# Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries

Combined and Consolidated Financial Report
December 31, 2011

**Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries**

**Contents**


| | |
|---|---|
| Independent Auditor's Report | 1 |
| Financial Statements | |
| Combined and Consolidated Balance Sheets | 2 |
| Combined and Consolidated Statements of Income | 3 |
| Combined and Consolidated Statements of Stockholders' and Members' Equity and Other Comprehensive Income (Loss) | 4 |
| Combined and Consolidated Statements of Cash Flows | 5 |
| Notes to Combined and Consolidated Financial Statements | 6 |

McGladrey

## Independent Auditor's Report

To the Board of Directors, Stockholders' and Members' of
Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries
Cape May, New Jersey

We have audited the accompanying combined and consolidated balance sheets of Atlantic Capes Fisheries, Inc. and its combined and consolidated Affiliates and Subsidiaries as of December 31, 2011 and 2010 and the related combined and consolidated statements of income, stockholders' and members' equity and other comprehensive income (loss) and cash flows for the years then ended. 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 auditing standards generally accepted in the 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 combined and consolidated financial statements referred to above present fairly, in all material respects, the financial position of Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries as of December 31, 2011 and 2010, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

McGladrey LLP

Philadelphia, Pennsylvania
May 31, 2012



Member of the RSM International network of independent accounting, tax and consulting firms.

**Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries**

**Combined and Consolidated Balance Sheets**
**December 31, 2011 and 2010**

| | 2011 | 2010 |
|---|---|---|
| **Assets** | | |
| Current Assets | | |
| Cash and cash equivalents | $ 348,953 | $ 432,607 |
| Accounts receivable, net of allowance for doubtful accounts of $300,000 in 2011 and $357,937 in 2010 | 27,026,171 | 23,917,743 |
| Inventory | 42,947,690 | 28,328,524 |
| Notes receivable, current portion | 3,960,914 | 586,610 |
| Prepaid expenses and other current assets | 3,527,525 | 1,011,185 |
| **Total current assets** | 77,811,253 | 54,276,669 |
| Property and Equipment, net | 19,938,884 | 17,855,186 |
| Other Assets | | |
| Cash and investments, Capital Construction Funds | 4,961,482 | 6,870,107 |
| Escrow, cash | - | 35,000 |
| Notes receivable, net of current portion | 914,310 | 1,220,392 |
| Notes receivable, officer | 5,702,963 | 5,168,360 |
| Other assets | 28,554 | 1,033,238 |
| Fishing licenses, net of amortization | 5,993,377 | 4,796,376 |
| Intangible assets, net of amortization | 893,874 | 1,212,934 |
| | 18,494,560 | 20,336,407 |
| **Total assets** | $ 116,244,697 | $ 92,468,262 |
| **Liabilities and Stockholders' and Members' Equity** | | |
| Current Liabilities | | |
| Lines of credit | $ 51,487,514 | $ 42,718,601 |
| Current portion of notes payable | 3,493,738 | 2,068,851 |
| Accounts payable | 6,529,756 | 8,179,044 |
| Accrued expenses | 1,693,041 | 1,145,522 |
| **Total current liabilities** | 63,204,049 | 54,112,018 |
| Long-Term Liabilities | | |
| Notes payable, net of current portion | 17,935,665 | 9,259,318 |
| Obligation under interest rate swap | 607,080 | 801,084 |
| | 18,542,745 | 10,060,402 |
| **Total liabilities** | 81,746,794 | 64,172,420 |
| Commitments and Contingencies (Note 10) | | |
| Stockholders' and Members' Equity | | |
| Common stock (Note 11) | 126,100 | 126,100 |
| Additional paid-in capital | 759,415 | 759,415 |
| Retained earnings | 31,691,360 | 25,492,338 |
| Members' and proprietor's capital | 1,706,162 | 1,642,906 |
| Accumulated other comprehensive loss | (14,672) | (3,364) |
| Treasury stock | (3,008) | (3,008) |
| **Total stockholders' and members' equity** | 34,265,357 | 28,014,387 |
| Non-controlling interests in subsidiaries | 232,546 | 281,455 |
| **Total equity** | 34,497,903 | 28,295,842 |
| **Total liabilities and stockholders' and members' equity** | $ 116,244,697 | $ 92,468,262 |

See Notes to Combined and Consolidated Financial Statements.

**Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries**

**Combined and Consolidated Statements of Income**
**Years Ended December 31, 2011 and 2010**

| | **2011** | 2010 |
|---|---|---|
| Net sales | **$ 177,471,168** | $ 143,100,228 |
| Cost of sales | **160,894,088** | 129,729,472 |
| Gross profit | **16,577,080** | 13,370,756 |
| Operating expenses | **9,177,544** | 8,951,292 |
| Income from operations | **7,399,536** | 4,419,464 |
| Other income (expense): | | |
| Interest expense | **(2,330,511)** | (2,120,107) |
| Gain on interest rate swap | **194,003** | 25,078 |
| Gain (loss) on sale/disposition of assets | **1,328,903** | (137,338) |
| Interest income | **62,264** | 60,336 |
| | **(745,341)** | (2,172,031) |
| Net income | **6,654,195** | 2,247,433 |
| Net loss attributable to the non-controlling interests in subsidiaries | **48,909** | 48,702 |
| **Net income attributable to Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries** | **$ 6,703,104** | $ 2,296,135 |

See Notes to Combined and Consolidated Financial Statements.

**Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries**

**Combined and Consolidated Statements of Stockholders' and Members' Equity and Other Comprehensive Income (Loss)**
**Years Ended December 31, 2011 and 2010**

| | Common Stock | Additional Paid-in Capital | Retained Earnings | Members' and Proprietor's Capital | Accumulated Other Comprehensive Income (Loss) | Treasury Stock | Non-controlling Interests | Total |
|---|---|---|---|---|---|---|---|---|
| Balance, January 1, 2010 | $ 126,100 | $ 759,415 | $ 23,638,791 | $ 1,633,380 | $ (43,255) | $ (3,008) | $ 311,822 | $ 26,423,245 |
| Comprehensive income (loss): | | | | | | | | |
| Net income (loss) | - | - | 2,026,921 | 269,214 | - | - | (48,702) | 2,247,433 |
| Unrealized gain | - | - | - | - | 39,891 | - | - | 39,891 |
| Total comprehensive income (loss) | - | - | 2,026,921 | 269,214 | 39,891 | - | (48,702) | 2,287,324 |
| Distributions | - | - | (173,374) | (259,688) | - | - | - | (433,062) |
| Capital contributed | - | - | - | - | - | - | 18,335 | 18,335 |
| Balance, December 31, 2010 | 126,100 | 759,415 | 25,492,338 | 1,642,906 | (3,364) | (3,008) | 281,455 | 28,295,842 |
| Comprehensive income (loss): | | | | | | | | |
| Net income (loss) | - | - | 6,403,396 | 299,708 | - | - | (48,909) | 6,654,195 |
| Foreign currency translation | - | - | - | - | 59,108 | - | - | 59,108 |
| Unrealized loss | - | - | - | - | (70,416) | - | - | (70,416) |
| Total comprehensive income (loss) | - | - | 6,403,396 | 299,708 | (11,308) | - | (48,909) | 6,642,887 |
| Distributions | - | - | (204,374) | (236,452) | - | - | - | (440,826) |
| Balance, December 31, 2011 | $ 126,100 | $ 759,415 | $ 31,691,360 | $ 1,706,162 | $ (14,672) | $ (3,008) | $ 232,546 | $ 34,497,903 |

See Notes to Combined and Consolidated Financial Statements.

**Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries**

**Combined and Consolidated Statements of Cash Flows**
**Years Ended December 31, 2011 and 2010**

| | 2011 | 2010 |
|---|---|---|
| Cash Flows from Operating Activities | | |
| Net income | $ 6,654,195 | $ 2,247,433 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 2,763,998 | 2,446,354 |
| Bad debt expense | 102,682 | 94,201 |
| Change in fair value of interest rate swap | (194,004) | (25,078) |
| CCF earnings | (61,829) | (37,148) |
| (Gain) loss on sale/disposition of assets | (1,328,903) | 137,338 |
| (Increase) decrease in: | | |
| Accounts receivable | (3,211,110) | (1,717,424) |
| Inventory | (14,619,166) | (118,025) |
| Prepaid expenses and other current assets | (1,087,116) | 2,097,262 |
| Other assets | 1,004,684 | 42,570 |
| Increase (decrease) in: | | |
| Accounts payable | (1,649,288) | 2,058,708 |
| Accrued expenses | 547,519 | 388,192 |
| **Net cash provided by (used in) operating activities** | (11,078,338) | 7,614,383 |
| Cash Flows from Investing Activities | | |
| Purchase of property and equipment | (4,381,963) | (1,471,911) |
| Acquisition of Fairtide Shellfish, Ltd. | - | (784,897) |
| CCF investments: | | |
| Deposits | (1,500,000) | (2,145,734) |
| Withdrawals | 3,400,038 | - |
| Escrow | 35,000 | 45,006 |
| Purchase of fishing licenses | (1,242,001) | (32,000) |
| Notes receivable | (3,068,222) | (949,856) |
| Officer receivables | (534,603) | (1,052,109) |
| **Net cash used in investing activities** | (7,291,751) | (6,391,501) |
| Cash Flows from Financing Activities | | |
| Borrowings under lines of credit, net | 8,768,913 | 1,329,531 |
| Proceeds from long-term debt | 12,581,160 | - |
| Repayment of notes payable | (2,479,926) | (1,876,298) |
| Deferred financing costs | (201,994) | (223,725) |
| Stockholders' and members' distributions | (440,826) | (433,062) |
| Investments by non-controlling interests | - | 18,335 |
| **Net cash provided by (used in) financing activities** | 18,227,327 | (1,185,219) |
| Effect of foreign exchange rates on cash | 59,108 | - |
| **Net increase (decrease) in cash and cash equivalents** | (83,654) | 37,663 |
| Cash and cash equivalents, beginning | 432,607 | 394,944 |
| Cash and cash equivalents, ending | $ 348,953 | $ 432,607 |
| Supplemental Disclosures of Cash Flow Information: | | |
| Interest paid | $ 2,728,915 | $ 2,405,158 |
| Supplemental Noncash Investing and Financing Activities: | | |
| Unrealized gain (loss) on CCF investments | $ (11,308) | $ 39,891 |

