public health and safety and has adopted regulations to limit greenhouse gas emissions from certain mobile sources and large stationary sources. Although the mobile source emissions regulations do not apply to greenhouse gas emissions from vessels, such regulation of vessels is foreseeable, and the EPA has in recent years received petitions from the California Attorney General and various environmental groups seeking such regulation. Any passage of climate control legislation or other regulatory initiatives by the IMO, European Union, the U.S. or other countries where we operate, or any treaty adopted at the international level to succeed the Kyoto Protocol, that restrict emissions of greenhouse gases could require us to make significant financial expenditures which we cannot predict with certainty at this time.

International Labour Organization

The International Labour Organization (ILO) is a specialized agency of the UN with headquarters in Geneva, Switzerland. The ILO has adopted the Maritime Labor Convention 2006 (MLC 2006). A Maritime Labor Certificate and a Declaration of Maritime Labor Compliance will be required to ensure compliance with the MLC 2006 for all ships above 500 gross tons in international trade. The MLC 2006 will enter into force one year after 30 countries with a minimum of 33% of the world's tonnage have ratified it. The MLC 2006 has not yet been ratified, but its ratification would require us to develop new procedures to ensure full compliance with its requirements.

Vessel Security Regulations

Since the terrorist attacks of September 11, 2001 in the United States, there have been a variety of initiatives intended to enhance vessel security such as the Maritime Transportation Security Act of 2002, or MTSA. To implement certain portions of the MTSA, in July 2003, the U.S. Coast Guard issued regulations requiring the implementation of certain security requirements aboard vessels operating in waters subject to the jurisdiction of the United States. The regulations also impose requirements on certain ports and facilities, some of which are regulated by the U.S. Environmental Protection Agency (EPA).

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Similarly, in December 2002, amendments to SOLAS created a new chapter of the convention dealing specifically with maritime security. The new Chapter V became effective in July 2004 and imposes various detailed security obligations on vessels and port authorities, and mandates compliance with the International Ship and Port Facilities Security Code, or the ISPS Code. The ISPS Code is designed to enhance the security of ports and ships against terrorism. To trade internationally, a vessel must attain an International Ship Security Certificate, or ISSC, from a recognized security organization approved by the vessel's flag state. Among the various requirements are:

- on-board installation of automatic identification systems to provide a means for the automatic transmission of safety-related information from among similarly equipped ships and shore stations, including information on a ship's identity, position, course, speed and navigational status;

- on-board installation of ship security alert systems, which do not sound on the vessel but only alert the authorities on shore;

- the development of vessel security plans;

- ship identification number to be permanently marked on a vessel's hull;

- a continuous synopsis record kept onboard showing a vessel's history including the name of the ship, the state whose flag the ship is entitled to fly, the date on which the ship was registered with that state, the ship's identification number, the port at which the ship is registered and the name of the registered owner(s) and their registered address; and

- compliance with flag state security certification requirements.

Ships operating without a valid certificate may be detained at port until it obtains an ISSC, or it may be expelled from port, or refused entry at port.

Furthermore, additional security measures could be required in the future which could have a significant financial impact on us. The U.S. Coast Guard regulations, intended to be aligned with international maritime security standards, exempt non-U.S. vessels from MTSA vessel security measures, provided such vessels have on board a valid ISSC that attests to the vessel's compliance with SOLAS security requirements and the ISPS Code.

Inspection by Classification Societies

Every oceangoing vessel must be "classed" by a classification society. The classification society certifies that the vessel is "in class," signifying that the vessel has been built and maintained in accordance with the rules of the classification society and complies with applicable rules and regulations of the vessel's country of registry and the international conventions of which that country is a member. In addition, where surveys are required by international conventions and corresponding laws and ordinances of a flag state, the classification society will undertake them on application or by official order, acting on behalf of the authorities concerned.

The classification society also undertakes on request other surveys and checks that are required by regulations and requirements of the flag state. These surveys are subject to agreements made in each individual case and / or to the regulations of the country concerned.

For maintenance of the class certification, regular and extraordinary surveys of hull, machinery, including the electrical plant and any special equipment classed are required to be performed as follows:

Annual Surveys. For seagoing ships, annual surveys are conducted for the hull and the machinery, including the electrical plant and where applicable for special equipment classed, within three months before or after each anniversary date of the date of commencement of the class period indicated in the certificate.

Intermediate Surveys. Extended annual surveys are referred to as intermediate surveys and typically are conducted two and one-half years after commissioning and each class renewal. Intermediate surveys are to be carried out at or between the second or third annual survey.

Special Surveys. Special surveys, also known as class renewal surveys, are carried out for the ship's hull, machinery, including the electrical plant, and for any special equipment classed, at the intervals indicated by the character of classification for the hull. At the special survey the vessel is thoroughly examined, including audio-gauging to determine the thickness of the steel structures. Should the thickness be found to be less than class requirements, the classification society would prescribe steel renewals. The classification society may grant a one year grace period for completion of the special survey. Substantial amounts of money may have to be spent for steel renewals to pass a special survey if the vessel experiences excessive wear and tear. In lieu of the special survey, every four or five years, depending on whether a grace period was granted or not, a ship owner has the option of arranging with the classification society for the vessel's hull or machinery to be on a continuous survey cycle, in which every part of the vessel would be surveyed within a five year cycle. At an owner's application, the surveys required for class renewal may be split according to an agreed schedule to extend over the entire period of class. This process is referred to as continuous class renewal.

We have made arrangements with the classification societies for most of our vessels to be on a continuous survey cycle for machinery. Hull surveys remain under the above mentioned survey regime which is uniform for all International Association of Classification Societies (IACS) members.

Currently our oceangoing and offshore vessels are scheduled for intermediate surveys and special surveys as follows:

Intermediate survey		Special survey	
Year	No. of vessels	Year	No. of vessels
2012	3	2012	3
2013	1	2013	1
2014	5	2014	1
2015	3	2015	4
2016	0	2016	4
2017	1	2017	0

Note: Maximum range period date has been considered.

All areas subject to survey as defined by the classification society are required to be surveyed at least once per class period, unless shorter intervals between surveys are prescribed elsewhere. The period between two subsequent surveys of each area must not exceed five years.

Most vessels are also drydocked every 30 to 36 months for inspection of the underwater parts and for repairs related to inspections. If any defects are found, the classification surveyor will issue a "recommendation" which must be rectified by the ship owner within prescribed time limits.

Most insurance underwriters make it a condition for insurance coverage that a vessel be certified as "in class" by a classification society which is a member of the International Association of Classification Societies, or IACS. All our oceangoing vessels are certified as being "in class".

Risk of Loss and Liability Insurance

General

The operation of any cargo vessel includes risks such as mechanical failure, collision, property loss, cargo loss or damage and business interruption due to political circumstances in foreign countries, hostilities and labor strikes. In addition, there is always an inherent possibility of marine disaster, including oil spills and other environmental

mishaps and the liabilities arising from owning and operating vessels in international trade.

We believe that we maintain insurance coverage against various casualty and liability risks associated with our business that we consider to be adequate based on industry standards and the value of our fleet, including hull and machinery and war risk insurance, loss of hire insurance at certain times for certain vessels, protection and indemnity insurance against liabilities to employees and third parties for injury, damage or pollution, strike covers for certain vessels and other customary insurance. While we believe that our present insurance coverage is adequate, we cannot guarantee that all risks will be insured, that any specific claim will be paid, or that we will always be able to obtain adequate insurance coverage at commercially reasonable rates or at all.

Hull and Machinery and War Risk Insurance

We maintain marine hull and machinery and war risk insurance, which includes the risk of actual or constructive total loss, for our wholly-owned and bareboat chartered vessels. At times, we also obtain for part of our fleet increased value coverage and additional freight insurance during periods of improved market rates, where applicable. This increased value coverage and additional freight coverage entitles us, in the event of total loss of a vessel, to some recovery for amounts not otherwise recoverable under the hull and machinery policy. When we obtain these additional insurances, our vessels will each be covered for at least their fair market value, subject to applicable deductibles (and some may include limitations on partial loss). We cannot assure you, however, that we will obtain this additional coverage on the same or commercially reasonable terms, or at all, in the future.

Loss of Hire

We maintain loss of hire insurance at certain times for certain vessels. Loss of hire insurance covers lost earnings resulting from unforeseen incidents or breakdowns that are covered by the vessel's hull and machinery insurance and result in loss of time to the vessel. Although loss of hire insurance will cover up to ninety days of lost earnings, we must bear the applicable deductibles, which generally range between the first 14 to 21 days of lost earnings. We intend to renew these insurance policies or replace them with other similar coverage if rates comparable to those on our present policies remain available. There can be no assurance that we will be able to renew these policies at comparable rates or at all. Future rates will depend upon, among other things, our claims history and prevailing insurance market rates.

Strike Insurance

Some of our vessels are covered for loss of time due to strikes (on board and in some cases on shore and on board). There can be no assurance that we will be able to renew these policies at comparable rates or at all.

Protection and Indemnity Insurance

Protection and indemnity insurance covers our legal liability for our shipping activities. This includes the legal liability and other related expenses of injury or death of crew, passengers and other third parties, loss or damage to cargo, fines and other penalties imposed by customs or other authorities, claims arising from collisions with other vessels, damage to other third-party property, pollution arising from oil or other substances and salvage, towing and other related costs, wreck removal and other risks. Coverage is limited for vessels in our Ocean and Offshore Businesses to approximately $6.98 billion with the exception of oil pollution liability, which is limited to $1.0 billion per vessel per incident. Vessels in our River Business have lower amounts of coverage.

This protection and indemnity insurance coverage is provided by protection and indemnity associations, or P&I Clubs, which are non-profit mutual assurance associations made up of members who must be either ship owners or ship managers. The members are both the insured parties and the providers of capital. The P&I Clubs in which our vessels are entered are currently members of the International Group of P&I Associations, or the International Group and are reinsured themselves and through the International Group in Lloyds of London and other first class reinsurance markets. We may be subject to calls based on each Club's yearly results. Similarly, the same P&I Clubs provide freight demurrage and defense insurance which, subject to applicable deductibles, covers all legal expenses in case of disputes, arbitrations and other proceedings related to our oceangoing vessels.

C. ORGANIZATIONAL STRUCTURE

Ultrapetrol (Bahamas) Limited is a company organized and registered as an International Business Company in the Commonwealth of the Bahamas since December 23, 1997.

Ultrapetrol (Bahamas) Limited has ownership (both direct and indirect) in the following companies:

COMPANY NAME	INCORPORATION JURISDICTION	OWNERSHIP (1)
Ultrapetrol (Bahamas) Limited	Bahamas	
Agencia Maritima Argenpar S.A.	Argentina	100.00%
Agriex Agenciamentos, Afretamentos e Apoio Maritimo Ltda.	Brazil	94.45%
Arlene Investments Inc.	Panama	100.00%
Bayshore Shipping Inc.	Panama	94.45%
Brinkley Shipping Inc.	Panama	100.00%
Cedarino, S.L.	Spain	100.00%
Compañía Paraguaya de Transporte Fluvial S.A.	Paraguay	100.00%
Corporación de Navegación Mundial S.A.	Chile	100.00%
Corydon International S.A.	Uruguay	100.00%
Dampierre Holdings Spain, S.L.	Spain	100.00%
Danube Maritime Inc.	Panama	100.00%
Dingle Barges Inc.	Liberia	100.00%
Eastham Barges Inc.	Liberia	100.00%
Elysian Ship Management Inc.	Florida	100.00%
Elysian Ship Management Ltd.	Bahamas	100.00%
General Ventures Inc.	Liberia	100.00%
Glasgow Shipping Inc.	Panama	94.45%
Gracebay Shipping Inc.	Panama	94.45%
Hallandale Commercial Corp.	Panama	100.00%
Ingatestone Holdings Inc.	Panama	94.45%
Kingly Shipping Ltd.	Bahamas	100.00%
Lewistown Commercial Corp.	Panama	94.45%
Lonehort S.A.	Uruguay	100.00%
Longmoor Holdings Inc.	Panama	100.00%
Lowrie Shipping Inc.	Panama	100.00%
Lowrie Shipping LLC	Delaware	100.00%
Majestic Maritime Ltd.	Bahamas	100.00%
Marine Financial Investment Corp.	Panama	100.00%
Maritima SIPSA S.A.	Chile	49.00%
Massena Port S.A.	Uruguay	100.00%
Noble Shipping Ltd.	Bahamas	100.00%
Obras Terminales y Servicios S.A.	Paraguay	50.00%
Oceanpar S.A.	Paraguay	100.00%
Packet Maritime Inc.	Panama	94.45%
Padow Shipping Inc.	Panama	94.45%
Palmdale Shipping Inc.	Panama	100.00%
Parabal S.A.	Paraguay	100.00%
Parfina S.A.	Paraguay	100.00%

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COMPANY NAME	INCORPORATION JURISDICTION	OWNERSHIP (1)
Princely International Finance Corp.	Panama	100.00%
Puerto del Sur S.A.	Paraguay	50.00%
Ravenscroft Holdings Inc.	Florida	100.00%
Ravenscroft Ship Management Inc.	Florida	100.00%
Ravenscroft Ship Management Ltd.	Bahamas	100.00%
Ravenscroft Ship Management Ltd.	UK	100.00%
Ravenscroft Ship Management S.A.	Uruguay	100.00%
Ravenscroft Shipping (Bahamas) S.A.	Bahamas	100.00%
Regal International Investments S.A.	Panama	100.00%
River Ventures LLC	Delaware	100.00%
Riverpar S.A.	Paraguay	100.00%
Riverview Commercial Corp.	Panama	100.00%
Sernova S.A.	Argentina	100.00%
Ship Management and Commercial Services Ltd.	Bahamas	100.00%
Ship Management Services Inc.	Florida	100.00%
Springwater Shipping Inc.	Panama	94.45%
Stanyan Shipping Inc.	Panama	100.00%
Thurston Shipping Inc.	Panama	100.00%
Topazio Shipping LLC	Delaware	94.45%
Tuebrook Holdings Inc.	Panama	100.00%
UABL Barges (Panama) Inc.	Panama	100.00%
UABL Limited	Bahamas	100.00%
UABL Paraguay S.A.	Paraguay	100.00%
UABL S.A.	Argentina	100.00%
UABL S.A.	Panama	100.00%
UABL Terminals (Paraguay) S.A.	Panama	100.00%
UABL Terminals Ltd.	Bahamas	100.00%
UABL Towing Services S.A.	Panama	100.00%
Ultrapetrol S.A.	Argentina	100.00%
UP (River) Ltd.	Bahamas	100.00%
UP Offshore (Bahamas) Ltd.	Bahamas	94.45%
UP Offshore (Panama) S.A.	Panama	94.45%
UP Offshore (UK) Ltd.	UK	94.45%
UP Offshore Apoio Maritimo Ltda.	Brazil	94.45%
UP Offshore Uruguay S.A.	Uruguay	94.45%
UP River (Holdings) Ltd.	Bahamas	100.00%
UP River Terminals (Panama) S.A.	Panama	100.00%
UPB (Panama) Inc.	Panama	100.00%
Woodrow Shipping Inc.	Panama	94.45%
Yataity S.A.	Paraguay	100.00%
Yvy Pora Fertilizantes S.A.	Paraguay	100.00%
Zubia Shipping Inc.	Panama	94.45%

(1) Direct or indirect ownership by Ultrapetrol (Bahamas) Limited.

D. PROPERTY, PLANT AND EQUIPMENT

Ravenscroft is headquartered in our own 16,007 square foot building located at 3251 Ponce de Leon Boulevard, Coral Gables, Florida, United States of America.

In addition we own a repair facility, a new shipyard for building barges or other vessels in Punta Alvear, Argentina, and through 50% joint venture participations, two grain loading ports in Paraguay (one of which can also load and discharge liquid cargos such as vegetable oils and petroleum products). We also own land large enough for the construction of two further terminals in Argentina.

We own and rent offices in Argentina and rent offices in Brazil, Paraguay and the United Kingdom. Finally we rent a shipyard in Ramallo, Argentina, where we operate two floating drydocks, one of which is owned by us.

ITEM 4A – UNRESOLVED STAFF COMMENTS

None.

ITEM 5 – OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion should be read in conjunction with the information included under the caption "Selected Financial Data," our historical consolidated financial statements and their notes included elsewhere in this annual report. This discussion contains forward-looking statements. For a discussion of the accuracy of these statements please refer to the section of this report titled "Cautionary Statement Regarding Forward Looking Statements" that reflect our current views with respect to future events and financial performance. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, such as those set forth in the section entitled "Risk Factors" in Item 3.D of this report and elsewhere in this annual report.

A. OPERATING RESULTS

Our Company

We are an industrial transportation company serving the marine transportation needs of its clients in the markets on which it focuses. It serves the shipping markets for containers, grain and soya bean products, forest products, minerals, crude oil, petroleum and refined petroleum products, as well as the offshore oil platform supply market with its extensive and diverse fleet of vessels. These include river barges and pushboats, platform supply vessels, tankers and two container feeder vessels.

- Our River Business, with 647 barges and 33 pushboats as of December 31, 2011, is the largest owner and operator of river barges and pushboats that transport dry bulk and liquid cargos through the Hidrovia Region of South America, a large region with growing agricultural, forest and mineral related exports. This region is crossed by navigable rivers that flow through Argentina, Bolivia, Brazil, Paraguay and Uruguay to ports serviced by ocean export vessels. These countries are estimated to account for approximately 51% of world soybean production in 2011, from 32% in 1995.

- Our Offshore Supply Business owns and operates vessels that provide critical logistical and transportation services for offshore petroleum exploration and production companies in the coastal waters of Brazil and the North Sea. Our Offshore Supply Business fleet currently consists of technologically advanced platform supply vessels, or PSVs. Together with the recently

received PSVs that were being built in China, UP Turquoise and UP Jasper, we now have seven PSVs currently in operation in Brazil under long term time charters with Petrobras and one operating in the North Sea under time charter with Nexen Petroleum UK Ltd. In addition, we have four vessels under construction in India with expected deliveries commencing in the second quarter of 2012.

- Our Ocean Business operates eight oceangoing vessels, including four Product Tankers that we employ in the South American coastal trade where we have preferential rights and customer relationships, two container feeder vessels, one Oceangoing Pushboat and one inland tank barge. Our Ocean Business fleet has an aggregate capacity of approximately 110,000 dwt.

Our business strategy is to continue to operate as a diversified marine transportation company with an aim to maximize our growth and profitability while limiting our exposure to the cyclical behavior of individual sectors of the transportation industry.

Developments in 2011

On February 2, 2011, we entered into a contract with a third party for the sale of six jumbo dry cargo barges built in our yard at Punta Alvear, Argentina which were delivered to the buyer over a three month period commencing March 2011.

On March 12, 2011, our PSV UP Turquoise initiated its four year charter contract with Petrobras after its arrival to Brazil on February 27, 2011.

On March 23, 2011, we received in Argentina, from the USA, three pushboats - Steven J Durbin (renamed Chaco X), H. Chibb (renamed San Pedro) and Rowena (renamed Venus) - acquired pursuant to the MOAs signed on February 4, 8 and 24, 2011, respectively.

On April 14, 2011, we voluntarily prepaid $15.0 million outstanding under the Banco BICE revolving credit line together with accrued and unpaid interests to such date.

On May 31, 2011, we signed a Mandate Letter with International Finance Corporation, or IFC, to process a possible financing of our River Business capital expenditure program of up to $25.0 million.

On June 14, 2011, we disbursed $1.7 million on account of the total purchase price for office space in Buenos Aires, Argentina. Additionally, we drew the second advance of $20.0 million under the $40.0 million DVB-Security facility in connection with the delivery of the eighth PSV in our Offshore Supply Business, UP Jasper, from Wison (Nantong) Heavy Industry Co., Ltd.

On August 11, 2011, we drew down $10.5 million under the Banco BICE $15.0 million revolving credit line.

On September 15, 2011, we paid $4.4 million corresponding to the fourth 20% installment due under the ship building contract for one of our four PSVs under construction in India, out of which $3.4 million were drawn down under our loan facility with DVB Bank AG and Natixis.

On September 28, 2011, our PSV UP Jasper arrived in Aberdeen, UK (North Sea), from China and subsequently entered into an 18-month time charter on September 29, 2011.

On September 28, 2011, we entered into a transportation contract, which was subsequently amended on October 7, 2011, with a first class international company whereby we agreed to transport 400,000 tons of iron ore over a period of one year starting January 1, 2012, and into a barge sale contract with the same customer for a total of twelve 2,500 DWT newbuilding jumbo barges to be delivered before the end of 2011. Our counterparts, however, failed to execute their obligations in respect of the barge construction contract wherefrom we have reserved all our rights under the respective agreements.

On October 24, 2011, we announced that our Board of Directors approved a share repurchase program for up to a total of $20.0 million of the Company's common stock through April 30, 2012.

On October 26, 2011, the Company repaid $5.5 million of the total amount outstanding under the $10.5 million revolving credit line with Banco BICE.

On November 5, 2011, our second re-engined pushboat, Asunción, was delivered. She now works on high specification, heavy-fuel oil based MAN-B&W engines.

On November 25, 2011, the Company repaid the remaining $5.0 million in connection with the revolving credit line with Banco BICE. We have not renewed this credit line.

On December 2, 2011, we signed a 10-year, $15.0 million Senior Credit Loan Agreement with IFC which together with the existing facility is secured by new barges built in our own yard and other existing river equipment, to partially finance our CAPEX plan for our River Business. The facility includes a grace period of two years. We drew down the $15.0 million available under this facility, on December 13, 2011.

On December 7, 2011, we entered into a Master Agreement whereby we agreed to sell fourteen newbuilt jumbo dry barges and granted an option to buy one pushboat, Cavalier VIII, to a third party.

On December 13, 2011, in connection with the Master Agreement dated December 7, 2011, one of our River Business subsidiaries entered into a Ship Management Agreement with a non-related third party to provide technical and crew management services for a period of one year and a possible extension.

On December 15, 2011, we signed a parallel 10-year, $10.0 million Senior Credit Loan Agreement with the OPEC Fund for International Development, or OFID, to be secured by a collateral sharing agreement with IFC.

On December 21, 2011, we received $5.3 million in final settlement of an arbitration for underperformance under a transportation contract entered into with a former client in our River Business.

On December 21, 2011, our third re-engined pushboat, Pampero I, was delivered. She is now 8,300 HP and works on high specification, heavy-fuel oil based MAN-B&W engines.

Recent Developments

On January 11, 2012, one of our subsidiaries initiated an arbitration proceeding in London, England, related to the non-performance of a barge sale contract and river transportation agreement. Under such arbitration the Company expects to be compensated for the losses and expenses which resulted from the breach of both agreements. The final amount to be awarded, if any, is however uncertain. The income will be taken into account if, when and to the extent the arbitration proceeding is favorably settled.

On January 24, 2012, we paid $4.4 million corresponding to the fourth 20% installment due under the ship building contract for one of our four PSVs under construction in India, out of which $3.4 million were drawn down under our loan facility with DVB Bank AG and Natixis.

On January 26, 2012, we drew down the $10.0 million available under the Senior Credit Loan signed with OFID on December 16, 2011.

On February 13, 2012, we sold an additional five newbuilt jumbo dry barges to the same third party. In addition, in accordance with such Master Agreement, the buyers purchased our pushboat Cavalier VIII for $3.9 million.

On February 13, 2012, according to Section 10.10 of the indenture pursuant to which our 7.25% Convertible Senior Notes Due 2017 were issued, the Conversion Rate of the Convertible Notes was adjusted from 133.1691 shares of Common Stock per $1,000 principal amount of Convertible Notes or an exercise price of $7.51 per share, to 163.1321 shares of Common Stock per $1,000 principal amount of Convertible Notes or an exercise price of $6.13 per share.

Factors Affecting Our Results of Operations

We organize our business and evaluate performance by the following business segments: the River Business, the Offshore Supply Business and the Ocean Business. In December 2008, we decided to discontinue the operations of our Passenger Business. The accounting policies of the reportable segments are the same as those for the consolidated

financial statements. We do not have significant inter-segment transactions.

Revenues

In our River Business, we currently contract for the carriage of cargoes, in the majority of cases, under contracts of affreightment, or COAs. Most of these COAs currently provide for adjustments to the freight rate based on changes in the price of fuel. When transporting containers or vehicles, we charge our clients on a per-trip per unit basis. In addition, we derive revenues from the sale of new barges built at our Punta Alvear yard to third parties.

In our Offshore Supply Business, we contract substantially all of our capacity under time charters to a charterer in Brazil. We may decide to employ our Indian-built PSVs in the North Sea spot and/or term market.

In our Ocean Business, we currently contract our tanker vessels on a time charter basis. In addition, we sell space on our container feeder vessels on a per Twenty Foot-Equivalent Unit, or TEU, basis which is very similar to a COA basis as far as recording of revenues and voyage expenses. Some of the differences between time charters and COAs are summarized below.

Time Charter (TC)

- We derive revenue from a daily rate paid for the use of the vessel and
- the charterer pays for all voyage expenses, including fuel and port charges.

Contract of Affreightment (COA)

- We derive revenue from a rate based on tonnage shipped expressed in dollars per metric ton of cargo and
- we pay for all voyage expenses, including fuel and port charges.

Our ships on time charters generate both lower revenues and lower expenses for us than those under COAs. At comparable price levels both time charters and COAs result in approximately the same operating income, although the operating margin as a percentage of revenues may differ significantly.

Time charter revenues accounted for 33% of the total revenues derived from transportation services in 2011 and COA revenues accounted for 67%. With respect to COA revenues derived from transportation service in 2011, 80% were in respect of repetitive voyages for our regular customers and 20% were in respect of single voyages for occasional customers.

Our river container vessels are paid on a rate based on each container shipped and is expressed in dollars per TEU. By comparison, these vessels' results are expressed similar to those vessels operating under a COA.

In our River Business, demand for our cargo carrying services is driven by agricultural, mining and petroleum related activities in the Hidrovia Region. Droughts and other adverse weather conditions, such as floods, could result in a decline in production of the agricultural products we transport, which would likely result in a reduction in demand for our services. Further, most of the operations in our River Business occur on the Parana and Paraguay Rivers and any changes adversely affecting navigability of either of these rivers, such as low water levels, could reduce or limit our ability to effectively transport cargo on the rivers.

In our Offshore Supply Business, we currently have seven of our PSVs operating under long-term charters with Petrobras in Brazil while our recently delivered Chinese-built PSV, UP Jasper, has initiated a time charter with Nexen

Petroleum UK Limited in the North Sea.

In our Ocean Business, we employed a significant part of our ocean fleet on time charter to different customers during 2011.

Expenses

Our operating expenses generally include the cost of all vessel management, crewing, spares and stores, insurance, lubricants, repairs and maintenance. Generally, the most significant of these expenses are repairs and maintenance, wages paid to marine personnel and marine insurance costs.

In addition to the vessel operating expenses, our other primary operating expenses in 2011 included general and administrative expenses related to ship management and administrative functions.

In our River Business, our voyage expenses include port expenses and bunkers as well as charter hire paid to third parties.

In our Offshore Supply Business, voyage expenses include offshore and brokerage commissions paid by us to third parties which provide brokerage services and bunker costs incurred when our vessels are repositioned between the North Sea and Brazil, which are fully covered by us.

In our Ocean Business, through our container feeder operation, our operating expenses include bunker costs which are fully covered by us, port expenses, Terminal Handling Costs, or THC, incurred in the regular operation of our container feeder service, agency fees paid by us to third parties. It also includes container leasing, storage and insurance expense.

Through our River Business, we own a repair facility for our river fleet at Pueblo Esther, Argentina, a new shipyard for building barges and other vessels in Punta Alvear, Argentina, land for the construction of two terminals in Argentina and 50% joint venture participations in two grain loading terminals in Paraguay. UABL also rents offices in Asuncion, Paraguay and Buenos Aires, Argentina and a repair and shipbuilding facility in Ramallo, Argentina, where we operate two floating dry docks, one of which is owned and one which is leased by us.

Through our Offshore Supply Business, we hold a lease for office space in Rio de Janeiro, Brazil. In addition, through Ravenscroft, we own a building located at 3251 Ponce de Leon Boulevard, Coral Gables, Florida, United States. We also own office space and hold a sublease to an additional office at Avenida Leandro N. Alem 986, Capital Federal, Buenos Aires, Argentina, and rent an office in Aberdeen, Scotland.

Foreign Currency Transactions

During 2011, 95% of our revenues were denominated in U.S. dollars. Also, for the year ended December 31, 2011, 4% of our revenues were denominated and collected in Brazilian reais and 1% were denominated and collected in British pounds. However, 38% of our total revenues were denominated in U.S. dollars but collected in Argentine pesos, Brazilian reais and Paraguayan guaranies. During 2011 significant amounts of our expenses were denominated in U.S. dollars and 9% of our total out of pocket operating expenses were paid in Argentine pesos, Brazilian reais and Paraguayan guaranies.

Our operating results, which we report in U.S. dollars, may be affected by fluctuations in the exchange rate between the U.S. dollar and other currencies. For accounting purposes, we use U.S. dollars as our functional currency. Therefore, revenue and expense accounts are translated into U.S. dollars at the average exchange rate prevailing during the month of each transaction.

Inflation, Rates of Exchange Variation and Fuel Price Increases

Inflationary pressures in the South American countries in which we operate may not be compensated in the short term by equivalent adjustments in the rate of exchange between the U.S. dollar and the local currencies. Additionally, revaluations of the local currencies against the U.S. dollar, even in the absence of inflation, have an incremental effect on the portion of our operating expenses incurred in those local currencies measured in U.S. dollars. Please see Foreign Currency Transactions.

If the London market for dollar loans between banks were to become volatile the spread between published LIBOR and the lending rates actually charged to banks in the London interbank market would widen. Interest in most loan agreements in our industry has been based on published LIBOR rates. After the financial crisis of the end of 2008, however, lenders have insisted on provisions that entitle them, in their discretion, to replace published LIBOR as the base for the interest calculation with their own cost-of-funds rate. Since then, we have been required to include similar provisions in some of our financings. If our lenders were to use the interest rate on their costs of funds instead of LIBOR in connection with such provisions, our lending costs could increase significantly, which would have an adverse effect on our profitability, earnings and cash flow.

As of December 31, 2011, the Company had $75.0 million of LIBOR-based variable rate borrowings under its credit facilities with IFC and OFID subject to an interest rate collar agreement, designated as cash flow hedge, to fix the interest rate of these borrowings within a floor of 1.69% and a cap of 5.0% per annum.

Additionally, as of December 31, 2011, the Company had other variable rate debt (due 2012 through 2021) totaling $142.4 million. These debts call for the Company to pay interest based on LIBOR plus a 120-365 basis point margin range. Recently, the $93.6 million facility with DVB and Natixis for the financing of our PSVs under construction in India has, within the terms and condition contained in the relevant loan agreement, used a cost of funds rate in replacement of LIBOR. The interest rates generally reset either quarterly or semi-annually. As of December 31, 2011, the weighted average interest rate on these borrowings was 3.1%.

A 1% increase in LIBOR or a 1% increase in the cost of funds used as base rate by some of our lenders would translate to a $1.4 million increase in our interest expense per year, which would adversely affect our earnings.

We have negotiated fuel price adjustment clauses in most of our contracts in the River Business. However, we may experience temporary misalignments between the adjustment of fuel in our freight contracts and our fuel purchase agreements (either positive or negative) because one may adjust prices on a monthly basis while the other adjusts prices weekly. Similarly, in some of our trades the adjustment formula may not be one hundred percent effective to reimburse us for fuel price fluctuations. Additionally, as our re-engining and repowering program progresses and more pushboats in our fleet start to consume heavy fuel (as opposed to diesel oil), the adjustment formulas in our transportation contracts will gradually cease to reflect the change in our fuel costs, resulting in gradually larger misalignments between such adjustments and our fuel purchases.

In the Offshore Supply Business, the risk of variation of fuel prices under the vessels' current employment is generally borne by the charterers, since the charterers are generally responsible for the supply and cost of fuel. During their positioning voyage from their delivery shipyard up to their area of operation and if and when a vessel is off-hire for technical or commercial reasons, fuel consumption will be for owners' account.

In our Ocean Business, for those vessels that operate under time charters, inflationary pressures on bunker (fuel oil) costs are not expected to have a material effect on the results of those vessels which are time chartered to third parties, since it is the charterers' responsibility to pay for fuel. When our ocean vessels are employed under COAs, however, freight rates for voyage charters are fixed on a per ton basis including bunker fuel for our account, which is calculated for the voyage at an assumed cost. A rise or fall in bunker prices may have a temporary negative or positive effect on results as the case may be as the actual cost of fuel purchased for the performance of a particular voyage or COA may be higher or lower than the price considered when calculating the freight for that particular voyage. Generally, in the long term, freight rates in the market should be sensitive to variation in the price of fuel. However, a sharp rise in bunker prices may have a temporary negative effect on results since freights generally adjust only after prices have settled at a higher level.

In our container feeder operation, the operation of our two container feeder vessels, M.V. Asturiano and M.V. Argentino, involves some degree of fuel price fluctuation risk since we have to pay for the cost of bunkers and although we can adjust our rates per TEU in connection with these variations, we may not always be able to, or may even be unable to, pass these variations to our customers (either fully or partially) in the future, which could have an adverse effect on our results of operations.

Seasonality

Each of our businesses has seasonal aspects, which affect their revenues on a quarterly basis. The high season for our River Business is generally between the months of March and September, in connection with the South American harvest and higher river levels. However, growth in the soy pellet manufacturing, minerals and forest industries may help offset some of this seasonality. The Offshore Supply Business operates year-round, particularly off the coast of Brazil, although weather conditions in the North Sea may reduce activity from December to February. In the Ocean Business, we employ our Product Tankers on time charters so there is no seasonality effect, while our container feeder service experiences a somewhat slower season during the first quarter due to the congestion at the main discharge terminal in Patagonia in connection with the cruise tourist season.

Results of Operations

Year Ended December 31, 2011, Compared to Year Ended December 31, 2010

The following table sets forth certain historical income statement data for the periods indicated derived from our statements of operations expressed in thousands of dollars. Operations of our Passenger Business are presented as discontinued on a net of tax basis.

	Year Ended December 31,		
	2011	2010	Percent Change
Revenues			
Attributable to River Business	$ 174,594	$ 120,024	45%
Attributable to Offshore Supply Business	64,606	54,283	19%
Attributable to Ocean Business	65,282	56,138	16%
Total revenues	304,482	230,445	32%
Voyage and manufacturing expenses			
Attributable to River Business	(87,021)	(46,661)	86%
Attributable to Offshore Supply Business	(4,083)	(3,493)	17%
Attributable to Ocean Business	(21,148)	(11,429)	85%
Total voyage expenses	(112,252)	(61,583)	82%
Running costs			
Attributable to River Business	(45,698)	(34,041)	34%
Attributable to Offshore Supply Business	(34,769)	(26,144)	33%
Attributable to Ocean Business	(31,888)	(29,154)	9%
Total running costs	(112,355)	(89,339)	26%
Amortization of drydocking and intangible assets	(4,253)	(4,491)	-5%
Depreciation of vessels and equipment	(34,891)	(29,880)	17%
Administrative and commercial expenses	(29,604)	(27,051)	9%
Other operating income, net	8,257	617	1238%
Operating profit	19,384	18,718	4%
Financial expense and other financial income (expenses), net	(37,978)	(26,417)	44%
Financial income	332	399	-17%
Gains on derivatives	(16)	10,474	-100%

Investment in affiliates	(1,073)	(341)	215%
Other, net	(621)	(875)	-29%
Total other income (expenses)	(39,356)	(16,760)	135%
(Loss) income from continuing operations before income taxes	$ (19,972)	$ 1,958	
Income tax benefit (expenses)	1,737	(6,363)	
(Loss) from continuing operations	(18,235)	(4,405)	314%
(Loss) from discontinued operations	$ --	$ (515)	-100%
Net Loss	$ (18,235)	$ (4,920)	271%
Net income (loss) attributable to non-controlling interest	570	451	26%
Net (loss) attributable to Ultrapetrol (Bahamas) Limited	(18,805)	(5,371)	250%
Amounts attributable to Ultrapetrol (Bahamas) Limited:			
(Loss) from continuing operations	(18,805)	(4,856)	287%
(Loss) from discontinued operations	--	(515)	-100%
Net (loss) attributable to Ultrapetrol (Bahamas) Limited	(18,805)	(5,371)	250%

Revenues. Total revenues from our River Business increased by 45% from $120.0 million in 2010 to $174.6 million in 2011. This $54.6 million increase is mainly attributable to a 14% increase in net tons transported which translated into a $16.0 million increase in revenues, a $14.4 million increase related to increases in freight revenues as a result of the fuel adjustment formula in our contracts of affreightments, coupled with a $2.6 million increase due to changes in cargo mix and average price increases and $2.5 million increase in other river revenues. The remaining $19.1 million increase is explained by the sale of twenty dry bulk cargo barges constructed at our yard in Punta Alvear for third parties.

Total revenues from our Offshore Supply Business increased by 19% from $54.3 million in 2010 to $64.6 million in 2011. This $10.3 million increase is primarily attributable to the $8.7 million additional revenue generated by our UP Turquoise which commenced its charter with Petrobras on March 12, 2011, to an increase in revenues of $2.7 million of our vessels UP Esmeralda and UP Safira on account of their fewer operational days during the first quarter of 2010 due to their positioning from the North Sea to Brazil in addition to time lost for their registration in Brazil, coupled with a $2.4 million increase on account of our UP Jasper which had a 10-day spot operation while repositioning from China to the North Sea in addition to its charter initiation with Nexen on September 29, 2011; partially offset by a $2.4 million decrease in revenues of our UP Agua-Marinha and UP Topazio on account of their drydocks held on the first quarter and second quarter of 2011, respectively, to a $0.9 million decrease related to the offhire days of our UP Rubi on account of repairs during the first quarter of 2011 and to a $0.2 million decrease on account of the drydock undergone by our UP Diamante during the fourth quarter of 2011.

Total revenues from our Ocean Business increased $9.1 million, from $56.1 million in 2010 to $65.3 million in 2011, or 16%. This increase is mainly attributable to a combined $26.3 million increase in revenues of our vessels M.V. Asturiano and M.V. Argentino which commenced operation on May 21, 2010, and January 10, 2011, respectively, coupled with a combined $2.5 million increase in revenues of our Product Tankers on account of charter rate adjustments in accordance with manning expense increases; partially offset by an $15.0 million decrease in revenues on account of the sale of our Princess Marisol and Princess Katherine which were sold and delivered on April 23, 2010, and September 15, 2010, respectively, and to a $4.2 million decrease related to the re-delivery of the Mediator I, which was under bareboat charter to us, on October 6, 2010.

Voyage and manufacturing expenses. In 2011, voyage and manufacturing expenses of our River Business were $87.0 million, as compared to $46.7 million for 2010, an increase of $40.3 million, or 86%. This increase is attributable to $17.1 million increase related to higher fuel costs associated to higher fuel prices and larger volumes consumed consistent with an increase in the volume of cargo transported, to a $12.7 million increase related to the manufacturing expenses incurred in the construction of barges for third parties in our Punta Alvear yard and to a $10.5 million increase related to higher port expenses, such as charge and discharge expenses, port dues and agency fees and third party harbor tug expenses, mainly attributable to larger volumes carried, as well as higher costs.

In 2011, voyage expenses of our Offshore Supply Business were $4.1 million, as compared to $3.5 million in 2010. This increase of $0.6 million, or 17%, is primarily attributable to a $1.3 million increase related to the positioning voyages of our UP Turquoise and UP Jasper from China to Brazil and the North Sea, respectively, coupled with a $0.2 million increase related to the operation of those vessels in their respective markets; partially offset by a $0.6 million decrease in the brokerage commissions of our UP Rubi, UP Agua-Marinha, UP Topazio and UP Diamante related to the greater off-hire days of these vessels during 2011, coupled with a $0.5 million decrease related to an importation tax incurred by our UP Esmeralda and UP Safira during 2010 when they were moved into Brazil.

In 2011, voyage expenses of our Ocean Business were $21.1 million, as compared to $11.4 million for 2010, an increase of $9.7 million, or 85%. This increase is primarily attributable to a $15.2 million increase in voyage expenses of our vessels M.V. Asturiano and M.V. Argentino which commenced operation on May 21, 2010, and January 10, 2011, respectively, and whose bunker costs and port expenses are borne by us; partially offset by a $1.8 million

decrease on account of the hire expenses of the Austral as a result of its bareboat contract renewal with her owners at a lower rate, a $1.5 million decrease on account of the re-delivery of the Mediator I to its owners (under bareboat charter to us) on October 6, 2010, and a $1.2 million decrease on account of the sale of our Princess Marisol and Princess Katherine on April 23, 2010, and September 15, 2010, respectively.