See Note 7 for additional cash flow information related to acquisition of Fairtide Shellfish, Ltd.

See Notes to Combined and Consolidated Financial Statements.

## Note 1. Nature of Operations

Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries (the "Company") form a vertically integrated seafood operation, which is primarily engaged in the catching, unloading, processing and selling of sea scallops. The Company also markets surf clams, oysters and various other seafood products. The products sold are either caught by the Company's vessel operators or are purchased from domestic fisherman. The products are sold to warehouse clubs, restaurants, fast food chains, supermarkets, hotels and other institutions throughout North America, Europe and Asia. The Companies included within the combined and consolidated financial statements are divided into seafood processing and dock services, vessel operators, vessel lessors, real estate lessors and aquaculture operations.

The combined and consolidated financial statements of Atlantic Capes Fisheries, Inc. and Affiliates and Subsidiaries consist of the following Companies:

Seafood Processors and Dock Services: Atlantic Capes Fisheries, Inc. (ACF), a New Jersey S-corporation, is in the business of processing seafood and providing dock services for vessels. ACF has locations in Cape May, New Jersey; New Bedford, Massachusetts; Bristol, Rhode Island and Seattle, Washington. The Cape May location provides services to affiliates as well as to other vessel operators along the eastern coast of the United States and customers throughout the world. The New Bedford and Seattle locations perform sales and marketing for the Company and the Bristol location processes seafood.

Point Pleasant Packaging, Inc. (PPP), a New Jersey S-corporation is in the business of processing seafood and providing dock services for vessels. PPP is located in Point Pleasant, New Jersey, where it provides its services to its affiliates as well as to other vessel operators along the eastern coast of the United States.

Vessel Operators: Sea Harvest, Inc. (SHI), a New Jersey S-corporation, is in the business of vessel operations. SHI leases vessels from Fishing Vessel Enterprises, Inc., Sea Products, Inc. and Edgar Seafood Products, Inc. SHI, which is located in Cape May, New Jersey, fishes for sea scallops, surf clams, squid and mackerel.

Vessel Lessors: Fishing Vessel Enterprises, Inc. (FVE), a New Jersey S-corporation, is in the business of leasing its vessels exclusively to SHI. During the years ended December 31, 2011 and 2010, FVE leased to SHI 14 vessels.

Sea Products, Inc. (SPI), a New Jersey S-corporation, is in the business of leasing vessels exclusively to SHI. During the years ended December 31, 2011 and 2010, SPI leased to SHI 1 vessel.

Edgar Seafood Products, Inc. (ESP), a New York S-corporation, is in the business of leasing vessels exclusively to SHI. During the years ended December 31, 2011 and 2010, ESP leased to SHI 2 vessels. Also, ESP leases a State of New York clam license to an unrelated vessel operator.

Real Estate Lessors: Oceanside Realty, Inc. (ORI), a New Jersey S-corporation, owns property at Point Pleasant Beach, New Jersey which is leased to PPP.

Dan Cohen Properties (DCP), a proprietorship, owns the property adjacent to the ORI property which is leased to PPP.

Maxie, Inc. (Maxie), a New Jersey S-corporation, owns property at Cape May, New Jersey which is leased to SHIP, Ltd., LLC.