Running costs. In 2011, running costs of our River Business were $45.7 million, as compared to $34.0 million in 2010, an increase of $11.7 million, or 34%. This increase in costs is mainly attributable to a $10.0 million increase in crew and maintenance costs as well as other running costs.

In 2011, running costs of our Offshore Supply Business were $34.8 million, as compared to $26.1 million in 2010, an increase of $8.7 million, or 33%. This increase in running costs is mainly attributable to a $5.0 million increase on account of the delivery of our UP Turquoise and UP Jasper on December 20, 2010, and June 10, 2011, respectively, coupled with a general increase in crew and maintenance costs of our PSV fleet of $3.7 million mainly attributable to the revaluation of the local currency against the U.S. dollar for part of 2011.

In 2011, running costs of our Ocean Business were $31.9 million, as compared to $29.2 million in 2010, an increase of $2.7 million, or 9%. This variation results mainly from a $6.0 million increase in running costs of our vessels M.V. Asturiano and M.V. Argentino which were delivered to us on April 16, 2010, and December 14, 2010, respectively, coupled with a $4.8 million increase in crew and maintenance costs of our Tanker vessels and Parana Petrol; partially offset by a $5.7 million decrease in running costs of our Capesize vessels Princess Nadia, Princess Marisol and Princess Katherine which were sold and delivered on January 28, 2010, April 23, 2010, and September 15, 2010, respectively, and by a $2.3 million decrease related to the re-delivery of the Mediator I on October 6, 2010, which was under bareboat charter to us. Also, in general, inflation in the local currency not reflected in an equivalent variation of the rate of exchange affected negatively our running costs for the period.

Amortization of drydocking and intangible assets. Amortization of drydocking and intangible assets in 2011 was $4.3 million, as compared to $4.5 million, a decrease of $0.2 million, or 5%. This decrease is primarily attributable to a $0.6 million decreased level of amortization of drydock of our dry barges and to the elimination of the amortization of drydock of $0.5 million on our sold Capesize vessel Princess Katherine; partially offset by an increased level of amortization of drydock of $0.5 million for our PSV fleet, coupled with an increased level of amortization of drydock of $0.4 million of our Amadeo Product Tanker.

Depreciation of vessels and equipment. Depreciation increased by $5.0 million, or 17%, to $34.9 million in 2011, as compared to $29.9 million in 2010. This increase is primarily attributable to $2.8 million associated to the entry into operation of our jumbo barges built at Punta Alvear, Argentina, by a $2.7 million increase in depreciation of our vessels M.V. Asturiano, M.V. Argentino, UP Turquoise and UP Jasper, which were delivered to us on April 16, 2010, December 14, 2010, December 20, 2010, and June 10, 2011, respectively, and by a $0.7 million increased depreciation related to the certification works performed on our Parana Petrol prior to its entry into operation; partially offset by a $1.6 million lower depreciation of our Capesize vessels Princess Marisol and Princess Katherine which were sold in 2010.

Administrative and commercial expenses. Administrative and commercial expenses were $29.6 million in 2011 as compared to $27.1 million in 2010, resulting in an increase of $2.5 million, or 9%. This increase is associated with increases in legal and other fees and increases in the cost of shore based personnel in our Ocean, River and Offshore Supply Businesses mainly as a result of general inflation in the local currency not reflected in an equivalent variation of the rate of exchange.

Other operating income, net. Total other operating income increased from $0.6 million in 2010 to $8.3 million in 2011, a $7.7 million increase. This increase is mainly explained by a $4.8 million increase related to a favorable arbitration settlement of our River Business subsidiary, $1.5 million loss of hire coverage insurance for the time lost by our UP Rubi during the first quarter of 2011, to a $1.3 million loss of hire coverage insurance for the time lost by our UP Diamante, and to a $0.6 million increase on account of an insurance claim of our UP Jasper; partially offset by $0.8 million loss of hire insurance cover for time lost of our UP Esmeralda in the first quarter of 2010.

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Operating profit. Operating profit for the year 2011 was $19.4 million, an increase of $0.7 million from $18.7 million operating profit in 2010. This increase is mainly attributable to a $3.2 million increase in our River Business operating profit from $10.2 million in 2010 to $13.1 million in 2011 including a $4.8 million increase related to a favorable arbitration settlement with a former client and by a $4.5 million operating profit resulting from barge sales to third parties, partially offset by higher operating costs; to a $0.4 million increase in operating profit of our Offshore Supply Business driven mainly by a $3.3 million increase related to the entry into operation of our UP Turquoise on March 12, 2011, and by a $2.2 million increase of our UP Esmeralda and UP Safira on account of their positioning from the North Sea to Brazil where they operated at higher rates than they obtained during 2010 in the North Sea, partially offset by a $4.4 million decrease of our UP Agua-Marinha and UP Topazio on account of their drydocks held on the first quarter and second quarter of 2011, respectively; and to a $2.6 million decrease in operating profit of our Ocean Business from a $2.1 million operating loss in 2010 to a $4.7 million operating loss in 2011 driven mainly by a $5.1 million decrease in operating profit related to the sale of our Capesize vessels Princess Marisol and Princess Katherine coupled with a $3.8 million general increase in costs in local currency, partially offset by a $5.2 million increase due to the operation of our two feeder container vessels M.V. Asturiano and M.V. Argentino.

Financial expense and other financial income (expenses), ne. Financial expense and other financial expenses increased $11.6 million to $38.0 million in 2011, as compared to $26.4 million in 2010. This increase is mainly attributable to a $5.5 million increase in financial expenses due to the issuance of the Convertible Notes, to a $2.1 million increase related to exchange rate differences, a $1.4 million increase related to the commitment fee and margin rate increase in our $93.6 million DVB-Natixis facility, to a $1.0 million increase related to the drawdowns under the DVB – Banco Security financing in connection with the deliveries of our UP Turquoise and UP Jasper, to a $0.8 million increase related to the interest capitalization on our $61.3 million DVB loan, and to a $0.4 million increase in the interest rate as a result of an interest rate collar derivative entered into with IFC in May 2010.

Financial income. Financial income in 2011 decreased by $0.1 million to $0.3 million from $0.4 million in 2010. This decrease is mainly attributable to lower interest received on lower average cash balances.

Gains on derivatives. Gain on derivative instruments decreased to zero in 2011, from $10.5 million in the same period of 2010. This decrease is attributable to the closing of our derivatives contracts due to the sale of our Capesize vessels Princess Nadia, Princess Marisol and Princess Katherine which were sold and delivered on January 28, 2010, April 23, 2010, and September 15, 2010, respectively.

Income taxes benefit (expenses). Income taxes benefit increased by $8.1 million, from an income tax expense of $6.4 million in 2010 to an income tax benefit of $1.7 million in 2011. This change is mainly explained by a decrease of $2.6 million in the current income tax expense and for a change of $5.4 million in the deferred income tax from a deferred income tax expense of $1.8 million in 2010 to a deferred income tax benefit of $3.6 million in 2011. The decrease in the current income tax expense is mainly explained by a decrease of $1.7 million in the income tax expense of our Offshore Supply Business operations in Brazil and for a one-time payment in 2010 of $1.3 million made to the tax authorities of Paraguay in full settlement of a claim pertinent to years 2002 to 2004; partially offset by an increase of $0.5 million in the income tax in Argentina. The change in the deferred income tax is mainly explained by a decrease of $4.7 million of the provision of the deferred tax for unrealized exchange differences in our Brazilian subsidiary due to the devaluation of the Brazilian real during 2011 as compared to a revaluation during 2010.

Non-controlling interest. Non-controlling interest increased by $0.1 million to $(0.6) million in 2011 as compared to $(0.5) in 2010. This increase is attributable to higher results of our subsidiary in the Offshore Supply Business where we have a non-controlling partner that owns 5.56% of our Offshore Supply Business.

(Loss) from discontinued operations. Losses from discontinued operations, net of tax, decreased by $0.5 million from a loss of $0.5 million in 2010 to zero in 2011. This decrease in loss is attributable to the expenses and overhead related

to our passenger vessel Blue Monarch which remained in lay up during 2009 until it was delivered to her new buyers on February 5, 2010.

Year Ended December 31, 2010, Compared to Year Ended December 31, 2009

The following table sets forth certain historical income statement data for the periods indicated derived from our statements of operations expressed in thousands of dollars. Operations of our Passenger Business are presented as discontinued operations on a net of tax basis.

	Year Ended December 31,		
	2010	2009	Percent Change
Revenues			
Attributable to River Business	$ 120,024	$ 79,477	51%
Attributable to Offshore Supply Business	54,283	35,419	53%
Attributable to Ocean Business	56,138	105,633	-47%
Total revenues	230,445	220,529	4%
Voyage expenses			
Attributable to River Business	(46,661)	(36,566)	28%
Attributable to Offshore Supply Business	(3,493)	(3,169)	10%
Attributable to Ocean Business	(11,429)	(20,840)	-45%
Total voyage expenses	(61,583)	(60,575)	2%
Running cost			
Attributable to River Business	(34,041)	(29,285)	16%
Attributable to Offshore Supply Business	(26,144)	(18,172)	44%
Attributable to Ocean Business	(29,154)	(32,575)	-11%
Total running costs	(89,339)	(80,032)	12%
Amortization of drydocking and intangible assets	(4,491)	(4,143)	8%
Depreciation of vessels and equipment	(29,880)	(37,609)	-21%
Loss on write-down of vessels	--	(25,000)	
Administrative and commercial expenses	(27,051)	(25,065)	8%
Other operating income, net	617	2,844	-78%
Operating profit (loss)	18,718	(9,051)	
Financial expense and other financial income (expenses), net	(26,417)	(23,237)	14%
Financial income	399	340	17%
Gains on derivatives	10,474	241	4,246%
Investment in affiliates	(341)	(28)	1,136%
Other, net	(875)	(707)	24%
Total other income (expenses)	(16,760)	(23,391)	-28%
Income (loss) from continuing operations before income taxes	$ 1,958	$ (32,442)	
Income taxes (expenses) benefit	(6,363)	(5,355)	19%
(Loss) Income from continuing operations	(4,405)	(37,797)	-88%
(Loss) from discontinued operations	$ (515)	$ (2,131)	-76%
Net Loss	$ (4,920)	$ (39,928)	-88%
Net income (loss) attributable to non-controlling interest	451	(90)	
Net (loss) income attributable to Ultrapetrol (Bahamas) Limited	(5,371)	(39,838)	-87%

Amounts attributable to Ultrapetrol (Bahamas) Limited:			
(Loss) from continuing operations	(4,856)	(37,707)	-87%
(Loss) from discontinued operations	(515)	(2,131)	-76%
Net (loss) attributable to Ultrapetrol (Bahamas) Limited	(5,371)	(39,838)	-87%

Revenues. Total revenues from our River Business increased by 51% from $79.5 million in 2009 to $120.0 million in 2010. This $40.5 million increase is mainly attributable to a 31.9% increase in net tons transported on account of a larger crop in Paraguay in 2010, as opposed to 2009 when a severe drought affected soybean production in the region and to a 7% increase in freight per ton due to average price increases and changes in cargo mix (excluding fuel passthrough); coupled with an increase in freight revenues of $9.3 million as a result of the fuel adjustment formula in our contracts of affreightment. This increase was marginally offset by a $1.6 million decrease in other river services revenue.

Total revenues from our Offshore Supply Business increased by 53% from $35.4 million in 2009 to $54.3 million in 2010. This $18.9 million increase is primarily attributable to the $6.6 million additional revenue generated by a full year operation of our UP Rubi delivered on August 7, 2009, to an increase in revenues of $7.2 million of our vessels UP Esmeralda and UP Safira which entered into long term charters with Petrobras in February 2010 after repositioning from the North Sea in December 2009, to the additional $2.6 million generated by the operation of our UP Agua-Marinha and UP Diamante under their renewed long-term time charters with Petrobras in Brazil at higher rates and to a $2.5 million increase in revenues of our UP Topazio which operated in Brazil during the whole of 2010, as opposed to 2009 when her repositioning generated a total time loss of 49 days.

Total revenues from our Ocean Business decreased $49.5 million, from $105.6 million in 2009 to $56.1 million in 2010, or a decrease of 47%. This decrease is mainly attributable to a decrease in net settlements of the FFA positions accounted for as cash flow hedges of $21.6 million, the sale of our Princess Susana on December 10, 2009, the sale of our Princess Nadia on January 28, 2010, the partial operation of our Princess Marisol and our Princess Katherine, which were sold on April 23, 2010, and September 15, 2010, respectively; coupled with lower time charter rates of the BCI in 2010 of $33,298 per day as opposed to $42,656 per day in 2009; partially offset by the entry into operation of the new feeder container vessel M.V. Asturiano on May 21, 2010, and by the positive rate adjustment on the charters of our Alejandrina, Miranda I and Austral.

Voyage expenses. In 2010, voyage expenses of our River Business were $46.7 million, as compared to $36.6 million for 2009, an increase of $10.1 million, or 28%. This increase is mainly attributable to the larger fuel consumption consistent with the 31.9% increase in net tons transported, coupled with an increase in fuel expense as a result of higher fuel prices in the period and increases in other port expenses such as charge and discharge expenses, port dues, custom charges and channel dues.

In 2010, voyage expenses of our Offshore Supply Business were $3.5 million, as compared to $3.2 million in 2009. This increase of $0.3 million, or 9%, is primarily attributable to increased expenses related to brokerage commissions as a result of the higher earnings incurred by our vessels during 2010 relative to 2009; partially offset by higher bunker expenses in 2009 attributable to the repositioning of our UP Topazio and UP Safira coupled with the contractual penalty associated with the late delivery of our UP Rubi to Petrobras that took place in 2009.

In 2010, voyage expenses of our Ocean Business were $11.4 million, as compared to $20.8 million for 2009, a decrease of $9.4 million, or 45%. This decrease is primarily attributable to a $13.4 million decrease in voyage expenses of our Capesize vessels Princess Susana, Princess Nadia, Princess Marisol and Princess Katherine which were sold in December 2009 and January, April and September 2010, respectively; partially offset by a $3.7 million increase in voyage expenses due to the entry into operation of our feeder container vessel M.V. Asturiano in May 2010.

Running costs. In 2010, running costs of our River Business were $34.0 million, as compared to $29.3 million in 2009, an increase of $4.7 million, or 16%. This increase in costs is mainly attributable to a higher number of pushboats in operation consistent with the increase in net tons transported during the period.

In 2010, running costs of our Offshore Supply Business were $26.1 million, as compared to $18.2 million in 2009, an increase of $7.9 million, or 44%. This increase in running costs is mainly attributable to the full year operation of our UP Rubi in 2010 which generated additional running costs of $2.7 million, to a $2.2 million increase in crew costs associated to the operation of our vessels in Brazil in 2010 as opposed to 2009 when our UP Esmeralda, UP Safira and UP Topazio were located in the North Sea and a $2.1 million increase in general maintenance costs of our vessels.

In 2010, running costs of our Ocean Business were $29.2 million, as compared to $32.6 million in 2009, a decrease of $3.4 million, or 10%. This variation results mainly from a $10.2 million decrease in running costs of our Capesize vessels Princess Susana, Princess Nadia, Princess Marisol and Princess Katherine which were sold in December 2009, January, April and September 2010, respectively; partially offset by a $3.6 million increase in running costs of our vessel M.V. Asturiano which initiated operation in May 2010 and by a $2.3 million increase in crew and maintenance costs of our Product tanker fleet.

Amortization of drydocking and intangible assets. Amortization of drydocking and intangible assets in 2010 was $4.5 million, as compared to $4.1 million, an increase of $0.4 million, or 10%. This increase is primarily attributable to a $0.5 million increase in drydock amortization of our PSV fleet (UP Esmeralda, UP Safira, UP Diamante), a joint amortization of drydock of our Amadeo and Princess Katherine of $0.6 million, a $0.3 million increase of the drydock amortization of our River fleet; partially offset by a reduced level of amortization of drydock of $0.7 million on the recently sold Capesize vessels Princess Susana and Princess Nadia and decrease of $0.4 million due to the full amortization of certain intangible assets of Ravenscroft Ship Management.

Depreciation of vessels and equipment. Depreciation decreased by $7.7 million, or 21%, to $29.9 million in 2010, as compared to $37.6 million in 2009. This decrease is primarily attributable to the sale of our Capesize vessels Princess Susana, Princess Nadia, Princess Katherine and Princess Marisol which accounted for a reduction of $13.3 million; partially offset by a $1.8 million increase in depreciation associated to the start of operation of our new shipyard at Punta Alvear, a $1.3 million increase in our dry barge fleet depreciation on our River Business, a $0.7 million increase related to the start of operations of our UP Rubi in August 2009 and a $0.5 million increase due to the start of operations of our container feeder vessel M.V. Asturiano delivered on April 16, 2010.

Administrative and commercial expenses. Administrative and commercial expenses were $27.1 million in 2010 as compared to $25.1 million in 2009, resulting in an increase of $2.0 million or 8%. This increase is mainly associated with $1.1 million increase in legal and other fees and $0.9 million increase in cost of personnel.

Loss on write-down of vessels. Loss on write-down of vessels was nil for 2010 as compared to the non-cash loss of $25.0 million included in 2009 corresponding to an impairment of the book value of our Princess Marisol.

Other operating income, net. Total other operating income decreased 78%, from $2.8 million in 2009 to $0.6 million in 2010, a $2.2 million decrease. This decrease is mainly attributable to a $0.7 million decrease in the results from the sale of vessels ($1.4 million gain on sale of the Princess Susana in 2009 as compared to $0.7 million total combined gain on the sales of Princess Nadia, Princess Marisol and Princess Katherine), coupled with a $2.1 million decrease in insurance income attributable to the Princess Susana, partially offset by $0.8 million income from insurance associated to one of our PSVs in 2010.

Operating (loss) profit. Operating profit for the year 2010 was $18.7 million, an increase of $27.8 million from $(9.1) million operating loss in 2009. This increase is mainly attributable to a $20.0 million increase in our River Business operating profit that resulted mainly from the increase in net tons transported year on year, a $9.9 million increase of our Offshore Supply Business operating profit mainly driven by the full year operation of our UP Rubi which was delivered on August 7, 2009, improved charter rates prevailing in Brazil relative to those earned in the North Sea during 2009 and less repositioning days lost during 2010 compared to 2009; partially offset by a $1.9 million decrease in our Ocean Business operating profit mainly explained by the sale of our Capesize vessel Princess Susana in 2009 and Princess Nadia, Princess Marisol and Princess Katherine in 2010.

Financial expense and other financial income (expenses). Financial expense and other financial expenses increased $3.2 million to $26.4 million in 2010, as compared to $23.2 million in 2009. This increase is mainly attributable to exchange rate fluctuations of foreign currencies against the U.S. dollar in 2010 as compared to 2009 coupled with an increase in amortized debt costs and an increase in interest expenses due to the discontinuation of interest capitalization upon start of operations at our Punta Alvear Yard; partially offset by a decrease in the average LIBO rate in 2010 compared to 2009.

Financial income. Financial income in 2010 increased by $0.1 million to $0.4 million from $0.3 million in 2009. This increase is mainly attributable to a higher cash balance held on average in 2010 as compared to 2009; partially offset by lower average interest rates in 2010 than the previous year.

Gains on derivatives. Gain on derivative instruments increased $10.3 million to $10.5 million in 2010, from $0.2 million in 2009. This increase was primarily attributable to a $10.5 million realized gain on the remaining FFA positions outstanding in 2010 as a result of the de-classification of those positions as cash from hedges for accounting purposes.

Income taxes (expenses). The income tax expense for 2010 was $6.4 million, compared to an expense of $5.4 million in 2009. This $1.0 million increase of the income tax expense is mainly attributable to the increase in the income tax expense of our Offshore Business deriving from the entry into operation of six PSVs in the Brazilian market as opposed to only four and a half, on average, during 2009 and the income tax expense of our River Business operations which includes a one-time payment in 2010 of $1.3 million made to the tax authorities of Paraguay in full settlement of a claim pertaining to years 2002 to 2004; partially offset by a lower provision of the deferred tax for unrealized exchange differences in our Brazilian subsidiary due to the lower revaluation of the Brazilian real during 2010 as compared to 2009.

Non-controlling interest. Non-controlling interest increased by $0.6 million to $(0.5) million in 2010 as compared to $0.1 million in 2009. This increase is attributable to higher results of our subsidiary in the Offshore Supply Business where we have a non-controlling partner that holds 5.56% of our Offshore Supply Business.

(Loss) from discontinued operations. Losses from discontinued operations, net of tax, decreased by $1.6 million from a loss of $2.1 million in 2009 to a loss of $0.5 million in 2010. This decrease in loss is mainly attributable to the expenses and overhead related to our passenger vessel Blue Monarch which remained in lay up during 2009 until it was delivered to her new buyers on February 5, 2010.

B. LIQUIDITY AND CAPITAL RESOURCES

We are a holding company and operate in a capital-intensive industry requiring substantial ongoing investments in revenue producing assets. Our subsidiaries have historically funded their vessel acquisitions through a combination of debt, shareholder loans, cash flow from operations and equity contributions.

The ability of our subsidiaries to make distributions to us may be restricted by, among other things, restrictions under our credit facilities and applicable laws of the jurisdictions of their incorporation or organization.

At December 31, 2011, we had aggregate indebtedness of $513.0 million, consisting of $180.0 million aggregate principal amount of our 2014 Notes, $80.0 million aggregate principal amount of our Convertible Notes, indebtedness of our subsidiary UP Offshore Apoio Maritimo Ltda. under a senior loan facility with DVB Bank AG, or DVB, of $7.8 million and $16.9 million under a loan facility with BNDES, indebtedness of our subsidiary UP Offshore (Bahamas) Ltd. of $53.2 million under two senior loan facilities with DVB and $37.5 million under an additional senior loan agreement with DVB and Banco Security as co-lenders, indebtedness of our subsidiary Ingatestone Holdings Inc. of $31.1 million under a senior loan facility with DVB and Natixis as co-lenders, indebtedness of our subsidiary Stanyan Shipping Inc. of $9.3 million under a senior loan facility with Natixis, indebtedness of our subsidiary Hallandale Commercial Corp. of $7.2 million under a senior loan facility with Nordea Bank, indebtedness of our subsidiaries UABL Barges (Panama) Inc., Marine Financial Investment Corp., Eastham Barges Inc. and UABL Paraguay S.A. of $60.0 million in the aggregate under two senior loan facilities with International Finance Corporation, or IFC, indebtedness of our subsidiary UABL Paraguay S.A. of $15.0 million under a senior loan facility with The OPEC Fund for International Development, or OFID, and indebtedness of our subsidiaries UABL Paraguay S.A. and Riverpar S.A. of $15.0 million under a senior loan facility with IFC and OFID as co-lenders and accrued interest of $4.8 million. Please refer to "Description of Credit Facilities and Other Indebtedness" elsewhere herein.

At December 31, 2011, we had cash and cash equivalents on hand of $34.1 million.

Operating Activities

During the year ended December 31, 2011, we generated $14.8 million in cash flow from operations compared to $18.9 million in the year ended December 31, 2010. This decrease of $ 4.1 million, or 22%, in cash flow from operations is mainly attributable to $12.6 million additional cash used to fund increases in assets, to $2.1 million of cash used in the decrease of liabilities and to a $2.6 million increase in funds used for general and administrative expenses; partially offset by $7.6 million increase in cash provided by other operating income coupled with $4.7 million decrease in cash used to fund drydocking expenditures. Finally, the Gross Profit Contribution, or GPC, overall increase in cash during the period was $0.4 million, resulting from an increase of $2.6 million in our GPC from our River Business mostly as a result of the higher net tons transported and higher average freight rates, coupled with the increase in GPC of our Offshore Supply Businesses of $1.1 million as a result of the operations of our UP Turquoise and UP Jasper which commenced their operations on March 12, 2011, and September 29, 2011, respectively; partially offset by the decrease in GPC of our Ocean Business of $3.3 million.

During the year ended December 31, 2010, we generated $18.9 million in cash flow from operations compared to $38.7 million in the year ended December 31, 2009. Cash flow from operating activities decreased by $19.8 million, to $18.9 million in 2010, from $38.7 million in 2009. This decrease of 51% in cash flow from operations is mainly attributable to $21.5 million additional cash used to fund increases in assets, partially offset by $14.5 million in cash generated by an increase in liabilities, coupled with a $3.0 million increase in cash used to fund drydocking expenditures (mainly in our Offshore Supply Business), a $2.3 million decrease in cash provided by other operating income and with a $2.5 million increase in funds used for general and administrative expenses. Finally, the GPC overall increase in cash used during the period was $0.4 million, resulting from a decrease of $36.7 million in our

GPC from our Ocean Business, which was almost entirely offset by the respective increases in GPC by our River and Offshore Supply Businesses of $25.7 million and $10.6 million respectively, mainly attributable to larger volumes carried on the River Business, to improved rates and more operating days on our Offshore fleet now fully operating in Brazil.

Investing Activities

During the year ended December 31, 2011, $35.5 million in the construction of new barges in our Punta Alvear, $9.4 million to refurbish barges and pushboats, $8.1 million related to the re-engining program, $6.6 million to fund the acquisition and commissioning of two line pushboat and one port pushboat, $2.4 million to complete the refurbishment and re-engining of our new pushboat Pampero I, $2.0 million to fund the construction of an additional port pushboat and $1.9 million for our new barge building yard, in our River Business; $13.5 million to fund the advances on the four PSVs that are being constructed in India and $5.2 million to fund the advances on the two PSVs delivered during 2011 from China, in our Offshore Supply Business; $2.1 million to fund additional improvements and steel replacement on our Parana Petrol , $1.8 million for the acquisition of office space in Buenos Aires, Argentina, $0.8 million to fund repairs made to our feeder container vessel, M.V. Argentino and we disbursed $0.1 million to acquire secondhand containers for our container feeder service, in our Ocean Business.

Financing Activities

Net cash provided by financing activities was $11.6 million during the year ended December 31, 2011, compared to $87.6 million during the year ended December 31, 2010, a $76.0 million decrease in cash provided by financing activities. This decrease in cash flow provided by financing activities is mainly attributable to a $76.1 million decrease in net proceeds from issuance of 7.25% Senior Convertible Notes due 2017, an increase of $25.5 million in revolving credit facility repayments, an increase of $2.0 million in scheduled repayments of long-term financial debt; partially offset by an increase of $16.9 million in proceeds from long-term financial debt, an increase of $10.5 million in revolving credit facility borrowings and by a $0.2 million increase in net cash provided by other financial activities.

Future Capital Requirements

Our near-term cash requirements are related primarily to funding operations, constructing new vessels, potentially acquiring other assets including second-hand ocean vessels, rebottoming some of our barges, funding the construction of barges in our new shipyard at Punta Alvear and replacing the engines in our line pushboats with new engines that burn heavy fuel which has been historically less expensive than the types of fuel currently used. We estimate that for 2012, our total investment in new barge construction, rebottoming of existing barges and reengining of our line pushboats, will range between $12.5 million and $25.0 million. We currently estimate that the construction of new vessels that are currently on order in India will require additional funds of approximately $26.4 million (provided no late delivery penalties are applied to the shipyard), which will be mainly financed with the undrawn proceeds committed under the DVB / Natixis loan facility. We expect to disburse an aggregate amount of $3.0 million in drydock expenses.

We may order additional vessels and or incur other capital expenditures, which are not discussed above or contemplated at this time. The funds will be disbursed at various times over the next few years and, accordingly, are subject to significant uncertainty. We may in the future incur indebtedness to fund some of our other initiatives, which we are currently funding through our cash flow from operations. We cannot provide assurance that our actual cash requirements will not be greater than we currently expect. If we cannot generate sufficient cash flow from operations, we may obtain additional sources of funding through capital market transactions, although it is possible these sources will not be available to us.

Critical Accounting Policies and Estimates

This discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues

and expenses and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

Critical accounting policies are those that reflect significant judgments or uncertainties and potentially lead to materially different results under different assumptions and conditions. We have described below what we believe are our most critical accounting policies that involve a high degree of judgment and the methods of their application. For a description of all of our significant accounting policies, see Note 2 to our audited consolidated financial statements.

Revenue Recognition

We record revenue when services are rendered, when we have signed a charter agreement or another evidence of an arrangement, pricing is fixed or determinable and collection is reasonably assured.

The Company does not begin recognizing revenue if the charter agreement has not been entered into with the customer, even if the vessel has discharged its cargo and is sailing to the anticipated load port on its next voyage.

We earn our revenues under time charters, bareboat charters, consecutive voyage charters or affreightment / voyage contracts and contracts for sale of barges to third parties. We earn and recognize revenue from time charters and bareboat charters on a daily basis. Within the shipping industry, there are two methods used to account for consecutive voyage charters or affreightment / voyage contracts: (1) ratably over the estimated length of each voyage and (2) completed voyage. The recognition of voyage revenues ratably over the estimated length of each voyage is the most prevalent method of accounting for voyage revenues and the method used by us. Under each method, voyages may be calculated on either a load-to-load or discharge- to-discharge basis. In applying its revenue recognition method, management believes that the discharge-to-discharge basis of calculating voyages more accurately estimates voyage results than the load-to-load basis. Since, at the time of discharge, management generally knows the next load port and expected discharge port, the discharge-to-discharge calculation of voyage revenues can be estimated with a greater degree of accuracy.

In our River Business we use the completed contract method for river barges built, which typically has construction periods of 30 days or less. Contracts are considered complete when title has passed, the customer has accepted the river barges and we do not retain risks or rewards of ownership of the river barges. Losses are accrued if manufacturing costs are expected to exceed manufacturing contract revenue.

Manufacturing expenses are primarily composed of steel costs which is the largest component of our raw materials and the cost of labor.

We account for multiple element arrangements, in accordance with ASC 605-25. For such transactions, revenue on arrangements that include multiple elements is allocated to each element based on the relative fair value of each element and fair value is determined by vendor-specific objective evidence of fair value (VSOE).

Insurance claims receivable

Insurance claims receivable comprise claims submitted relating to Hull and Machinery (H&M), Protection and Indemnity (P&I), Loss of Hire (LOH) and Strike insurance coverage. They are recorded when the recovery of an insurance claim is probable. Deductible amounts related to covered incidents are expensed in the period of occurrence of the incident. The amount of the receivable is based on the type of the claim. These receivables are estimated based upon the insured losses incurred on damages to the vessels and historical experience with similar claims. These claims are subject to uncertainty related to the results of negotiated settlements and other developments.

Depreciation

We state vessels and equipment at cost less accumulated depreciation. This cost includes the purchase price and all directly attributable costs (initial repairs, improvements and delivery expenses, interest and on-site supervision costs incurred by us during the construction periods). We also capitalize subsequent expenditures for conversions, renewals or major improvements when they appreciably extend the life, increase the earning capacity or improve the safety features of our vessels.

We compute depreciation net of the estimated scrap value, which is equal to the product of each vessel's lightweight tonnage and estimated scrap value in US dollars per lightweight ton, or lwt. We use scrap value at the time the vessel was purchased or delivered by the shipyard, which will likely fluctuate over time. The estimated scrap value ranges from $180 to $300 per lwt. Estimated scrap values are based on price levels in effect at the time vessels are purchased.

We record depreciation using the straight-line method over the estimated useful lives of our vessels. Useful life is determined through economic analysis, such as reviewing existing fleet plans, obtaining appraisals and comparing estimated lives to other industrial transportation companies that operate similar fleets. Second hand vessels are assigned lives that are generally consistent with the experience of Ultrapetrol, the practice of other industrial transportation companies and laws or regulations affecting the vessels operations.

Drydocking

Within the shipping industry, two methods are used to account for drydockings: (1) the deferral method, in which drydocking costs are capitalized and then amortized over the estimated period to the next scheduled drydocking and (2) the incurred method, in which drydocking costs are expensed as incurred. We use the deferral method and amortize drydocking costs on a straight-line basis over the period to the next drydock, generally 24 to 36 months. The costs we incur at the dry-dock yard are mainly comprised of steel renewals, painting the vessel's hull and sides, recoating cargo and fuel tanks and performing engine and equipment maintenance activities which have to be made in order to bring or keep the vessel into compliance with classification standards. We expense expenditures for maintenance and minor repairs as we incur them. We believe the deferral method better matches costs with revenue than expensing the costs as incurred. We use judgment when estimating the period between drydocks performed, which can result in adjustments to the amortization expense if the subsequent drydock is expected earlier than anticipated. In estimating the periods, we primarily have relied upon actual experience with the same or similar vessels types, current and projected future market information and recommendations from classification societies.

Impairment of long-lived assets

We perform tests for impairment of long-lived assets whenever events or circumstances suggest that long-lived assets may not be recoverable. An impairment is only deemed to have occurred if the forecasted undiscounted future cash flows related to the assets are less than the carrying value of the assets. If the forecasted cash flows from long lived assets are less than the carrying value of such assets, then we must write down the carrying value to its estimated fair value. This assessment is made at the individual vessel level if separately identifiable cash flow information for each vessel is available. The cash flow period is based on the remaining lives of the vessels, which range from 4 to 24 years. Forecasting future cash flows involves the use of significant estimates and assumptions. Revenue and expense assumptions used in the cash flow projections are consistent with internal projections and reflect our current economic outlook.

In developing estimates of future cash flows, the Company must make assumptions about future charter rates, ship operating expenses, estimated scrap values and the estimated remaining useful lives of the vessels. These assumptions are based on historical trends as well as future expectations. Although management believes that the assumptions used to evaluate potential impairment are reasonable and appropriate, such assumptions are highly subjective.

During 2009, given the overriding effects of the global economic slowdown, demand for the dry-bulk Ocean Business vessels was soft. Accordingly, based upon the information that was known to it as of December 31, 2009, the Company recorded an impairment charge of $25.0 million to write down the carrying amount of its Capesize vessel, Princess Marisol, to its estimated fair value as of December 31, 2009.

Freight Forward Agreements (FFA)

From time to time we enter into FFAs either via a clearing house or over the counter with an objective to utilize them as hedging instruments that reduce our exposure to volatility in the spot market rates earned by certain of our vessels in the normal course of our Ocean Business.

We recognize all of our derivative instruments as either assets or liabilities in the balance sheet at fair value. The accounting for changes in the fair value (i.e., gains or losses) of a derivative financial instrument depends on whether it has been designated and qualifies as part of a hedging relationship and the type of hedging relationship.

For derivative financial instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative financial instrument is reported as a component of other comprehensive income and

reclassified into earnings in the same line item associated with the hedged transaction in the same period or periods which the hedged transaction affects earnings. The ineffective portion of a derivative's change in fair value is immediately recognized in income.

Derivative financial instruments that are not designated as hedges are adjusted to fair value through income.

We believe our FFAs have been highly effective during their term in offsetting changes in cash flow attributable to the volatility in spot market rates in our Ocean Business. When FFAs are in effect we perform both a prospective and retrospective assessment to this effect, at least quarterly, including assessing the possibility of counterparty default. If we determine that a derivative is no longer expected to be highly effective, we discontinue hedge accounting prospectively and recognize subsequent changes in the fair value of the hedge on our consolidated statements of income. The Company assesses the effectiveness of the hedging program using the dollar offset method. Under this method hedge effectiveness is measured by comparing the overall changes in the expected cash flows of the hedge contracts with the changes in the expected cash flows for the forecasted time charter revenues.

As a result of the sale of our vessels Princess Marisol and Princess Katherine, as described in the Developments in 2010 section, FFA positions maturing between May and December 2010 were no longer probable of occurring and thus no longer qualified as effective cash flow hedges. During the year ended December 31, 2010, the Company recorded an aggregate realized gain of $10.7 million.

Quantitative and Qualitative Disclosures about Market Risks

Inflation and Fuel Price Increases

Inflation may have a material impact on our operations, as certain of our operating expenses (e.g., crewing, insurance and drydocking costs) are subject to fluctuations as a result of market forces. A sudden outburst or a very high level of inflation can have a negative impact on our results.

Inflationary pressures on bunker (fuel oil) costs are not expected to have a material effect on our future operations in the case of those ocean vessels and our offshore supply vessels which are time chartered to third parties since it is the charterers who pay for fuel. If our ocean vessels are employed under COAs, freight rates for voyage charters are generally sensitive to the price of a ship's fuel. However, a sharp rise in bunker prices may have a temporary negative effect on our results since freight rates generally adjust only after prices settle at a higher level.

In our River Business, we have most of our freight agreements adjusted by a bunker price adjustment formula, in other cases we have periodic renegotiations which adjust for fuel prices and in other cases we adjust the fuel component of our cost into the freights on a seasonal or yearly basis as our COAs roll over.

Interest Rate Fluctuation

We are exposed to market risk from changes in interest rates, which may adversely affect our results of operations and financial condition.

On May 7, 2010, through UABL Limited, our holding subsidiary in the River Business, we entered into an interest rate collar transaction with IFC through which we expect to hedge our exposure to interest volatility under our financings with IFC and OFID from June 2010 to June 2016. The initial notional amount is $75.0 million (subsequently adjusted in accordance with the amortization schedule under these financings), with UABL Limited being the USD Floor Rate seller at a floor strike rate of 1.69% and IFC being the USD Cap Rate seller at a cap strike rate of 5.00%. As of December 31, 2011, and 2010 the aggregate fair value of the collar resulted in a loss of $2.0 million and $0.6 million, respectively. During 2011 and 2010 we incurred unrealized losses from the collar amounting to $2.0 million and $1.1 million, respectively, and we also incurred realized losses of $1.0 million and $0.4 million, respectively. Should LIBOR remain at levels below 1.69% which is our floor, we will continue to incur losses from this financial instrument.

We have two interest rate swaps maturing through 2018 with an aggregate notional amount of $9.4 million at December 31, 2011. We entered into these agreements to hedge our exposure to interest rate fluctuations with respect to our borrowings in our Offshore Supply Business. These agreements call for the Company to pay a fixed interest rate of 6.122% and 6.37%, respectively, and receive interest payments based on LIBOR. As of December 31, 2011, and 2010 the aggregate fair value of the swaps resulted in a loss of $0.9 million and $0.3 million, respectively. During 2011 and 2010 we incurred unrealized losses from the swaps amounting to $0.6 million and zero, respectively and we also incurred realized losses of $0.2 million and zero, respectively.

Additionally, as of December 31, 2011, the Company had other variable rate debt (due 2012 through 2021) totaling $142.4 million. These debts call for the Company to pay interest based on LIBOR plus a 120-365 basis point margin range. Recently, the $93.6 million facility with DVB and Natixis for the financing of our PSVs under construction in India has, within the terms and condition contained in the relevant loan agreement, used a cost of funds rate in replacement of LIBOR. The interest rates generally reset either quarterly or semi-annually. As of December 31, 2011, the weighted average interest rate on these borrowings was 3.1%.

A 1% increase in LIBOR or a 1% increase in the cost of funds used as base rate by some of our lenders would translate to a $1.4 million increase in our interest expense per year, which would adversely affect our earnings.

Foreign Currency Fluctuation

We are an international company and while our financial statements are reported in U.S. dollars, some of our operations are conducted in foreign currencies. We use the U.S. dollar as our functional currency and therefore our future operating results may be affected by fluctuations in the exchange rate between the U.S. dollar and other currencies. A large portion of our revenues is denominated in U.S. dollars as well as a significant amount of our expenses. However, changes in currency exchange rates could affect our reported revenues and even our margins if costs incurred in multiple currencies are different than, or proportionally different from, the currencies in which we receive our revenues. We maintain tax credits in local currencies, which may be negatively impacted if those currencies revalue relative to the U.S. dollar.

Forward Freight Agreements

As stated in the Baltic Exchange's website (www.balticexchange.com), "Forward Freight Agreements, or FFAs, are 'over the counter' products made on a principal-to-principal basis. As such, they are flexible and not traded on any exchange. Contracts traded will normally be based on the terms and conditions of the FFABA standard contracts amended as agreed between the principals. The main terms of an agreement cover: (a) the agreed route, (b) the day, month and year of settlement, (c) contract quantity and (d) the contract rate at which differences will be settled. Settlement is between counter parties in cash typically within five days following the settlement date. Commissions will be agreed between principal and broker. The broker, acting as intermediary only, is not responsible for the performance of the contract. Cleared contracts, instead, also known simply as futures, are settled on a daily basis through a clearing house and settlements are based on a close-of-play trading price. At the end of each day, traders pay or receive the difference between the price of the paper contract and the market index."