SHIP I, LLC (SHIP), a Delaware limited liability company, owns the building located on the Maxie, Inc. property which is leased to ACF.

## Note 1. Nature of Operations (Continued)

Aquaculture: Dalian Atlantic Capes Fisheries Co., Ltd (Dalian ACF) is a foreign partnership which primarily sources Chinese seafood products.

Qingdao Laodong Seafood Good Varieties Cultivated Co., Ltd (Qingdao) is a foreign partnership which operates a shellfish aquaculture farm.

## Note 2. Summary of Significant Accounting Policies

Principles of Combination and Consolidation: The combined and consolidated financial statements include the accounts of Atlantic Capes Fisheries, Inc. and its affiliates, Point Pleasant Packing, Inc., Sea Harvest, Inc., Fishing Vessel Enterprises, Inc., Sea Products, Inc., Edgar Seafood Products, Inc., Oceanside Realty, Inc., Dan Cohen Properties, Maxie, Inc., and SHIP I, LLC and its majority-owned subsidiaries Dalian Atlantic Capes Fisheries Co., Ltd. and Qingdao Laodong Seafood Good Varieties Cultivated Co., Ltd. The Company consolidates variable interest entities in which the Company bears a majority of the risk to the entities' expected losses or stands to gain from a majority of the entities' expected returns. The interests that the Company does not own are included as a component of equity in "non-controlling interests in subsidiaries" on the balance sheet. Investments in partnerships in which the Company has no more than a 50% partnership interest are recorded using the equity method. All intercompany accounts and transactions of combined and consolidated affiliates and subsidiaries have been eliminated in combination and consolidation.

Revenue Recognition: Revenue from the sale of seafood products is recognized, net of any discounts, when the products are shipped and the customer assumes the risk of loss. Revenue from food processing and dock services is recognized upon completion of the services. Intercompany leasing transactions are eliminated in combination.

Use of Estimates: The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The most significant estimates and assumptions underlying the financial statements and accompanying notes generally involve revenue recognition, fair value of intangible assets, depreciable lives of long-lived assets, allowance for doubtful accounts and the reserve for slow moving or obsolete inventory.

Cash and Cash Equivalents: For purposes of reporting the statements of cash flows, the Company considers all cash accounts, which are not subject to withdrawal restrictions or penalties, and all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Accounts Receivable: Accounts receivable are carried at original invoice amount, less an estimate made for doubtful accounts, based on a review of all outstanding amounts on a monthly basis. Management determines the allowance for doubtful accounts by regularly evaluating individual customer receivables and considering a customer's financial condition, credit history and current economic conditions. Trade receivables are written-off when deemed uncollectible. Recoveries of trade receivables previously written-off are recorded when received. A trade receivable is considered to be past due if any portion of the receivable balance is outstanding for more than 90 days. Interest may be charged on past due accounts receivable. Management has determined that an allowance was deemed necessary for the years ended December 31, 2011 and 2010 in the amounts of $300,000 and $357,937, respectively. Certain of the Company's accounts receivable balances are insured by a third-party.

Inventory: Inventory is recorded at the lower of cost or market; cost is determined using the weighted average method. Processing costs are added to cost for all frozen inventory.

**Note 2. Summary of Significant Accounting Policies (Continued)**

Investments: The Company has a portfolio of debt and marketable equity securities. Management determines the appropriate classifications of securities at the time of purchase and reevaluates such designation as of each balance sheet date. The investments held by the Company consist principally of mutual funds, real estate investment trusts and bonds which are classified as available-for-sale. Available-for-sale securities are carried at fair value, with the unrealized gains and losses reported as a component of other comprehensive income (loss) within stockholders' and members' equity. The Company considers declines in fair value of investments to be temporary as the Company's intent is to retain the investments for a period of time sufficient to allow for recoveries in the market.

Risks and Uncertainties: Interest rate risk refers to the impact of interest rate changes in the Company's financial position. Interest rate changes directly impact the fair value of fixed income securities held by the Company. Interest rate changes will also have an indirect impact on the other investments held by the Company.

Foreign currency risk is the risk that the value of a foreign currency denominated asset or liability will fluctuate due to changes in foreign exchange rates.

Market risk is the risk that the market value of an investment will fluctuate as a result of changes in market price.

Credit risk arises from the potential for an issuer or other counterparty to default on its contractual obligations to the Company. Investments are recorded at fair value. This represents the maximum credit risk exposure to the Company.

Property and Equipment: Property and equipment are stated at cost. Expenditures for major renewals, improvement provisions and betterments are capitalized and minor repairs and maintenance are charged to expense as incurred. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, which range from three years to thirty-nine years. The Company reviews assets for impairment on an annual basis. If circumstances arise between measurement periods, the Company will evaluate the assets for impairment. If a vessel is considered to be impaired and beyond repair, then the vessel's license can be transferred to another vessel of similar size and purpose. For the years ended December 31, 2011 and 2010, no vessels were considered impaired.

Fishing Licenses: Fishing licenses for sea scallops are considered to be definite lived assets and are amortized over the life of the registered vessel. Amortization expense for the years ended December 31, 2011 and 2010 was $45,000. A fishing license for sea scallops cannot be sold unless it is attached (married) to a vessel.

Fishing licenses for surf clams and other fish are considered to be indefinite lived assets and are not amortized. These licenses are bifurcated from the value of the vessel. Fishing licenses for surf clams and other fish at December 31, 2011 and 2010 are $5,993,377 and $4,796,376, respectively. These assets are tested annually for impairment. For the years ended December 31, 2011 and 2010 no licenses were considered to be impaired.

Other Current Assets: On July 27, 2008, the F/V Erin Renee sank during the performance of routine maintenance being performed at an unrelated vessel repair facility. During the year ended December 31, 2010, the Company determined the vessel was temporarily out of service and wrote off the remaining book value of the asset in the amount of $770,045. This charge was offset by an expected recovery from the repair facility. The Company filed a claim with the repair facility's insurance carrier and was awarded a judgment of $2,342,378 in September, 2011. The judgment was received by the company in January, 2012. The vessel's license has not been considered impaired as a result of this event. The amount of $2,342,378 is included in other current assets.

## Note 2. Summary of Significant Accounting Policies (Continued)

Goodwill and Intangible Assets: Goodwill is the excess of the purchase price paid over the fair value of the net assets of the acquired businesses. Goodwill is subject to annual impairment testing. Other intangible assets, which consist primarily of non-contractual customer relationships, sales contracts, patents and technology, are amortized over their estimated useful lives. The Company accounts for goodwill in accordance with Accounting Standards Codification ("ASC") Topic 350 ("ASC 350"), *Goodwill and Other Intangible Assets*. ASC 350 establishes standards for the accounting of intangible assets that are acquired individually or with a group of other assets and the accounting for goodwill and other intangible assets after they have been initially recognized in the financial statements. In accordance with ASC 350, amortization of goodwill is not permitted. Goodwill and other intangible assets are tested at least annually for impairment by comparing the fair value of the recorded assets to their carrying amount. If the carrying amount of the intangible asset exceeds its fair value, an impairment loss is recognized. The annual evaluation of intangible assets require the use of estimates about future operating results of each reporting unit to determine their estimated fair value. Changes in forecasted operations can materially affect these estimates. Once an impairment of an intangible asset has been recorded, it cannot be reversed. An impairment loss would be recognized when estimated undiscounted cash flows expected to result from the use of the asset and its eventual disposition is less than the carrying amount. The Company performs their annual impairment testing on December 31. Impairment, if any, is assessed using discounted cash flows. No impairment of long-lived assets has occurred during the years ended December 31, 2011 and 2010.

The Company accounts for its other intangible assets in accordance with ASC 350. In accordance with ASC 350, intangible assets that have a definite-life are amortized on a straight-line basis over their estimated useful lives. The useful life of covenants not to compete, customer relationships and trade names is five years.

At December 31, 2011 and 2010, the intangible assets were as follows:

| | 2011 | 2010 |
|---|---|---|
| Covenants not to compete | $ 45,000 | $ 45,000 |
| Customer relationships | 1,415,000 | 1,415,000 |
| Trade names | 580,000 | 580,000 |
| Deferred financing fees | 520,145 | 318,151 |
| | 2,560,145 | 2,358,151 |
| Accumulated amortization | 1,666,271 | 1,145,217 |
| | $ 893,874 | $ 1,212,934 |

The Company will recognize amortization expense related to intangibles on a yearly basis as follows:

| | |
|---|---|
| 2012 | $ 430,831 |
| 2013 | 162,366 |
| 2014 | 108,699 |
| 2015 | 79,199 |
| 2016 and thereafter | 112,779 |
| | $ 893,874 |

The Company does not have goodwill recorded at December 31, 2011 or 2010.

**Note 2. Summary of Significant Accounting Policies (Continued)**

Income Taxes: At December 31, 2011, all corporations have elected to be treated as "S" corporations under the Internal Revenue Code and do not pay federal income taxes at the corporate level. Rather, the stockholders' are taxed directly on the "S" corporations' taxable income. Thus, no provision for federal income taxes is included for these "S" corporations in these combined and consolidated financial statements.