We enter into FFAs for trading purposes or to utilize them as hedges to reduce our exposure to changes in the rates earned by some of our vessels in the normal course of our Ocean Business. When using FFAs as hedges, we aim at managing the financial risk associated with fluctuating market conditions. FFAs generally cover periods ranging from one month to one year and involve contracts to provide a fixed number of theoretical days of voyages at fixed rates. FFAs have been executed through LCH, a London clearing house, with whom we started to trade during May 2007 (but may also be agreed through other clearing houses) and "over the counter" (OTC) in which case each party is generally accepting the signature of the other party as sufficient guarantee of its obligations under the contract.

At December 31, 2011, there are no outstanding positions on FFAs.

Description of Credit Facilities and Other Indebtedness

9% First Preferred Ship Mortgage Notes due 2014

On November 24, 2004, we completed an offering of $180.0 million of 9% First Preferred Ship Mortgage Notes due 2014, or the 2014 Notes, through a private placement to institutional investors eligible for resale under Rule 144A and Regulation S, or the Note Offering. The net proceeds of the Note Offering were used to repay our 10.5% First Preferred Ship Mortgage Notes due 2008, or the Prior Notes, certain other existing credit facilities and to fund an escrow account.

Interest on the Notes is payable semi-annually on May 24 and November 24 of each year. The Notes are senior obligations guaranteed by some of our subsidiaries directly involved in our Ocean and River Businesses. The Notes are secured by first preferred ship mortgages on 13 river pushboats, two oceangoing barges and 335 river barges.

The Notes are subject to certain covenants, including, among other things, limiting our and our subsidiaries' ability to incur additional indebtedness or issue preferred stock, pay dividends to shareholders, incur liens or execute sale leasebacks of certain principal assets and certain restrictions on our consolidating with or merging into any other person.

Upon the occurrence of a change of control event, each holder of the Notes shall have the right to require us to repurchase such notes at a purchase price in cash equal to 101% of the principal amount thereof plus accrued and unpaid interest. A change of control means:

- if any person beneficially owns more than 35% of our voting stock and Inversiones Los Avellanos S.A., or Los Avellanos, Hazels (Bahamas) Investments Inc., or Hazels, SIPSA S.A. and their affiliates, or the Permitted Holders, together beneficially own a lesser percentage and do not control the election of the majority of the board of directors of the Company, or

- during any period of two consecutive years, individuals who at the beginning of such period constituted our board of directors (together with any new directors whose election by such board of directors or whose nomination for election by our shareholders was approved by a vote of 66 2/3% of our directors then still in office who were either directors at the beginning of such period or whose election or nomination for election was previously so approved) cease for any reason to constitute a majority of the board of directors then in office; or

- our merger or consolidation with or into another Person or the merger of another Person with or into us, or the sale of all or substantially all of our assets (determined on a consolidated basis) to another person other than (A) a transaction in which the survivor or transferee is a person that is controlled by the Permitted Holders or (B) a transaction following which (1) in the case of a merger or consolidation transaction, holders of securities that represented 100% of our common stock eligible to vote on matters requiring a shareholder vote immediately prior to such transaction (or other securities into which such securities are converted as part of such merger or consolidation transaction) own directly or indirectly at least a majority of the voting power of the common stock eligible to vote on matters requiring a shareholder vote of the surviving Person in such merger or consolidation transaction immediately after such transaction and (2) in the case of a sale of assets transaction, each transferee becomes an obligor in respect of the Notes and a subsidiary of the transferor of such assets.

In the first quarter of 2005, pursuant to a registration rights agreement, we completed a registered exchange offer in which we exchanged registered Notes for the Notes that were originally issued in order to allow the Notes to be eligible for trading in the public markets.

7.25% Convertible Senior Notes due 2017

On December 23, 2010, we closed the offering of $80.0 million aggregate principal amount of convertible senior notes due 2017, or the Convertible Notes, which consisted of $70.0 million aggregate principal amount of notes and the full exercise of the initial purchasers' overallotment option of $10.0 million. The Convertible Notes were offered and sold to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended, or the Securities Act, and non-U.S. persons in accordance with Regulation S promulgated under the Securities Act, by the initial purchasers of the notes.

The Convertible Notes are fully payable on January 15, 2017, and pay interest semi-annually in arrears, in January 15 and July 15 each year, at the rate of 7.25% per annum.

Holders of the Convertible Notes may convert their notes, at their option, into shares of common stock of the Company, at any time prior to January 15, 2017. The conversion rate will equal 163.1321 shares of common stock per $1,000 (one thousand U.S. dollars) principal amount of the Convertible Notes (equivalent to an initial conversion price of $6.13 per share of our common stock). The conversion rate may be subject to further adjustment in

accordance with the indenture governing the Convertible Notes.

Only on and after January 15, 2015, do all, but not less than all, the Convertible Notes become redeemable for cash by us at 100% of their principal amount.

The Convertible Notes contain a "reset" feature wherefrom the conversion rate was adjusted on February 13, 2012, as a consequence of the fact that the volume weighted average price of our common stock for each of the 20 trading days beginning on January 17, 2012, was less than $6.13 per share.

The Convertible Notes are senior, unsecured obligations and rank or will rank equal in right of payment with our existing and future senior, unsecured debt and will be senior in right of payment to any future debt that is expressly subordinated to the notes. The Convertible Notes will be structurally subordinated to all debt and other liabilities and commitments of our subsidiaries, including trade payables and any guarantees that they may provide with respect to any of our existing or future debt and will be effectively subordinated to any secured debt that we may incur to the extent of the assets securing such debt.

As of December 31, 2011, no conversions were exercised by holders of the Convertible Notes.

Loan Agreement with DVB Bank AG (DVB AG) of up to $15.0 million:

On January 17, 2006, UP Offshore Apoio Maritimo Ltda. (a wholly owned subsidiary of the Offshore Supply Business) as Borrower, Packet Maritime Inc. and Padow Shipping Inc. as Guarantors and UP Offshore as Holding Company entered into a $15.0 million loan agreement with DVB AG for the purposes of providing post delivery financing of one PSV named UP Agua-Marinha delivered in February 2006.

This loan is divided into two tranches:
– Tranche A, amounting to $13.0 million, shall be repaid by (i) 120 consecutive monthly installments of $75,000 each beginning in March 2006 and (ii) a balloon repayment of $4.0 million together with the 120th installment. The loan accrues interest at LIBOR rate plus a margin of 2.25% per annum, and

– Tranche B, amounting to $2.0 million, shall be repaid by 36 consecutive monthly installments of $56,000 each beginning in March 2006 which accrues interest at LIBOR rate plus a margin of 2.875% per annum.

On January 24, 2007, UP Offshore Apoio Maritimo Ltda. and DVB AG amended and restated the margin of both tranches to 1.20% per annum effective since February 1, 2007.

The loan is secured by a mortgage on the UP Agua-Marinha and is jointly and severally irrevocable and unconditionally guaranteed by Packet Maritime Inc. and Padow Shipping Inc. The loan also contains customary covenants that limit, among other things, the Borrower's and the Guarantors' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreement governing the facility also contains customary events of default. If an event of default occurs and is continuing, DVB AG may require the entire amount of the loan be immediately repaid in full. Further, the loan agreement requires until February 2009 that the UP Agua-Marinha pledged as security had an aggregate market value of at least 117.6% of the value of the loan amount and at all times thereafter an aggregate market value of at least 133.3% of the value of the loan.

The aggregate outstanding principal balance of the loan was $7.8 million at December 31, 2011.

Loan Agreement with DVB Bank AG (DVB AG) of up to $61.3 million:

On December 28, 2006, UP Offshore (Bahamas) Ltd., as Borrower, entered into a $61.3 million loan agreement with DVB AG for the purpose of refinancing three PSVs named UP Esmeralda, UP Safira and UP Topazio. The loan is divided into two advances and shall be repaid by 40 consecutive quarterly installments as set forth in the repayment schedule therein.

The loan must be repaid by (i) 9 consecutive quarterly installments of $1.2 million each beginning in March 2007 followed by 3 consecutive quarterly installments of $1.3 million each, 25 of $1.1 million and 3 of $1.3 million and (ii) a balloon repayment of $16.0 million payable simultaneously with the 40th quarterly installment. The loan accrues interest at LIBOR plus 1.20% per annum.

The loan is secured by a mortgage on the UP Esmeralda, UP Safira, UP Topazio and UP Agua Marinha (together, the Mortgaged Vessels) and is jointly and severally irrevocable and unconditionally guaranteed by Ultrapetrol (Bahamas) Ltd., UP Offshore Apoio Maritimo Ltda., Packet Maritime Inc., Topazio Shipping LLC and Padow Shipping Inc. The loan also contains customary covenants that limit, among other things, the Borrower's and the Guarantors' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreement governing the facility also contains customary events of default. If an event of default occurs and is continuing, DVB AG may require the

entire amount of the loan be immediately repaid in full. Further, the loan agreement requires upon the until the third anniversary of the final advance under the loan, the Mortgaged Vessels pledged as security have an aggregate market value of at least 117.6% of the value of the loan amount and at all times thereafter an aggregate market value of at least 133.3% of the value of the loan.

The aggregate outstanding principal balance of the loan was $38.3 million at December 31, 2011.

Loan Agreement with Natixis of $13.6 million:

On January 29, 2007, Stanyan Shipping Inc. (a wholly owned subsidiary in the Ocean Business and the owner of the Alejandrina) as Borrower and Ultrapetrol (Bahamas) Limited as Guarantor and Holding Company entered into a $13.6 million loan agreement with Natixis for the purpose of providing post delivery financing of one Panamanian flag small product tanker named Alejandrina .

The loan must be repaid by (i) 40 consecutive quarterly installments of $0.2 million each beginning in June 2007 and (ii) a balloon repayment of $4.5 million payable simultaneously with the 40th quarterly installment. The loan accrues interest at 6.38% per annum during the first five years of the loan and LIBOR plus 1.00% per annum thereafter for so long as the Alejandrina remains chartered under standard conditions or 1.20% per annum otherwise.

The loan is secured by a mortgage on the Alejandrina and is guaranteed by Ultrapetrol (Bahamas) Limited. The loan also contains customary covenants that limit, among other things, the Borrower's and the Guarantors' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreement governing the facility also contains customary events of default.

The aggregate outstanding principal balance of the loan was $9.3 million at December 31, 2011.

Loan Agreement with DVB Bank AG (DVB AG) of $25.0 million:

On October 31, 2007, UP Offshore (Bahamas) Ltd., as Borrower, entered into a $25.0 million loan agreement with DVB AG for the purpose of providing post delivery financing of one Brazilian flag PSV named UP Diamante.

The loan shall be repaid by (i) 8 consecutive quarterly installments of $0.75 million each beginning in February 2008 followed by 24 consecutive quarterly installments of $0.5 million each and 8 of $0.25 million and (ii) a balloon repayment of $5.0 million payable simultaneously with the 40th quarterly installment. The loan accrues interest at LIBOR plus 1.50% per annum.

The loan is secured by a mortgage on the UP Diamante and is jointly and severally irrevocable and unconditionally guaranteed by Ultrapetrol (Bahamas) Ltd, Packet Maritime Inc., Padow Shipping Inc., Topazio Shipping LLC, UP Offshore Apoio Maritimo Ltda., and UP Offshore (Uruguay) S.A. The loan also contains customary covenants that limit, among other things, the Borrower's and the Guarantors' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreement governing the facility also contains customary events of default. If an event of default occurs and is continuing, DVB AG may require the entire amount of the loans be immediately repaid in full. Further, the loan agreements require until 2009 that the PSVs pledged as security have an aggregate market value of at least 117.6% of the value of the loan amounts and at all times thereafter an aggregate market value of at least 133.3% of the value of the loans.

The aggregate outstanding principal balance of the loan was $15.0 million at December 31, 2011.

Loan Agreement with Nordea Bank Finland PLC (Nordea Bank) of $20.2 million:

On November 30, 2007, Hallandale Commercial Corp., as Borrower, Ultrapetrol (Bahamas) Ltd., as Guarantor, and Tuebrook Holdings Inc., as Pledgor, entered into a $20.2 million loan agreement with Nordea Bank for the purpose of providing post delivery financing of our Panamanian flag Product Tanker, Amadeo.

The loan shall be repaid by (i) 12 consecutive quarterly installments of $0.8 million each beginning in March 2008 followed by 12 consecutive quarterly installments of $0.5 million each and (ii) a balloon repayment of $5.2 million payable simultaneously with the 24th quarterly installment. The loan accrues interest at LIBOR plus 1.25% per annum. The loan is secured by a mortgage on the Amadeo and is jointly and severally irrevocable and unconditionally guaranteed by Ultrapetrol (Bahamas) Ltd. The loan also contains customary covenants that limit, among other things, the Borrower's and the Guarantors' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreement governing the facility also contains customary events of default.

On June 5, 2009, we agreed with Nordea Bank Finland PLC to fully and voluntarily prepay $4.1 million of the outstanding amount without any contractual penalty or breakage costs. As from that date, the loan shall be repaid by (i) the remaining 6 consecutive quarterly installments of $0.6 million each followed by 12 consecutive quarterly installments of $0.4 million each and (ii) a balloon repayment of $4.1 million payable simultaneously with the 18th quarterly installment. The loan accrues interest at LIBOR plus 1.25% per annum.

The aggregate outstanding principal balance of the loan was $7.2 million at December 31, 2011.

Loan Agreement with DVB Bank AG (DVB AG) and Natixis of up to $93.6 million:

On June 24, 2008, Ingatestone Holdings Inc., as Borrower and Ultrapetrol (Bahamas) Limited, UP Offshore (Bahamas) Ltd., Bayshore Shipping Inc., Gracebay Shipping Inc., Springwater Shipping Inc. and Woodrow Shipping Inc. (all of these our subsidiaries in the Offshore Supply Business), as joint and several Guarantors, entered into a senior secured term loan facility of up to $93.6 million with DVB AG and Natixis, as co-lenders, to finance the construction and delivery of our four PSVs being constructed in India.

This loan is divided into two tranches:

Tranche A, amounting to $60.0 million, to be made available for each ship in the amount of up to $15.0 million in multiple advances for the payment of installments of the contract price due under the applicable shipbuilding contract. This tranche accrues interest at LIBO rate plus a margin of 1.5% and shall be repaid by (i) 40 quarterly installments of $0.25 million per ship and (ii) a balloon repayment of $5.0 million per ship together with the last installment. The first quarterly repayment shall commence on the date falling three months after the delivery date of such ship. During the pre-delivery period, advances of Tranche A in respect of each ship shall not exceed $3.45 million per advance and in the aggregate for each ship the lesser of (i) 60% of the relevant construction cost and (ii) $13.8 million.

Tranche B, amounting to $33.6 million, to be made available for each ship in the amount of up to $8.4 million in a single advance on the delivery date of such ship. This tranche accrues interest at LIBO rate plus a margin of 1.75% per annum and shall be repaid by 20 quarterly installments of $0.42 million per ship. The first quarterly repayment shall commence on the date falling three months after the delivery date of such ship.

The loan contains customary covenants which are similar to the stipulated covenants in previous loans entered with DVB AG. The agreements governing the facility also contain customary events of default. If an event of default occurs and is continuing, DVB AG and Natixis may require the entire amount of the loans be immediately repaid in full.

On December 9, 2010, we amended the loan. As part of the amendment, the availability period was extended through June 30, 2012, and the margin over LIBOR was increased to 3.0% p.a. during the vessel's construction and to 2.0% p.a. as from delivery.

On November 30, 2011, we signed a second amendment to the loan agreement, which extended the availability period through December 31, 2012, on a vessel by vessel basis.

As of December 31, 2011, we have drawn down $31.1 million as first advance all of the Tranche A applicable to our four PSVs under construction in India.

Loan Agreement with International Finance Corporation (IFC) of $25.0 million:

On September 15, 2008, UABL Paraguay S.A., as Borrower, and IFC entered into a loan agreement to partially finance: (i) the replacement of existing pushboat engines and conversion of pushboats to install such engines, (ii) the enlargement and re-bottoming of existing barges, (iii) the construction and acquisition of additional pushboats and barges and (iv) supplies and related equipment for the foregoing.

The loan has a grace period of 4 years followed by 9 consecutive semi-annual installments of $1.09 million and 8 consecutive semi-annual installments of $1.90 million, beginning in June 2012. The loan accrues interest at LIBOR plus a spread between 1.875% and 3.250%, obtained from the Guarantor Prospective Debt Service Coverage ratio as indicated in the agreement, beginning with 3.00% in December 2008.

The loan is secured by a mortgage on part of our River Business fleet. The loan requires certain financial ratios and contains various restrictive covenants such as limiting the Borrower's ability to declare or pay any dividend, to incur capital expenditures, leases, or enter into derivative transactions (except for fuel swaps), among others.

The aggregate outstanding principal balance of the loan was $25.0 million at December 31, 2011.

Loan Agreement with International Finance Corporation (IFC) of $35.0 million:

On September 15, 2008, UABL Barges (Panama) Inc., UABL Towing Services S.A., Marine Financial Investment Corp. and Eastham Barges Inc. (all our subsidiaries in the River Business), as Borrowers, and IFC entered into a loan agreement to partially finance: (i) the replacement of existing pushboat engines and conversion of pushboats to install such engines, (ii) the enlargement and re-bottoming of existing barges, (iii) the construction and acquisition of additional pushboats and barges and (iv) supplies and related equipment for the foregoing.

The loan has a grace period of 4 years followed by 9 consecutive semi-annual installments of $1.52 million and 8 consecutive semi-annual installments of $2.66 million, beginning in June 2012. The loan accrues interest at LIBOR plus a spread between 1.875% and 3.250%, obtained from the Guarantor Prospective Debt Service Coverage ratio as indicated in the agreement, beginning with 3.00% in December 2008.

The loan is secured by a mortgage on part of our River Business fleet. The loan requires certain financial ratios and contains various restrictive covenants such as limiting the Borrower's ability to declare or pay any dividend, to incur capital expenditures, leases, or enter into derivative transactions (except for fuel swaps), among others.

The aggregate outstanding principal balance of the loan was $35.0 million at December 31, 2011.

Loan Agreement with The OPEC Fund for International Development (OFID) of $15.0 million:

On November 28, 2008, UABL Paraguay S.A., as Borrower, and OFID entered into a loan agreement to partially finance: (i) the replacement of existing pushboat engines and conversion of pushboats to install such engines, (ii) the enlargement and re-bottoming of existing barges, (iii) the construction and acquisition of additional pushboats and barges and (iv) supplies and related equipment for the foregoing.

The loan has a grace period of 4 years followed by 9 consecutive semi annual installments of $0.65 million and 8 consecutive semi annual installments of $1.14 million, beginning in June 2012. The loan accrues interest at LIBOR plus a spread between 1.875% and 3.250%, obtained from the Guarantor Prospective Debt Service Coverage ratio as indicated in the agreement, beginning with 3.00% in December 2008.

The loan is secured by a mortgage on part of our River Business fleet. The loan requires certain financial ratios and contains various restrictive covenants such as limiting the Borrower's ability to declare or pay any dividend, to incur capital expenditures, leases, or enter into derivative transactions (except for fuel swaps) among others.

The aggregate outstanding principal balance of the loan was $15.0 million at December 31, 2011.

Loan Agreement with BNDES of $18.7 million:

On August 20, 2009, UP Offshore Apoio Maritimo Ltda. (a wholly owned subsidiary in the Offshore Supply Business) as Borrower entered into an $18.7 million loan agreement with BNDES to partially post-finance the construction of our PSV UP Rubi.

The loan must be repaid by 204 consecutive monthly installments of $0.1 million each beginning in April 2010. The loan accrues interest at 3.0% fixed rate per annum until maturity on March 2027.

The loan is secured by a Stand-By Letter of Credit (SBLC) facility dated as of October 30, 2009, of up to $21.5 million issued by DVB Bank SE and guaranteed by Ultrapetrol (Bahamas) Limited. The SBLC accrues a fee fixed at 2.0% per annum on the outstanding amount and a fee equal to 1.0% on the settlement date on the settlement amount.

As Facility Guarantor, UP Offshore (Bahamas) Ltd., under the SBLC facility, shall maintain certain financial covenants including: (i) an average balance of available cash in a demand deposit of not less than $5.0 million during each financial year, (ii) an equity ratio of not less than 30%, (iii) a minimum equity of $75.0 million and (iv) a ratio of consolidated EBITDA to consolidated debt service of at least 1.5.

The aggregate outstanding principal balance of the loan was $16.9 million at December 31, 2011.

Loan Agreement with DVB Bank SE (DVB SE) and Banco Security of $40.0 million:

On December 9, 2010, our subsidiary UP Offshore (Bahamas) Limited entered into a loan agreement with DVB Bank SE and Banco Security relating to a senior secured term loan facility in the amount of up to $40.0 million to partially finance the acquisition of two PSVs constructed for us, UP Turquoise and UP Jasper. This facility will be drawn in two advances, each in the approximate amount of $20.0 million, on the delivery of each of the respective PSVs. The maturity date of the facility is eight years from the initial drawdown, but no later than December 31, 2018. The security for the loan facility includes a guarantee by us and first priority Panamanian ship mortgages on each of the PSVs.

Each advance shall be repaid by (i) 32 consecutive quarterly installments of $0.4 million and (ii) a balloon repayment of $6.7 million concurrently with the 32nd quarterly installment. The loan accrues interest at LIBOR plus 3.0% per annum.

The aggregate outstanding principal balance of the loan was $37.5 million at December 31, 2011.

Loan Agreement with International Finance Corporation (IFC) of $15.0 million:

On December 2, 2011, UABL Paraguay S.A. and Riverpar S.A. as joint and several Borrowers, and IFC entered into a loan agreement to partially finance: (i) the construction and acquisition of 64 additional barges, (ii) the modification to 9 existing pushboats necessary to replace their engines, (iii) the re-bottoming of 50 existing barges and (iv) the construction and acquisition of additional pushboats and ancillary equipment.

The loan has a grace period of 2 years followed by 17 consecutive semi-annual installments of $0.9 million beginning in June 2013. The loan accrues interest at LIBOR plus 3.65% per annum.

The loan is secured by a mortgage on part of our River Business fleet. The loan requires certain financial ratios and contains various restrictive covenants such as limiting the Borrower's ability to declare or pay any dividend, to incur capital expenditures, leases, or enter into derivative transactions (except for fuel swaps), among others.

The aggregate outstanding principal balance of the loan was $15.0 million at December 31, 2011.

Loan Agreement with The OPEC Fund for International Development (OFID) of $10.0 million:

On December 15, 2011, UABL Paraguay S.A. and Riverpar S.A. as joint and several Borrowers, and OFID entered into a parallel loan agreement to partially finance: (i) the construction and acquisition of 64 additional barges, (ii) the modification to 9 existing pushboats necessary to replace their engines, (iii) the re-bottoming of 50 existing barges and (iv) the construction and acquisition of additional pushboats and ancillary equipment.

The loan has a grace period of 2 years followed by 17 consecutive semi-annual installments of $0.6 million beginning in June 2013. The loan accrues interest at LIBOR plus 3.65% per annum.

The loan is secured through a collateral sharing agreement with the IFC. The loan requires certain financial ratios and contains various restrictive covenants such as limiting the Borrower's ability to declare or pay any dividend, to incur capital expenditures, leases, or enter into derivative transactions (except for fuel swaps), among others.

At December 31, 2011, no disbursement has been made in accordance with such facility.

C. RESEARCH AND DEVELOPMENT, PATENTS AND LICENSES, ETC.

Not Applicable.

D. TREND INFORMATION

We believe the following developments and initiatives will have a significant impact on the operations of our various businesses.

River Business

- Expansion and fuel efficiency initiatives – We continue working on our re-engining program for which we have contracted and received 25 heavy fuel engines with MAN Diesel. Such program was initiated in June 2006 and consists of replacing diesel engines in 11 of our main line pushboats with new engines that will burn heavy fuel oil which has been historically less expensive than the types of fuel currently used. As of December 31, 2011, we have completed the installation of 10 engines and put into operation four of our main pushboats, including one newbuilding. Three pushboats with 7 more engines are currently under conversion.

- The pushboat Zonda I has already begun its operation on May 22, 2010, and Pampero I has been operational since December 21, 2011. They both have 3 heavy fuel propelled engines totaling 8,300 HP which make them the most powerful pushboats in the Hidrovia.

- Construction of new barge building yard – On December 15, 2009, we inaugurated our barge building yard in Punta Alvear, Argentina. For our own account, the yard has since built 21 jumbo tank barges and 37 jumbo dry barges up to and including December 31, 2011. The yard was at a production rate of one jumbo dry barge per week basis one shift and, basis a second shift, increased it to approximately 1.7 barges per week. We expect that the successive addition of barges to our fleet will significantly increase our carrying capacity positively impacting our future revenues. In addition, we expect that the new yard will also build barges for third parties with a positive impact on earnings.

Offshore Supply Business

- New vessels – Our eighth PSV, UP Jasper, which was under construction in China, was delivered to us in June 2011. In addition, we have four PSVs under construction in India, the first of which, UP Jade, is expected to be delivered during the second quarter of 2012.

Ocean Business

- Container feeder service – Regular service with two vessels, M.V. Asturiano and M.V. Argentino. The Southbound leg has remained at high utilization rates with healthy rates while we have increased the utilization rate in the northbound leg also to high levels with domestic cargoes returning to Buenos Aires and transshipment cargoes which are loaded from other southern ports in Patagonia such as Bahia Blanca or Puerto Madryn and carried with our service to Buenos Aires for export. Growth opportunity still available in Patagonia service and possible expansion to Brazil which is Argentina's main commercial partner and whose demand may provide us with opportunities to call ports in the southern part of the country.

E. OFF-BALANCE SHEET ARRANGEMENTS

We do not have any off-balance sheet arrangements.

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F. TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

The following schedule summarizes our contractual obligations and commercial commitments as of December 31, 2011. The amounts below include both principal and interest payments.

Contractual Obligations

		Payments due by period			
	Total	Current (a)	Two to three years (b)	Four to five years (c)	After five years (d)
			(Dollars in thousands)		
1. Long – term debt obligations (e)					
- DVB Bank AG (up to $15.0 million)					
Tranche A	$ 7,750	$ 900	$ 1,800	$ 5,050	$ --
Tranche B	--	--	--	--	--
- DVB Bank AG (up to $61.3 million)	38,250	4,300	8,600	25,350	--
- DVB Bank AG (up to $25.0 million)	15,000	2,000	4,000	3,000	6,000
- Nordea Bank Finland PLC	7,212	1,568	5,644	--	--
- Natixis	9,303	908	1,816	1,816	4,763
- IFC UABL Paraguay	25,000	2,174	4,348	5,163	13,315
- IFC UABL	35,000	3,044	6,087	7,228	18,641
- OFID	15,000	1,304	2,609	3,098	7,989
- DVB / Natixis (up to $93.6 million)					
Tranche A	31,050	863	4,777	4,777	20,633
Tranche B	--	--	--	--	--
- BNDES	16,928	1,110	2,220	2,220	11,378
- 9% Senior Notes 2014 ($180.0 million)	180,000	--	180,000	--	--
- DVB-Security (up to $40 million)	37,500	3,333	6,667	6,667	20,833
- 7.25% Senior Convertible Notes 2017 ($80.0 million)	80,000	--	--	--	80,000
- IFC UABL III Loan (up to $15.0 million)	15,000	--	3,529	3,529	7,942
- OFID UABL III Loan (up to $10.0 million)	--	--	--	--	--
Total long – term debt obligations	$ 512,993	$ 21,504	$ 232,097	$ 67,898	$ 191,494
Estimated interest on long-term debt obligations					
- DVB Bank AG (up to $15.0 million)					

Tranche A	$ 445	133	216	96	--
Tranche B	--	--	--	--	--
- DVB Bank AG (Up to $61.3 million)	2,529	663	1,090	776	--
- DVB Bank AG (Up to $25.0 million)	1,209	301	475	314	119
- Nordea Bank Finland PLC	217	123	94	--	--
- Natixis	777	272	274	209	22
- IFC UABL Paraguay	5,730	1,104	1,908	1,519	1,199
- IFC UABL	8,021	1,546	2,671	2,126	1,678
- OFID	3,437	662	1,145	911	719
- DVB / Natixis (up to $93.6 million)					
Tranche A	7,452	1,405	2,193	1,823	2,031
Tranche B	--	--	--	--	--
- BNDES	3,950	501	897	763	1,789
- DVB Bank SE (SBLC)	873	437	436	--	--
- 9% Senior Notes 2014 ($180.0 million)	48,600	16,200	32,400	--	--
- DVB-Security (up to $40.0 million)	7,985	1,579	2,714	2,137	1,555
- 7.25% Senior Convertible Notes 2017 ($80.0 million)	31,900	5,800	11,600	11,600	2,900
- IFC UABL III Loan (up to $15.0 million)	3,542	645	1,173	872	852
- OFID UABL III Loan (up to $10.0 million)	--	--	--	--	--
Total estimated interest on long – term debt obligations	126,667	31,371	59,286	23,146	12,864
2. Operating lease obligations	$ 6,272	$ 2,912	$ 3,061	$ 299	$ --
3. Purchase obligations					
- Vessel construction					
Bharati Shipyard (f)	30,818	30,818	--	--	--
Total purchase obligations	$ 30,818	$ 30,818	$ --	--	--
Total Contractual Obligations	676,750	86,605	294,444	91,343	204,358

(a) Represents the period from January 1, 2012 through December 31, 2012.
(b) Represents the period from January 1, 2013 through December 31, 2014.
(c) Represents the period from January 1, 2015 through December 31, 2016.
(d) Represents the period after December 31, 2016.
(e) Represents principal amounts due on outstanding debt obligations, current and long-term, as of December 31, 2011. Amounts do not include interest payments.
(f) $30,818 of pending contractual obligations fully financed with pre-delivery proceeds from the DVB/Natixis loan facility. Additionally, such loan facility provides up to $33,600 as post-delivery financing subject to compliance with certain covenants.

The interest rate and term assumptions used in these calculations are contained in the following table:

Obligation	Principal at December 31, 2011	Interest Rate	Period From-To
- DVB Bank AG (up to $15.0 million)			
Tranche A	$ 7,750	1.78%	01/01/2012 – 02/14/2016
Tranche B	--	1.78%	--
- DVB Bank AG (up to $61.3 million)	38,250	1.78%	01/01/2012 – 12/14/2016
- DVB Bank AG (up to $25.0 million)	15,000	2.08%	01/01/2012 – 10/31/2017
- Nordea Bank Finland PLC	7,212	1.83%	01/01/2012 – 12/5/2013
- Natixis (up to $13.6 million)	9,303	6.38%	01/01/2012 – 02/20/2012
- Natixis (up to $13.6 million)	9,076	1.78%	02/21/2012 – 02/21/2017
- IFC UABL Paraguay	25,000	4.44%	01/01/2012 – 06/15/2020
- IFC UABL	35,000	4.44%	01/01/2012 – 06/15/2020
- OFID	15,000	4.44%	01/01/2012 – 06/15/2020
- DVB / Natixis (up to $93.6 million)			
Tranche A	31,050	% 4.85(1)	01/01/2012 – 12/31/2019 (1)
Tranche B (2)	--	--	--
- BNDES	16,928	3.00%	01/01/2012 – 03/10/2027
- DVB Bank SE (SBLC)	21,500	2.00%	01/01/2012 – 11/11/2013
- DVB-Security (up to $30.0 million)	28,125	3.58%	01/01/2012 – 12/31/2018
- DVB-Security (up to $10.0 million)	9,375	6.39%	01/01/2012 – 12/31/2018
- IFC UABL III Loan (up to $15.0 million)	15,000	4.23%	01/01/2012 – 06/15/2021

- OFID UABL III Loan (up to $10.0 million)	--	4.23%	26/01/2012 – 06/15/2021

(1) Tranche A carries interest at 4.85% per annum until the delivery date of the corresponding vessel. As from delivery, Tranche A's spread is adjusted downwards by 1% and, thus, an interest rate of 3.85% is used in the table here above as from the assumed delivery dates of each PSV.

(2) See note (f) here above. Tranche B was not drawn down as of December 31, 2011.

Interest expense calculations begin on January 1, 2012, end on the respective maturity dates and are based on contractual terms with the exception of the IFC/OFID credit facilities and DVB/Security credit facility. The Company, through its subsidiaries, has entered into interest rate collar and interest rate swap agreements related to borrowings under its IFC/OFID and DVB/Security credit facilities, respectively, whereby it has converted most of its variable rate borrowings into fixed rate borrowings. For purpose of this table, the Company has assumed the fixed rates of interest in calculating its obligations.

We believe, based upon current levels of operation, that cash flow from operations, combined with other sources of funds, will provide adequate liquidity to fund required payments of principal and interest on our debt, including interests under the 2014 Notes and the Convertible Notes, complete anticipated capital expenditures and fund working capital requirements.

Our ability to make scheduled payments of principal, or to pay interest on, or to refinance, our indebtedness, including the 2014 Notes and the Convertible Notes, or to fund planned capital expenditures will depend on our ability to generate cash from our operations in the future. Our ability to generate cash is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control.

G. SAFE HARBOR

Forward-looking information discussed in this Item 5 includes assumptions, expectations, projections, intentions and beliefs about future events. These statements are intended as "forward-looking statements". We caution that assumptions, expectations, projections, intentions and beliefs about future events may and often do vary from actual results and the differences can be material. Please see "Cautionary Statement Regarding Forward-Looking Statements" in this annual report.

ITEM 6. – DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. DIRECTORS AND EXECUTIVE OFFICERS

Set forth below are the names, ages and positions of our directors, executive officers and key employees. Our board of directors is elected annually and each director elected holds office until his successor has been duly elected and qualified, except in the event of his death, resignation, removal or the earlier termination of his term of office. George Wood has agreed to serve on our audit committee. Officers are elected from time to time by vote of our board of directors and hold office until a successor is elected. The business address of each of our executive officers and directors is H&J Corporate Services Ltd., Ocean Centre, Montagu Foreshore, East Bay St., P.O. Box SS-19084, Nassau, Bahamas.

Name	Age	Position
Felipe Menendez Ross	57	Chief Executive Officer, President and Director
Ricardo Menendez Ross	62	Executive Vice President and Director
Leonard J. Hoskinson	58	Chief Financial Officer, Secretary and Director
Michael C. Hagan	65	Director
George Wood	66	Director
Fernando Barros Tocornal	54	Director
Alberto G. Deyros	56	Chief Accountant

Biographical information with respect to each of our directors, executives and key personnel is set forth below.

Felipe Menendez Ross. Mr. Menendez has been President, Chief Executive Officer and a Director of the Company since incorporation in December 1997 and is the brother of Ricardo Menendez. Mr. Menendez commenced his career in shipping in 1974. He is President and has been a Director of Ultrapetrol S.A. since its incorporation in 1992 as well as the President and CEO of UABL. Mr. Menendez is also a Director of SIPSA S.A., or SIPSA, a Chilean publicly traded company controlled by the Menendez family. Mr. Menendez has been, and continues to be, actively involved in other businesses associated with the Menendez family, as well as other companies affiliated with SIPSA.

Ricardo Menendez Ross. Mr. Menendez is the Executive Vice President of the Company and CEO of UP Offshore and has been a Director of the Company since incorporation in December 1997 and is the brother of Felipe Menendez. Mr. Menendez began his career in the shipping industry in 1970 with Compania Chilena de Navegacion Interoceania S.A. and has continuously been involved in the management of the Menendez family's shipping interests. He is the President of Oceanmarine and has been the Executive Vice President and a Director of Ultrapetrol S.A. since it was formed in 1992. Mr. Menendez is also a Director of SIPSA and remains involved in the management of other Menendez family businesses. Mr. Menendez has been a member of the board of The Standard Steamship Owners' Protection & Indemnity Association (Bermuda) Limited (a member of the International Group of Protection & Indemnity Associations) since 1993 and is currently its Chairman. Mr. Menendez is also a Director of UABL.

Leonard J. Hoskinson. Mr. Hoskinson is the Chief Financial Officer of the Company, was appointed Director of the Company in March 2000 and assumed the position of Secretary six months later. Mr. Hoskinson has been employed by the Company and its affiliates for over 22 years. Prior to that, he had an international banking career spanning over 20 years specializing in ship finance and culminating as the Head of Shipping for Marine Midland Bank NA in New York (now part of the HSBC banking group). He is also a Director of UABL.

Michael C. Hagan. Mr. Hagan has been a Director since October 2006. He has served as Chief Executive Officer of American Commercial Lines (ACL) from 1991 to 2003 and has served as Executive Vice President from 1989 to 1991. ACL was at the time one of the largest inland river-oriented businesses engaged in barge transportation, marine terminal and marine equipment manufacturing businesses with peak sales of $850.0 million. Mr. Hagan started his career within ACL in American Commercial Barge Lines (ACBL), a subsidiary of ACL, where he was responsible for the sales and marketing of their inland barge operation. He then became Sales VP for CSX Transportation Railroad, with sales volume of $2.5 billion per annum in bulk and manufactured products as well as liquid chemicals. Mr. Hagan holds a B.S. in Business Administration from Brescia University. Mr. Hagan is a member of the National Waterways Foundation board of Directors and is a past Chairman of the American Waterways Operators.

George Wood. Mr. Wood has been a Director since October 2006. He has recently retired as managing director of Chancery Export Finance LLC (Chancery), a firm licensed by the Export Import Bank of the United States of America (ExIm Bank). Chancery provides ExIm Bank guaranteed financing for purchase of U.S. manufactured capital goods by overseas buyers. Prior to his designation as Managing Director of Chancery, Mr. Wood worked as Managing Director of Baltimore based Bengur Bryan & Co. (Bengur Bryan) providing investment-banking services to transportation related companies in the global maritime, U.S. trucking, motor coach and rail industries. Before his employment with Bengur Bryan in 2000, Mr. Wood was employed for 27 years in various managerial positions at the First National Bank of Maryland which included managing the International Banking Group as well as the bank's specialized lending divisions in leasing, rail, maritime and motor coach industries, encompassing a risk asset portfolio of $1.2 billion. Mr. Wood is a member of the board of Baltic Trading Inc. as well as part of the Audit Committee and Nominating and Governance Committee. Baltic Trading Inc. is a shipping company focused on the dry bulk industry spot market and is currently trading on the NYSE. Mr. Wood holds a B.S. in Economics and Finance from University of Pennsylvania and an MBA from University of North Carolina and became a CPA in 1980. Mr. Wood presently serves as member of the Boards of Atlanta-based Infinity Rails and Wawa Inc. Mr. Wood recently served for two years on the Board of LASCO Shipping Co.

Fernando Barros Tocornal. Mr. Barros is an Attorney and founding partner of the Chilean law firm of Barros & Errazuriz. Mr. Barros has vast experience in commercial, corporate and tax law, with an extensive practice in connection with the creation and development of financial, industrial and service companies. Likewise, Mr. Barros is a member of the National Board of Arbitrators, appointed by the President of Chile and is also a member of the Arbitration and Mediation Center of the Chamber of Commerce of Santiago and of the National Center of Arbitration, as well as acting as a private arbitrator. As part of his academic activities, Mr. Barros was a professor of Commercial and Economic Law; he is a member of the Board of Universidad Finis Terrae, where he also served as Dean of the

School of Law between 2000 and 2003. He is also a member of the Consulting Committee of the Pro Bono Foundation of Chile and part of the board of the Chilean non profit association for the entrepreneur development and corporate governance, ICARE. Mr. Barros is also a Director of Chilean listed companies including SIPSA S.A., the Chilean parent company of Ultrapetrol (Bahamas) Ltd.

Alberto G. Deyros. Mr. Deyros is the Chief Accountant of the Company and was appointed in April 2006. Mr. Deyros has been employed by the Company and its subsidiaries for more than ten years. Prior to that, he specialized in ship administration management over a period of more than 20 years. Mr. Deyros is a Certified Public Accountant and a graduate of Universidad de Buenos Aires.

B. COMPENSATION

The aggregate annual net cost to us for the compensation paid to members of the board of directors and our executive officers was $4.3 million for the fiscal year ended December 31, 2011. Neither the Company nor any of its subsidiaries provides retirement benefits.