Also, the limited liability companies and foreign partnerships are not taxable entities. The members of SHIP and the partners of Dalian ACF and Qingdao pay federal and state income taxes, as applicable, directly on their proportionate share of the income or loss. The proprietorship only represents one segment of income for such proprietor. Thus, no provision for federal and state income taxes is included in the combined and consolidated financial statements for SHIP, Dalian, Qingdao or DCP.

The Company follows Financial Accounting Standards Board ("FASB") guidance on accounting for uncertainty in income taxes. Management evaluated the Company's tax positions and concluded that the Company had taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance. With few exceptions, the Company is no longer subject to income tax examinations by the U.S. federal, state, or local tax authorities for years before 2008.

Advertising Costs: Advertising costs are expensed as incurred. Advertising costs incurred for 2011 and 2010 were $32,738 and $25,954, respectively.

Shipping and Handling Fees and Costs: Amounts billed to a customer, related to shipping and handling in a sales transaction, are classified as revenue.

Foreign Currencies: Assets and liabilities of foreign partnerships are translated into U.S. dollars at the exchange rate on the balance sheet date. Gains and losses upon translation are deferred and reported as a component of other comprehensive income. The results of foreign subsidiary partnerships are translated using average monthly rates of exchange during each reporting period.

Comprehensive Income (Loss): The Company reports comprehensive income in its statement of stockholders' and members' equity and other comprehensive income (loss). Comprehensive income (loss) represents changes in stockholders' and members' equity from non-owner sources. For the years 2011 and 2010, the only items of comprehensive income (loss) for the Company were unrealized gain (loss) on investments and foreign currency translation.

Derivatives: The Company uses interest rate-swaps to convert floating-rate loans to fixed rates. All derivative financial instruments are recognized as either assets or liabilities at their fair value in the balance sheet with the changes in the fair value reported in current-period earnings. These instruments are classified on the balance sheet as other assets or long-term liabilities. The change in the fair market value is recorded on the income statement as gain on interest rate swap. At December 31, 2011 and 2010, the notional principal amounts were $6,428,260 and $7,726,632, respectively, which reduce as debt principal payments are made, maturing on February 2, 2015. Under the swap agreements, the Company pays interest at fixed rates of 6.25% and 7.19% and receives interest at a variable rate equal to LIBOR, based on notional amount. For the years ended December 31, 2011 and 2010, the Company recognized gains of $194,003 and $25,078, respectively, on these instruments. A swap liability totaling $607,080 and $801,084 is included as an obligation under interest rate swap at December 31, 2011 and 2010.

The Company is exposed to a credit loss in the event of non performance by the other party to the interest rate swap agreement. However, the Company does not anticipate non performance by the other party.

**Note 2. Summary of Significant Accounting Policies (Continued)**

Fair Value of Financial Instruments: At December 31, 2011 and 2010, the Company had the following financial instruments: cash and cash equivalents, accounts and other receivables, accounts payable, revolving line of credit borrowings, long-term debt and interest rate swap agreements. The carrying value of cash and cash equivalents, accounts and other receivables and accounts payable approximate their fair value because of their short-term nature. The carrying amount of the long-term debt and revolving line of credit borrowings approximates fair value because the interest rates fluctuate with market interest rates. The interest rate swap is carried at fair value based on quoted market prices from the issuer of the instrument.

Recently Issued Accounting Standards: In June 2011, the FASB issued new accounting guidance related to the presentation of comprehensive income that eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholders' and members' equity. The amendments require that all nonowner changes in stockholders' and members' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The amendments do not change the items that must be reported n other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance is effective for fiscal years ending after December 31, 2012. The Company is currently evaluating which presentation option it will utilize for comprehensive income in its consolidated financial statements. The adoption of this guidance will not impact the Company's financial position, results of operations or cash flows and will only impact the presentation of other comprehensive income in the financial statements.

In May 2011, the FASB issued updated accounting guidance related to fair value measurements and disclosures that result in common fair value measurements and disclosures between U.S. GAAP and International Financial Reporting Standards. This guidance includes amendments that clarify the application of existing fair value measurement requirements, in addition to other amendments that change principles or requirements. This guidance is effective for annual periods beginning after December 15, 2011. The adoption of this guidance is not expected to have a material effect on the Company's consolidated financial statements. The guidance will primarily impact the Company's disclosures, but otherwise is not expected to have a material impact on the Company's consolidated financial statements.

Reclassifications: Certain reclassifications were made to the 2010 financial statements to conform to the 2011 presentation.

Subsequent Events: The Company has evaluated its subsequent events (events occurring after December 31, 2011) through May 31, 2012, which represents the date the financial statements were issued.