In connection with our IPO we granted in September 2006 to certain members of our board of directors stock options for 348,750 shares of common stock with an exercise price of $11 per share. These options expire ten years after their issuance date. To date, none of these options had been exercised by their holders.

Management Agreements

For the day to day management of our operations, we and / or our subsidiaries have entered into administrative and management agreements to provide specific services for our operations. We refer you to "Related Party Transactions" in Item 7.B of this report.

C. BOARD PRACTICES

Our audit committee is composed of Mr. Wood, who is one of our independent directors and is responsible for reviewing our accounting controls and recommending to the board of directors the engagement of our outside auditors. Our corporate governance practices are in compliance with Bahamian law and we are exempt from many of the corporate governance provisions of the Nasdaq Marketplace Rules other than those related to the establishment of an audit committee.

We have certified to Nasdaq that our corporate governance practices are in compliance with, and are not prohibited by, the laws of The Bahamas. Therefore, we are exempt from many of Nasdaq's corporate governance practices other than the requirements regarding the disclosure of a going concern audit opinion, submission of a listing agreement, notification of material non-compliance with Nasdaq corporate governance practices and the establishment of an audit committee in accordance with Nasdaq Marketplace Rules 4350(d)(3) and 4350(d)(2)(A)(ii). The practices that we follow in lieu of Nasdaq's corporate governance rules are as follows:

- We do not have a board of directors with a majority of independent directors, nor are we required to under Bahamian law. However, we have two independent directors.

- In lieu of holding regular meetings at which only independent directors are present, our entire board of directors, may hold regular meetings, as is consistent with Bahamian law.

- In lieu of an audit committee comprising three independent directors, our audit committee will have at least one member, which is consistent with Bahamian law. The member of the audit committee is a financial expert. We cannot guarantee that at least one member of our audit committee will continue to meet this description.

- In lieu of a nomination committee comprising independent directors, our board of directors will be responsible for identifying and recommending potential candidates to become board members and recommending directors for appointment to board committees. Shareholders may also identify and recommend potential candidates to become board members in writing. No formal written charter has been prepared or adopted because this process is outlined in our memorandum of association.

- In lieu of a compensation committee comprising independent directors, our board of directors will be responsible for establishing the executive officers' compensation and benefits. Under Bahamian law, compensation of the executive officers is not required to be determined by an independent committee.

- In lieu of obtaining an independent review of related party transactions for conflicts of interests, consistent with Bahamian law requirements, our memorandum of association provides that related party transactions must be approved by disinterested directors and in certain circumstances, supported by a fairness opinion.

- Pursuant to our articles of association, we are required to obtain shareholder approval in order to issue additional securities.

- As a foreign private issuer, we are not required to solicit proxies or provide proxy statements to Nasdaq pursuant to Nasdaq corporate governance rules or Bahamian law. Consistent with Bahamian law and as provided in our articles of association, we will notify our shareholders of meetings between 15 and 60 days before the meeting. This notification will contain, among other things, information regarding business to be transacted at the meeting. In addition, our memorandum of association provides that shareholders must give us 90 days advance notice to properly introduce any business at a meeting of the shareholders. Our memorandum of association also provides that shareholders may designate a proxy to act on their behalf (in writing or by telephonic or electronic means as approved by our board from time to time).

Other than as noted above, we are in full compliance with all other applicable Nasdaq corporate governance standards.

The employment agreements of the executive members of our board of directors contain standard termination provisions (which include termination: (i) upon death or disability, (ii) with or without cause, and (iii) with or without good reason).

D. EMPLOYEES

As of December 31, 2011, we employed 1,467 employees, consisting of 554 land-based employees and 913 seafarers as crew on our vessels, of which 312 were in our River Business, 168 were in our Offshore Supply Business and 433 were in our Ocean Business. This represents a 15% increase with respect to December 31, 2010, mainly attributable to more operational pushboats in the river at December 31, 2011, as compared to December 31, 2010, to the entry into operation of our UP Turquoise and UP Jasper on March 12, 2011, and September 29, 2011, respectively and to the entry into operation of our feeder container vessel M.V. Argentino on January 10, 2011. Some of these employees were employed through various manning agents depending on the nationality as listed below:

• Indian crew:	Orient Ship Management & Manning Pvt., Ltd., Mumbai, India
• Argentine crew:	Ravenscroft Ship Management S.A., a subsidiary, Montevideo, Uruguay
• Paraguayan crew:	Ravenscroft Ship Management S.A., a subsidiary, Montevideo, Uruguay

Our crew is employed under the standard collective bargaining agreements with the seafarers' union in their respective countries. The crew is employed on contractual terms valid for a fixed duration of service on board the vessels. We ensure that all the crew employed on board our vessels have the requisite experience, qualifications and certification to comply with all international regulations and shipping conventions. Our training requirements for the crew exceed the

applicable statutory requirements. We always man our vessels above the safe manning requirements of the vessels' flag state in order to ensure proper maintenance and safe operation of the vessels. We have in force special programs such as a performance-related incentive bonus, which is paid to some of our senior officers upon rejoining our ships. This ensures retention of qualified and competent staff.

E. SHARE OWNERSHIP

For information concerning the share ownership in our Company of our officers and directors, please see Item 7 — Major Shareholders and Related Party Transactions.

ITEM 7 – MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. MAJOR SHAREHOLDERS

The following table sets forth information regarding the owners of more than five percent of our common stock as of March 15, 2012. The address of Inversiones Los Avellanos S.A., and Hazels (Bahamas) Investments Inc. is Ocean Centre, Montagu Foreshore, East Bay St., P.O. Box SS-19084, Nassau, Bahamas.

Name	Number of Shares Beneficially Owned	Percent of Shares Beneficially Owned	Voting Percentage
Inversiones Los Avellanos S.A. (1) (2) (3) (10)	7,864,085	26.2%	71.0%
Hazels (Bahamas) Investments Inc. (1) (2) (4) (10)	7,864,085	26.2%	71.0%
FMR LLC (5)	4,789,465	16.0%	6.3 %
Franklin Resources, Inc. (6)	2,543,517	8.5%	3.3 %
Wellington Management Company, LLP (7)	2,059,199	6.9%	2.7%
Marathon Asset Management LLP (8)	2,021,397	6.7%	2.6 %
All directors and executive officers as a group (9) (10)	9,026,379	29.7%	72.2%

The table here above does not consider for the purposes of calculating number of shares owned and the related percent of shares beneficially owned, any holdings disclosed by holders of our Convertible Notes due 2017 as of the date here above.

(1) Inversiones Los Avellanos S.A., or Los Avellanos, and Hazels (Bahamas) Investments Inc., or Hazels, are each entitled to seven votes for each share of common stock that they hold since the Company's IPO in October 2006 as well as for any seven-vote shares originally held by Solimar Holdings Ltd. and later purchased by either Los Avellanos or Hazels.

(2) Los Avellanos and Hazels have entered into an agreement pursuant to which they have agreed to vote their respective shares together in all matters where a vote of our shareholders is required. (See "Related Party Transactions" in Item 7.B. of this report).

(3) 4,735,517 shares entitled to seven votes per share plus 3,128,568 shares owned by Hazels (of which only 150,719 are entitled to one vote per share with the remaining shares being entitled to seven votes per share).

(4) 3,128,568 shares (2,977,849 entitled to seven votes per share and 150,719 entitled to one vote per share) plus 4,735,517 shares owned by Los Avellanos (all of them entitled to seven votes per share).

(5) Based on Nasdaq OMX Corporate Intelligence, except for voting percentage which is based on Company calculations.

(6) As per Schedule 13G/A filed with US Securities and Exchange Commission on February 9, 2012, except for voting percentage which is based on Company calculations. Company does not make any representation on the accuracy of the information filed by third parties included here for information purposes only.

(7) As per Schedule 13G filed with US Securities and Exchange Commission on February 14, 2012, except for voting percentage which is based on Company calculations. Company does not make any representation on the accuracy of the information filed by third parties included here for information purposes only.

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(8) As per Schedule 13G/A filed with US Securities and Exchange Commission on January 30, 2012, except for voting percentage which is based on Company calculations. Company does not make any representation on the accuracy of the information filed by third parties included here for information purposes only.

(9) Los Avellanos and Hazels are controlled by members of the Menendez family, including Felipe Menendez R., our President, Chief Executive Officer and a director, and Ricardo Menendez R., our Executive Vice President and a director. Los Avellanos is a wholly-owned subsidiary of SIPSA S.A. and Hazels is 99.8% owned by Los Avellanos.

(10) Includes 733,797 shares of restricted stock issued to companies controlled by our Chief Executive Officer, our Executive Vice President and our Chief Financial Officer. Includes 348,750 shares of common stock issuable within 60 days upon exercise of options granted to these companies which have vested, as well as 79,747 shares of restricted stock issued to our non-executive directors as part of their compensation for the services rendered to us as board members.

During 2010, Hazels (Bahamas) Investments Inc. acquired 2,977,690 shares of the Company from Solimar Holdings Ltd.

In connection with the Approved Share Buyback Plan dated October 24, 2011, the Company has not bought back shares of its common stock as of December 31, 2011.

B. RELATED PARTY TRANSACTIONS

There are no revenues derived from transactions with related parties for each of the years ended December 31, 2011, 2010 and 2009. As of December 31, 2011, 2010 and 2009, the balances of the accounts receivable from and payables to all related parties were approximately $6.5 million, $5.4 million and $5.0 million, respectively.

Shipping Services Argentina S.A. (Formerly I. Shipping Services S.A.)

We and our subsidiaries also contract with related parties for various services. Pursuant to a commercial agreement and an agency agreement with us, Shipping Services Argentina S.A. (formerly I. Shipping Services S.A.) has agreed to perform the duties of commercial agent for our container feeder service and port agent for us in Argentina. Shipping Services Argentina S.A. is indirectly controlled by the Menendez family, which includes Felipe Menendez R. and Ricardo Menendez R. For these services, we pay Shipping Services Argentina S.A. commissions and fees. For each of the years ended December 31, 2011, 2010 and 2009 the amounts paid and / or accrued for such services amounted to $0.5 million, $0.2 million and $0.1 million, respectively. We believe that payments made under the above agreements reflect market rates for the services provided and are similar to what third parties pay for similar services.

Certain of our directors and senior management hold similar positions with our related parties. Felipe Menendez R., who is our President, Chief Executive Officer and a director, is also a director of Maritima SIPSA S.A. and Shipping Services Argentina S.A. Ricardo Menendez R., who is our Executive Vice President and one of our directors, is also the President of Shipping Services Argentina S.A. and is a director of Maritima SIPSA S.A. In light of their positions with such entities, these officers and directors may experience conflicts of interest in selecting between our interests and those of Maritima SIPSA S.A. and Shipping Services Argentina S.A.

Navalia S.A. (Formerly Navalia S.R.L)

Pursuant to a commercial and an agency agreement with us, Navalia S.A., or Navalia, has agreed to perform the duties of commercial agent for our container feeder service and port agent for us in Ushuaia, Argentina. Navalia is directly controlled by the Menendez family, which includes Felipe Menendez R. and Ricardo Menendez R. For these services, we pay Navalia commissions and fees. For the year ended December 31, 2011, the amounts paid and / or accrued for such services amounted to $3.0 million. We believe that payments made under the above agreements reflect market rates for the services provided and are similar to what third parties pay for similar services.

Commercial Commissions paid to Firmapar Corp. (Formerly Comintra Enterprise Ltd.)

In 2003, UP Offshore (Bahamas) Ltd. signed a commercial agreement with Firmapar Corp., or Firmapar, one of its shareholders. Under this agreement Firmapar agreed to assist UP Offshore (Bahamas) Ltd. regarding the commercial activities of UP Offshore (Bahamas) Ltd.'s fleet with the Brazilian offshore oil industry. Firmapar's responsibilities, among others, include marketing the PSVs in the Brazilian market and negotiating the time charters or other revenues contracts with prospective charterers of the PSVs.

The parties agreed that Firmapar's professional fees under this agreement shall be 2% of the gross time charters revenues from Brazilian charters collected by UP Offshore (Bahamas) Ltd. on a monthly basis.

Firmapar's services in connection with this agreement began on June 25, 2003, and, unless terminated earlier, end on June 25, 2013.

UP Offshore (Bahamas) Ltd. may terminate this agreement (a) at any time upon 30 days notice if (i) PSVs representing more than 50% of the gross time charter revenues of UP Offshore (Bahamas) Ltd. arising from contracts in Brazil are sold or (ii) Ultrapetrol and LAIF cease owning, jointly or separately, more than 50% of UP Offshore (Bahamas) Ltd.'s outstanding voting stock; (b) Firmapar breaches any material term of this agreement; (c) in the event of gross negligence or material failure to perform the services by Firmapar, or (d) upon mutual agreement.

In the event of termination under subsections (a) or (d) above, such termination shall not be effective unless and until UP Offshore (Bahamas) Ltd. shall have also paid to Firmapar $2.5 million (less any fees already paid to Firmapar through the termination date). Other than the figures mentioned above no further indemnification will be due by UP Offshore (Bahamas) Ltd. to Firmapar.

For the years ended December 31, 2011, 2010 and 2009 the amounts paid and/or accrued for such services amounted to $1.1 million, $1.1 million and $0.4 million, respectively.

Operations in OTS S.A.'s terminal

UABL Paraguay, our subsidiary in the River Business, operates the terminal that pertains to Obras Terminales y Servicios S.A. (OTS S.A.), a related party. For the years ended December 31, 2011, 2010 and 2009, UABL Paraguay paid to OTS S.A. $0.8 million, $1.0 million and $1.0 million, respectively, for this operation.

SIPSA S.A.

There were no intercompany activities between SIPSA S.A. and us for any of the years ended December 31, 2011, 2010 and 2009.

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Registration Rights Agreement

We are parties to a registration rights agreement with Los Avellanos, Hazels and Solimar, our shareholders prior to our IPO, pursuant to which we granted them and certain of their transferees, the right, under certain circumstances and subject to certain restrictions, including restrictions included in the lock-up agreements to which Los Avellanos, Hazels and Solimar are party, to require us to register under the Securities Act shares of our common stock held by Los Avellanos, Hazels or Solimar. Under the registration rights agreement, Los Avellanos, Hazels and Solimar have the right to request that we register the sale of shares held by them on their behalf and may require that we make available shelf registration statements permitting sales of shares into the market from time to time over an extended period. We are required to pay all registration expenses in connection with the demand registrations under the registration rights agreement except that the underwriters' expenses reimbursement will be limited to one counsel. In addition, Los Avellanos, Hazels and Solimar have the ability to exercise certain piggyback registration rights in connection with registered offerings initiated by us, for which we must pay all expenses.

On October 27, 2009, Solimar requested us to effect the registration of 2,977,690 registrable common shares issued in their name. On November 27, 2009, we filed a Registration Statement on Form F-3 and subsequently amended it on February 18, 2010. On March 12, 2010, we filed a second amendment to our F-3. The Registration Statement was declared effective on February 18, 2010, and subsequently withdrawn on July 22, 2010, in connection with a transaction concluded on July 15, 2010, through which Hazels (Bahamas) Investments Inc., an original shareholder (each party in the transaction was a shareholder in Ultrapetrol prior to its Initial Public Offering) acquired 2,977,690 shares representing a 100% of the holdings that Solimar had in Ultrapetrol.

Under such transaction (concluded on July 15, 2010) all rights of Solimar pursuant to the Registration Rights Agreement have been transferred to Hazels.

Shareholders Agreement

Solimar, Los Avellanos and Hazels are party to a second amended and restated shareholders agreement, dated September 21, 2006, that became effective on October 18, 2006, that contains, among other things, provisions relating to director designation rights, restrictions of transfers of stock held by them and an agreement to vote their shares together on certain matters.

On July 15, 2010, Hazels acquired 2,977,690 shares representing 100% of the holdings that Solimar had in Ultrapetrol. Under such transaction all rights of Solimar pursuant to the Registration Rights Agreement have been transferred to Hazels.

Employment Agreements

We have entered into employment contracts with our President and Chief Executive Officer, Felipe Menendez R., our Executive Vice President, Ricardo Menendez R., our Chief Financial Officer, Leonard J. Hoskinson and our Chief Accountant, Mr. Alberto G. Deyros. Each of these employment agreements had an initial term of three years from October 18, 2006, and were subject to one year renewals at our written election. In addition, on July 20, 2006, we entered into separate consulting agreements that became effective October 18, 2006, with companies controlled by our chief executive officer, executive vice president, chief financial officer and chief accountant for work they performed for us in various different jurisdictions. Some of these consulting agreements obligate us to grant these companies an aggregate of 310,000 shares of restricted stock for which we expect to incur charges over the three year period of the agreement equal in the aggregate to the number of shares granted multiplied by $11.00 (the IPO price) and 348,750 shares issuable upon the exercise of options with an exercise price of $11.00 (the IPO price) pursuant to the Plan.

On October 29, 2009, we renewed these employment agreements as well as the consulting agreements for three years. Some of these consulting agreements obligate us to grant these companies an aggregate of 329,375 shares of restricted stock for which we expect to incur charges over the three year period of the agreements equal in the aggregate to the number of shares granted multiplied by $5.11 (the quoted price of the share at the grant date). In addition, those consulting agreements also provide for up to 329,375 additional shares of restricted stock subject to performance of the consultants upon discretion of the disinterested members of our Board of Directors.

C. INTERESTS OF EXPERTS AND COUNSEL

Not Applicable.

ITEM 8 – FINANCIAL INFORMATION

A. CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION

See Item 18 for reference to financial information.

Legal Proceedings

UABL – Ciudad del Este Customs Authority

On September 21, 2005, the local Customs Authority of Ciudad del Este, Paraguay issued a finding that certain UABL entities owe taxes to that authority in the amount of $2.2 million, together with a fine for non-payment of the taxes in the same amount, in respect of certain operations of our River Business for the prior three-year period. This matter was referred to the Central Customs Authority of Paraguay, or the Paraguay Customs Authority. We believed that this finding was erroneous and UABL formally replied to the Paraguay Customs Authority contesting all of the allegations upon which the finding was based. After review of the entire operations for the claimed period, the Paraguayan Central Tax Authorities, asserting their jurisdiction over the matter, confirmed that the UABL entities did pay their taxes on the claimed period, but held a dissenting view on a third issue (the tax base used by the UABL entities to calculate the applicable withholding tax). The primary case was appealed by the UABL entities before the Tax and Administrative Court, and when summoned, the Paraguayan Tax Authorities filed an admission, upon which the Court on November 24, 2006, confirmed that the UABL entities were not liable for the first two issues. Nevertheless, the third issue continued, and through a resolution which was provided to UABL on October 13, 2006, the Paraguayan Undersecretary for Taxation confirmed that, in his opinion, UABL was liable for a total of approximately $0.5 million and applied a fine of 100% of that amount. UABL entered a plea with the respective court contending the interpretation on the third issue where it claimed to be equally not liable. On October 19, 2007, we presented a report by an expert highly favorable to our position. On March 26, 2009, the Tax and Administrative Court decided that UABL was not liable for the third issue under discussion (the tax base used by UABL's entities to calculate the applicable withholding tax). On April 2, 2009, the Paraguayan Tax Authorities appealed the Tax and Administrative Courts decision to the Supreme Court. On September 22, 2010, the Paraguayan Supreme Court revoked the March 26, 2009, ruling of the Tax and Administrative Court and confirmed the decision of the Paraguayan undersecretary for taxation which condemned UABL Paraguay S.A. to pay approximately $605,000 non-withheld taxes, $685,000 in fines and $1,251,000 in accrued due interest. We appealed the decision of the Supreme Court, seeking to clarify its ruling based on the Bona Fide basis of the UABL arguments recognized by the Court expressly in its ruling and on this appeal sought to eliminate fines and interest. Finally, in a signed agreement with the Tax Authorities on October 14, 2010, UABL paid the total amount of $1,294,000 in full and final settlement of the claim and agreed to drop its appeal to the Supreme Court. In parallel with this ruling the Office of the Treasury Attorney initiated an action in respect of the other two issues concerned in this litigation (which had been terminated on November 24, 2006, with the admission of the Central Tax Authorities that no taxes were due for these two issues and the consequent dropping of the action by the plaintiffs) to review certain formal aspects of the case on the grounds that the Paraguay Customs Department did not represent the interests of Paraguay. UABL submitted a defense in relation to the action commenced by the Office of the Treasury Attorney. Subsequently, the Office of the Treasury Attorney filed a response with regard to our defense. The evidentiary stage of the proceedings commenced in November 2011. Aside from the mentioned procedures, the Customs Authorities of Paraguay have reopened the proceedings against UABL S.A., UABL Paraguay S.A. and Yataity S.A. in connection with the possible reopening of the case pending a decision of the reopening of the case in court. Counsel notified the Customs to hold the proceedings pending a decision of the

court and also contest any new investigation into the matter on the grounds that the action is time barred. We have been advised by UABL's counsel in the case that there is only a remote possibility that a judicial court would find UABL liable for any of these taxes or fines still in dispute or that the final outcome of these proceedings could have a material adverse effect on the Company.

UABL International S.A. – Bolivian Tax Authority

On November 3, 2006, and April 25, 2007, the Bolivian Tax Authority (Departamento de Inteligencia Fiscal de la Gerencia Nacional de Fiscalización) issued a notice in the Bolivian press advising that UABL International S.A. would owe taxes to that authority. On June 18, 2007, legal counsel in Bolivia submitted points of defense to the Bolivian tax authorities. On August 27, 2007 the Bolivian tax authorities gave notice of a resolution determining the taxes (value added tax, transaction tax and income tax) that UABL International S.A. would owe to them in the amount of approximately $5.8 million (including interest and fines). On October 10, 2007, legal counsel in Bolivia gave notice to the Bolivian tax authorities of the lawsuit commenced by UABL International S.A. to refute the resolution above mentioned. On August 1, 2008, UABL International S.A. was served with a notice informing that the Bolivian Tax Authorities had replied to the lawsuit. On August 22, 2008, a hearing and judicial inspection took place at Puerto Quijano, Bolivia. On August 30, 2008, both parties submitted their arguments to the judge, completing this part of the case. On August 12, 2009, UABL International S.A. was served with a judgment of a Bolivian court ruling on certain taxes allegedly due by UABL International S.A. On August 22, 2009, UABL International S.A. submitted an appeal to the lower court judgment to which Bolivian tax authorities have contested. The Court of appeal confirmed the judgment of the Lower Court. UABL International S.A. has submitted a cassation appeal (an appeal on points of law) which is currently pending before the Bolivian Supreme Court. On the other hand, on June 26, 2008, the same Bolivian court ordered a preemptive embargo against all barges owned by UABL International S.A. that may be registered in the International Bolivian Registry of Ships, or RIBB. According to local counsel this preemptive embargo under Bolivian law has no effect over the Company's right to use its assets nor does it have any implication over the final decision of the court, the substance of the matter and in this case it is ineffective since UABL International S.A. did not have any assets owned by it registered in the RIBB. Moreover, UABL International S.A. had challenged the judge's decision to place the embargo. On November 15, 2008, the lower court reconfirmed the embargo. UABL International S.A. appealed the decision of the lower court, which was later reconfirmed by a higher court. The shares of UABL International S.A. have ceased to belong to our Company and we have been advised by local counsel that there is only a remote possibility that we would finally be found liable for any of these taxes or fines and / or that these proceedings will have financial material adverse impact on the consolidated financial position or results of operations of the Company.

UABL Paraguay S.A. – Paraguayan Customs Asuncion

On April 7, 2009, the Paraguayan Customs in Asuncion commenced administrative proceedings against UABL Paraguay S.A. alleging infringement of Customs regulations due to lack of submission of import clearance documents in Paraguay for bunkers purchased between January 9, 2007, and December 23, 2008, from YPF-Repsol S.A. in Argentina. Since those bunkers were purchased for consumption onboard pushboats, UABL Paraguay S.A. submitted a defense on April 23, 2009, requesting the closing of those proceedings based on the non-infringement of Customs regulations; however the proceedings were not closed. On August 21, 2009, as part of the evidence to be rendered in the Customs proceedings UABL Paraguay S.A. submitted a technical report of the Paraguayan Coast Guard stating that all parcels of bunkers purchased by UABL Paraguay S.A. from YPF-Repsol S.A. were consumed onboard the push boats. We were advised that the Paraguayan Customs in Ciudad del Este also commenced administrative proceedings against UABL Paraguay S.A. for the same reasons as the Customs in Asuncion, however those proceedings have been suspended. Customs Authorities appraised the bunkers and determined the corresponding import tax and fine in the amount of $2.0 million. On March 22, 2010, the Customs in Asuncion issued their ruling on the matter imposing a fine of Gs. 54,723,820 (approximately $11,700), and UABL Paraguay S.A. was going to pay the fine with the aim to end these proceedings but the Director of Customs in Asunción decided to render null that ruling and ordered evidence to be filed in respect of years 2003 to 2006 before issuing the final ruling. In parallel with this ruling the denouncing parties in Ciudad del Este submitted remedies against the decision of Customs in Asuncion arguing that such ruling was taken without bringing both dossiers together. In a similar manner, on September 20, 2010, the Paraguayan Customs in Asuncion received a complaint against UABL Paraguay S.A. alleging infringement

of Customs regulations due to lack of submission of import clearance documents in Paraguay for bunkers purchased during 2009 and 2010, from YPF-Repsol S.A. in Argentina. UABL Paraguay S.A. submitted its defense together with all documents related to the bunker purchases. Our local counsel is of the opinion that remedies will be rejected and therefore that there is only a remote possibility that UABL Paraguay S.A. will finally be found liable for any such taxes or fines and / or that these proceedings will have financial material adverse impact on the consolidated financial position or results of operations of the Company.

Oceanpar S.A. and UABL Paraguay S.A. - Customs investigation in connection with re-importation of barges subject to conversion

Oceanpar S.A. was notified of this investigation on June 17, 2011. The matter under investigation is whether UABL Paraguay S.A. paid all import taxes and duties corresponding to the re-importation of barges submitted to conversion in foreign yards. On June 24, 2011 Oceanpar S.A. and UABL Paraguay submitted the evidence of all payments effected in 2008 corresponding to the re-importation of these barges. Our Counsel has advised that there is only a remote chance that these proceedings will have a material adverse impact on the financial results of the Company.

Various other legal proceedings involving us may arise from time to time in the ordinary course of business. However, we are not presently involved in any other legal proceedings that, if adversely determined, would have a material adverse effect on us.

Dividend Policy

The payment of dividends is in the discretion of our board of directors. We have not paid a dividend to date. Any determination as to dividend policy will be made by our board of directors and will depend on a number of factors, including the requirements of Bahamian law, our future earnings, capital requirements, financial condition and future prospects and such other factors as our board of directors may deem relevant.

Section 35 of the International Business Companies Act, 2000 (Chapter 309, Statute Laws of The Bahamas, 2000 Edition) provides that, subject to any limitations in its Memorandum or Articles, a company may, by a resolution of directors, declare and pay dividends in money, shares or other property. However, in accordance with Section 35 of the said Act, dividends shall only be declared and paid if the directors determine that immediately after the payment of the dividend:

(a) the company will be able to satisfy its liabilities as they become due in the ordinary course of its business; and

(b) the realizable value of the assets of the company will not be less than the sum of its total liabilities, other than deferred taxes, as shown in the books of account and its issued and outstanding share capital and, in the absence of fraud, the decision of the directors as to the realizable value of the assets of the company is conclusive unless a question of law is involved.

Our ability to pay dividends is restricted by the 2014 Notes, which we issued in 2004. In addition, we may incur expenses or liabilities, including extraordinary expenses, which could include costs of claims and related litigation expenses, or be subject to other circumstances in the future that reduce or eliminate the amount of cash that we have available for distribution as dividends or for which our board of directors may determine requires the establishment of reserves. The payment of dividends is not guaranteed or assured and may be discontinued at any time at the discretion of our board of directors. Because we are a holding company with no material assets other than the stock of our subsidiaries, our ability to pay dividends is dependent upon the earnings and cash flow of our subsidiaries and their ability to pay dividends to us. If there is a substantial decline in any of the markets in which we participate, our earnings will be negatively affected, thereby limiting our ability to pay dividends.

B. SIGNIFICANT CHANGES

None.

ITEM 9 – THE OFFER AND LISTING

A. Information regarding the price history of the stock listed:

(a) High and low market prices for the five most recent full financial years

	Financial Year Ended December 31,				
Per share prices	2007	2008	2009	2010	2011
High	$ 27.04	$ 17.44	$ 5.72	$ 7.92	$ 6.67
Low	$ 12.80	$ 1.84	$ 1.79	$ 4.05	$ 2.12

(b) High and low market prices for each full financial quarter for the two most recent full financial years

Per share prices	Q1 2010	Q2 2010	Q3 2010	Q4 2010	Q1 2011	Q2 2011	Q3 2011	Q4 2011
High	$ 6.34	$ 6.52	$ 6.49	$ 7.92	$ 6.67	$ 5.86	$ 5.31	$ 3.54
Low	$ 4.38	$ 4.31	$ 4.05	$ 5.97	$ 4.74	$ 4.75	$ 2.23	$ 2.12

(c) High and low market prices for each month, for the most recent six months:

Per share prices	September 2011	October 2011	November 2011	December 2011	January 2012	February 2012
High	$ 3.42	$ 3.19	$ 3.54	$ 3.08	$ 3.48	$ 3.10
Low	$ 2.23	$ 2.12	$ 2.24	$ 2.47	$ 2.60	$ 2.67

B. PLAN OF DISTRIBUTION

Not Applicable.

C. MARKETS

Our Common Stock is listed on The Nasdaq Global Select Market under the symbol "ULTR".

D. SELLING SHAREHOLDERS

Not Applicable.

E. DILUTION

Not Applicable.

F. EXPENSES OF THE ISSUE

Not Applicable.

ITEM 10 – ADDITIONAL INFORMATION

A. SHARE CAPITAL

Not Applicable.

B. MEMORANDUM AND ARTICLES OF ASSOCIATION

The following summarizes certain provisions of the Company's Second Amended and Restated Memorandum of Association and Fourth Amended and Restated Articles of Association, or the Memorandum and Articles of Association. This summary is qualified in its entirety by reference to the International Business Companies Act, 2000 and the Company's Memorandum and Articles of Association. Information on where investors can obtain copies of the Memorandum and Articles of Association is described under the heading "Documents on Display" under this Item.

Objects and Purposes

The Company is incorporated in the Commonwealth of The Bahamas ("The Bahamas") under the name Ultrapetrol (Bahamas) Limited. The Registered Office of the Company is situated at Ocean Centre, Montagu Foreshore, East Bay Street, P.O. Box SS-19084, Nassau, Bahamas. The Registered Agent of the Company is H & J Corporate Services Ltd., Ocean Centre, Montagu Foreshore, East Bay Street, P.O. Box SS-19084, Nassau, Bahamas.

Clause 4 of the Memorandum provides that the purpose of the Company is to engage in any lawful act or activity for which companies organized under the Actor any successor law to the Act that is at any time in force in The Bahamas, may now or hereafter be permitted to engage.

Directors

The Company must have a board of directors (the "Board of Directors") comprising a minimum number of five directors and a maximum number of seven directors. The Board of Directors is required to meet at least quarterly and to direct and oversee the management and affairs of the Company, exercisinge all the powers of the Company that are not expressly reserved to its shareholders under the Articles, the Act or any other laws of The Bahamas. The Board of Directors may from time to time, in its discretion, fix the amounts which shall be payable to members of the Board of Directors and to members of any committee, for attendance at the meetings of the Board of Directors or of such committee and for services rendered to the Company.

Subject always to the Act, the Company shall not enter into:

(i) any merger or consolidation involving the Company on the one hand and any Named Shareholder (as defined in the Memorandum) that is a shareholder of the Company, any affiliate of such Named Shareholder (as defined in the Memorandum) or any member of the Company's management or Board of Directors or their respective affiliates (each an "Interested Party") on the other hand;

(ii) any sale, lease or other direct or indirect disposition of all or substantially all of the Company's and its subsidiaries' assets in a transaction or series of related transactions to one or more Interested Parties;

(iii) any merger or consolidation or sale, lease or other direct or indirect disposition of all or substantially all of the Company's and its subsidiaries' assets in a transaction or series of related transactions that would result in the receipt of different types or amounts of consideration per share by one or more Interested Parties on the one hand, and any other of the shareholders of the Company, on the other hand; and

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(iv) any business transaction between the Company or its subsidiaries on the one hand and one or more Interested Parties on the other hand, involving a value in excess of $2.0 million;

without (A) having previously obtained, at the Company's expense, a fairness opinion confirming that the proposed transaction is fair from a financial standpoint for the Company and with respect to a transaction described in paragraph (iii) above, for those shareholders which are not Interested Parties and (B) such proposed transaction being approved by a majority of disinterested directors of the Company. Any fairness opinion pursuant to the preceding sentence shall be rendered by an internationally recognized investment banking, auditing or consulting firm (or, if the proposed transaction involves the sale or purchase of a vessel or other floating assets, by an internationally recognized shipbroker) selected by the Company's disinterested directors and engaged on behalf of the Company and/or its shareholders. To qualify as a disinterested director, a director must not have a personal interest in the transaction at hand and must not otherwise have a relationship that, in the opinion of the Board of Directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. Further, should any such transaction require shareholder approval, it must be approved by a majority vote of those shareholders entitled to vote that are not Interested Parties.

In this connection, the Act provides that subject to any limitations in the Memorandum and the Articles and any unanimous shareholder agreement, no such agreement or transaction is void or voidable by reason that the director is present at the meeting of directors that approves the agreement or transaction or that the vote of the director is counted for that purpose. Such agreement or transaction is valid if the material facts of the director's interest in the agreement or transaction and his interest in or relationship to any other party to the agreement or transaction are disclosed in good faith or are known to the shareholders entitled to vote at a meeting of the shareholders and the agreement or transaction is approved or ratified by resolution of the shareholders. A director who has an interest in any particular business to be considered at a meeting of directors may be counted for the purpose of determining whether the meeting is duly constituted. A director need not be a member of the Company and no shareholding qualification shall be necessary to qualify a person as a director.

Share Rights, Preferences, Restrictions

Dividends may be declared in conformity with applicable law by and at the discretion of, the Board of Directors at any regular or special meeting. Dividends may be declared and paid in cash, stock or other property of the Company.

Subject as therein provided, the Articles may be amended, added to, altered or repealed, or new Articles may be adopted, at any annual or special meeting of the shareholders by the vote of holders of a majority of the votes of the shares issued and outstanding and entitled to vote at such meeting of shareholders. At all meetings of shareholders of the Company, except as otherwise expressly provided by law, there must be present, either in person or by proxy, shareholders of record holding at least a majority of the votes of the shares issued and outstanding and entitled to vote at such meetings in order to constitute a quorum, but if less than a quorum is present, a majority of those shares present either in person or by proxy shall have power to adjourn any meeting until a quorum shall be present. If after an adjournment an adjourned meeting is held, for the purpose of such adjourned meeting in order to establish a quorum there must be present, either in person or by proxy, shareholders of record holding at least a one-third of the votes of the shares issued and outstanding and entitled to vote at such adjourned meeting.

If a quorum is present and except as otherwise expressly provided by law, the affirmative vote of a majority of the votes represented at the meeting shall be the act of the shareholders of the Company. At any meeting of shareholders of the Company, with respect to a matter for which a shareholder is entitled to vote, each such shareholder shall be entitled to one (1) vote for each share of Common Stock it holds; provided that the Named Shareholders, as such term is defined in the Memorandum of Association, shall be entitled to seven (7) votes for each share of Common Stock held by it that was initially acquired by a Named Shareholder prior to the completion of the Company's initial public

offering (which right shall be personal and non-transferable, unless to another Named Shareholder or Permitted Transferee, as such term is defined in the Memorandum of Association), or with respect to such shares sold by one Named Shareholder to another Named Shareholder subject to the limitations set forth in the Memorandum of Association. Each shareholder may exercise such voting right either in person or by proxy provided, however, that no proxy shall be valid after the expiration of eleven months from the date such proxy was authorized unless otherwise provided in the proxy. A duly executed proxy shall be irrevocable if it states that it is irrevocable and if and only as long as, it is coupled with an interest sufficient to support an irrevocable power. A shareholder may revoke any proxy which is not irrevocable by attending the meeting and voting in person or by filing an instrument in writing revoking the proxy or another duly executed proxy bearing a later date with the Secretary of the Company.

Notice of every annual and special meeting of shareholders of the Company, other than any meeting the giving of notice of which is otherwise prescribed by law, stating the date, time, place and purpose thereof and in the case of special meetings, the name of the person or persons at whose direction the notice is being issued, must be given personally or sent by mail, telegraph, cablegram, telex, teleprinter or such other method (including electronic mail) as permitted by the United States Securities and Exchange Commission and the NASDAQ Marketplace Rules on the date thereof, at least fifteen (15) but not more than sixty (60) days before such meeting, to each shareholder of record entitled to vote thereat and to each shareholder of record who, by reason of any action proposed at such meeting would be entitled to have his shares appraised if such action were taken and the notice shall include a statement of that purpose and to that effect. If mailed, notice is deemed to have been given when deposited in the mail, directed to the shareholder at his address as the same appears on the record of shareholders of the Company or at such address as to which the shareholder has given notice to the Secretary of the Company. Notice of a meeting need not be given to any shareholder who submits a signed waiver of notice, whether before or after the meeting, or who attends the meeting without protesting prior to the conclusion thereof the lack of notice to him.

There are no limitations under the laws of The Bahamas on the rights of non-resident or foreign shareholders to hold or exercise voting rights.

C. MATERIAL CONTRACTS

None.

D. EXCHANGE CONTROLS

Under Bahamian law, there are currently no restrictions on the export or import of capital, including foreign exchange controls or restrictions that affect the remittance of dividends, interest or other payments to non-resident holders of our common stock.

E. TAX CONSIDERATIONS

The following is a discussion of the material Bahamian and U.S. federal income tax considerations relevant to an investment decision by a U.S. Holder and a Non-U.S. Holder, each as defined below, with respect to our common stock. This discussion does not purport to deal with the tax consequences of owning shares of our common stock to all categories of investors, some of which, such as dealers in securities, investors whose functional currency is not the U.S. dollar and investors that own, actually or under applicable constructive ownership rules, 10% or more of our common stock, may be subject to special rules. This discussion deals only with holders who purchase our common stock in connection with this offering and hold our common stock as a capital asset. You are encouraged to consult your own tax advisors concerning the overall tax consequences arising in your own particular situation under U.S. federal, state, local or foreign law of the ownership of our common stock.

Any material tax considerations relevant to an investment decision by a U.S. Holder or Non-U.S. Holder, each as defined below, with respect to securities registered under this registration statement other than our common stock, will be described in a prospectus supplement issued in connection with the offering of such securities.

Bahamian Tax Considerations

In the opinion of Higgs & Johnson, our Bahamian counsel, the following are the material Bahamian tax consequences of our activities to us and shareholders of our common stock. We are incorporated in the Commonwealth of The Bahamas. Under current Bahamian law, we are not subject to tax on income or capital gains, and no Bahamian withholding tax will be imposed upon payments of dividends by us to our shareholders for a period of twenty years from our date of incorporation.

U.S. Federal Income Tax Considerations

In the opinion of Seward & Kissel LLP, our U.S. counsel, the following are the material U.S. federal income tax consequences to the Company of its activities and to U.S. Holders and Non-U.S. Holders, of our common stock. The following discussion of U.S. federal income tax matters is based on the Code, judicial decisions, administrative pronouncements, and existing and proposed regulations issued by the U.S. Department of the Treasury, all of which are subject to change, possibly with retroactive effect. The discussion below is based, in part, on the description of our business as described in "Prospectus Summary" above and assumes that we conduct our business as described in that section. References in the following discussion to "we" and "us" are to Ultrapetrol (Bahamas) Limited and its subsidiaries on a combined basis.

U.S. Federal Income Taxation of Our Company

Taxation of Operating Income: in General

We anticipate that we will earn substantially all our income from the hiring or leasing of vessels for use on a time, voyage or bareboat charter basis or from the performance of services directly related to those uses, which we refer to as "shipping income."

Unless exempt from U.S. federal income taxation under the rules of Section 883 of the Code, or Section 883, as discussed below, we will be subject to U.S. federal income tax on our shipping income that is treated as derived from sources within the United States, to which we refer as U.S.-source shipping income. For these purposes, U.S.-source shipping income includes 50% of our shipping income that is attributable to transportation that begins or ends, but that does not both begin and end, in the United States.

Shipping income attributable to transportation that both begins and ends in the United States is considered to be 100% from sources within the United States. We are not permitted by law and therefore do not expect to engage in transportation that produces income which is considered to be 100% from sources within the United States.

Shipping income attributable to transportation exclusively between non-U.S. ports will be considered to be 100% derived from sources outside the United States. Shipping income derived from sources outside the United States will not be subject to any U.S. federal income tax.

In the absence of exemption from tax under Section 883, our gross U.S.-source shipping income would be subject to a 4% tax imposed without allowance for deductions as described below.

Exemption of Operating Income from U.S. Federal Income Taxation

Under Section 883 of the Code and the final Treasury Regulations promulgated thereunder, or the final regulations, a foreign corporation will be exempt from U.S. federal income taxation on its U.S.-source shipping income if:

(1) it is organized in a qualified foreign country which, as defined, is one that grants an "equivalent exemption" to corporations organized in the United States in respect of each category of shipping income for which exemption is being claimed under Section 883 and to which we refer to as the Country of Organization Test; and

(2) either

(A) more than 50% of the value of its stock is beneficially owned, directly or indirectly, by qualified shareholders which as defined includes individuals who are "residents" of a qualified foreign country which we refer to as the 50% Ownership Test, or

(B) its stock, or that of its 100% parent, is "primarily and regularly traded on an established securities market" in a qualified foreign country or in the U.S., which we refer to as the Publicly-Traded Test.

The Commonwealth of The Bahamas and Panama, the jurisdictions where we and our vessel-owning subsidiaries are incorporated, each have been officially recognized by the IRS as a qualified foreign country that grants the requisite equivalent exemption from tax in respect of each category of shipping income we and our subsidiaries earn and currently expect to earn in the future. Therefore, we and each of our subsidiaries will be exempt from U.S. federal income taxation with respect to our U.S. source shipping income if we satisfy either the 50% Ownership Test or the Publicly-Traded Test. We do not believe that we are able to satisfy the 50% Ownership Test due to the widely-held ownership of our stock. Our ability and that of our subsidiaries to qualify for exemption under Section 883 is solely dependent upon satisfaction of the Publicly-Traded Test as discussed below.

The final regulations provide, in pertinent part, that stock of a foreign corporation will be considered to be "primarily traded" on an established securities market if the number of shares of each class of stock that are traded during any taxable year on all established securities markets in that country exceeds the number of shares in each such class that are traded during that year on established securities markets in any other single country. Our common stock, which is our sole class of issued and outstanding stock, is "primarily traded" on the Nasdaq Global Select Market.

Under the final regulations, our common stock will be considered to be "regularly traded" on an established securities market if one or more classes of our stock representing more than 50% of our outstanding shares, by total combined voting power of all classes of stock entitled to vote and total value, will be listed on the market, which we refer to as the listing threshold. Since our common stock is listed on the Nasdaq Global Select Market, we satisfy the listing requirement.

It is further required that with respect to each class of stock relied upon to meet the listing threshold (i) such class of stock is traded on the market, other than in minimal quantities, on at least 60 days during the taxable year or 1/6 of the days in a short taxable year; and (ii) the aggregate number of shares of such class of stock traded on such market during the taxable year is at least 10% of the average number of shares of such class of stock outstanding during such year or as appropriately adjusted in the case of a short taxable year. We believe we will satisfy the trading frequency and trading volume tests. Even if this were not the case, the final regulations provide that the trading frequency and trading volume lists will be deemed satisfied if, as we expect to be the case with our common stock, such class of stock is traded on an established market in the United States and such stock is regularly quoted by dealers making a market in such stock.

Notwithstanding the foregoing, the final regulations provide, in pertinent part, that a class of stock will not be considered to be "regularly traded" on an established securities market for any taxable year in which 50% or more of the issued and outstanding shares of such class of stock are owned, actually or constructively under specified stock attribution rules, on more than half the days during the taxable year by persons who each own 5% or more of the vote and value of such class of stock, which we refer to as the 5 Percent Override Rule.

For purposes of being able to determine the persons who own 5% or more of our stock, or the 5% Shareholders, the final regulations permit us to rely on those persons that are identified on Schedule 13G and Schedule 13D filings with the Commission as having a 5% or more beneficial interest in our common stock. The final regulations further provide that an investment company identified on a filing with the Commission on Schedule 13G or Schedule 13D which is registered under the Investment Company Act of 1940, as amended, will not be treated as a 5% Shareholder for such purposes.

We anticipate that our 5% Shareholders may own a majority of our common stock. If our 5% Shareholders own a majority of our common stock, then we will be subject to the 5% Override Rule unless we can establish that among the closely-held group of 5% Shareholders, there are sufficient 5% Shareholders that are qualified shareholders for purposes of Section 883 to preclude non-qualified shareholders in the closely-held group from owning 50% or more of our common stock for more than half the number of days during the taxable year. In order to establish this, sufficient

5% Shareholders that are qualified shareholders would have to comply with certain documentation and certification requirements designed to substantiate their identity as qualified shareholders.

We believe that we will be able to establish that a sufficient number of shares of our common stock are owned by qualified shareholders among our 5% Shareholders in order to qualify for the benefits of Section 883. However, there can be no assurance that we will be able to continue to satisfy the substantiation requirements in the future.

Taxation in the Absence of Exemption

To the extent the benefits of Section 883 are unavailable, our U.S.-source shipping income, to the extent not considered to be "effectively connected" with the conduct of a U.S. trade or business, as described below, would be subject to a 4% tax imposed by Section 887 of the Code on a gross basis, without the benefit of deductions. Since under the sourcing rules described above, no more than 50% of our shipping income would be treated as being derived from U.S. sources, the maximum effective rate of U.S. federal income tax on our shipping income would never exceed 2% under the 4% gross basis tax regime.

To the extent the benefits of the Section 883 exemption are unavailable and our U.S.-source shipping income is considered to be "effectively connected" with the conduct of a U.S. trade or business, as described below, any such "effectively connected" U.S.-source shipping income, net of applicable deductions, would be subject to the U.S. federal corporate income tax currently imposed at rates of up to 35%. In addition, we may be subject to the 30% "branch profits" taxes on earnings effectively connected with the conduct of such trade or business, as determined after allowance for certain adjustments, and on certain interest paid or deemed paid attributable to the conduct of its U.S. trade or business.

Our U.S.-source shipping income would be considered "effectively connected" with the conduct of a U.S. trade or business only if:

- we have, or are considered to have, a fixed place of business in the United States involved in the earning of shipping income; and

- substantially all of our U.S.-source shipping income is attributable to regularly scheduled transportation, such as the operation of a vessel that follows a published schedule with repeated sailings at regular intervals between the same points for voyages that begin or end in the United States.

We do not intend to have, or permit circumstances that would result in having any vessel operating to the United States on a regularly scheduled basis. Based on the foregoing and on the expected mode of our shipping operations and other activities, we believe that none of our U.S.-source shipping income will be "effectively connected" with the conduct of a U.S. trade or business.

U.S. Taxation of Gain on Sale of Vessels

If we and our subsidiaries qualify for exemption under Section 883 in respect of the shipping income derived from the international operation of our vessels, then gain from the sale of any such vessel should likewise be exempt from tax under Section 883. In the absence of the benefits of exemption under Section 883, we and our subsidiaries will not be subject to U.S. federal income taxation with respect to gain realized on a sale of a vessel, provided the sale is considered to occur outside of the United States under U.S. federal income tax principles. In general, a sale of a vessel will be considered to occur outside of the United States for this purpose if title to the vessel, and risk of loss with respect to the vessel, pass to the buyer outside of the United States. It is anticipated that any sale of a vessel by us will be considered to occur outside of the United States.

U.S. FEDERAL INCOME TAXATION OF U.S. HOLDERS

As used herein, the term "U.S. Holder" means a beneficial owner of common stock that is a U.S. citizen or resident, U.S. corporation or other U.S. entity taxable as a corporation, an estate the income of which is subject to U.S. federal income taxation regardless of its source, or a trust if a court within the United States is able to exercise primary

jurisdiction over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust.

If a partnership holds our common stock, the tax treatment of a partner will generally depend upon the status of the partner and upon the activities of the partnership. If you are a partner in a partnership holding our common stock, you are encouraged to consult your tax advisor.

Distributions

Subject to the discussion of passive foreign investment companies below, any distributions made by us with respect to our common stock to a U.S. Holder will generally constitute dividends, which may be taxable as ordinary income or "qualified dividend income" as described in more detail below, to the extent of our current or accumulated earnings and profits, as determined under U.S. federal income tax principles. Distributions in excess of our earnings and profits will be treated first as a nontaxable return of capital to the extent of the U.S. Holder's tax basis in his common stock on a dollar-for-dollar basis and thereafter as capital gain. Because we are not a U.S. corporation, U.S. Holders that are corporations will not be entitled to claim a dividends received deduction with respect to any distributions they receive from us. Dividends paid with respect to our common stock will generally be treated as '"passive category income" or, in the case of certain types of U.S. Holders, as "general category income" for purposes of computing allowable foreign tax credits for U.S. foreign tax credit purposes.

Dividends paid on our common stock to a U.S. Holder who is an individual, trust or estate (a "U.S. Individual Holder") should be treated as "qualified dividend income" that is taxable to such U.S. Individual Holders at preferential tax rates (through 2012) provided that: (1) our common stock is readily tradable on an established securities market in the United States (such as the Nasdaq Global Select Market on which our common stock is traded); (2) we are not a passive foreign investment company for the taxable year during which the dividend is paid or the immediately preceding taxable year (which we do not believe we are, have been or will be); and (3) the U.S. Individual Holder has owned the common stock for more than 60 days in the 121-day period beginning 60 days before the date on which the common stock becomes ex-dividend. Any dividends paid by the Company which are not eligible for these preferential rates will be taxed as ordinary income to a U.S. Individual Holder. Legislation has previously been introduced in the U.S. Congress, which would prevent our dividends from qualifying for these preferential rates prospectively from the date of enactment.

Special rules may apply to any "extraordinary dividend" — generally, a dividend equal to or in excess of ten percent of a shareholder's adjusted basis (or fair market value in certain circumstances) in a share of common stock — paid by us. If we pay an "extraordinary dividend" on our common stock that is treated as "qualified dividend income," then any loss derived by a U.S. Individual Holder from the sale or exchange of such common stock will be treated as long-term capital loss to the extent of such dividend. Depending upon the amount of a dividend paid by us, such dividend may be treated as an "extraordinary dividend."

Sale, Exchange or other Disposition of Common Stock

Assuming we do not constitute a passive foreign investment company for any taxable year, a U.S. Holder generally will recognize taxable gain or loss upon a sale, exchange or other disposition of our common stock in an amount equal to the difference between the amount realized by the U.S. Holder from such sale, exchange or other disposition and the U.S. Holder's tax basis in such stock. Subject to the discussion of extraordinary dividends above, such gain or loss will be treated as long-term capital gain or loss if the U.S. Holder's holding period is greater than one year at the time of the sale, exchange or other disposition. Such capital gain or loss will generally be treated as U.S.-source income or loss, as applicable, for U.S. foreign tax credit purposes. A U.S. Holder's ability to deduct capital losses is subject to certain limitations.

Passive Foreign Investment Company Status and Significant Tax Consequences

Special U.S. federal income tax rules apply to a U.S. Holder that holds stock in a foreign corporation classified as a passive foreign investment company for U.S. federal income tax purposes. In general, we will be treated as a passive foreign investment company with respect to a U.S. Holder if, for any taxable year in which such holder held our common stock, either:

- at least 75% of our gross income for such taxable year consists of passive income (e.g., dividends, interest, capital gains and rents derived other than in the active conduct of a rental business); or

- at least 50% of the average value of the assets held by the corporation during such taxable year produce, or are held for the production of, passive income.

For purposes of determining whether we are a passive foreign investment company, we will be treated as earning and owning our proportionate share of the income and assets, respectively, of any of our subsidiary corporations in which we own at least 25% of the value of the subsidiary's stock. Income earned, or deemed earned, by us in connection with the performance of services would not constitute passive income. By contrast, rental income would generally constitute "passive income" unless we were treated under specific rules as deriving our rental income in the active conduct of a trade or business.

Based on our current operations and future projections, we do not believe that we are, have been, nor do we expect to become, a passive foreign investment company with respect to any taxable year. Although there is no legal authority directly on point, our belief is based principally on the position that, for purposes of determining whether we are a passive foreign investment company, the gross income we derive or are deemed to derive from the period chartering and voyage chartering activities of our wholly-owned subsidiaries should constitute services income, rather than rental income. Correspondingly, such income should not constitute passive income and the assets that we and our wholly-owned subsidiaries own and operate in connection with the production of such income, in particular, the vessels, should not constitute passive assets for purposes of determining whether we are a passive foreign investment company. We believe there is substantial legal authority supporting our position consisting of case law and IRS pronouncements concerning the characterization of income derived from period charters and voyage charters as services income for other tax purposes. However, there is also authority which characterizes time charter income as rental income rather than services income for other tax purposes. It should be noted that in the absence of any legal authority specifically relating to the statutory provisions governing passive foreign investment companies, the IRS or a court could disagree with our position. In addition, although we intend to conduct our affairs in a manner to avoid being classified as a passive foreign investment company with respect to any taxable year, we cannot assure you that the nature of our operations will not change in the future.

As discussed more fully below, if we were to be treated as a passive foreign investment company for any taxable year, a U.S. Holder would be subject to different taxation rules depending on whether the U.S. Holder makes an election to treat us as a "Qualified Electing Fund," which election we refer to as a QEF election. As an alternative to making a QEF election, a U.S. Holder should be able to make a "mark-to-market" election with respect to our common stock, as discussed below. In addition, if we were to be treated as a passive foreign investment company for any taxable year after 2010, a U.S. Holder would be required to file an annual report with the Internal Revenue Service for that year with respect to such holder's common stock.

Taxation of U.S. Holders Making a Timely QEF Election

If a U.S. Holder makes a timely QEF election, which U.S. Holder we refer to as an "Electing Holder", the Electing Holder must report each year for U.S. federal income tax purposes his pro rata share of our ordinary earnings and our net capital gain, if any, for our taxable year that ends with or within the taxable year of the Electing Holder, regardless of whether or not distributions were received from us by the Electing Holder. The Electing Holder's adjusted tax basis in the common stock will be increased to reflect taxed but undistributed earnings and profits. Distributions of earnings and profits that had been previously taxed will result in a corresponding reduction in the adjusted tax basis in the common stock and will not be taxed again once distributed. An Electing Holder would generally recognize capital gain or loss on the sale, exchange or other disposition of our common stock. A U.S. Holder would make a QEF election with respect to any year that our company is a passive foreign investment company by filing one copy of IRS Form 8621 with his U.S. federal income tax return and a second copy in accordance with the instructions to such form. If we were aware that we were to be treated as a passive foreign investment company for any taxable year, we would provide each U.S. Holder with all necessary information in order to make the QEF election described above.

Taxation of U.S. Holders Making a "Mark-to-Market" Election

Alternatively, if we were to be treated as a passive foreign investment company for any taxable year and, as we anticipate, our stock is treated as "marketable stock," a U.S. Holder would be allowed to make a "mark-to-market" election with respect to our common stock, provided the U.S. Holder completes and files IRS Form 8621 in accordance with the relevant instructions and related Treasury Regulations. If that election is made, the U.S. Holder generally would include as ordinary income in each taxable year the excess, if any, of the fair market value of the common stock at the end of the taxable year over such holder's adjusted tax basis in the common stock. The U.S. Holder would also be permitted an ordinary loss in respect of the excess, if any, of the U.S. Holder's adjusted tax basis in the common stock over its fair market value at the end of the taxable year, but only to the extent of the net amount previously included in income as a result of the mark-to-market election. A U.S. Holder's tax basis in his common stock would be adjusted to reflect any such income or loss amount. Gain realized on the sale, exchange or other disposition of our common stock would be treated as ordinary income and any loss realized on the sale, exchange or other disposition of the common stock would be treated as ordinary loss to the extent that such loss does not exceed the net mark-to-market gains previously included in income by the U.S. Holder.

Taxation of U.S. Holders Not Making a Timely QEF or Mark-to-Market Election

Finally, if we were to be treated as a passive foreign investment company for any taxable year, a U.S. Holder who does not make either a QEF election or a "mark-to-market" election for that year, to whom we refer as a Non-Electing Holder, would be subject to special rules with respect to (1) any excess distribution (i.e., the portion of any distributions received by the Non-Electing Holder on our common stock in a taxable year in excess of 125% of the average annual distributions received by the Non-Electing Holder in the three preceding taxable years, or, if shorter, the Non-Electing Holder's holding period for the common stock) and (2) any gain realized on the sale, exchange or other disposition of our common stock. Under these special rules:

- the excess distribution or gain would be allocated ratably over the Non-Electing Holders' aggregate holding period for the common stock;
- the amount allocated to the current taxable year would be taxed as ordinary income; and
- the amount allocated to each of the other taxable years would be subject to tax at the highest rate of tax in effect for the applicable class of taxpayer for that year and an interest charge for the deemed deferral benefit would be imposed with respect to the resulting tax attributable to each such other taxable year.

These penalties would not apply to a pension or profit sharing trust or other tax-exempt organization that did not borrow funds or otherwise utilize leverage in connection with its acquisition of our common stock. If a Non-Electing Holder who is an individual dies while owning our common stock, such holder's successor generally would not receive a step-up in tax basis with respect to such stock.

U.S. FEDERAL INCOME TAXATION OF "NON-U.S. HOLDERS"

A beneficial owner of common stock that is not a U.S. Holder is referred to herein as a Non-U.S. Holder.

Dividends on Common Stock

Non-U.S. Holders generally will not be subject to U.S. federal income tax or withholding tax on dividends received from us with respect to our common stock, unless that income is effectively connected with the Non-U.S. Holder's conduct of a trade or business in the United States. If the Non-U.S. Holder is entitled to the benefits of a U.S. income tax treaty with respect to those dividends, that income is generally taxable only if it is attributable to a permanent establishment maintained by the Non-U.S. Holder in the United States.

Sale, Exchange or Other Disposition of Common Stock

Non-U.S. Holders generally will not be subject to U.S. federal income tax or withholding tax on any gain realized upon the sale, exchange or other disposition of our common stock, unless:

- the gain is effectively connected with the Non-U.S. Holder's conduct of a trade or business in the United States. If the Non-U.S. Holder is entitled to the benefits of an income tax treaty with respect to that gain, that gain is generally taxable only if it is attributable to a permanent establishment maintained by the Non-U.S. Holder in the United States; or
- the Non-U.S. Holder is an individual who is present in the United States for 183 days or more during the taxable year of disposition and other conditions are met.

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If the Non-U.S. Holder is engaged in a U.S. trade or business for U.S. federal income tax purposes, the income from the common stock, including dividends and the gain from the sale, exchange or other disposition of the stock that is effectively connected with the conduct of that trade or business will generally be subject to regular U.S. federal income tax in the same manner as discussed in the previous section relating to the taxation of U.S. Holders. In addition, in the case of a corporate Non-U.S. Holder, its earnings and profits that are attributable to the effectively connected income, which are subject to certain adjustments, may be subject to an additional branch profits tax at a rate of 30%, or at a lower rate as may be specified by an applicable income tax treaty.

Backup Withholding and Information Reporting

In general, dividend payments, or other taxable distributions, made within the United States to a non-corporate U.S. Holder will be subject to information reporting requirements. Such payments will also be subject to backup withholding tax if a non-corporate U.S. Holder:

- fails to provide an accurate taxpayer identification number;
- is notified by the IRS that it has failed to report all interest or dividends required to be shown on its federal income tax returns; or
- in certain circumstances, fails to comply with applicable certification requirements.

Non-U.S. Holders may be required to establish their exemption from information reporting and backup withholding by certifying their status on IRS Form W-8BEN, W-8ECI or W-8IMY, as applicable.

If a Non-U.S. Holder sells its common stock to or through a U.S. office or broker, the payment of the proceeds is subject to both U.S. backup withholding and information reporting unless such holder certifies that it is a non-U.S. person, under penalties of perjury, or otherwise establishes an exemption. If a Non-U.S. Holder sells its common stock through a non-U.S. office of a non-U.S. broker and the sales proceeds are paid to such holder outside the United States then information reporting and backup withholding generally will not apply to that payment. However, U.S. information reporting requirements, but not backup withholding, will apply to a payment of sales proceeds, even if that payment is made to a Non-U.S. Holder outside the United States, if such holder sells its common stock through a non-U.S. office of a broker that is a U.S. person or has some other contacts with the United States.

Backup withholding tax is not an additional tax. Rather, a holder generally may obtain a refund of any amounts withheld under backup withholding rules that exceed its income tax liability by filing a refund claim with the IRS.

Pursuant to recently enacted legislation, individuals who are U.S. Holders (and to the extent specified in applicable Treasury regulations, certain individuals who are Non-U.S. Holders and certain U.S. entities) who hold "specified foreign financial assets" (as defined in Section 6038D of the Code) are required to file IRS Form 8938 with information relating to the asset for each taxable year in which the aggregate value of all such assets exceeds $75,000 at any time during the taxable year or $50,000 on the last day of the taxable year (or such higher dollar amount as prescribed by applicable Treasury regulations). Specified foreign financial assets would include, among other assets, our common shares, unless the shares held through an account maintained with a U.S. financial institution. Substantial penalties apply to any failure to timely file IRS Form 8938, unless the failure is shown to be due to reasonable cause and not due to willful neglect. Additionally, in the event an individual U.S. Holder (and to the extent specified in applicable Treasury regulations, an individual Non-U.S. Holder or a U.S. entity) that is required to file IRS Form 8938 does not file such form, the statute of limitations on the assessment and collection of U.S. federal income taxes of such holder for the related tax year may not close until three years after the date that the required information is filed. U.S. Holders (including U.S. entities) and Non-U.S. Holders are encouraged consult their own tax advisors regarding their

reporting obligations under this legislation.

F. DIVIDEND AND PAYING AGENTS

Not Applicable.

G. STATEMENTS BY EXPERTS

Not Applicable.

H. DOCUMENTS ON DISPLAY

The Company is subject to the informational requirements of the Securities and Exchange Act of 1934, as amended. In accordance with these requirements we file reports and other information with the Securities and Exchange Commission. These materials, including this annual report and the accompanying exhibits may be inspected and copied at the public reference facilities maintained by the Commission at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. You may obtain information on the operation of the public reference room by calling 1 (800) SEC-0330 and you may obtain copies at prescribed rates from the Public Reference Section of the Commission at its principal office in Washington, D.C. 20549. The SEC maintains a website (http://www.sec.gov.) that contains reports, proxy and information statements and other information regarding registrants that file electronically with the SEC. In addition, documents referred to in this annual report may be inspected at the Company's headquarters at Ocean Centre, Montague Foreshore East Bay Street, Nassau, Bahamas.

I. SUBSIDIARY INFORMATION

Not Applicable.

ITEM 11 – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See "Item 5 — Operating and Financial Review and Prospects — Quantitative and Qualitative Disclosures About Market Risk."

ITEM 12 – DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not Applicable.

PART II

ITEM 13 – DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None.

ITEM 14 – MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

None.

ITEM 15 – CONTROLS AND PROCEDURES

(a) Disclosure Controls and Procedures

Management assessed the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Rule 13a-15(e) of the Exchange Act, as of the end of the period covered by this annual report (as of December 31, 2011). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective as of the evaluation date.

(b) Management's Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) promulgated under the Exchange Act.

Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. The Company's system of internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements. Management has performed an assessment of the effectiveness of the Company's internal controls over financial reporting as of December 31, 2011, based on the provisions of Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, or COSO. Based on its assessment, management, including the Company's chief executive and chief financial officer, determined that the Company's internal controls over financial reporting were effective as of December 31, 2011, based on the criteria in Internal Control—Integrated Framework issued by COSO.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree or compliance with the policies or procedures may deteriorate.

Pistrelli, Henry Martin y Asociados S.R.L., members of Ernst & Young Global, the Company's independent registered public accounting firm, who audited the financial statements included in the Annual Report, has audited and reported on the effectiveness of the Company's internal controls over financial reporting as of December 31, 2011, as

stated in their report which appears elsewhere in this Annual Report.

(c) Attestation Report of Independent Registered Public Accounting Firm

The Attestation Report appears under Item 18 and is incorporated herein by reference.

(d) Changes in Internal Control over Financial Reporting

There have been no changes in internal control over financial reporting that occurred during the year covered by this annual report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 16A – AUDIT COMMITTEE FINANCIAL EXPERT

We have established an audit committee composed of one board member that is responsible for reviewing our accounting controls and recommending to the board of directors the engagement of our outside auditors. The sole member of the audit committee, Mr. George Wood, is an independent director and the audit committee financial expert.

ITEM 16B – CODE OF ETHICS

The Company has adopted a code of ethics applicable to the Company's principal executive officer and principal financial officer, principal accounting officer or controller, which complies with the definition of a "code of ethics", set out in Section 406(c) of the Sarbanes-Oxley Act of 2002.

We will provide to any person without charge, upon request, a copy of the code of ethics. Written requests for such copies must be sent to the Company Secretary at our principal executive offices at Ultrapetrol (Bahamas) Limited, c/o H&J Corporate Services Ltd., Ocean Center, Montagu Foreshore, East Bay Street, Nassau, Bahamas, P.O. Box SS-19084.

ITEM 16C – PRINCIPAL ACCOUNTANT FEES AND SERVICES

Pistrelli, Henry Martin y Asociados S.R.L. member of Ernst & Young Global is the independent registered public accounting firm that audits the financial statements of the Company and its subsidiaries.

Aggregate fee for professional services rendered for the Company by Pistrelli, Henry Martin y Asociados S.R.L. and other member firms of Ernst & Young Global in 2010 and 2011 in each of the following categories were:

	Year ended December 31,	
	2011	2010
	(in thousands of U.S. dollars)	
Audit fees	1,099	1,263
Audit-related fees	--	--
Tax fees	190	142
All other fees	--	--
Total fees	1,289	1,405

Audit fees include fees associated with the annual audit of the Company and subsidiaries, statutory audits of subsidiaries required internationally, comfort letters and SEC filings in connection with our public offerings of our common stock.

Tax fees relate to tax compliance and tax advice.

Prior to our initial public offering, all audit, audit-related and non audit services provided by our independent auditor were pre-approved by the board of directors. Since our initial public offering, all such services are pre-approved by our audit committee, which was formed at the time of our initial public offering.

ITEM 16D – EXEMPTIONS FROM LISTING STANDARDS FOR AUDIT COMMITTEES.

Not Applicable.

ITEM 16E – PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PERSONS.

No such purchases were made in the period covered by this report.

ITEM 16F – CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANT

None.

ITEM 16G – CORPORATE GOVERNANCE

As a foreign private issuer, as defined in Rule 3b-4 under the Exchange Act, the Company is permitted to follow certain corporate governance rules of its home country, the Bahamas, in lieu of NASDAQ's corporate governance rules, or the NASDAQ Rules. The Company complies fully with the NASDAQ Rules, except that the Company's corporate governance practices deviate from the NASDAQ Rules in the following ways:

- The Company does not have a board of directors with a majority of independent directors. However, the Company does have two independent directors.
- In lieu of holding regular meetings at which only independent directors are present, the Company's entire board of directors may hold regular meetings.
- In lieu of an audit committee comprising three independent directors, the Company's audit committee has one member, who meets the NASDAQ requirement of a financial expert.
- In lieu of a nomination committee comprising independent directors, the Company's board of directors will be responsible for identifying and recommending potential candidates to become board members and recommending directors for appointment to board committees. Shareholders may also identify and recommend potential candidates to become board members in writing. No formal written charter has been prepared or adopted because this process is outlined in the Company's memorandum of association.
- In lieu of a compensation committee comprising independent directors, our board of directors will be responsible for establishing the executive officers' compensation and benefits. Under Bahamian law, compensation of the executive officers is not required to be determined by an independent committee.
- In lieu of obtaining an independent review of related party transactions for conflicts of interests, the Company's memorandum of association provides that related party transactions must be approved by disinterested directors and in certain circumstances, supported by a fairness opinion.
- Pursuant to the Company's articles of association, the Company is required to obtain shareholder approval in order to issue additional securities.
-

As a foreign private issuer, the Company is not required to solicit proxies or provide proxy statements to NASDAQ pursuant to NASDAQ corporate governance rules or Bahamian law.

ITEM 16H – MINE SAFETY DISCLOSURE

Not Applicable.

PART III

ITEM 17 – FINANCIAL STATEMENTS

Not Applicable.

ITEM 18 – FINANCIAL STATEMENTS

The following financial statements listed below and set forth on pages F-1 through F-53, together with the report of independent registered public accounting firm are filed as part of this annual report:

ULTRAPETROL (BAHAMAS) LIMITED AND
SUBSIDIARIES

Consolidated Financial Statements for the years
ended December 31, 2011, 2010 and 2009
with Reports of Independent Registered Public Accounting
Firm

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES

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ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS AT DECEMBER 31, 2011 AND 2010
(Stated in thousands of U.S. dollars, except par value and share amounts)

	At December 31,	
	2011	2010
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$34,096	$105,570
Restricted cash	6,819	1,661
Accounts receivable, net of allowance for doubtful accounts of $841 and $555 in 2011 and 2010, respectively	30,993	24,675
Operating supplies	4,520	3,176
Prepaid expenses	3,212	3,643
Other receivables	26,392	24,153
Other current assets	101	117
Total current assets	106,133	162,995
NONCURRENT ASSETS		
Other receivables	15,370	5,796
Restricted cash	1,483	1,183
Vessels and equipment, net	671,445	612,696
Dry dock	5,088	5,688
Investments in and receivables from affiliates	6,851	6,824
Intangible assets	976	1,151
Goodwill	5,015	5,015
Other assets	12,573	13,145
Deferred income tax assets	5,353	9,304
Total noncurrent assets	724,154	660,802
Total assets	$830,287	$823,797
LIABILITIES AND EQUITY		
CURRENT LIABILITIES		
Accounts payable	$33,990	$24,054
Accrued interest	4,769	2,278
Current portion of long-term financial debt	21,504	27,586
Other current liabilities	13,625	10,759
Total current liabilities	73,888	64,677
NONCURRENT LIABILITIES		
Long-term financial debt	491,489	471,793
Deferred income tax liabilities	12,951	16,142
Other liabilities	1,788	2,391
Total noncurrent liabilities	506,228	490,326
Total liabilities	580,116	555,003
EQUITY		

Common stock, $0.01 par value: 100,000,000 authorized shares; 30,011,628 and 29,943,653 shares outstanding in 2011 and 2010, respectively	339	338
Additional paid-in capital	272,302	271,224
Treasury stock: 3,923,094 shares at cost	(19,488)	(19,488)
Retained earnings (deficit)	(6,819)	11,986
Accumulated other comprehensive income (loss)	(2,037)	(597)
Total Ultrapetrol (Bahamas) Limited stockholders' equity	244,297	263,463
Noncontrolling interest	5,874	5,331
Total equity	250,171	268,794
Total liabilities and equity	$830,287	$823,797

The accompanying notes are an integral part of these consolidated financial statements and should be read in conjunction herewith.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009
(Stated in thousands of U.S. dollars, except share and per share data)

	For the years ended December 31,		
	2011	2010	2009
REVENUES	$ 304,482	$ 230,445	$ 220,529
OPERATING EXPENSES (1)			
Voyage and manufacturing expenses	(112,252)	(61,583)	(60,575)
Running costs	(112,355)	(89,339)	(80,032)
Depreciation and amortization	(39,144)	(34,371)	(41,752)
Administrative and commercial expenses	(29,604)	(27,051)	(25,065)
Loss on write-down of vessels	-	-	(25,000)
Other operating income, net	8,257	617	2,844
	(285,098)	(211,727)	(229,580)
Operating profit (loss)	19,384	18,718	(9,051)
OTHER INCOME (EXPENSES)			
Financial expense	(35,426)	(25,925)	(24,248)
Foreign currency (losses) gains, net	(2,552)	(492)	1,011
Financial income	332	399	340
(Loss) gains on derivatives, net	(16)	10,474	241
Investments in affiliates	(1,073)	(341)	(28)
Other, net	(621)	(875)	(707)
Total other income (expenses)	(39,356)	(16,760)	(23,391)
(Loss) Income from continuing operations before income taxes	(19,972)	1,958	(32,442)
Income taxes benefit (expense)	1,737	(6,363)	(5,355)
(Loss) from continuing operations	(18,235)	(4,405)	(37,797)
(Loss) from discontinued operations	-	(515)	(2,131)
Net (loss)	(18,235)	(4,920)	(39,928)
Net income (loss) attributable to noncontrolling interest	570	451	(90)
Net (loss) attributable to Ultrapetrol (Bahamas) Limited	$ (18,805)	$ (5,371)	$ (39,838)
Amounts attributable to Ultrapetrol (Bahamas) Limited:			
(Loss) from continuing operations	$ (18,805)	$ (4,856)	$ (37,707)
(Loss) from discontinued operations	-	(515)	(2,131)
Net (loss) attributable to Ultrapetrol (Bahamas) Limited	$ (18,805)	$ (5,371)	$ (39,838)
(LOSS) PER SHARE OF ULTRAPETROL (BAHAMAS) LIMITED - BASIC AND DILUTED:			
From continuing operations	$ (0.64)	$ (0.16)	$ (1.28)

From discontinued operations	-	(0.02)	(0.07)
	$ (0.64)	$ (0.18)	$ (1.35)
Basic and diluted weighted average number of shares	29,547,365	29,525,025	29,426,429

(1) Operating expenses included $4,622, $1,542 and $619 in 2011, 2010 and 2009, respectively, from related parties.

The accompanying notes are an integral part of these consolidated financial statements and should be read in conjunction herewith.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009
(Stated in thousands of U.S. dollars, except share data)

	Ultrapetrol (Bahamas) Limited stockholders' equity							
Balance	Shares amount	Common stock	Additional paid-in capital	Treasury stock	Retained earnings (deficit)	Accumulated other comprehensive income (loss)	Noncontrolling interest	Total equity
December 31, 2008	29,519,936	$ 334	$ 268,425	$ (19,488)	$ 57,195	$ 65,423	$ 4,970	$ 376,859
Compensation related to options and restricted stock granted	423,717	4	1,533	-	-	-	-	1,537
Comprehensive loss:								
Net loss	-	-	-	-	(39,838)	-	(90)	(39,928)
Effect of derivative financial instruments	-	-	-	-	-	(49,885)	-	(49,885)
Total comprehensive loss								(89,813)
December 31, 2009	29,943,653	338	269,958	(19,488)	17,357	15,538	4,880	288,583
Compensation related to restricted stock granted	-	-	1,266	-	-	-	-	1,266
Comprehensive loss:								
Net loss	-	-	-	-	(5,371)	-	451	(4,920)
Effect of derivative financial instruments	-	-	-	-	-	(16,135)	-	(16,135)
Total comprehensive loss								(21,055)
December 31, 2010	29,943,653	338	271,224	(19,488)	11,986	(597)	5,331	268,794

Compensation related to restricted stock granted	67,975	1	1,078	-	-	-	-	1,079
Comprehensive loss:								
Net loss	-	-	-	-	(18,805)	-	570	(18,235)
Effect of derivative financial instruments	-	-	-	-	-	(1,440)	(27)	(1,467)
Total comprehensive loss								(19,702)
December 31, 2011	30,011,628	$ 339	$ 272,302	$ (19,488)	$ (6,819)	$ (2,037)	$ 5,874	$ 250,171

The accompanying notes are an integral part of these consolidated financial statements and should be read in conjunction herewith.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009
(Stated in thousands of U.S. dollars)

	For the years ended December 31,		
	2011	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES			
Net (loss)	$(18,235)	$(4,920)	$(39,928)
Adjustments to reconcile net (loss) to total cash flows provided by operating activities:			
Loss from discontinued operations	-	515	2,131
Depreciation of vessels and equipment	34,891	29,880	37,609
Amortization of dry docking	4,078	4,186	3,425
Expenditure for dry docking	(3,478)	(8,204)	(5,242)
(Loss) gains on derivatives, net	16	(10,474)	(241)
Debt issuance expense amortization	2,323	1,340	1,026
Amortization of intangible assets	175	305	718
(Gain) on sale of vessels	-	(724)	(1,415)
Net losses from investments in affiliates	1,073	341	28
Allowance for doubtful accounts	598	359	(21)
Loss on write-down of vessels	-	-	25,000
Share - based compensation	1,079	1,266	1,537
Changes in assets and liabilities:			
(Increase) decrease in assets:			
Accounts receivable	(6,916)	(8,632)	1,401
Other receivables, operating supplies and prepaid expenses	(12,302)	(2,827)	7,940
Other	(2,261)	1,369	2,170
Increase (decrease) in liabilities:			
Accounts payable	10,324	10,661	(7,609)
Other payables	3,407	6,403	9,055
Other	-	-	1,095
Net cash provided by operating activities from continuing operations	14,772	20,844	38,679
Net cash (used in) provided by operating activities from discontinued operations	(15)	(1,950)	37
Total cash flows provided by operating activities	14,757	18,894	38,716
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of vessels and equipment	(97,863)	(105,247)	(90,095)
Proceeds from disposals of vessels, net	-	36,584	9,840
Other investing activities, net	-	12,574	(3,343)
Net cash (used in) investing activities from continuing operations	(97,863)	(56,089)	(83,598)
Net cash provided by investing activities from discontinued operations	-	1,950	-
Total cash flows used in investing activities	(97,863)	(54,139)	(83,598)
CASH FLOWS FROM FINANCING ACTIVITIES			
Scheduled repayments of long-term financial debt	(13,286)	(11,292)	(13,594)
Early repayment of long-term financial debt	-	-	(22,894)

Revolving credit facility borrowings	10,500	-	-
Revolving credit facility repayments	(25,500)	-	-
Proceeds from issuance of 7.25% Senior Convertible Notes, net of issuance costs	-	76,095	-
Proceeds from long-term financial debt	41,900	25,000	29,079
Other financing activities, net	(1,982)	(2,189)	(367)
Net cash provided by (used in) financing activities from continuing operations	11,632	87,614	(7,776)
Net (decrease) increase in cash and cash equivalents	(71,474)	52,369	(52,658)
Cash and cash equivalents at the beginning of year (including $304, $304 and $2,546 related to discontinued operations)	105,570	53,201	105,859
Cash and cash equivalents at the end of year (including $289, $304 and $304 related to discontinued operations)	$34,096	$105,570	$53,201

The accompanying notes are an integral part of these consolidated financial statements and should be read in conjunction herewith.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. NATURE OF OPERATIONS AND CORPORATE ORGANIZATION

Nature of operations

Ultrapetrol (Bahamas) Limited ("Ultrapetrol Bahamas", "Ultrapetrol", "the Company", "us" or "we") is a company organized and registered as a Bahamas Corporation since December 1997.

We are a shipping transportation company serving the marine transportation needs of our clients in the markets on which we focus. We serve the shipping markets for containers, grain soybean, forest products, minerals, crude oil, petroleum, and refined petroleum products, as well as the offshore oil platform supply market, through our operations in the following three segments of the marine transportation industry. In our River Business we are an owner and operator of river barges and push boats in the Hidrovia region of South America, a region of navigable waters on the Parana, Paraguay and Uruguay Rivers and part of the River Plate, which flow through Brazil, Bolivia, Uruguay, Paraguay and Argentina. The Company also has a shipyard that should promote organic growth and from time to time made external sales. In our Offshore Supply Business we own and operate vessels that provide logistical and transportation services for offshore petroleum exploration and production companies, in the coastal waters of Brazil and the North Sea. In our Ocean Business, we are an owner and operator of oceangoing vessels that transport petroleum products and a container line service in the Argentine cabotage trade.

2. SIGNIFICANT ACCOUNTING POLICIES

a) Basis of presentation and principles of consolidation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

The consolidated financial statements include the accounts of the Company and its subsidiaries, both majority and wholly owned. Significant intercompany accounts and transactions have been eliminated in this consolidation. Investments in 50% or less owned affiliates, in which the Company exercises significant influence, are accounted for by the equity method.

b) Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the years. Significant estimates have been made by management, including the allowance for doubtful accounts, insurance claims receivable, useful lives and valuation of vessels, hedge accounting, recoverability of tangible and intangible assets and certain accrued liabilities. Actual results may differ from those estimates.

c) Revenues and related expenses

Revenue is recorded when services are rendered, the Company has a signed charter agreement or other evidence of an arrangement, prices are fixed or determinable and collection is reasonably assured.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The primary source of the Company's revenue, freight transportation by river barges, ocean-going vessels or PSVs, is recognized based on time charters, bareboat charters, consecutive voyage charters or affreightment / voyage contracts.