## Note 3. Capital Construction Fund

The Company participates in the Capital Construction Fund (CCF), a special investment program administered by two agencies within the Federal Government – the Department of Transportation's Maritime Administration (MARAD) and the Department of Commerce's National Oceanic and Atmospheric Administration (NOAA). MARAD administers the program with respect to vessels operated in the commerce of the United States other than in the fisheries. NOAA administers the program with respect to vessels operated in the fisheries of the United States.

This program allows commercial fisheries to invest a portion of their income in interest-bearing trust funds, to be used to acquire, construct or recondition fishing vessels. The CCF program was created to assist owners and operators of United States-flag vessels in accumulating the large amounts of capital necessary for the modernization and expansion of the U.S. merchant marine. The program encourages construction, reconstruction, or acquisition of vessels through the deferment of Federal income taxes on certain deposits of money or other property placed into a CCF.

CCF vessels must be built in the United States and documented under the laws of the United States for operation.

Deposits to an ordinary income account create an immediate tax deduction. At December 31, 2011 and 2010, the following affiliated companies have amounts deposited in CCF ordinary income accounts:

| | 2011 | 2010 |
|---|---|---|
| Fishing Vessel Enterprises, Inc. | $ 4,710,661 | $ 5,620,297 |
| Sea Harvest, Inc. | 104,692 | 1,104,033 |
| Edgar | 146,129 | 145,777 |
| | $ 4,961,482 | $ 6,870,107 |

Qualified withdrawals from CCF accounts reduce the depreciable basis (for income tax purposes only) of fishing vessels acquired, constructed, or reconditioned by 100% of the amount withdrawn.

Cash and investments, CCF as of December 31, 2011 and 2010 include:

| | 2011 | 2010 |
|---|---|---|
| Restricted cash - ordinary income account | $ 3,013,091 | $ 6,405,193 |
| Restricted investments, at aggregate fair value | 1,948,391 | 464,914 |
| | $ 4,961,482 | $ 6,870,107 |

### Note 3. Capital Construction Fund (Continued)

Cash and investments, CCF activity for the years ended December 31, 2011 and 2010:

| | 2011 | 2010 |
|---|---|---|
| Balance, beginning | $ 6,870,107 | $ 4,647,334 |
| Deposits | 1,500,000 | 2,145,734 |
| Withdrawals | (3,400,038) | - |
| Earnings | 61,829 | 37,876 |
| Unrealized gain (loss) | (70,416) | 39,163 |
| Balance, ending | $ 4,961,482 | $ 6,870,107 |

Restricted investments classified as available-for-sale as of December 31, 2011 and 2010 include:

| | 2011 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gain | Gross Unrealized Loss | Fair Value |
| Equity securities | $ 2,022,171 | $ - | $ 73,780 | $ 1,948,391 |

| | 2010 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gain | Gross Unrealized Loss | Fair Value |
| Equity securities | $ 468,279 | $ - | $ 3,365 | $ 464,914 |

### Note 4. Credit Risk Concentrations

Cash: The Company's policy is to limit the amount of credit exposure to any one financial institution by placing its cash with financial institutions it evaluates as being credit worthy.

Credit Risk: In the normal course of business, the Company extends unsecured credit to its customers. All credit is extended to customers based upon management's evaluation of creditworthiness, and generally collateral is not required. The Company's principal credit risk is limited to its customer base, which is located throughout North America, Europe and Asia.

Business Risk: The Company's raw materials of scallops are harvested from natural stocks contained in U.S. waters in the U.S. Atlantic Exclusive Economic Zone, north of Virginia.

### Note 5. Inventory

Inventory consisted of the following as of December 31, 2011 and 2010:

| | 2011 | 2010 |
|---|---|---|
| Fish | $ 42,180,276 | $ 27,652,006 |
| Packaging material | 689,345 | 637,931 |
| Fuel and oil | 78,069 | 38,587 |
| | $ 42,947,690 | $ 28,328,524 |

### Note 6. Property and Equipment

Property and equipment consisted of the following as of December 31, 2011 and 2010:

| | 2011 | 2010 |
|---|---|---|
| Fishing vessels and improvements | $ 25,030,839 | $ 21,828,553 |
| Land | 422,604 | 422,604 |
| Buildings | 4,645,688 | 4,248,625 |
| Docks and improvements | 2,954,997 | 2,911,123 |
| Machinery and equipment | 3,927,109 | 3,691,486 |
| Motor vehicles | 231,011 | 183,341 |
| | 37,212,248 | 33,285,732 |
| Less: accumulated depreciation | 17,273,364 | 15,430,546 |
| | $ 19,938,884 | $ 17,855,186 |

Depreciation expense for the years ended December 31, 2011 and 2010 was $2,197,944 and $1,990,370, respectively.