Revenue from time charters and bareboat charters is earned and recognized on a daily basis. Revenue from affreightment / voyage contracts and consecutive voyage charters is recognized based upon the percentage of voyage completion. In our River Business, a voyage is deemed to commence upon the departure of the discharged barge of the previous voyage and is deemed to end upon the completion of discharge of the current voyage. The percentage of voyage completion is based on the miles transited at the balance sheet date divided by the total miles expected for the voyage. The position of the barge at the balance sheet date is determined by locating the position of the pushboat with the barge in tow through the use of a global positioning system ("GPS").

The Company does not begin recognizing revenue if the charter agreement has not been entered into with the customer, even if the vessel has discharged its cargo and is sailing to the anticipated load port on its next voyage.

Demurrage income represents charges made to the charterer when loading or discharging time exceeds the stipulated time in the voyage charter and is recognized as it is earned.

The recognition of revenue due to shortfalls on take or pay contracts occurs at the end of each declaration period. A declaration period is defined as the time period in which the contract volume obligation was to be met. If the volume was not met during that time period, then the amount of billable revenue resulting from the failure to perform will be calculated and recognized as it is billed.

Vessel voyage costs, primarily consisting of port, canal and bunker expenses that are unique to a particular charter, are paid for by the charterer under time charter arrangements or by the Company under voyage charter arrangements. The commissions paid in advance are deferred and amortized over the related voyage charter period to the extent commissions are earned as the Company's revenues are earned. Bunker expenses are capitalized when acquired as operating supplies and subsequently charged to voyage expenses as consumed. All other voyage expenses and other vessel operating expenses are expensed as incurred.

From time to time we provide ship salvage services under Lloyd's Standard Form of Salvage Agreement ("LOF"). The Company recognizes costs as incurred on these LOF services. Revenue is recorded at the time the LOF settlement or arbitration award occurs. In those cases where a minimum salvage remuneration is guaranteed or determined by contract then such minimum amount is recognized in revenue when services are rendered.

In its River Business the Company uses the completed contract method for river barges built which typically have construction periods of 30 days or less. Contracts are considered complete when title has passed, the customer has accepted the river barges and the Company does not retain risks or rewards of ownership of the river barges. Losses are accrued if manufacturing costs are expected to exceed manufacturing contract revenue.

Manufacturing expenses, primarily consisting of steel cost; which is the largest component of our raw materials and the cost of labor.

The Company accounts for multiple element arrangements, in accordance with ASC 605-25. For such transactions, revenue on arrangements that include multiple elements is allocated to each element based on the relative fair value of each element, and fair value is determined by vendor-specific objective evidence of fair value (VSOE).

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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d) Foreign currency translation

The Company uses the US dollar as its functional currency. Receivables and payables denominated in foreign currencies are translated into US dollars at the rate of exchange at the balance sheet date, while revenues and expenses are translated using the average exchange rate for each month. Certain subsidiaries enter into transactions denominated in currencies other than their functional currency. Changes in currency exchange rates between the functional currency and the currency in which a transaction is denominated are included in the consolidated statements of operations in the period in which the currency exchange rate changes.

e) Cash and cash equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. Cash equivalents consist of money market instruments and interest-bearing deposits. The credit risk associated with cash and cash equivalents is considered to be low due to the high credit quality of the financial institutions with which the Company operates.

f) Restricted cash

Certain of the Company's loan agreements require the Company to fund: (a) a loan retention account equivalent to the next loan installment (depending on the frequency of the repayment elected by the Company, i.e. quarterly or semi annually) plus interest which is used to fund the loan installments coming due, (b) a drydocking account which is restricted for use and can only be used for the purpose of paying for drydocking or special survey expenses and (c) cash deposits required as collateral with certain banks under the Company's borrowing arrangements.

g) Accounts receivable

Substantially all of the Company's accounts receivable are due from international oil companies, international grainhouses and traders. The Company performs ongoing credit evaluations of its trade customers and generally does not require collateral. Expected credit losses are provided for in the consolidated financial statements for all expected uncollectible accounts.

Accounts receivable from one customer of Ultrapetrol Ocean and Offshore Supply Business accounted for 24% and one customer of Ultrapetrol River Business accounted for 17% of total consolidated accounts receivable as of December 31, 2011.

Accounts receivable from one customer of Ultrapetrol Ocean and Offshore Supply Business accounted for 28% and one customer of Ultrapetrol River Business accounted for 14% of total consolidated accounts receivable as of December 31, 2010.

Changes in the allowance for doubtful accounts for the three years ended December 31, 2011, were as follow:

	For the years ended December 31,		
	2011	2010	2009
Balance at January 1	$555	$411	$432
Provision	598	377	443

Recovery	-	(18)	(464)
Amounts written off (1)	(312)	(215)	-
Balance at December 31	$841	$555	$411

(1) Accounts charged to the allowance when collection efforts cease.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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h) Concentrations of credit risk

The Company is exposed to concentrations of credit risk associated with its cash and cash equivalents, restricted cash and derivative instruments. The Company minimizes its credit risk relating to these positions by monitoring the financial condition of the financial institutions and counterparties involved and by primarily conducting business with large, well-established financial institutions and diversifying its counterparties. The Company does not currently anticipate nonperformance by any of its significant counterparties. The Company is also exposed to concentrations of credit risk relating to its receivables due from customers in the industries in which operates. The Company does not generally require collateral or other security to support its outstanding receivables. The Company minimizes its credit risk relating to receivables by performing ongoing credit evaluations and, to date, credit losses have not been material.

i) Insurance claims receivable

Insurance claims receivable comprise claims submitted relating to hull and machinery (H&M), protection and indemnity (P&I), loss of hire (LOH) and strike insurance coverage. They are recorded when the recovery of an insurance claim is probable. Deductible amounts related to covered incidents are expensed in the period of occurrence of the incident. The credit risk associated with insurance claims receivable is considered low due to the high credit quality and funded status of the insurance underwriters and P&I clubs in which the Company is either a client or a member. Insurance claims receivable, included in other receivables in the accompanying balance sheets, amounts to $4,531 and $1,881 at December 31, 2011 and 2010, respectively.

j) Operating supplies

Such amounts consist principally of fuel and supplies that are recorded at the lower of cost or market and are charged to operating expenses as consumed determined on a first-in, first-out basis.

k) Vessels and equipment, net

Vessels and equipment are stated at cost less accumulated depreciation. This cost includes the purchase price and all directly attributable costs (initial repairs, improvements and delivery expenses, interest and on-site supervision costs incurred during the construction periods). Subsequent expenditures for conversions renewals or major improvements are also capitalized when they appreciably extend the life, increase the earning capacity or improve the safety of the vessels.

New barges built for the River Business segment in our own shipyard in Punta Alvear, Argentina are capitalized at cost.

Depreciation is computed net of the estimated scrap value which is equal to the product of each vessel's lightweight tonnage and estimated scrap value per lightweight ton and is recorded using the straight-line method over the estimated useful lives of the vessels. Acquired secondhand vessels are depreciated from the date of their acquisition over the remaining estimated useful life.

From time to time, the Company acquires vessels which have already exceeded the Company's useful life policy, in which case the Company depreciates such vessels based on its best estimate of such vessel's remaining useful life, typically until the next survey or certification date.

Improvements to leased property are amortized over the shorter of their economic life or the respective lease term.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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The estimated useful life of each of the Company's major categories of assets is as follows:

	Useful life (in years)
Ocean-going vessels	24 to 27
PSVs	24
River barges and push boats	35
Buildings	20 to 30
Furniture and equipment	5 to 15

However, when regulations place limitations over the ability of a vessel to trade, its useful life is adjusted to end at the date such regulations become effective. Currently, these regulations do not affect any of our vessels.

At the time vessels are disposed of, the assets and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recorded in other operating income.

Long-lived assets are reviewed for impairment, whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the sum of the expected future undiscounted cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and carrying value of the asset. The amount of an impairment charge, if any, would be determined using discounted cash flows expected to result from the use of the asset and its eventual disposition.

Given the overriding effects of the global economic slowdown, demand for the dry-bulk Ocean Business vessels was soft during 2009. Accordingly, the Company based upon the information that was known to it as of December 31, 2009 recorded an impairment charge of $25,000 to write down the carrying amount of its Capesize Princess Marisol to its estimated fair value as of December 31, 2009.

l) Dry dock costs

The Company's vessels must be periodically drydocked and pass inspections to maintain their operating classification, as mandated by maritime regulations. Costs incurred to drydock a vessel / pushboat are deferred and amortized using the straight-line method over the period to the next drydock, generally 24 to 36 months. Drydocking costs incurred are comprised of: painting the vessel's hull and sides, recoating cargo and fuel tanks, and performing other engine and equipment maintenance activities to bring the vessel into compliance with classification standards. The unamortized portion of dry dock costs for vessels that are sold are written off and included in the calculation of the resulting gain or loss in the year of the vessel's sale.

Expenditures for maintenance and minor repairs are expensed as incurred.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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m) Investments in affiliates

These investments are accounted for by the equity method. At December 31, 2011 and 2010 and for each of the three years in the period ended December 31, 2011, this includes our interest in 50% of Puertos del Sur S.A. and Obras Terminales y Servicios S.A. ("OTS S.A.") and in 49% of Marítima Sipsa S.A.

n) Identifiable intangible assets

The Company's intangible assets arose as a result of the Ravenscroft acquisition in 2006, and consist principally of a safety management system which is being amortized over its useful life of eight years using the straight-line method.

Accumulated amortization at December 31, 2011 and 2010 amounted to $1,006 and $831, respectively and amortization for the three years ended December 31, 2011 amounted to $175, $305 and $718, respectively. Amortization of intangible assets for the five years subsequent to December 31, 2011 is expected to be $175 in each of 2012 and 2013 and $44 in 2014.

o) Goodwill

Goodwill is recorded when the purchase price paid for an acquisition exceeds the estimated fair value of net identified tangible and intangible assets acquired. The Company performs an annual impairment test of goodwill and further periodic tests to the extent indicators of impairment develop between annual impairment tests. The Company's impairment review process compares the fair value of the reporting unit to its carrying value, including the goodwill related to the reporting unit. To determine the fair value of the reporting unit, the Company uses a discounted future cash flow ("DCF") approach that uses estimates for revenue, costs and appropriate discount rates, among others. These various estimates are reviewed each time the Company tests goodwill for impairment and many are developed as part of the Company's routine business planning and forecasting process. The Company believes its estimates and assumptions are reasonable; however, variations from those estimates could produce materially different results.

p) Other assets

This account corresponds to costs incurred to issue debt net of amortization costs, which are being amortized over the term of the debt using the effective interest rate method. Amortization for debt issuance expense for the three years ended December 31, 2011 totaled $2,323, $1,340 and $1,026, respectively, and is included in financial expense in the accompanying consolidated statements of operations.

q) Accounts payable

Accounts payable at December 31, 2011 and 2010 consists of insurance premium payables, operating expenses, and customers advances collected, among others.

r) Comprehensive income (loss)

Comprehensive (loss) income is the total of net (loss) income and all other changes in equity of a company that result from transactions and other economic events of a reporting period other than transactions with owners. Comprehensive income (loss) is reflected in the consolidated statements of changes in equity.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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The components of accumulated other comprehensive income (loss) in the consolidated balance sheets were as follows:

	At December 31,	
	2011	2010
Unrealized net losses on interest rate collar	$(1,727)	$(716)
Unrealized net losses on interest rate swap	(482)	(34)
Unrealized net gains on EURO hedge	145	153
Accumulated other comprehensive income (loss)	(2,064)	(597)
Amounts attributable to noncontrolling interest	(27)	-
Amounts attributable to Ultrapetrol (Bahamas) Limited	$(2,037)	$(597)

At December 31, 2011, the Company expects that it will reclassify $749 of net losses on interest rate collar and interest rate swap from accumulated other comprehensive income (loss) to earnings during the next twelve months related to the payments of interest of our variable interest rate debt that will affect earnings for 2012.

The components of the change in the accumulated unrealized net income (losses) on derivative financial instruments were as follows:

	For the years ended December 31,		
	2011	2010	2009
Reclassification adjustments for amounts included in net (loss):			
–Revenues	$-	$(6,193)	$(32,279)
–Voyage and manufacturing expenses	-	-	490
–Depreciation and amortization	(8)	(9)	(8)
–Financial expense	1,129	401	-
–(Loss) gains on derivatives, net	-	(10,710)	-
Change in unrealized impact on:			-
–Interest rate collar	(1,964)	(1,117)	-
–Interest rate swap	(624)	(34)	-
–FFA	-	1,527	(18,088)
	$(1,467)	$(16,135)	$(49,885)
Amounts attributable to noncontrolling interest	(27)	-	-
Amounts attributable to Ultrapetrol (Bahamas) Limited	$(1,440)	$(16,135)	$(49,885)

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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s) Derivative financial instruments

The Company from time to time uses derivative financial instruments to reduce risk from foreign currency fluctuations, changes in spot market rates for oceangoing vessels, changes in interest rate and changes in bunker fuel prices.

The Company recognizes all of its derivative instruments as either assets or liabilities in the balance sheet at fair value. The accounting for changes in the fair value (i.e., gains or losses) of a derivative financial instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship.

For derivative financial instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative financial instrument is reported as a component of other comprehensive income (loss) and reclassified into earnings in the same line item associated with the hedged transaction in the same period or periods during which the hedged transaction affects earnings. The ineffective portion of a derivative's change in fair value is immediately recognized in income.

Derivative financial instruments that are not designated as hedges for accounting purposes are adjusted to fair value through income.

t) Earnings per share

Basic (loss) per share is computed by dividing the net (loss) by the weighted average number of common shares outstanding during the relevant periods net of shares held in treasury. Diluted (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common shares result in the issuance of such shares. In determining dilutive shares for this purpose the Company assumes, through the application of the treasury stock and if-converted methods, all restricted stock grants have vested, all common shares have been issued pursuant to the exercise of all outstanding stock options and all common shares have been issued pursuant to the conversion of all outstanding convertible notes.

For the years ended December 31, 2011, 2010 and 2009, the Company had a net loss from continuing operations and therefore the effect of potentially dilutive securities was antidilutive and the following securities were not included in shares outstanding for purposes of computing diluted (loss) per share.

The Company excluded from the computation of diluted (loss) per share of Ultrapetrol (Bahamas) Limited 13,051,000 shares for the potential conversion of all outstanding convertible notes, as the effect of their inclusion in the computation would have been antidilutive for the period the convertible notes were issued until December 31, 2011 and 2010.

For the years ended December 31, 2011 and 2010 diluted (loss) per share of Ultrapetrol (Bahamas) Limited excluded 705,000 and 520,000, respectively, of certain share awards as the effect of their inclusion in the computation would have been antidilituve.

For the years ended December 31, 2011, 2010 and 2009, the Company excluded from the computation of diluted (loss) per share options to purchase 348,750 common shares. These options were outstanding during these years but were excluded because they were antidilutive, as the option exercise price was greater than the average market price

of the common share.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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The following table sets forth the computation of basic and diluted (loss) per share attributable to Ultrapetrol (Bahamas) Limited.

	For the years ended December 31,		
	2011	2010	2009
(Loss) from continuing operations	$(18,805)	$(4,856)	$(37,707)
(Loss) from discontinued operations	-	(515)	(2,131)
Net (loss)	$(18,805)	$(5,371)	$(39,838)

	For the years ended December 31,		
	2011	2010	2009
Basic and diluted weighted average number of shares	29,547,365	29,525,025	29,426,429
Basic and diluted (loss) per share:			
From continuing operations	$(0.64)	$(0.16)	$(1.28)
From discontinued operations	-	(0.02)	(0.07)
	$(0.64)	$(0.18)	$(1.35)

u) Stock compensation

Stock-based compensation cost is measured at the date of grant, based on the calculated fair value of the award, and is recognized as expense over the employee's service period, which is generally the vesting period of the equity grant. The fair value of performance based restricted common stock awards that are probable of being earned is expensed over the performance periods as the awards vest. The Company does not estimate forfeitures in its expense calculations as forfeiture history has been minor.

v) Other operating income, net

For the three years ended December 31, 2011, this account includes:

	For the years ended December 31,		
	2011	2010	2009
Arbitration award (1)	$4,748	$-	$-
Gain on sale of vessels, net	-	724	1,415
Claims against insurance companies, net	3,543	(46)	1,429
Other	(34)	(61)	-
	$8,257	$617	$2,844

(1) One of our subsidiaries in the River Business, UABL Paraguay S.A., made a claim against a former customer in an arbitration proceeding where we claim damages for an underperformance under a transportation contract. On

December 2, 2011 a final amount of $5,308 was awarded to the Company, which was collected on December 21, 2011. Due to the disputed nature of the claim, the Company had not recognized any income related to the claim and now since the arbitration proceeding was favorably settled and collected recognizing an income of $4,748, after deducting related legal fees of $560.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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w) Income taxes

The Company accounts for deferred income taxes under the liability method. Under this method, deferred income tax assets and liabilities are established for temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities at each period end corresponding to those jurisdictions subject to income taxes. Deferred tax assets are recognized for all deductible temporary differences and an offsetting valuation allowance is recorded to the extent that it is not more likely than not that the deferred tax assets will be realized. Deferred tax is measured based on tax rates and laws enacted or substantively enacted at the balance sheet date in any jurisdiction.

Income tax regulations in the different countries in which we operate are subject to interpretation by taxing authorities. As a result, our judgment in the determination of uncertain income tax positions could be interpreted differently. In this sense, the income tax returns of our primary income tax jurisdictions remain subject to examination by related tax authorities. The tax returns are open to examination from 3 to 7 years.

x) Recent accounting pronouncements

In June 2011, the Financial Accounting Standards Board ("FASB") amended its guidance on the presentation of comprehensive income. Under the amended guidance, an entity has the option to present comprehensive income in either one continuous statement or two consecutive financial statements. A single statement must present the components of net income and total net income, the components of other comprehensive income and total other comprehensive income, and a total for comprehensive income. In a two-statement approach, an entity must present the components of net income and total net income in the first statement. That statement must be immediately followed by a financial statement that presents the components of other comprehensive income, a total for other comprehensive income, and a total for comprehensive income. The option under the current guidance that permits the presentation of components of other comprehensive income as part of the statement of changes in equity has been eliminated. The amendment becomes effective on January 1, 2012 and is applied retrospectively. Early adoption is permitted. This guidance will not have an impact on the Company's consolidated financial position, results of operations or cash flows as it is disclosure-only in nature.

3. DRY DOCK

The capitalized amounts in dry dock at December 31, 2011 and 2010 were as follows:

	At December 31,	
	2011	2010
Original book value	$19,786	$16,308
Accumulated amortization	(14,698)	(10,620)
Net book value	$5,088	$5,688

For the three years ended December 31, 2011 amortization expense was $4,078, $4,186 and $3,425, respectively.

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4. VESSELS AND EQUIPMENT, NET

The capitalized cost of the vessels and equipment, and the related accumulated depreciation at December 31, 2011 and 2010 were as follows:

	At December 31,	
	2011	2010
Ocean-going vessels	$127,468	$124,596
River barges and pushboats	398,391	331,801
PSVs	199,453	171,385
Advances for PSV construction	68,149	77,106
Furniture and equipment	10,458	8,861
Building, land, operating base and shipyard	52,491	49,179
Total original book value	856,410	762,928
Accumulated depreciation	(184,965)	(150,232)
Net book value	$671,445	$612,696

For the three years ended December 31, 2011 depreciation expense was $34,891, $29,880 and $37,609, respectively.

Certain interest costs incurred during the construction of vessels are capitalized as part of the assets' carrying values and are depreciated over such assets' estimated useful lives. Capitalized interest for the three years ended December 31, 2011 totaled $0, $1,010 and $2,354, respectively.

ACQUISITIONS AND DISPOSALS

Ocean Business

During 2010, we purchased and took delivery of two feeder container vessels for an aggregate total purchase price of $26,200.

During 2010, we sold and delivered three Capesize vessels for an aggregate total sale price of $36,584 net of commissions and Ultrapetrol recognized a net gain on sale of vessel of $724.

During 2009, we sold and delivered one Capesize vessel, for a total sale price of $9,840 net of commissions and Ultrapetrol recognized a gain on sale of vessel of $1,415.

River Business

During 2011, we purchased three pushboats, for a total aggregate purchase price of $2,900. The Company has also incurred $2,000 in additional direct costs relating to these acquisitions.

During 2011, forty-two barges had been built (twenty-seven of which had commenced their operation) in our own shipyard in Punta Alvear, Argentina for a total cost of $31,400.

During 2010, sixteen barges had been built (seven of which had commenced their operation) in our own shipyard in Punta Alvear, Argentina for a total cost of $18,400.

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Subsequent events

On February 13, 2012, the Company signed a memorandum of agreement (MOA) to sell its pushboat Cavalier VIII for a total sale price of $3,850, which was delivered to the buyer on February 24, 2012.

Offshore Supply Business

On December 21, 2007, UP Offshore (Bahamas) Ltd. (our holding company in the Offshore Supply Business) signed two contracts with a shipyard in China to construct two PSVs. The price for each new PSV to be constructed in China was $26,400 to be paid in five installments of 20% of the contract price each, prior to delivery. On December 20, 2010 we took delivery of the first Chinese PSV UP Turquoise and on June 10, 2011, we took delivery of the second one, named UP Jasper.

On February 21 and June 13, 2007, UP Offshore (Bahamas) Ltd. (our holding company in the Offshore Supply Business) signed shipbuilding contracts with a shipyard in India for construction of four PSVs with a combined cost of $88,052, with contracted deliveries extended to 2012. The purchase price is to be paid in five installments of 20% of the contract price each, prior to delivery. As of December 31, 2011, UP Offshore (Bahamas) Ltd. had paid installments on these contracts totaling $57,233, which are recorded as Advances for PSV construction.

As of December 31, 2011, the Company had remaining commitments of $30,819 on non-cancellable contracts for the construction of four PSVs in India scheduled for delivery in 2012.

Subsequent events

On January 24, 2012 we paid $4,400 corresponding to the fourth 20% installment of one of our PSVs under construction in India, out of which $3,450 were drawn down under our loan facility with DVB Bank and Natixis.

5. LONG-TERM DEBT AND OTHER FINANCIAL DEBT

Balances of long-term financial debt were as follows:

			At December 31, 2011			2010
Borrower	Financial institution / Other	Due-year	Nominal value Current	Noncurrent	Total	Total
Ultrapetrol (Bahamas) Ltd.	Private Investors	2014	$-	$180,000	$180,000	$180,000
Ultrapetrol (Bahamas) Ltd.	Private Investors	2017	-	80,000	80,000	80,000
Ultrapetrol (Bahamas) Ltd.	BICE	2011	-	-	-	15,000
UP Offshore Apoio Marítimo Ltda.	DVB AG	Through 2016	900	6,850	7,750	8,650

UP Offshore (Bahamas) Ltd.	DVB AG	Through 2016	4,300	33,950	38,250	42,550
UP Offshore (Bahamas) Ltd.	DVB AG	Through 2017	2,000	13,000	15,000	17,000
UP Offshore (Bahamas) Ltd.	DVB SE + Banco Security	Through 2018	3,333	34,167	37,500	20,000
Ingatestone Holdings Inc.	DVB AG + Natixis	Through 2019	863	30,187	31,050	24,150
UP Offshore Apoio Marítimo Ltda.	BNDES	Through 2027	1,110	15,818	16,928	18,038
Stanyan Shipping Inc.	Natixis	Through 2017	908	8,395	9,303	10,211
Hallandale Commercial Corp.	Nordea	Through 2013	1,568	5,644	7,212	8,780
UABL Paraguay S.A.	IFC	Through 2020	2,174	22,826	25,000	25,000
UABL Paraguay S.A.	OFID	Through 2020	1,304	13,696	15,000	15,000
UABL Barges and others	IFC	Through 2020	3,044	31,956	35,000	35,000
UABL Paraguay S.A. and Riverpar S.A.	IFC	Through 2021	-	15,000	15,000	-
December 31, 2011			$21,504	$491,489	$512,993	
December 31, 2010			$27,586	$471,793		$499,379

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Aggregate annual future payments due to the long-term financial debt were as follows:

Year ending December 31		
2012	$	21,504
2013		28,870
2014		203,227
2015		23,227
2016		44,671
Thereafter		191,494
Total	$	512,993

9% First Preferred Ship Mortgage Notes due 2014

On November 24, 2004 the Company completed a debt offering of $180,000 of 9% First Preferred Ship Mortgage Notes due 2014 (the "2014 Senior Notes"), through a private placement to institutional investors eligible for resale under Rule 144A and Regulation S (the "Offering"). The net proceeds of the Offering were used to repay the 2008 Senior Notes, certain other existing credit facilities and to fund some vessel acquisitions.

Interest on the 2014 Senior Notes is payable semi-annually on May 24 and November 24 of each year and principal is due on November 24, 2014. The 2014 Senior Notes are senior obligations guaranteed by the Company's subsidiaries directly involved in our Ocean and River Business. At December 31, 2011, the 2014 Senior Notes are secured by first preferred ship mortgages on 13 river pushboats, 2 oceangoing barges and 335 river barges.

The 2014 Senior Notes are subject to certain covenants, including, among others, limiting the parent's and guarantor subsidiaries' ability to incur additional indebtedness or issue preferred stock, pay dividends to stockholders, incur liens or execute sale leasebacks of certain principal assets and certain restrictions on the Company consolidating with or merging into any other person.

Upon the occurrence of a change of control event, each holder of the 2014 Senior Notes shall have the right to require the Company to repurchase such notes at a purchase price in cash equal to 101% of the principal amount thereof plus accrued and unpaid interest. Our indenture governing our 2014 Senior Notes describes the circumstances that are considered a change of control event.

In the first quarter of 2005 the SEC declared effective an exchange offer filed by the Company to register substantially identical senior notes to be exchanged for the 2014 Senior Notes pursuant to a registration rights agreement, to allow the 2014 Senior Notes be eligible for trading in the public markets.

Although Ultrapetrol (Bahamas) Limited, the parent company, subscribed the issued Notes, principal and related expenses will be paid through funds obtained from the operations of the Company's subsidiaries.

The 2014 Senior Notes Indenture includes certain terms under which a subsidiary may be classified as an Unrestricted Subsidiary. The Board of Directors determined that UP Offshore (Bahamas) Limited (the holding company of our Offshore Supply Business) has met those criteria and on October 29, 2009, the board of Directors of Ultrapetrol (Bahamas) Limited declared UP Offshore (Bahamas) Limited, as an Unrestricted Subsidiary pursuant to the terms of the Indenture. Subsequently, on December 3, 2010 the Board of Directors decided to reclassify UP Offshore

(Bahamas) Limited as Restricted Subsidiary pursuant to the terms of the Indenture.

At December 31, 2011 the net book value of the assets pledged as a guarantee of the 2014 Senior Notes was $68,700.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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7.25% Convertible Senior Notes due 2017

On December 23, 2010, the Company completed the sale of $80,000 aggregate principal amount of its 7.25% Convertible Senior Notes due 2017 (the "2017 Convertible Notes") through a private placement to institutional investors eligible for resale under Rule 144A and Regulation S. The Convertible Notes are senior and unsecured obligations of the Company. Interest on the 2017 Convertible Notes is payable semi-annually on January 15 and July 15 of each year, commencing on July 15, 2011. Unless earlier converted, redeemed or repurchased, the 2017 Convertible Notes are due on January 15, 2017.

The 2017 Convertible Notes are convertible after January 28, 2011, at the option of the holder, into common stock at an initial conversion rate equal to 133.1691 shares of the Company common stock per $1 principal amount of 2017 Convertible Notes (equivalent to an initial conversion price of approximately $7.51 per share), which is subject to adjustment.

If the arithmetic average of the daily volume weighted average price per share of the Company common stock for each of the 20 consecutive trading days beginning on January 17, 2012 is less than $6.13, then the conversion rate will be increased such that the conversion price as adjusted would represent the greater of (i) 122.5% of such arithmetic average of the daily volume weight average price and (ii) $6.13.

On or after January 15, 2015, the Company may redeem for cash all, but not less than all, of the 2017 Convertible Notes if the last reported sale price of the Company common stock equals or exceeds 130% of the applicable conversion for a specific period of time at 100% of the principal amount of the 2017 Convertible Notes to be redeemed, plus any accrued and unpaid interest to, but excluding, the redemption date.

Upon a fundamental change occurring, as defined in the 2017 Convertible Notes Indenture, each holder of the 2017 Convertible Notes, shall have the right to require the Company to repurchase the 2017 Convertible Notes in cash at a price equal to 100% of the principal amount of the 2017 Convertible Notes to be repurchased, plus any accrued and unpaid interest to, but excluding, the fundamental change repurchase date.

If a fundamental change occurs under the 2017 Convertible Notes Indenture, the Company will pay a make-whole premium upon the conversion of the 2017 Convertible Notes in connection with any such transaction by increasing the applicable conversion rate. The make-whole premium will be determined by reference to the 2017 Convertible Notes Indenture and is based on the date on which the fundamental change becomes effective and the market stock price of the Company common stock on that date. In no event shall the conversion rate exceed 163.1321 shares per $1 principal amount.

The Indenture of the 2017 Convertible Notes also contains customary events of default and cross-default provisions. If an event of default occurs and is continuing the Trustee or holders of the 25% of the 2017 Convertible Notes may require the entire amount of the Convertible Notes be immediately repaid in full.

At December 31, 2011 and 2010, the if-converted value of the 2017 Convertible Notes does not exceed their principal amount.

At December 31, 2011 and 2010 the 2017 Convertible Notes are disclosed on the Company's consolidated balance sheets as long-term debt at face value.

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As from February 14, 2012, the conversion rate has been adjusted to 163.1321 shares of the Company common stock per $1 principal amount of 2017 Convertible Notes (equivalent to a price of approximately $ 6.13 per share) as a consequence of the arithmetic average of the daily volume weighted average price per share of the Company common stock for the period from January 17, 2012 to February 13, 2012 (both inclusive) was $2.76.

Revolving non-secured credit facility with Banco BICE

During 2007, Ultrapetrol Bahamas Ltd. entered into a three-year, $10,000, revolving non-secured credit facility with Banco BICE. This loan accrued interest at LIBOR plus 1.625% per annum.

On October 8, 2010, we amended the credit agreement between us and Banco BICE. In connection with this amendment, the credit agreement was extended for one year and increased to $15,000, its margin was increased to 3.4% per annum over LIBOR and certain other changes were made to its guarantees and covenants. On October 14, 2010 we drew down $5,000 under the amended facility, resulting in a total of $15,000 drawn down under the credit facility with Banco BICE at December 31, 2010.

On April 14, 2011, we voluntarily prepaid $15,000 outstanding under the Banco BICE revolving non-secured credit facility together with accrued and unpaid interest to such date. The line remained fully available for drawdown until its final maturity on October 12, 2011.

On August 11, 2011, we drew down $10,500 under the revolving non-secured credit facility. Subsequently, the Company repaid $5,500 and $5,000 on October 26, 2011 and on November 25, 2011, respectively. There is not outstanding amount as of December 31, 2011.

Loans with DVB Bank AG (DVB AG)

a) Senior secured term loan facility of up to $15,000: On January 17, 2006 UP Offshore Apoio Maritimo Ltda. (UP Offshore Apoio) as Borrower, Packet Maritime Inc. (Packet) and Padow Shipping Inc. (Padow) as Guarantors and UP Offshore (Bahamas) Ltd. (UP Offshore) as Holding Company (all of these our subsidiaries in the Offshore Supply Business) entered into a senior secured term loan facility of up to $15,000 with DVB AG for the purposes of providing post delivery financing of our PSV named UP Agua Marinha.

This loan is divided into two tranches:

- Tranche A, amounting to $13,000, accrues interest at LIBOR plus a margin of 1.20% per annum and shall be repaid by (i) 120 consecutive monthly installments of $75 each beginning in March 2006 and (ii) a balloon repayment of $4,000 together with the 120th installment.

- Tranche B, amounting to $2,000 and accrues interest at LIBOR plus a margin of 1.20% per annum and shall be repaid by 36 consecutive monthly installments of $56 each beginning in March 2006.

For the year ended December 31, 2011, the weighted average interest rate was 1.46% and the respective interest rates ranged from 1.41% to 1.51%, including margins.

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b) Senior secured term loan facility of up to $61,306: On December 28, 2006 UP Offshore (Bahamas) Ltd. as Borrower, Packet, Padow, UP Offshore Apoio and Topazio Shipping LLC (collectively the owners of our PSVs UP Safira, UP Esmeralda, UP Agua Marinha and UP Topazio) and Ultrapetrol (Bahamas) Limited as Guarantors entered into a senior secured term loan facility of up to $61,306 with DVB AG for the purposes of providing post delivery re-financing of our PSVs named UP Safira, UP Esmeralda and UP Topazio.

The loan bears interest at LIBOR plus 1.20% per annum with quarterly principal and interest payments and matures in December 2016. The regularly scheduled principal payments are due quarterly and range from $1,075 to $1,325, with a balloon installment of $16,000 in December 2016. If a PSV is sold or becomes a total loss, the Borrower shall prepay the loan in an amount equal to the stipulated value of such PSV, which is initially stipulated in $18,750 and shall be reduced in the amount of $388 on each repayment date.

For the year ended December 31, 2011, the weighted average interest rate was 1.50% and the respective interest rates ranged from 1.45% to 1.54%, including margins.

c) Senior secured term loan facility of up to $25,000: On October 31, 2007 UP Offshore (Bahamas) Ltd. as Borrower entered into a senior secured term loan facility of up to $25,000 with DVB AG for the purposes of providing post delivery re-financing of our PSV named UP Diamante.

The Banks, at their discretion, may replace LIBOR as base rate for the interest calculation with their cost-of-funds rate.

The loan bears interest at LIBOR plus 1.50% per annum with quarterly principal and interest payments and matures in November 2017. The regularly scheduled payments commenced in February 2008 and are comprised of 8 installments of $750 each, 24 of $500 each and 8 of $250 each with a balloon installment of $5,000 in November 2017.

For the year ended December 31, 2011, the weighted average interest rate was 1.78% and the respective interest rates ranged from 1.75% to 1.80%, including margins.

All of these loans are secured by a first priority mortgage on the UP Safira, UP Esmeralda, UP Topazio, UP Agua Marinha and UP Diamante a first priority assignment of the time charters, a first priority assignment of the earnings, insurances and requisition compensation of the vessels, a first priority assignment of any charter, or other employment contracts exceeding 12 months and are jointly and severally irrevocable and unconditionally guaranteed by Packet, Padow, UP Offshore Apoio, Topazio Shipping LLC and Ultrapetrol (Bahamas) Limited. The loans also contain customary covenants that limit, among other things, the Borrowers' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreements governing the facility also contain customary events of default. If an event of default occurs and is continuing, DVB AG may require the entire amount of the loans be immediately repaid in full. Further, the loan agreements require that the PSVs pledged as security have an aggregate market value of at least 133.3% of the value of the loans.

At December 31, 2011 the combined outstanding principal balance under the loan agreements was $61,000 and the aggregate net book value of the assets pledged was $89,200.

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Senior secured term loan facility with DVB Bank AG (DVB AG) and Natixis of up to $93,600

On June 24, 2008 Ingatestone Holdings Inc., as Borrower, and UP Offshore (Bahamas) Ltd., Bayshore Shipping Inc., Gracebay Shipping Inc., Springwater Shipping Inc. and Woodrow Shipping Inc. (all of these our subsidiaries in the Offshore Supply Business) and Ultrapetrol (Bahamas) Limited, as joint and several Guarantors, entered into a senior secured term loan facility of up to $93,600 with DVB AG and Natixis (the "Banks"), as co-lender, to finance the construction and delivery of our PSVs being built in India.

On December 9, 2010, the Borrower, the Guarantors and the Banks amended the credit agreement. In connection with this amendment, the margin of both tranches was increased, the repayment amount of Tranche A was increased by $38 to $288 and the availability period was extended through June 30, 2012, among other changes. An amendment fee of 0.50% of the total amount of the loan was paid.

On November 30, 2011 the Borrower, the Guarantors and the Banks further amended the credit agreement. In connection with this amendment, the availability period was extended through December 31, 2012 in respect of the advances of Tranche A and through June 30, 2013 in respect of the advances of Tranche B, on a vessel by vessel basis. An amendment fee of 0.20% of the total amount of the loan was paid.

A quarterly commitment fee is payable based on the average undrawn amount of the committed amount at a rate of 0.50% per annum through December 2010 and at a rate of 1.50% per annum thereafter.

This loan is divided into two tranches:

- Tranche A, amounting to $60,000, to be made available for each ship in the amount of up to $15,000 in multiple advances for the payment of installments of the contract price due under the applicable shipbuilding contract. This tranche accrues interest at LIBOR (base rate) plus a margin of 3.0% during each ship's construction period, and then the margin is lowered to 2.0% and shall be repaid by (i) quarterly installments of $288 per ship and (ii) a balloon repayment of all amounts outstanding at December 31, 2019. The first quarterly repayment shall commence on the date falling three months after the delivery date of such ship.

During the pre-delivery period, advances of Tranche A in respect of each ship shall not exceed $3,450 per advance and in the aggregate for each ship the lesser of (i) 60% of the relevant construction cost and (ii) $13,800.

- Tranche B, amounting to $33,600, to be made available for each ship in the amount of up to $8,400 in a single advance on the delivery date of such ship. This tranche accrues interest at LIBOR (base rate) plus a margin of 2.0% per annum and shall be repaid by 20 quarterly installments of $420 per ship. The first quarterly repayment shall commence on the date falling three months after the delivery date of such ship.

The Banks, at their discretion, may replace LIBOR as base rate for the interest calculation with their cost-of-funds rate.

For the year ended December 31, 2011, the weighted average interest rate was 3.86% and the respective interest rates ranged from 3.55% to 4.36%, including margins.

As Facility Guarantor, UP Offshore (Bahamas) Ltd. shall comply with certain financial covenants including: (i) an average balance of available cash in a demand deposit of not less than $5,000 during each financial year, (ii) an equity ratio of not less than 30%, (iii) a minimum equity of $75,000 and, (iv) a ratio of consolidated EBITDA to consolidated

debt service of at least 1.5 (on a rolling four quarter basis, tested as of the last day of each fiscal quarter).

The loan contains customary covenants which are similar to the stipulated covenants in previous loans entered with DVB AG. The agreements governing the facility also contain customary events of default. If an event of default occurs and is continuing, DVB AG and Natixis may require the entire amount of the loans be immediately repaid in full.

During the year ended December 31, 2011, the Company drew down $6,900 under Tranche A of this loan facility.

At December 31, 2011 the aggregate outstanding principal balance of the loan was $31,050.

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On January 24, 2012 we drew down $3,450 under Tranche A of this loan facility.

Seventeen-year term $18,730 credit facility with Brazilian Development Bank (BNDES)

On August 20, 2009, UP Offshore Apoio (our subsidiary in the Offshore Supply Business) as Obligor, UP Offshore (Bahamas) Ltd., as Facility Guarantor and Ultrapetrol (Bahamas) Ltd., as Limited Guarantor, entered into a seventeen-year fixed interest credit facility for $18,730 with BNDES to partially post-finance the construction of our PSV UP Rubi.

The loan shall be repaid by 204 consecutive monthly installments beginning in April 2010. The loan accrues interest at 3% per annum.

On October 30, 2009, UP Offshore Apoio entered into a Standby Letter of Credit Facility Agreement (the "Letter") with DVB Bank SE relating to a $21,500 Standby Letter of Credit Facility which guarantees the BNDES credit facility from November 11, 2009 to November 11, 2013. The Letter requires PSV UP Rubi to be pledged as security and its fair market value shall be not less than 133.3% of the outstanding amount of the Letter and is guaranteed by UP Offshore (Bahamas) Ltd. and Ultrapetrol (Bahamas) Limited as Facility Guarantor and Limited Guarantor, respectively.

Under the Letter, UP Offshore Apoio is to pay an up front fee equal to 1.5% of the outstanding amount, an annual commission fee fixed of 2.0% per annum on the outstanding amount and a fee equal to 1.0% on the settlement date on the settlement amount.

As Facility Guarantor, UP Offshore (Bahamas) Ltd. shall comply with certain financial covenants including: (i) an average balance of available cash in a demand deposit of not less than $5,000 during each financial year, (ii) an equity ratio of not less than 30%, (iii) a minimum equity of $75,000 and, (iv) a ratio of consolidated EBITDA to consolidated debt service of at least 1.5 (on a rolling four quarter basis, tested as of the last day of each fiscal quarter).

At December 31, 2011, the outstanding principal balance under this loan agreement was $16,928 and the aggregate net book value of the asset pledged was $25,600.

Loan Agreement with DVB Bank SE (DVB SE) and Banco Security of up to $40,000:

On December 9, 2010 UP Offshore (Bahamas) Ltd., as Borrower, and Glasgow Shipping Inc. and Zubia Shipping Inc. (all of these our subsidiaries in the Offshore Supply Business) and Ultrapetrol (Bahamas) Limited and Corporación de Navegación Mundial S.A., as joint and several Guarantors, entered into a senior secured term loan facility of up to $40,000 with DVB SE and Banco Security, as co-lenders, to partially finance the construction and delivery of our two PSVs being constructed in China.

The loan is drawn in two advances, each in the amount of $20,000, on the delivery of each of the respective PSVs, accrues interest at LIBOR (base rate) plus a margin of 3.0% and shall be repaid by (i) 32 equal quarterly consecutive installments of $417 each, together with a balloon payment equal to the outstanding balance of such advance payable concurring with the last repayment installment in respect of such advance. The first installment in respect of each advance shall be repaid on the date falling three months after the drawdown date in respect of such advance and the

last installment and balloon payment in respect of such advance shall be repaid on the earlier of the date falling eight years after the drawdown date in respect of such advance or December 31, 2018.

The co-lenders, at their discretion, may replace LIBOR as base rate for the interest calculation with their cost-of-funds rate.

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For the year ended December 31, 2011, the weighted average interest rate was 4.11% and the respective interest rates ranged from 4.06% to 4.15%, including margins and interest rate swaps.

The loan contains customary covenants which are similar to the stipulated covenants in previous loans entered with DVB AG. The agreements governing the facility also contain customary events of default. If an event of default occurs and is continuing, DVB SE and Banco Security may require the entire amount of the loan be immediately repaid in full.

The loan is secured by a first priority mortgage on UP Turquoise and UP Jasper, a first priority assignment of the time charters, a first priority assignment of the earnings, insurances and requisition compensation of the vessels, a first priority assignment of any charter, or other employment contracts exceeding 12 months. Further, the loan agreements require that the PSVs pledged as security have an aggregate fair market value of at least 133.3% of the value of the loan during the period from the first drawdown date until the fourth anniversary thereof or at least 66.7% of the value of the loan at any time thereafter.

UP Offshore (Bahamas) Limited as Guarantor shall maintain certain financial covenants including: (i) an average balance of available cash in a demand deposit of not less than $5,000, (ii) an equity ratio of not less than 30%, (iii) a minimum equity of $75,000 and, (iv) a ratio of consolidated EBITDA to consolidated debt service of at least 1.5 (on a rolling four quarter basis, tested as of the last day of each fiscal quarter).

On December 16, 2010, we have drawn down the first advance of $20,000 in connection with the delivery of UP Turquoise.

On June 14, 2011, we have drawn down the second advance of $20,000 in connection with the delivery of UP Jasper.

At December 31, 2011 the outstanding principal balance was $37,500 and the aggregate net book value of the assets pledged was $53,100.

Senior secured term loan with Natixis of up to $13,616

On January 29, 2007 Stanyan Shipping Inc. (a wholly owned subsidiary in the Ocean Business and the owner of the Alejandrina) drew down an amount of $13,616 under a loan agreement with Natixis (the "Lender") to provide post-delivery financing secured by the vessel. The loan, which matures in February 2017, shall be repaid by 40 equal quarterly installments of $227 with a balloon installment of $4,536. The loan accrues interest at 6.38% per annum for the first five years of the loan and LIBOR plus 1.20% per annum thereafter.

The loan is secured by a mortgage on the Alejandrina, a first priority assignment of the time charters, a first priority assignment of the earnings, insurances and requisition compensation of the vessels, a first priority assignment of any charter, or other employment contracts exceeding 12 months and is guaranteed by Ultrapetrol (Bahamas) Limited. The Lender may also require additional security, if at any time the fair market value of the ship becomes less than the 125% of the aggregate value of the loan. With respect to the above and in relation to any potential loan security shortfall, the Company provided an amount of $1,629 as additional security in accordance with the related loan agreement. Such amount represents restricted cash and it has been reflected under restricted cash, current in the accompanying consolidated balance sheet as of December 31, 2011. On February 8, 2012, the Company further funded $442 in cash as additional security.

The loan also contains customary covenants that limit, among other things, the Borrower's and the Guarantors' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreement governing the facility also contains customary events of default. If an event of default occurs and is continuing, Nataxis may require the entire amount of the loan be immediately repaid in full.

At December 31, 2011 the outstanding principal balance was $9,303 and the aggregate net book value of the assets pledged was $14,900.

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Senior secured term loan with Nordea Bank Finland PLC (Nordea Bank) of $20,200

On November 30, 2007, Hallandale Commercial Corp. (our wholly owned subsidiary in the Ocean Business and the owner of the Amadeo) as Borrower, Ultrapetrol (Bahamas) Ltd., as Guarantor, and Tuebrook Holdings Inc. (our wholly owned subsidiary in the Ocean Business and the holding company of Hallandale Commercial Corp.), as Pledgor, entered into a $20,200 loan agreement with Nordea Bank for the purpose of providing post delivery financing of the vessel.

The loan after the voluntary prepayment of $4,143 on June 6, 2009, shall be repaid by (i) 6 consecutive quarterly installments of $588 each followed by 12 consecutive quarterly installments of $392 each, and (ii) a final balloon repayment of $4,076 payable simultaneously with the last installment. The loan accrues interest at LIBOR plus 1.25% per annum.

For the year ended December 31, 2011, the weighted average interest rate was 1.55% and the respective interest rates ranged from 1.50% to 1.58%, including margins.

The loan is secured by a mortgage on the Amadeo vessel, a first priority assignment of the time charters, a first priority assignment of the earnings, insurances and requisition compensation of the vessels, a first priority assignment of any charter, or other employment contracts exceeding 12 months and is jointly and severally irrevocably and unconditionally guaranteed by Ultrapetrol (Bahamas) Ltd. The Lender may also require additional security, if at any time the fair market value of the ship becomes less than the 130% of the aggregate value of the loan. The loan also contains customary covenants that limit, among other things, the Borrower's and the Guarantors' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, merge or consolidate, change lines of business and amend the terms of subordinated debt. The agreement governing the facility also contains customary events of default. If an event of default occurs and is continuing, Nordea Bank may require the entire amount of the loan be immediately repaid in full.

As Guarantor, Ultrapetrol (Bahamas) Ltd. shall maintain certain financial covenants including: (i) a ratio of financial indebtedness to tangible net worth of not greater than 2.5 to 1.0 and (ii) a EBITDA to interest expense of not less than 2.0 for the last four fiscal quarters prior to the relevant date of calculation.

The aggregate outstanding principal balance of the loan was $7,212 at December 31, 2011, and the aggregate net book value of the asset pledged was $22,800.

Loan with International Finance Corporation ("IFC") and OPEC Fund for International Development (OFID)

a) 2008 Loan facility of up to $25,000

On September 15, 2008 UABL Paraguay S.A. (our subsidiary in the River Business), as Borrower, UABL (Bahamas) Limited as Guarantor and IFC entered into a loan agreement to partially finance: (i) the replacement of existing pushboat engines and conversion of pushboats to install such engines, (ii) the enlargement and re-bottoming of existing barges, (iii) the construction and acquisition of additional pushboats and barges and (iv) supplies and related equipment for the foregoing.

The loan shall be repaid in semi-annual installments of $1,087 for the first 9 payments and $1,902 for the last 8 payments, beginning in June 2012. The loan accrues interest at LIBOR plus a margin which will be calculated considering a percentage ranging between 1.875% to 3.250% obtained from the Guarantor Prospective Debt Service Coverage Ratio as indicated in the agreement.

For the year ended December 31, 2011, the weighted average interest rate was 4.61% and the respective interest rates ranged from 4.44% to 4.94%, including margins and interest rate collar.

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The loan is secured by a mortgage on part of our Liberian River Business fleet. The loan agreement requires that the aggregate fair market value of the Liberian mortgaged barges and pushboats dividing by the outstanding amount of the 2008 loans facility to be 1.3 during the period between the first disbursement of the loan and November 24, 2013 (one year prior to the final maturity date of the 2014 Senior Notes) and at all time thereafter 1.6. The loan contains various restrictive covenants, among others, that limit the Borrower's ability to declare or pay any dividend, incur capital expenditures, leases, enter into any derivative transaction, except hedging arrangements for fuel. The Borrower shall maintain certain financial covenants including: (i) a debt to equity ratio of not more than 2.0 and (ii) a historical debt service coverage ratio of not less than 1.0 for the last four fiscal quarters prior to the relevant date of calculation.

As Guarantor, UABL Limited shall maintain certain financial covenants including; (i) a consolidated debt to equity ratio of no more than 1.4, (ii) a historical debt service coverage ratio on a consolidated basis of not less than 1.3 and (iii) a consolidated current ratio of at least 1.0 for the last four fiscal quarters prior to the relevant date of calculation.

b) 2008 Loan facility of up to $35,000

On September 15, 2008 UABL Barges (Panama) Inc., UABL Towing Services S.A., Marine Financial Investment Corp. and Eastham Barges Inc. (all our subsidiaries in the River Business), as Borrowers, UABL (Bahamas) Limited as Guarantor and IFC entered into a loan agreement to partially finance: (i) the replacement of existing pushboat engines and conversion of pushboats to install such engines, (ii) the enlargement and re-bottoming of existing barges, (iii) the construction and acquisition of additional pushboats and barges and (iv) supplies and related equipment for the foregoing.

The loan shall be repaid in semi-annual installments of $1,522 for the first 9 payments and $2,663 for the last 8 payments, beginning in June 2012. The loan accrues interest at LIBOR plus a margin which will be calculated considering a percentage ranging between 1.875% to 3.250% obtained from the Guarantor Prospective Debt Service Coverage Ratio as indicated in the agreement.

For the year ended December 31, 2011, the weighted average interest rate was 4.61% and the respective interest rates ranged from 4.44% to 4.94%, including margins and interest rate collar.

The loan is secured by a mortgage on part of our Liberian River Business fleet. The loan agreement requires that the aggregate fair market value of the Liberian mortgaged barges and pushboats dividing by the outstanding amount of the 2008 loans facility to be 1.3 during the period between the first disbursement of the loan and November 24, 2013 (one year prior to the final maturity date of the 2014 Senior Notes) and at all time thereafter 1.6. The loan contains various restrictive covenants, among others, that limit the each Borrower's ability to declare or pay any dividend, incur capital expenditures, leases, enter into any derivative transaction, except hedging arrangements for fuel.

As Guarantor, UABL Limited shall maintain certain financial covenants including; (i) a consolidated debt to equity ratio of no more than 1.4, (ii) a historical debt service coverage ratio on a consolidated basis of not less than 1.3 and (iii) a consolidated current ratio of at least 1.0.

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c) 2008 Parallel Loan facility of up to $15,000

On November 28, 2008 UABL Paraguay S.A. (our subsidiary in the River Business), as Borrower, UABL (Bahamas) Limited as Guarantor and OFID entered into a loan agreement of up to $15,000 to partially finance: (i) the replacement of existing pushboat engines and the conversion of pushboats to install such engines, (ii) the enlargement and re-bottoming of existing barges, (iii) the construction and acquisition of additional pushboats and barges and (iv) supplies and related equipment for the foregoing.

The loan shall be repaid in semi-annual installments of $652 for the first 9 payments and $1,141 for the last 8 payments, beginning in June 2012. The loan accrues interest at LIBOR plus a margin which will be calculated considering a percentage ranging between 1.875% to 3.250% obtained from the Guarantor Prospective Debt Service Coverage Ratio.

For the year ended December 31, 2011, the weighted average interest rate was 4.61% and the respective interest rates ranged from 4.44% to 4.94%, including margins and interest rate collar.

The loan is secured by a mortgage on a portion of our Liberian River Business fleet. The loan agreement requires that the aggregate fair market value of the Liberian mortgaged barges and pushboats dividing by the outstanding amount of the 2008 loans facility to be 1.3 during the period between the first disbursement of the loan and November 24, 2013 (one year prior to the final maturity date of the 2014 Senior Notes) and at all time thereafter 1.6. The loan contains various restrictive covenants, among others, that limit the Borrower's ability to declare or pay any dividend, incur capital expenditures, leases, enter into any derivative transaction, except hedging arrangements for fuel. The Borrower shall maintain certain financial covenants including: (i) a debt to equity ratio of not more than 2.0 and (ii) a historical debt service coverage ratio of not less than 1.0.
As Guarantor, UABL Limited shall maintain certain financial covenants including; (i) a consolidated debt to equity ratio of no more than 1.4, (ii) a historical debt service coverage ratio on a consolidated basis of not less than 1.3 and (iii) a consolidated current ratio of at least 1.0.

d) 2011 Loan facility of up to $15,000

On December 2, 2011 UABL Paraguay S.A. and Riverpar S.A. (our subsidiaries in the River Business), as joint and several Borrowers, UABL (Bahamas) Limited as Guarantor and IFC entered into a loan agreement to partially finance: (i) the construction and acquisition of 64 additional barges, (ii) the modification to 9 existing pushboats necessary to replace their engines, (iii) the re-bottoming of 50 existing barges, and (iv) the construction and acquisition of additional pushboats and ancillary equipment.

The loan shall be repaid in semi-annual installments of $882 beginning on June 15, 2013 and ending on June 15, 2021. The loan accrues interest at LIBOR plus a margin of 3.65% per annum.

For the year ended December 31, 2011, the weighted average interest rate was 5.34%, including margins and interest rate collar.

The loan is secured by a mortgage principally on part of our Paraguayan and Liberian River Business fleet. The loan agreement requires that the aggregate fair market value of the Paraguayan and others mortgaged barges and pushboats dividing by the outstanding amount of the 2011 loans facility to be at any time prior to the refinancing of the 2014 Senior Notes not less than 3.0 and at any time thereafter, not less than 1.6. Further, the loan agreement requires that the aggregate fair market value of the Liberian mortgaged barges and pushboats dividing by the outstanding amount of

the 2011 loans facility to be at all times equal to or higher than 3.0.

The loan contains various restrictive covenants, among others, that limit the Borrowers' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, incur capital expenditures, leases and enter into any derivative transaction, except hedging agreements for fuel, interest rate or foreign currency in the ordinary course of business. The Borrowers shall maintain certain financial covenants including: (i) a debt to equity ratio on a consolidated basis of not more than 2.0 and (ii) a historical debt service coverage ratio on a consolidated basis of not less than 1.2 for the last four fiscal quarters prior to the relevant date of calculation.

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e) 2011 Parallel Loan facility of up to $10,000

On December 15, 2011 UABL Paraguay S.A. and Riverpar S.A. (our subsidiaries in the River Business), as joint and several Borrowers, UABL (Bahamas) Limited as Guarantor and OFID entered into a parallel loan agreements to partially finance: (i) the construction and acquisition of 64 additional barges, (ii) the modification to 9 existing pushboats necessary to replace their engines, (iii) the re-bottoming of 50 existing barges, and (iv) the construction and acquisition of additional pushboats and ancillary equipment.

The loan shall be repaid in semi-annual installments of $588 beginning on June 15, 2013 and ending on June 15, 2021. The loan accrues interest at LIBOR plus a margin of 3.65% per annum.

The loan is secured through a collateral sharing agreement with the IFC. The loan agreement requires that the aggregate fair market value of the Paraguayan and others mortgaged barges and pushboats dividing by the outstanding amount of the 2011 loans facility to be at any time prior to the refinancing of the 2014 Senior Notes not less than 3.0 and at any time thereafter, not less than 1.6. Further, the loan agreement requires that the aggregate fair market value of the Liberian mortgaged barges and pushboats dividing by the outstanding amount of the 2011 loans facility to be at all times equal to or higher than 3.0.

The loan contains various restrictive covenants, among others, that limit the Borrowers' ability to incur additional indebtedness, grant liens over their assets, sell assets, pay dividends, repay indebtedness, incur capital expenditures, leases and enter into any derivative transaction, except hedging agreements for fuel, interest rate or foreign currency in the ordinary course of business. The Borrowers shall maintain certain financial covenants including: (i) a debt to equity ratio on a consolidated basis of not more than 2.0 and (ii) a historical debt service coverage ratio on a consolidated basis of not less than 1.2 for the last four fiscal quarters prior to the relevant date of calculation.

The agreements governing the facilities also contain customary events of default. If an event of default occurs and is continuing, IFC and OFID may require the entire amount of the loan be immediately repaid in full.

At December 31, 2011 the Company has not made draw downs under the 2011 Parallel Loan facility.

At December 31, 2011, the aggregate outstanding principal balance under 2008 and 2011 loan agreements with OFID and IFC was $90,000 and the aggregate net book value of the assets pledged was $109,200.

Subsequent events

On January 26, 2012 the Company drew down $10,000 under the 2011 Parallel Loan facility.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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6. FINANCIAL INSTRUMENTS

The fair value of an asset or liability is the price that would be received to sell an asset or transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Company utilizes a fair value hierarchy that maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value and defines three levels of inputs that may be used to measure fair value. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are observable inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly, including quoted prices for similar assets or liabilities in active markets, quoted prices in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or inputs derived from observable market data. Level 3 inputs are unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities.

The Company's liabilities as of December 31, 2011 that are measured at fair value on a recurring basis are summarized below:

	Level 1	Level 2	Level 3
Current liabilities:			
-Interest rate collar (included in other liabilities)	-	582	-
-Interest rate swap (included in other liabilities)	-	251	-
Noncurrent liabilities:			
-Interest rate collar (included in other liabilities)	-	1,145	-
-Interest rate swap (included in other liabilities)	-	643	-

The estimated fair value of the Company's other financial assets and liabilities were as follows:

	At December 31,			
	2011		2010	
	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
ASSETS				
Cash and cash equivalents	$ 34,096	$ 34,096	$ 105,570	$ 105,570
Restricted cash (current and noncurrent portion)	8,302	8,302	2,844	2,844
LIABILITIES				
Long term financial debt (current and non-current portion – Note 5) (1)	$ 512,993	$ 468,393	$ 499,379	$ 502,136

(1) The fair value of long term financial debt is measured using Level 2 fair value inputs.

The carrying value of cash and cash equivalents and restricted cash approximates fair value. The fair value of long-term financial debt was estimated based upon quoted market prices or by using discounted cash flow analyses based on estimated current rates for similar types of arrangements. Generally, the carrying value of variable interest rate debt, approximates fair value. It was not practicable to estimate the fair value of the Company's investments in 50% owned companies because of the lack of quoted market prices and the inability to estimate fair value without incurring excessive costs. Considerable judgment was required in developing certain of the estimates of fair value and accordingly the estimates presented herein are not necessarily indicative of the amounts that the Company could realize in a current market exchange.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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7. DERIVATIVE INSTRUMENTS AND HEDGING STRATEGIES

Assets and liabilities arising from outstanding derivative positions are included in the accompanying consolidated balance sheets as other receivables and other liabilities, as follows:

	At December 31, 2011		
	Noncurrent other receivables	Current other liabilities	Noncurrent other liabilities
Derivatives designated as hedging instruments			
Interest rate collar (cash flow hedge)	$-	$582	$1,145
Interest rate swap (cash flow hedge)	-	251	643
	$-	$833	$1,788

	At December 31, 2010		
	Noncurrent other receivables	Current other liabilities	Noncurrent other liabilities
Derivatives designated as hedging instruments			
Interest rate collar (cash flow hedge)	$642	$791	$567
Interest rate swap (cash flow hedge)	-	160	129
	$642	$951	$696

The Company evaluates the risk of counterparty default by monitoring the financial condition of the financial institutions and counterparties involved, by primarily conducting business with large, well-established financial institutions and international traders, and diversifying its counterparties. The Company does not currently anticipate nonperformance by any of its counterparties.

CASH FLOW HEDGE

FFA

From April 2008 onwards, the Company entered into FFAs either via a clearing house or over the counter with the objective to utilize them as hedging instruments to reduce its exposure to changes in the spot market rates earned by its vessels in the Capesize fleet. These FFAs involve a contract to provide a fixed number of theoretical days of voyages at fixed rates. These contracts are net settled each month with the Company receiving a fixed rate per day and paying the average rate of the C4TC Index. The FFAs are hedging the fluctuation in the revenues of the Capesize fleet which is contracted at the average rate of the C4TC Index.

At December 31, 2011 and 2010 there are no outstanding positions on FFAs.

As result of the sale of Princess Marisol and Princess Katherine in 2010, FFA positions maturing between May and December 2010 were no longer probable of occurring and thus no longer qualified as effective cash flow hedges.

During the year ended December 31, 2010, the Company recorded an aggregate realized gain of $10,710, in connection with these FFA positions, which are reflected in the Company's consolidated statements of operations as Other income (expenses) – (loss) gains on derivatives, net.

During the years ended December 31, 2010 and 2009, the Company received net cash settlements for its FFA positions totaling, $16,666 and $32,279, respectively.

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INTEREST RATE COLLAR AGREEMENT

On May 7, 2010, through UABL Limited, our holding subsidiary in the River Business, we entered into an interest rate collar transaction with International Finance Corporation (IFC) through which we expect to hedge our exposure to interest volatility under our financings with IFC and OFID from June 2010 to June 2016. The initial notional amount is $75,000 (subsequently adjusted in accordance with the amortization schedule under these financings), with UABL Limited being the USD Floor Rate seller at a floor strike rate of 1.69%, and IFC being the USD Cap Rate seller at a cap strike rate of 5.00%. This contract qualifies for hedge accounting and as such changes in its fair value are included in other comprehensive income (loss) in the consolidated financial statements. The fair value of this agreement equates to the amount that would be paid or received by the Company if the agreement were cancelled at the reporting date, taking into account current and prospective interest rates and creditworthiness of the Company.

As of December 31, 2011, the total notional amount of the interest rate collar is $75,000.

INTEREST RATE SWAP AGREEMENTS

On December 16, 2010, through UP Offshore (Bahamas) Ltd., our holding subsidiary in the Offshore Supply Business, we entered into an interest rate swap transaction with Banco Security through which we expect to hedge our exposure to interest volatility under our financing with Banco Security and DVB Bank SE from December 2010 to December 2018. The initial notional amount is $5,000 (subsequently adjusted in accordance with the amortization schedule under this financing) with UP Offshore (Bahamas) Ltd. paying a fixed interest rate of 3.67% and receiving a variable interest rate based on LIBOR on the notional amount.

As of December 31, 2011, the total notional amount of the interest rate swap is $4,583.

Additionally, on June 14, 2011, through UP Offshore (Bahamas) Ltd., our holding subsidiary in the Offshore Supply Business, we entered into a second interest rate swap transaction with Banco Security through which we expect to hedge our exposure to interest volatility under our financing with Banco Security and DVB Bank SE from June 2011 to December 2018. The initial notional amount is $5,000 (subsequently adjusted pro rata in accordance with the amortization schedule under this financing) with UP Offshore (Bahamas) Ltd. paying a fixed interest rate of 3.122% and receiving a variable interest rate based on LIBOR on the notional amount.

As of December 31, 2011, the total notional amount of the interest rate swap is $4,792.

These contracts qualify for hedge accounting and as such changes in its fair value are included in other comprehensive income (loss) in the consolidated financial statements. The fair value of these agreements equate to the amount that would be paid or received by the Company if the agreement were cancelled at the reporting date, taking into account current and prospective interest rates and creditworthiness of the Company.

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OTHER DERIVATIVE INSTRUMENTS

Forward currency exchange contracts

From time to time the Company entered into and settled forward currency exchange contracts. These contracts were not designated as cash flow hedges and the changes in fair value were reflected in Other income (expenses) - (loss) gains on derivatives, net.

At December 31, 2011 and 2010, there are no outstanding positions on forward currency exchange contracts.

During the year ended December 31, 2009 the Company received cash settlements totaling $2,638 for these positions.

(Loss) gains on derivatives, net included in the accompanying consolidated statements of operations for the three years ended December 31, 2011 are as follows:

	For the years ended December 31,		
	2011	2010	2009
FFA	$-	$10,475	$-
Forward currency exchange contracts	-	-	241
Other	(16)	(1)	-
	$(16)	$10,474	$241

8. COMMITMENTS AND CONTINGENCIES

The Company is subject to legal proceedings, claims and contingencies arising in the ordinary course of business. When such amounts can be estimated and the contingency is probable, management accrues the corresponding liability. While the ultimate outcome of lawsuits or other proceedings against the Company cannot be predicted with certainty, management does not believe the costs of such actions will have a material effect on the Company´s consolidated financial position or results of operations.

a) UABL – Ciudad del Este Customs Authority

On September 21, 2005 the local Customs Authority of Ciudad del Este, Paraguay issued a finding that certain UABL entities owe taxes to that authority in the amount of $2,200, together with a fine for non-payment of the taxes in the same amount, in respect of certain operations of our River Business for the prior three-year period. This matter was referred to the Central Customs Authority of Paraguay.

After review of the entire case the Paraguayan Central Tax Authorities who have jurisdiction over the matter have confirmed the Company has no liability in respect of two of the three matters at issue, while they held a dissenting view on the third issue. Through a Resolution which was notified to UABL on October 13, 2006 the Paraguayan Undersecretary for Taxation has confirmed that, in his opinion, the Company is liable for a total of approximately $500 and has applied a fine of 100% of this amount. On November 24, 2006, the court confirmed that UABL were not liable for the first two issues. The Company has entered a plea with the respective court contending the interpretation on the third issue under consideration where the Company claims to be equally non-liable.

On March 26, 2009, the Tax and Administrative Court decided that UABL was not liable for the third issue under discussion (the tax base used by UABL's entities to calculate the applicable withholding tax). On April 2, 2009, the Paraguayan Tax Authorities appealed the Tax and Administrative Court decision. On September 22, 2010 the Paraguayan Supreme Court revoked the March 26, 2009, ruling of the Tax and Administrative Court and confirmed the decision of the Paraguayan Undersecretary for Taxation.

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For the year ended December 31, 2010 the Company recorded a charge totaling $1,294 for the full and final settlement of this claim.

In parallel with this ruling the Office of the Treasury Attorney has initiated an action in respect of the other two issues concerned in this litigation (which had been terminated on November 24, 2006, with the admission of Central Tax Authorities that no taxes were due for these two issues and the consequent dropping of the action by the plaintiffs) to review certain formal aspects of the case on the grounds that the Paraguay Customs Department did not represent the interests of Paraguay. UABL has submitted a defense in relation to the action commenced by the Office of the Treasury Attorney. Subsequently, the Office of the Treasury Attorney filed a response with regard to Company´s defense. The evidentiary stage of the proceedings commenced in November 2011. Aside from the mentioned procedures, the Customs Authorities of Paraguay have reopened the proceedings against UABL S.A., UABL Paraguay S.A. and YATAITY S.A. in connection with the possible reopening of the case pending a decision of the reopening of the case in court. Counsel notified the Customs to hold the proceedings pending a decision of the court and also contest any new investigation into the matter on the grounds that the action is time barred. We have been advised by UABL's counsel in the case that there is only a remote possibility that a judicial court would find UABL liable for any of these taxes or fines still in dispute or that the final outcome of these proceedings could have a material adverse impact on the consolidated financial position or results of operations of the Company.

UABL Paraguay S.A. - Paraguayan Customs Asunción

On April 7, 2009, the Paraguayan Customs in Asunción commenced administrative proceedings against UABL Paraguay S.A. alleging infringement of Customs regulations (smuggling) due to lack of submission of import clearance documents in Paraguay for some bunkers purchased between January 9, 2007 and December 23, 2008 from YPF-Repsol S.A. in Argentina. Since those bunkers were purchased for consumption on board pushboats, UABL Paraguay S.A. submitted a defense on April 23, 2009, requesting the closing of those proceedings based on the non-infringement of Customs regulations; however the proceedings were not closed. On August 21, 2009, as part of the evidence to be rendered in the Customs proceedings UABL Paraguay S.A. submitted a technical report of the Paraguayan Coast Guard stating that all parcels of bunkers purchased by UABL Paraguay S.A. from YPF-Repsol S.A. were consumed onboard the push boats. We were advised that the Paraguayan Customs in Ciudad del Este also commenced administrative proceedings against UABL Paraguay S.A. for the same reasons as the Customs in Asuncion; however those proceedings have been suspended. Customs Authorities appraised the bunkers and determined the corresponding import tax and fine to be $2,000. On March 22, 2010 the Customs in Asuncion issued their ruling on the matter imposing a fine of Gs. 54.723.820 (approximately $12), and UABL Paraguay S.A. will be paying the fine with the aim to end these proceedings. In parallel with this ruling the denouncing parties in Ciudad del Este submitted remedies against the decision of Customs in Asuncion arguing that such ruling was taken without bringing both dossiers together. Our legal counsel has recently advised that the Director of Customs in Asuncion decided to render null the ruling dated March 22, 2010 and ordered evidence to be filed in respect of years 2003 to 2006 before issuing the final ruling. In a similar manner, on September 20, 2010 the Paraguayan Customs in Asuncion received a complaint against UABL Paraguay S.A. alleging infringement of Customs regulations due to lack of submission of import clearance documents in Paraguay for bunkers purchased during 2009 and 2010, from YPF-Repsol S.A. in Argentina. UABL Paraguay S.A. submitted its defense together with all documents related to the bunker purchases.

Our legal counsel is of the opinion that remedies will be rejected and therefore that there is only a remote possibility that UABL Paraguay S.A. will finally be found liable for any such taxes or fines and / or that these proceedings will have financial material adverse impact on the consolidated financial position or results of operations of the Company.

Oceanpar S.A. and UABL Paraguay S.A. - Customs investigation in connection with reimportation of barges subject to conversion

Oceanpar S.A. was notified of this investigation on June 17, 2011. The matter under investigation is whether UABL Paraguay S.A. paid all import taxes and duties corresponding to the reimportation of barges submitted to conversion in foreign yards. On June 24, 2011 Oceanpar S.A. and UABL Paraguay S.A. submitted the evidence of all payments effected in 2008 corresponding to the reimportation of these barges. Our Counsel has advised that there is only a remote possibility that these proceedings will have a material adverse impact on our consolidated financial position or results of operations of the Company.

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b) Tax claim in Bolivia

On November 3, 2006 and April 25, 2007, the Bolivian Tax Authority ("Departamento de Inteligencia Fiscal de la Gerencia Nacional de Fiscalización") issued a notice in the Bolivian press advising that UABL International S.A. would owe taxes to that authority. On June 18, 2007, legal counsel in Bolivia submitted points of defense to the Bolivian tax authorities.

On August 27, 2007 the Bolivian tax authorities gave notice of a resolution determining the taxes (value added tax, transaction tax and income tax) that UABL International S.A. would owe to them in the amount of approximately $5,800 (including interest and fines). On October 10, 2007, legal counsel in Bolivia gave notice to the Bolivian tax authorities of the lawsuit commenced by UABL International S.A. to refute the resolution above mentioned.

On August 1, 2008, UABL International S.A. was served with a notice informing that the Bolivian Tax Authorities had replied to the lawsuit started by us. On August 22, 2008 a hearing and judicial inspection took place at Puerto Quijano, Bolivia. On August 30, 2008 both parties submitted their arguments to the judge, completing this part of the case. On August 12, 2009, UABL International S.A. was served with a judgment of a Bolivian court ruling on certain taxes allegedly due by UABL International S.A. On August 22, 2009, UABL International S.A. submitted an appeal to the lower court judgment to which Bolivian tax authorities have contested. The Court of appeal confirmed the judgment of the Lower Court. UABL International S.A. has submitted a cassation appeal (an appeal on points of law) which is currently pending before the Bolivian Supreme Court.

On June 26, 2008, the same Bolivian court ordered a preemptive embargo against all barges owned by UABL International S.A. that may be registered in the International Bolivian Registry of Ships, or RIBB. According to Company's local counsel this preemptive embargo under Bolivian law has no effect over the Company's right to use its assets nor does it have any implication over the final decision of the court, the substance of the matter and in this case it is ineffective since UABL International S.A. did not have any assets owned by it registered in the RIBB. Moreover, UABL International S.A. had challenged the judge's decision to place the embargo. On November 15, 2008, the lower court reconfirmed the embargo. UABL International S.A. appealed the decision of the lower court, which was later reconfirmed by a higher court. The shares of UABL International S.A. have ceased to belong to our Company and we have been advised by legal counsel that there is only a remote possibility that we would finally be found liable for any of these taxes or fines and / or that these proceedings will have financial material adverse impact on the consolidated financial position or results of operations of the Company.

c) Lease obligations

The Company and its subsidiaries lease buildings for office spaces and a ship repair facility under various operating leases, which expire from 2012 to 2016 and which generally have renewal options at similar terms. Rental expense under continuing obligations for the three years ended December 31, 2011 was $1,119, $1,048 and $891, respectively. At December 31, 2011, obligations under the companies' operating leases for office spaces and a ship repair facility with initial or remaining lease terms longer than one year were as follows:

Year ending December 31		
2012	$	1,361
2013		1,060
2014		709
2015		231

2016		68
Total	$	3,429

On April 6, 2008 we entered into a three-year bareboat charter for an 11,299 dwt, 2006 built product tanker, the M/T Austral which was extended for minimum 35 and maximum 37 months commencing on December 1, 2010. The minimum obligations for the remaining term subsequent to December 31, 2011 are $1,551 in 2012 and $1,292 in 2013. On March 25, 2009 we entered into a one-year bareboat charter for a 5,706 dwt, 2008 built product tanker, the M/T Mediator which was re-delivered to her owner on October 6, 2010. Rent expense for the three years ended December 31, 2011 was $1,557, $4,940 and $4,808, respectively. When cash rental payments are not made on a straight–line basis, we recognize variable rental expense on a straight – line basis over the lease term.

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d) Charters-out

The future minimum revenues, before reduction for brokerage commissions, expected to be received on time charter agreements of our eight PSVs in our Offshore Supply Business chartered seven in South America and one in North Sea, which terms are longer than one year were as follows:

Year ending December 31		
2012	$	73,012
2013		22,076
2014		10,623
2015		1,942
Total	$	107,653

The future minimum revenues, before reduction for brokerage commissions of three of our handy size-small product tanker vessels (one of them leased) in our Ocean Business chartered in South America, expected to be received on time charter agreements, which terms are longer than one year were as follows:

Year ending December 31		
2012	$	21,152
2013		13,591
2014		4,965
Total	$	39,708

Revenues from time charter agreements are generally not received when a vessel, is off-hire, which includes time required for normal periodic maintenance of the vessel. In arriving at the minimum future charter revenues, an estimated time off-hire to perform periodic maintenance on each vessel has been deducted, although there is no assurance that such estimate will be reflective of the actual off-hire in the future. The scheduled future minimum revenues should not be construed to reflect total shipping revenues for any of the periods.

e) Other

At December 31, 2011, we employed several employees as crew on our vessels, land-based employees and shipyard workers. These seafarers and shipyard workers are covered by industry-wide collective bargaining agreements that set basic standards applicable to all companies who hire such individuals in these industries. Because most of our employees are covered by these industry-wide collective bargaining agreements, failure of industry groups to renew these agreements may disrupt our operations and adversely affect our earnings. In addition, we cannot assure that these agreements will prevent labor interruptions. While we have had no significant labor interruption in the past we do not believe any labor interruptions will disrupt our operations and harm our financial performance.

On our River Business, different degrees of unionization of our employees and crewmembers may lead to a change or leveling of such unionization, which could result in higher costs for us, thus affecting our results of operations. Furthermore, due to the unionized nature of our activity in South America, while in the process of negotiating such

leveling, our operations may be affected by strikes in our River and Ocean businesses, causing us to suffer delays due to lack of the necessary crewing onboard our pushboats and ocean vessels. In our barge building facility at Punta Alvear, our workforce is also mainly unionized and negotiations over wages and conditions may have very little bearing on negotiations we have with our other employees and crew members.

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9. INCOME TAXES

The Company operates through its subsidiaries, which are subject to several tax jurisdictions, as follows:

a) Bahamas

The earnings from shipping operations were derived from sources outside the Bahamas and such earnings were not subject to Bahamian taxes.

b) Panama

The earnings from shipping operations were derived from sources outside Panama and such earnings were not subject to Panamanian taxes.

c) Paraguay

Our subsidiaries in Paraguay are subject to Paraguayan corporate income taxes.

d) Argentina

Our subsidiaries in Argentina are subject to Argentine corporate income taxes.

In Argentina, the tax on minimum presumed income ("TOMPI"), supplements income tax since it applies a minimum tax on the potential income from certain income generating-assets at a 1% tax rate. The Companies' tax obligation in any given year will be the higher of these two tax amounts. However, if in any given tax year TOMPI exceeds income tax, such excess may be computed as payment on account of any excess of income tax over TOMPI that may arise in any of the ten following years.

e) Brazil

Our subsidiaries in Brazil are subject to Brazilian corporate income taxes.

Income taxes in Brazil include federal income tax and social contribution (which is an additional federal income tax). Income tax is computed at the rate of 15%, plus a surtax of 10% on the amount that exceeds Brazilian reais 240,000 (equivalent to $129 at December 31, 2011) based on pretax income, adjusted for additions and exclusions established by the Brazilian tax legislation. Social contribution is calculated at the rate of 9%, on pretax income, in conformity with the tax law.

UP Offshore Apoio Maritimo Ltda., has foreign currency exchange gains recognized for tax purposes only in the period the debt (including intercompany transactions) is extinguished. A deferred income tax liability is recognized in the period the foreign currency exchange rate changes equal to the future taxable income at the applicable tax rate.

f) Chile

Our subsidiary in the Ocean Business, Corporación de Navegación Mundial S.A. (Cor.Na.Mu.S.A.) is subject to Chilean corporate income taxes.

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g) United Kingdom (UK)

Our subsidiary in the Offshore Supply Business, UP Offshore (UK) Limited, is not subject to corporate income tax in the United Kingdom, rather, it qualifies under UK tonnage tax rules and pays a flat rate based on the net tonnage of qualifying PSVs.

h) United States of America (US)

Under the U.S. Internal Revenue Code of 1986, as amended, or the Code, 50% of the gross shipping income of our vessel owning or chartering subsidiaries attributable to transportation that begins or ends, but that does not both begin and end, in the U.S. are characterized as U.S. source shipping income. Such income is subject to 4% U.S. federal income tax without allowance for deduction, unless our subsidiaries qualify for exemption from tax under Section 883 of the Code and the Treasury Regulations promulgated thereunder.

For the three years ended December 31, 2011, our subsidiaries did not derive any US source shipping income. Therefore our subsidiaries are not subject to any U.S. federal income taxes, except our ship management services provided by Ravenscroft.

Income tax expense (benefit) from continuing operations (which includes TOMPI) is comprised of:

	For the years ended December 31,		
	2011	2010	2009
Current income tax expense	$1,904	$4,529	$1,352
Deferred income tax expense (benefit)	(3,641)	1,834	4,003
	$(1,737)	$6,363	$5,355

Ultrapetrol's pre-tax income for the three years ended December 31, 2011 was taxed in foreign jurisdictions (principally Argentina, Brazil and Paraguay).

The table below shows for each jurisdiction's total income tax expense and statutory tax rate:

	For the years ended December 31,		
	2011	2010	2009
Brazil (34%)	$-	$1,723	$1,062
Argentina (35%)	1,110	623	129
Paraguay (10%)	403	1,725	153
Others	391	458	8
Current income tax expense	1,904	4,529	1,352
Deferred income tax expense (benefit)	(3,641)	1,834	4,003
Income tax expense (benefit)	$(1,737)	$6,363	$5,355

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Reconciliation of income tax expense (benefit) to taxes calculated based on the statutory tax rate is as follows:

	For the years ended December 31,		
	2011	2010	2009
(Loss) income from continuing operations before income taxes	$ (19,972)	$ 1,958	$ (32,442)
Sources not subject to income tax	20,835	8,609	28,035
	863	10,567	(4,407)
Tax rate	35 %	35 %	35 %
Tax expense (benefit) at statutory tax rate	302	3,698	(1,542)
Rate differential	(184)	(306)	(442)
Increase in valuation allowance	197	1,215	446
Effects of foreign exchange changes related to our foreign subsidiaries	(4,020)	1,174	5,768
Others	1,968	582	1,125
Income tax expense (benefit)	$ (1,737)	$ 6,363	$ 5,355

The Company's deferred income tax assets have been reduced by intercompany profits from the sale of river barges within the group and deferred. The Company deferred income tax expense in Argentina in 2011 amounted $4,630, which were reflected as non-current assets and recognized as income tax expense as the river barges are consumed through depreciation.

At December 31, 2011, Argentinean subsidiaries had a consolidated credit related to TOMPI of $3,861 ($167 current and $3,694 noncurrent) that expires from 2012 through 2021. At December 31, 2011, Argentinean subsidiaries had accumulated benefit from tax loss carryforwards ("NOLs") for a consolidated total of $833 that expire in (2012 through 2016). The Company believes it is more likely than not that the Company's subsidiaries NOLs and TOMPI credit, with exception of $804 of NOLs and $542 of TOMPI credit, will be utilized through the turnaround of existing temporary differences, future taxable income, tax strategies or a combination thereof.

As of December 31, 2011, the valuation allowance for deferred tax assets is reduced from $1,661 in 2010 to $1,346 in 2011. The decrease is a result of the reduction of deferred tax asset due to utilization of tax loss carryforwards in Argentina in 2011.

At December 31, 2011, the Brazilian subsidiaries had benefit from NOLs for a consolidated total of $1,262 that do not expire but the usage is limited to 30% of the taxable income in any year.

The components of net deferred income tax liabilities included on the balance sheets were as follows:

	At December 31,	
	2011	2010
Deferred income tax assets		
Other, deferred income tax current assets	$286	$153
NOLs	2,339	5,074
TOMPI credit	3,694	3,469
Other	3,453	2,422

Total deferred income tax noncurrent assets	9,486	10,965
Valuation allowance of deferred income tax assets	(1,346)	(1,661)
Net deferred income tax noncurrent assets	8,140	9,304
Deferred income tax liabilities		
Vessels and equipment, net	11,292	8,339
Intangible assets	332	391
Unrealized exchange differences	3,851	7,120
Other	263	292
Total deferred income tax noncurrent liabilities	15,738	16,142
Net deferred income tax liabilities	$(7,312)	$(6,685)

As of January 1, 2011 and 2010, and for the years ended December 31, 2011 and 2010, the Company did not have any unrecognized tax positions. In addition, the Company does not expect to hold unrecognized tax positions within the next twelve months. Furthermore, the Company has elected to classify interest and penalties related to unrecognized tax positions, if and when required, as part of financial and operating expenses, respectively, in the consolidated statements of operations. For the years ended December 31, 2011 and 2010, the Company has no accrued interest and penalties related to unrecognized tax positions.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

10. RELATED PARTY TRANSACTIONS

At December 31, 2011 and 2010, the balances of current receivables from related parties were $57 and $150, and balances of current payable to related parties were $1,158 and $190, respectively.

At December 31, 2011 and 2010 the balances of noncurrent receivables from related parties were as follows:

	At December 31,	
	2011	2010
Puertos del Sur S.A. and OTS S.A. (1)	$6,478	$5,378

(1) Includes $2,280, which corresponds to a loan that accrues interest at a nominal interest rate of 7% per year, payable semi-annually.

Voyage expenses paid to related parties

For the three years ended December 31, 2011, the voyage expenses paid to related parties were as follows:

	For the years ended December 31,		
	2011	2010	2009
Commercial commissions (1)	$1,147	$1,101	$448
Agency fees (2)	3,475	441	171
Total	$4,622	$1,542	$619

(1) Commercial commissions

Pursuant to a commercial agreement signed between UP Offshore (Bahamas) Ltd. (our subsidiary in the Offshore Supply Business) and Firmapar Corp. (formerly Comintra), a minority shareholder of this, the parties agreed that Firmapar Corp. charges a 2% of the gross time charters revenues from Brazilian charters collected by UP Offshore (Bahamas) Ltd. on a consolidated basis beginning on June 25, 2003 and ending on June 25, 2013.

(2) Agency fees

Pursuant to a commercial and an agency agreement with Ultrapetrol S.A., UABL S.A. and Ravenscroft, Shipping Services Argentina S.A. (formerly I. Shipping Service S.A.) and Navalia S.A. companies of the same control group as Inversiones Los Avellanos S.A., have agreed to perform the duties of port agent for us in Argentina.

Operations in OTS S.A.'s terminal

UABL Paraguay, our subsidiary in the River Business, operates the terminal that pertains to OTS S.A., a 50% owned company.

For the three years ended December 31, 2011, UABL Paraguay S.A. paid to OTS S.A. $1,057, $991 and $1,023, respectively, for this operation.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

11. SHARE CAPITAL

Common shares and shareholders

On September 21, 2006, Inversiones Los Avellanos S.A., Hazels (Bahamas) Investments Inc. and Solimar Holdings Ltd. (collectively the "Original Shareholders") signed a second amended and restated shareholders agreement. The shares held directly by our Original Shareholders expressly are entitled to seven votes per share and all other holders of our common stock are entitled to one vote per share. The special voting rights of the Original Shareholders are not transferable, unless to another Original Shareholder.

On July 15, 2010, Solimar Holdings Ltd. sold to Hazels (Bahamas) Investments Inc. both Original Shareholders and shareholders of the Company before of our initial public offering 2,977,690 shares of Ultrapetrol common stock.

At December 31, 2011, the outstanding common shares are 30,011,628 par value $.01 per share.

At December 31, 2011 our shareholders Inversiones Los Avellanos S.A. and Hazels (Bahamas) Investments Inc. (a wholly owned subsidiary of Inversiones Los Avellanos S.A.) hold 4,735,517 and 3,128,568, respectively, which represent 15.8% and 10.4%, respectively. The joint voting power for these shares represents 71.0% of the total voting power and is combined pursuant to an agreement between the Original Shareholders who have agreed to vote their respective shares together in all matters where a vote of Ultrapetrol (Bahamas) Limited's shareholders is required.

Inversiones Los Avellanos S.A. and Hazels (Bahamas) Investments Inc. are controlled by members of the Menendez family, including Felipe Menendez R., our president, chief executive officer and a director, and Ricardo Menendez R., our executive vice president and a director. As such, they have the ability to exert influence over the operations of the Company.

On January 28, 2011 the shareholders of the Company at a Special General Meeting approved the issuance of up to 13,100,000 shares of common stock if and when holders of the Company's $80,000 7.25% Convertible Senior Notes due 2017 elect to convert their notes pursuant its term. The conversion rate of the Convertible Notes, which is subject to adjustment, shall not exceed 163.1321 shares of common stock per $1 principal amount.

2008 Share repurchase program

Ultrapetrol's Board of Directors has approved a share repurchase program, effective March 17, 2008, for up to a total of $50,000 of the Company's common stock through December 31, 2008. The expiration date of the share repurchase program was extended by the Board of Directors until September 30, 2009, when it finally expired.

At December 31, 2011 the Company had repurchased a total of 3,923,094 common shares, at a total cost of $19,488.

2011 Share repurchase program

Ultrapetrol's Board of Directors has approved a share repurchase program, effective October 24, 2011, for up to a total of $20,000 of the Company's common stock through April 30, 2012. Share repurchases may be made by the Company and certain of its affiliates from time to time in open market transactions at prevailing market prices or in privately negotiated transactions.

During the year ended December 31, 2011, the Company did not acquire any common share.

Registration rights agreement

On September 21, 2006, prior to its initial public offering the Company entered into a registration rights agreement with Inversiones Los Avellanos S.A., Hazels (Bahamas) Investments Inc. and Solimar Holdings Ltd., its shareholders of record immediately prior to the initial public offering, pursuant to which the Company has granted them and certain of their transferees, the right, under certain circumstances and subject to certain restrictions, including any applicable lock-up agreements then in place, to require the Company to register under the Securities Act shares of its common stock held by them. Under the registration rights agreement, these persons will have the right to request the Company to register the sale of shares held by them on their behalf and may also require to make available shelf registration statements permitting sales of shares into the market from time to time over an extended period. In addition, these persons will have the ability to exercise certain piggyback registration rights in connection with registered offerings requested by shareholders or initiated by the Company.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

12. SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

Interest and income taxes paid for the three years ended December 31, 2011, from continuing operations were as follows:

	For the years ended December 31,		
	2011	2010	2009
Interest paid	$26,866	$21,750	$21,983
Income taxes paid	316	100	38

13. BUSINESS AND GEOGRAPHIC SEGMENT INFORMATION

The Company organizes its business and evaluates performance by its operating segments, Ocean, River and Offshore Supply Business. The accounting policies of the reportable segments are the same as those for the consolidated financial statements (Note 2). The Company does not have significant intersegment transactions. These segments and their respective operations are as follows:

River Business: In our River Business, we own and operate several dry and tanker barges, and push boats. In addition, we use one barge from our ocean fleet, the Alianza G2, as a transfer station. The dry barges transport basically agricultural and forestry products, iron ore and other cargoes, while the tanker barges carry petroleum products, vegetable oils and other liquids.

We operate our pushboats and barges on the navigable waters of Parana, Paraguay and Uruguay Rivers and part of the River Plate in South America, also known as the Hidrovia region.

The company also has a shipyard that should promote organic growth and from time to time made external sales.

Offshore Supply Business: We operate our Offshore Supply Business, using PSVs owned by UP Offshore (Bahamas), which seven are employed in the Brazilian market and one in the North Sea. PSVs are designed to transport supplies such as containerized equipment, drill casing, pipes and heavy loads on deck, along with fuel, water, drilling fluids and bulk cement in under deck tanks and a variety of other supplies to drilling rigs and platforms.

Ocean Business: In our Ocean Business, we operate eight oceangoing vessels: four product tankers (one of which is on lease to us), two container feeder vessels under a container line service in Argentina cabotage trade, one oceangoing tug and one tank barge under the trade name Ultrapetrol. Our Handy size/small product tanker vessels transport liquid bulk goods such as petroleum and petroleum derivatives on major trade routes around the globe.

All of the Company's operating revenues were derived from its foreign operations. The following represents the Company's revenues attributed by geographical region in which services are provided to customers.

	For the years ended December 31,		
	2011	2010	2009
Revenues (1)			

–South America	$267,420	$199,585	$127,378
–Europe	19,910	19,923	69,546
–Central America	16,499	5,624	3,525
–Asia	426	4,094	18,123
–Other	227	1,219	1,957
	$304,482	$230,445	$220,529

(1) Classified by country of domicile of charterers.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company's vessels are highly mobile and regularly and routinely moved between countries within a geographical region of the world. In addition, these vessels may be redeployed among the geographical regions as changes in market conditions dictate. Because of this mobility, long-lived assets, primarily vessels and equipment cannot be allocated to any one country.

The following represents the Company's vessels and equipment based upon the assets' physical location as of the end of each applicable period presented:

	At December 31,	
	2011	2010
Vessels and equipment, net		
–South America	$572,512	$504,200
–Europe	26,571	-
–Asia	68,149	104,225
–Other	4,213	4,271
	$671,445	$612,696

For the year ended December 31, 2011, 87% of the Company's revenues are concentrated in South America and at December 31, 2011, 85% of the Company's vessels and equipment are located in South America.

For the year ended December 31, 2011 revenues from charterers domiciled in Argentina, Brazil, Uruguay and Paraguay represented 29%, 25%, 20% and 12%, of the Company's consolidated revenues, respectively.

For the year ended December 31, 2010 revenues from charterers domiciled in Argentina, Brazil, Uruguay and Paraguay represented 30%, 27%, 13% and 19%, of the Company's consolidated revenues, respectively.

For the year ended December 31, 2009 revenues from charterers domiciled in Argentina and Brazil represented 20% and 16% of the Company's consolidated revenues, respectively.

As a result, the Company's financial condition and results of operations depend, to a significant extent, on macroeconomic, regulatory and political conditions prevailing in South America.

Revenue by segment consists only of services provided to external customers, as reported in the consolidated statement of operations. Resources are allocated based on segment profit or loss from operation, before interest and taxes.

Identifiable assets represent those assets used in the operations of each segment.

The following schedule presents segment information about the Company's operations for the year ended December 31, 2011:

	River Business	Offshore Supply Business	Ocean Business	Total

Revenues	$174,594	$64,606	$65,282	$304,482
Running and voyage and manufacturing expenses	132,719	38,852	53,036	224,607
Depreciation and amortization	20,139	9,436	9,569	39,144
Segment operating (loss) profit	13,138	10,999	(4,753)	19,384
Segment assets	392,549	263,094	124,527	780,170
Investments in and receivables from affiliates	6,595	-	256	6,851
Loss from investment in affiliates	(1,042)	-	(31)	(1,073)
Additions to long-lived assets (1)	73,265	19,502	3,345	96,112

(1) Excludes $1,751, which corresponds to additions to corporate assets.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following schedule presents segment information about the Company's operations for the year ended December 31, 2010:

	River Business	Offshore Supply Business	Ocean Business	Total
Revenues	$120,024	$54,283	$56,138	$230,445
Running and voyage and manufacturing expenses	80,702	29,637	40,583	150,922
Depreciation and amortization	17,248	7,178	9,945	34,371
Segment operating (loss) profit	10,244	10,611	(2,137)	18,718
Segment assets	351,388	245,865	104,334	701,587
Investments in and receivables from affiliates	6,537	-	287	6,824
Loss from investment in affiliates	(322)	-	(19)	(341)
Additions to long-lived assets	67,942	7,141	30,164	105,247

The following schedule presents segment information about the Company's operations for the year ended December 31, 2009:

	River Business	Offshore Supply Business	Ocean Business	Total
Revenues	$79,477	$35,419	$105,633	$220,529
Running and voyage and manufacturing expenses	65,851	21,341	53,415	140,607
Depreciation and amortization	13,904	5,903	21,945	41,752
Segment operating (loss) profit	(9,651)	930	(330)(2)	(9,051)
Segment assets	249,760	238,368	173,305	661,433
Investments in and receivables from affiliates	6,484	-	306	6,790
Income (Loss) from investment in affiliates	(48)	-	20	(28)
Additions to long-lived assets	38,817	43,566	7,712	90,095

(2) Includes an impairment charge for Princess Marisol of $25,000.

Reconciliation of total assets of the segments to amount included in the consolidated balance sheets were as follow:

	At December 31, 2011	2010
Total assets for reportable segments	$780,170	$701,587
Other assets	16,021	16,640
Corporate cash and cash equivalents	34,096	105,570
Consolidated total assets	$830,287	$823,797

For the year ended December 31, 2011 revenues from one customer of Ultrapetrol Ocean and Offshore Supply Business represented $86,400 or 28% of the Company' s consolidated revenues and revenues from one customer of Ultrapetrol River Business represented $60,200 or 20% of the Company's consolidated revenues.

For the year ended December 31, 2010 revenues from one customer of Ultrapetrol Ocean and Offshore Supply Business represented $75,200 or 33% of the Company's consolidated revenues and revenues from one customer of Ultrapetrol River Business represented $50,400 or 22% of the Company's consolidated revenues.

For the year ended December 31, 2009 revenues from one customer of Ultrapetrol Ocean and Offshore Supply Business represented $41,400 or 19% of the Company's consolidated revenues and revenues from one customer of Ultrapetrol River Business represented $24,000 or 11% of the Company's consolidated revenues.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

14. STOCK COMPENSATION

We have adopted the 2006 Stock Incentive Plan, or the 2006 Plan, dated July 20, 2006 which entitles certain of our officers, key employees and directors to receive restricted stock, stock appreciation rights, stock options, dividend equivalent rights, unrestricted stock, restricted stock units or performance shares. Under the 2006 Plan, a total of 5,000,000 shares of common stock have been reserved for issuance. The 2006 Plan is administered by our Board of Directors. Under the terms of the 2006 Plan, our Board of Directors is able to grant new options exercisable at a price per share to be determined by our Board of Directors. Under the terms of the 2006 Plan, no options would be able to be exercised until at least one year after the closing of our IPO (October 18, 2006). Any shares received on exercise of the options would not be able to be sold until one year after the date of the stock option grant. All options will expire ten years from the date of grant. The 2006 Plan expires ten years from the closing of our IPO.

In addition, on July 20, 2006 we entered into separate consulting agreements that became effective upon completion of our IPO (October 18, 2006) with companies controlled by our chief executive officer, executive vice president, chief financial officer and chief financial accountant for work they perform for us in various different jurisdictions. On October 29, 2009 the consulting agreements were renewed for a three-year period.

In connection with the new consulting agreements, in 2009, the Company awarded a total of 329,375 shares of restricted common stock at no cost to three companies controlled by our chief executive officer, executive vice president and chief financial officer. These shares are non-transferable until they vest, which occurs at the end of the three-year period. During the vesting period, the shares have voting rights and cash dividends will be paid if declared. The fair market value of each share on the grant date was $5.11.

In 2009, the Company granted a total of 329,375 shares of restricted common stock at no cost to three companies controlled by our chief executive officer, executive vice president and chief financial officer with performance periods of January 1, 2010 through December 31, 2010; January 1, 2011 through December 31, 2011; and January 1, 2012 to December 31, 2012. At the end of each performance period,

the number of shares of stock subject to the awards is determined by comparing the EBITDA achieved during the period to the EBITDA contained in the Company's annual budget adjusted in accordance with the disinterested members of the Board of Directors if deemed necessary. These performance based stock awards are also subject to continued employment.

In connection with the consulting agreements signed in 2006, the Company awarded a total of 310,000 shares of restricted common stock at no cost to two companies, one of which is controlled by our chief executive officer and the other by our executive vice president, which were fully vested. The fair market value of each share on the grant date was $11.00.

On November 29, 2010, 12,689 shares were granted to a non-employee director. These shares are non-transferable until they vest, which occurs in annual installments of 1,015, 5,837 and 5,837 shares on October 13, 2011, December 5, 2011 and 2012, respectively. The fair market value of each share on the grant date was $6.83.

On December 5, 2009 the Company granted a total of 97,164 shares of restricted common stock at no cost to its non-employee directors. These shares are non-transferable until they vest, which occurs over a three year period. During the vesting period, the shares have voting rights and cash dividends will be paid if declared. The fair market value of each share on the grant date was $4.92.

During 2010, 39,136 shares were fully forfeited since the resignation of two non-employee directors.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
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On December 5, 2006, the Company granted a total of 36,952 shares of restricted common stock at no cost to its non-employee directors which were all vested on December 5, 2009. The fair market value of each share on the grant date was $12.99.

Activity with respect to restricted common stock is summarized as follows:

	For the years ended December 31,		
	2011	2010	2009
Nonvested shares outstanding at January 1	703,827	755,914	115,652
Granted	-	12,689	755,914
Vested	(23,046)	(25,640)	(112,830)
Forfeited	-	(39,136)	(2,822)
Nonvested shares outstanding at December 31	680,781	703,827	755,914

Total stock based compensation expense as a result of all of these grants was $1,079 in 2011, $1,266 in 2010 and $1,163 in 2009 ($402 in 2011 and $576 in 2010 related with the performance based restricted common stock), and is recorded in the same line item as cash compensation. The unrecognized compensation cost at December 31, 2011 was $1,269 and the weighted average remaining life for unrecognized compensation was 0.8 years. A portion of this expense is subject to achievement of the EBITDA for the performance based restricted common stock.

In addition, in 2006 the Company awarded to three companies, one of which is controlled by our chief executive officer, one by our executive vice president and the other by our chief financial officer, stock options to purchase a total of 348,750 shares of common stock at an exercise price of $11.00 per share. These stock options vest ratably over a three-year period and expire ten years from the date of grant and are fully vested. The fair value of the options granted was estimated on the date of grant using the Black-Scholes option pricing model.

There is no activity during 2011, 2010 and 2009 with respect to the Company's stock options.

Outstanding options at December 31, 2011 had an aggregate intrinsic value less than the aggregate strike price for those options based on the market price of $2.98 per share at that date. At December 31, 2011, 348,750 stock options are outstanding, with an exercise price of $11.00 per share and have a remaining contractual life of 4.8 years.

Total stock based compensation expense related to the stock options was $0 in 2011 and 2010 and $374 in 2009 and is recorded in the same line items as cash compensation.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

15. DISCONTINUED OPERATIONS

During 2008, the Company decided to discontinue its operations in the Passenger Business.

On February 5, 2010, the Blue Monarch was sold and delivered to her new owner for $1,950, with no impact in earnings.

For all periods presented the Passenger Business operations have been reported as discontinued operations net of income taxes.

The impact of discontinued operations on net (loss) per share of Ultrapetrol (Bahamas) Limited in all periods presented is disclosed in the consolidated statements of operations.

Discontinued operations, net of income taxes consist of the following:

	For the years ended December 31,		
	2011	2010	2009
Running and voyage expenses	$-	$(365)	$(1,252)
Other income (expenses), net	-	(150)	(879)
Loss from discontinued operations	$-	$(515)	$(2,131)

At December 31, 2011 and 2010, assets of discontinued operations are $ nil. At December 31, 2011 and 2010 there are no liabilities of discontinued operations.

16. SUPPLEMENTAL GUARANTOR INFORMATION

On November 24, 2004, the Company issued $180,000 9% First Preferred Ship Mortgage Notes due 2014.

The 2014 Senior Notes are fully and unconditionally guaranteed on a joint and several basis by Company's subsidiaries directly involved in our Ocean and River Business.

The Indenture provides that the 2014 Senior Notes and each of the guarantees granted by Subsidiaries, other than the Mortgage, are governed by, and construed in accordance with, the laws of the state of New York. Each of the mortgaged vessels is registered under either the Panamanian flag, or another jurisdiction with similar procedures. All of the Subsidiary Guarantors are outside of the United States.

Supplemental condensed consolidating financial information for the Guarantor Subsidiaries for the 2014 Senior Notes is presented below. This information is prepared in accordance with the Company's accounting policies. This supplemental financial disclosure should be read in conjunction with the consolidated financial statements.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING BALANCE SHEET

AT DECEMBER 31, 2011
(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Current assets					
Receivables from related parties	$297,324	$101,196	$30,751	$ (429,214)	$ 57
Other current assets	3,773	46,055	56,248	-	106,076
Total current assets	301,097	147,251	86,999	(429,214)	106,133
Noncurrent assets					
Vessels and equipment, net	-	212,324	460,066	(945)	671,445
Investment in affiliates	201,323	-	373	(201,323)	373
Other noncurrent assets	6,825	7,850	63,704	(26,043)	52,336
Total noncurrent assets	208,148	220,174	524,143	(228,311)	724,154
Total assets	$509,245	$367,425	$611,142	$ (657,525)	$ 830,287
Current liabilities					
Payables to related parties	$-	$127,664	$302,708	$ (429,214)	$ 1,158
Current portion of long-term financial debt	-	3,478	18,026	-	21,504
Other current liabilities	4,948	19,223	27,055	-	51,226
Total current liabilities	4,948	150,365	347,789	(429,214)	73,888
Noncurrent liabilities					
Due to affiliates	$-	$26,043	$-	$ (26,043)	$ -
Long-term financial debt net of current portion	260,000	51,522	179,967	-	491,489
Other noncurrent liabilities	-	218	14,521	-	14,739
Total noncurrent liabilities	260,000	77,783	194,488	(26,043)	506,228
Total liabilities	264,948	228,148	542,277	(455,257)	580,116
Equity of Ultrapetrol (Bahamas) Limited	244,297	139,277	68,865	(208,142)	244,297
Noncontrolling interest	-	-	-	5,874	5,874
Total equity	244,297	139,277	68,865	(202,268)	250,171
Total liabilities and equity	$509,245	$367,425	$611,142	$ (657,525)	$ 830,287

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING BALANCE SHEET

AT DECEMBER 31, 2010
(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Current assets					
Receivables from related parties	$279,377	$81,452	$16,887	$ (377,566)	$ 150
Other current assets	42,887	31,024	88,934	-	162,845
Total current assets	322,264	112,476	105,821	(377,566)	162,995
Noncurrent assets					
Vessels and equipment, net	-	189,590	424,109	(1,003)	612,696
Investment in affiliates	210,506	-	1,446	(210,506)	1,446
Other noncurrent assets	8,478	10,343	27,839	-	46,660
Total noncurrent assets	218,984	199,933	453,394	(211,509)	660,802
Total assets	$541,248	$312,409	$559,215	$ (589,075)	$ 823,797
Current liabilities					
Payables to related parties	$-	$109,242	$268,514	$ (377,566)	$ 190
Current portion of long-term financial debt	15,000	-	12,586	-	27,586
Other current liabilities	2,785	17,554	16,562	-	36,901
Total current liabilities	17,785	126,796	297,662	(377,566)	64,677
Noncurrent liabilities					
Long-term financial debt net of current portion	260,000	40,000	171,793	-	471,793
Other noncurrent liabilities	-	1,776	16,757	-	18,533
Total noncurrent liabilities	260,000	41,776	188,550	-	490,326
Total liabilities	277,785	168,572	486,212	(377,566)	555,003
Equity of Ultrapetrol (Bahamas) Limited	263,463	143,837	73,003	(216,840)	263,463
Noncontrolling interest	-	-	-	5,331	5,331
Total equity	263,463	143,837	73,003	(211,509)	268,794
Total liabilities and equity	$541,248	$312,409	$559,215	$ (589,075)	$ 823,797

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

FOR THE YEAR ENDED DECEMBER 31, 2011
(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Revenues	$-	$129,340	$190,630	$ (15,488)	$ 304,482
Operating expenses	(8,490)	(112,238)	(179,800)	15,430	(285,098)
Operating (loss) profit	(8,490)	17,102	10,830	(58)	19,384
Investment in affiliates	(7,886)	-	(1,073)	7,886	(1,073)
Other (expenses) income	(2,429)	(23,212)	(12,642)	-	(38,283)
(Loss) income before income taxes	(18,805)	(6,110)	(2,885)	7,828	(19,972)
Income taxes benefit (expense)	-	1,550	187	-	1,737
(Loss) income from continuing operations	(18,805)	(4,560)	(2,698)	7,828	(18,235)
Loss from discontinued operations	-	-	-	-	-
Net (loss) income	(18,805)	(4,560)	(2,698)	7,828	(18,235)
Net income attributable to noncontrolling interest	-	-	-	570	570
Net (loss) income attributable to Ultrapetrol (Bahamas) Limited	$(18,805)	$(4,560)	$(2,698)	$ 7,258	$ (18,805)

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

FOR THE YEAR ENDED DECEMBER 31, 2010
(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Revenues	$-	$106,014	$133,015	$ (8,584)	$ 230,445
Operating expenses	(8,332)	(89,245)	(122,676)	8,526	(211,727)
Operating (loss) profit	(8,332)	16,769	10,339	(58)	18,718
Investment in affiliates	8,153 (1)	-	(341)	(8,153)	(341)
Other (expenses) income	(5,192)	(1,197)	(10,030)	-	(16,419)
(Loss) income before income taxes	(5,371)	15,572	(32)	(8,211)	1,958
Income taxes benefit (expense)	-	313	(6,676)	-	(6,363)
(Loss) income from continuing operations	(5,371)	15,885	(6,708)	(8,211)	(4,405)
Loss from discontinued operations	-	-	(515)	-	(515)
Net (loss) income	(5,371)	15,885	(7,223)	(8,211)	(4,920)
Net income attributable to noncontrolling interest	-	-	-	451	451
Net (loss) income attributable to Ultrapetrol (Bahamas) Limited	$(5,371)	$15,885	$(7,223)	$ (8,662)	$ (5,371)

(1) Includes a loss of $ 515 related to discontinued operations.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

FOR THE YEAR ENDED DECEMBER 31, 2009
(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Revenues	$-	$130,119	$95,447	$ (5,037)	$ 220,529
Operating expenses	(8,710)	(93,615)	(132,234)	4,979	(229,580)
Operating profit (loss)	(8,710)	36,504	(36,787)	(58)	(9,051)
Investment in affiliates	(31,064) (1)	-	(28)	31,064	(28)
Other income (expenses)	(64)	(15,792)	(7,507)	-	(23,363)
Income (loss) before income taxes	(39,838)	20,712	(44,322)	31,006	(32,442)
Income taxes benefit (expense)	-	1,211	(6,566)	-	(5,355)
Income (loss) from continuing operations	(39,838)	21,923	(50,888)	31,006	(37,797)
Loss from discontinued operations	-	-	(2,131)	-	(2,131)
Net (loss) income	(39,838)	21,923	(53,019)	31,006	(39,928)
Net (loss) attributable to noncontrolling interest	-	-	-	(90)	(90)
Net (loss) income attributable to Ultrapetrol (Bahamas) Limited	$(39,838)	$21,923	$(53,019)	$ 31,096	$ (39,838)

(1) Includes a loss of $2,131 related to discontinued operations.

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF CASH FLOW

FOR THE YEAR ENDED DECEMBER 31, 2011

(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Net (loss)	$(18,235)	$(4,560)	$(2,128)	$ 6,688	$ (18,235)
Loss from discontinued operations	-	-	-	-	-
Adjustments to reconcile net income to net cash provided by operating activities from continuing operations	12,134	21,396	6,165	(6,688)	33,007
Net cash (used in) provided by operating activities from continuing operations	(6,101)	16,836	4,037	-	14,772
Net cash (used in) operating activities from discontinued operations	-	-	(15)	-	(15)
Net cash (used in) provided by operating activities	(6,101)	16,836	4,022	-	14,757
Intercompany sources	(17,947)	(1,322)	(6,774)	26,043	-
Non-subsidiary sources	-	(42,907)	(54,956)	-	(97,863)
Net cash (used in) investing activities	(17,947)	(44,229)	(61,730)	26,043	(97,863)
Intercompany sources	-	26,043	-	(26,043)	-
Non-subsidiary sources	(15,000)	14,963	11,669	-	11,632
Net cash (used in) provided by financing activities	(15,000)	41,006	11,669	(26,043)	11,632
Net increase (decrease) in cash and cash equivalents	$(39,048)	$13,613	$(46,039)	$ -	$ (71,474)

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF CASH FLOW

FOR THE YEAR ENDED DECEMBER 31, 2010
(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Net (loss) income	$(4,920)	$13,169	$5,307	$ (18,476)	$ (4,920)
Loss from discontinued operations	-	-	515	-	515
Adjustments to reconcile net income to net cash provided by operating activities from continuing operations	(1,601)	(2,539)	10,913	18,476	25,249
Net cash (used in) provided by operating activities from continuing operations	(6,521)	10,630	16,735	-	20,844
Net cash (used in) operating activities from discontinued operations	-	-	(1,950)	-	(1,950)
Net cash (used in) provided by operating activities	(6,521)	10,630	14,785	-	18,894
Intercompany sources	(60,822)	(16,189)	-	77,011	-
Non-subsidiary sources	-	(3,850)	(52,239)	-	(56,089)
Net cash (used in) investing activities from continuing operations	(60,822)	(20,039)	(52,239)	77,011	(56,089)
Net cash provided by investing activities from discontinued operations	-	-	1,950	-	1,950
Net cash (used in) investing activities	(60,822)	(20,039)	(50,289)	77,011	(54,139)
Intercompany sources	-	-	77,011	(77,011)	-
Non-subsidiary sources	75,281	-	12,333	-	87,614
Net cash provided by financing activities	75,281	-	89,344	(77,011)	87,614
Net increase (decrease) in cash and cash equivalents	$7,938	$(9,409)	$53,840	$ -	$ 52,369

ULTRAPETROL (BAHAMAS) LIMITED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF CASH FLOW

FOR THE YEAR ENDED DECEMBER 31, 2009
(stated in thousands of U.S. dollars)

	Parent	Combined subsidiary guarantors	Combined subsidiary non guarantors	Consolidating adjustments	Total consolidated amounts
Net (loss) income	$(39,928)	$22,079	$(53,265)	$ 31,186	$ (39,928)
Loss from discontinued operations	-	-	2,131	-	2,131
Adjustments to reconcile net income to net cash provided by operating activities from continuing operations	32,907	4,599	70,156	(31,186)	76,476
Net cash (used in) provided by operating activities from continuing operations	(7,021)	26,678	19,022	-	38,679
Net cash provided by operating activities from discontinued operations	-	-	37	-	37
Net cash (used in) provided by operating activities	(7,021)	26,678	19,059	-	38,716
Intercompany sources	(36,476)	(12,737)	-	49,213	-
Non-subsidiary sources	-	(13,538)	(70,060)	-	(83,598)
Net cash (used in) investing activities from continuing operations	(36,476)	(26,275)	(70,060)	49,213	(83,598)
Intercompany sources	(54)	-	49,267	(49,213)	-
Non-subsidiary sources	(125)	44	(7,695)	-	(7,776)
Net cash (used in) provided by financing activities from continuing operations	(179)	44	41,572	(49,213)	(7,776)
Net (decrease) increase in cash and cash equivalents	$(43,676)	$447	$(9,429)	$ -	$ (52,658)

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING

To the Board of Directors of
ULTRAPETROL (BAHAMAS) LIMITED:

We have audited Ultrapetrol (Bahamas) Limited's internal control over financial reporting as of December 31, 2011, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Ultrapetrol (Bahamas) Limited's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying "Management's Annual Report on Internal Control over Financial Reporting". Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States of America). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Ultrapetrol (Bahamas) Limited maintained, in all material respects, effective internal control over financial reporting at December 31, 2011, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States of America), the consolidated balance sheets of Ultrapetrol (Bahamas) Limited and subsidiaries at December 31, 2011 and 2010, and the related consolidated statements of operations, changes in equity and cash flows for each of

the three years in the period ended December 31, 2011 of Ultrapetrol (Bahamas) Limited and subsidiaries and our report dated March 15, 2012 expressed an unqualified opinion thereon.

Buenos Aires, Argentina
March 15, 2012

/S/ PISTRELLI, HENRY MARTIN Y ASOCIADOS S.R.L.
Member of Ernst & Young Global

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors of
ULTRAPETROL (BAHAMAS) LIMITED:

We have audited the accompanying consolidated balance sheets of Ultrapetrol (Bahamas) Limited and subsidiaries at December 31, 2011 and 2010, and the related consolidated statements of operations, changes in equity and cash flows for each of the three years in the period ended December 31, 2011. 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 (United States of America). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Ultrapetrol (Bahamas) Limited and subsidiaries at December 31, 2011 and 2010, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2011, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States of America), Ultrapetrol (Bahamas) Limited's internal control over financial reporting at December 31, 2011, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 15, 2012 expressed an unqualified opinion thereon.

Buenos Aires, Argentina
March 15, 2012

/S/ PISTRELLI, HENRY MARTIN Y ASOCIADOS S.R.L.
Member of Ernst & Young Global

Item 19 – EXHIBIT INDEX

Exhibit Number	Description
1.1	Fifth Amended and Restated Articles of Association of Ultrapetrol (Bahamas) Limited.*
1.2	Second Amended and Restated Memorandum of Association of Ultrapetrol (Bahamas) Limited**
1.3	Articles of Incorporation (English translation) and By-laws of Baldwin Maritime Inc.***
1.4	Articles of Incorporation (English translation) and By-laws of Bayham Investments S.A.***
1.5	Articles of Incorporation (English translation) and By-laws of Cavalier Shipping Inc.***
1.6	Bylaws (English translation) of Corporacion De Navegacion Mundial S.A.***
1.7	Articles of Incorporation (English translation) and By-laws of Danube Maritime Inc.***
1.8	Articles of Incorporation and By-laws of General Ventures Inc.***
1.9	Articles of Incorporation (English translation) and By-laws of Imperial Maritime Ltd. (Bahamas) Inc.***
1.10	Articles of Incorporation (English translation) and By-laws of Kattegat Shipping Inc.***
1.11	Memorandum of Association and Articles of Association of Kingly Shipping Ltd.***
1.12	Memorandum of Association and Articles of Association of Majestic Maritime Ltd.**
1.13	Articles of Incorporation and Bylaws of Massena Port S.A. (English translation)***
1.14	Memorandum of Association and Articles of Association of Monarch Shipping Ltd.***
1.15	Memorandum of Association and Articles of Association of Noble Shipping Ltd.***
1.16	Articles of Incorporation (English translation) and Bylaws (English translation) of Oceanpar S.A.***
1.17	Articles of Incorporation (English translation) and By-laws of Oceanview Maritime Inc.***
1.18	Articles of Incorporation and Bylaws of Parfina S.A. (English translation)***
1.19	Articles of Incorporation (English translation) and By-laws of Parkwood Commercial Corp.***
1.20	Articles of Incorporation (English translation) and By-laws of Princely International Finance Corp.***
1.21	Memorandum of Association (English translation) and Articles of Association of Regal International Investments S.A.***
1.22	Articles of Incorporation (English translation) and By-laws of Riverview Commercial Corp.***
1.23	Memorandum of Association and Articles of Association of Sovereign Maritime Ltd.***
1.24	Articles of Incorporation (English translation) and By-laws of Stanmore Shipping Inc.***
1.25	Articles of Incorporation (English translation) and By-laws of Tipton Marine Inc.***
1.26	Articles of Incorporation (English translation) and By-laws of Ultrapetrol International S.A.***
1.27	Articles of Incorporation and Bylaws of Ultrapetrol S.A. (English translation)***
1.28	Memorandum of Association and Articles of Association of UP Offshore (Holdings) Ltd.***
2.1	Form of Global Exchange Notes (attached as Exhibit A to Exhibit 4.3).***
2.2	Registration Rights Agreement dated November 10, 2004.***
2.3	Indenture dated November 24, 2004.***
2.4	Form of Subsidiary Guarantee (attached as Exhibit F to Exhibit 10.4).***

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4.1	Stock Purchase Agreement dated March 21, 2006 by and between Ultrapetrol (Bahamas) Limited and LAIF XI, LTD****
4.2	Stock Purchase Agreement dated March 20, 2006 by and among Ultrapetrol (Bahamas) Limited, Crosstrade Maritime Inc, and Crosstrees Maritime Inc.****
4.3	Loan agreement dated as of September 15, 2008, between UABL Paraguay S.A., a subsidiary of Ultrapetrol (Bahamas) Limited, and International Finance Corporation+
4.4	Loan agreement dated September 15, 2008 between certain subsidiaries of Ultrapetrol (Bahamas) Limited, as joint and several borrowers, and International Finance Corporation+
4.5	Loan agreement dated as of November 28, 2008, between UABL Paraguay S.A., a subsidiary of Ultrapetrol (Bahamas) Limited, and The OPEC Fund for International Development+
4.6	Loan agreement dated as of June 24, 2008, pursuant to which one of Ultrapetrol (Bahamas) Limited's subsidiaries is a borrower and Ultrapetrol (Bahamas) Limited and certain of its other subsidiaries are joint and several guarantors+
4.7	Indenture dated as of December 23, 2010 for 7.25% Convertible Senior Notes Due 2017
4.8	Loan agreement dated as of December 2, 2011, between UABL Paraguay S.A. and Riverpar S.A., as joint and several co-Borrowers, and International Finance Corporation
4.9	Loan agreement dated as of December 15, 2011, between UABL Paraguay S.A. and Riverpar S.A., as joint and several co-Borrowers, and The OPEC Fund for International Development
7	Statement of Ratio of Earning to Fixed Charges
8.1	Subsidiaries of Ultrapetrol (Bahamas) Limited ++
12.1	Section 302 Certification of Chief Executive Officer
12.2	Section 302 Certification of Chief Financial Officer
13.1	Section 906 Certification of Chief Executive Officer
13.2	Section 906 Certification of Chief Financial Officer

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* Incorporated by reference to the Registration Statement on Form F-1/A of Ultrapetrol (Bahamas) Limited filed April 18, 2007 (Reg. No. 333-141485).

** Incorporated by reference to the Registration Statement on Form F-1/A of Ultrapetrol (Bahamas) Limited filed September 26, 2006 (Reg. No. 333-132856).

*** Incorporated by reference to the Registration Statement on Form F-4 of Ultrapetrol Bahamas) Limited filed January 24, 2005 (Reg. No. 333-122254).

**** Incorporated by reference to the Registration Statement on Form F-1 of Ultrapetrol (Bahamas) Limited filed March 30, 2006 (Reg. No. 333-132856).

\+ Incorporated by reference to the Company's Report on Form 6-K submitted on February 18, 2010.

++ Incorporated by reference to the Company's Form 20-F filed March 13, 2008.

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

ULTRAPETROL (BAHAMAS) LIMITED

By: /s/ Felipe Menendez Ross
Name: Felipe Menendez Ross
Title: Chief Executive Officer, President and Director

March 15, 2012