### Note 7. Acquisitions

On December 21, 2010, the Company acquired certain assets of Fairtide Shellfish, Ltd. ("Fairtide") for a purchase price of $784,897 in cash plus accounts receivable from Fairtide of $508,502 plus a $200,000 note to the seller plus the assumption of certain liabilities and the cancellation of indebtedness of Fairtide to the Company in an effort to consolidate the Company's position as a market leader in the hand shucked clam business. The purchase price was allocated based on the fair value of the assets acquired. The allocated fair value of the assets acquired was as follows:

| | |
|---|---|
| Cash | $ 39,715 |
| Accounts and loans receivable | 828,234 |
| Inventory | 143,730 |
| Intangible assets | 590,000 |
| Property and equipment | 141,000 |
| Total assets acquired | 1,742,679 |
| Accounts payable and accrued expenses | 230,751 |
| Current liabilities | 18,529 |
| Fair value of net assets acquired | $ 1,493,399 |

All acquisition-related costs, including legal, professional and other expenses, were expensed in the period incurred and not included in the purchase price.

## Note 8. Lines of Credit

The Company has a $46,000,000 line of credit with Farm Credit East, ACA which expires on December 1, 2012. Interest accrues and is payable monthly on the unpaid balance of LIBOR plus 3.5% (3.80% at December 31, 2011). The line is collateralized by eligible accounts receivable and inventory, clam tags and a mortgaged fishing vessel. Outstanding borrowings under the line of credit were $43,861,545 and $33,908,601 at December 31, 2011 and 2010, respectively. The agreement contains various covenants, which require, among other restrictions, the maintenance of certain financial ratios. During the year ended December 31, 2010 and during 2011, the Company was in violation of certain covenants. The Company received a waiver of such violations.

The Company had a $33,000,000 line of credit with Wachovia Bank which expired on November 30, 2009. The line of credit was extended until January 15, 2010 at which time the Company entered into Line of Credit Agreement with Farm Credit East, ACA. Interest accrued and was payable monthly on the unpaid balance of LIBOR plus 3.0% (3.26% at December 31, 2010). The line was collateralized by accounts receivable and mortgaged fishing vessels. The line was repaid and terminated during the year ended December 31, 2010. The agreement contained various covenants, which required, among other restrictions, the maintenance of certain financial ratios.

The Company has a $7,000,000 line of credit with Cape Bank which expires on June 1, 2012. Interest accrues and is payable monthly on the unpaid balance at the bank's prime rate plus 0.50% (3.75% at December 31, 2011) with a floor of 5.0% and a ceiling of 7.50%. The line is collateralized by surf clam fishing licenses and assignments of vessel mortgages. Outstanding borrowings under the line of credit were $6,025,969 and $7,000,000 at December 31, 2011 and 2010, respectively.

The Company has access to a $2,000,000 line of credit issued to Daniel Cohen, personally, which expires on November 1, 2012. Interest accrues and is payable on the unpaid balance at the bank's prime rate (3.25% on December 31, 2011) with a floor of 4.50%. The line is collateralized by surf clam fishing licenses. Outstanding borrowings under the line of credit were $1,600,000 and $1,750,000 at December 31, 2011 and 2010, respectively.

Interest expense on lines of credit for the years ended December 31, 2011 and 2010, was $1,534,025 and $1,324,633, respectively.

## Note 9. Notes Payable

| | 2011 | 2010 |
|---|---|---|
| Farm Credit East | | |
| $12,000,000 term note maturing in August, 2021. The loan is collateralized by fishing vessels and a limited personal guarantee of Dan Cohen. The loan is to be repaid in monthly installments of $100,000 plus interest which accrues on the unpaid principal balance of the note at a rate per annum equal to one-month LIBOR plus 3.75% (4.03% at December 31, 2011). | $ 11,600,000 | $ - |
| Wells Fargo | | |
| $16,000,000 term note maturing in February, 2015. The loan is collateralized by fishing vessels and personally guaranteed by Dan Cohen. The loan is to be repaid monthly in amounts ranging from $157,289 and $199,005 plus interest which accrues on the unpaid principal balance of the note at a rate per annum equal to one-month LIBOR plus 3.0% (3.27% at December 31, 2011). | 7,113,119 | 9,046,819 |
| Wells Fargo | | |
| $2,500,000 term note in the name of Dan Cohen and Oceanside Realty, Inc. Monthly principal payments between $4,000 and $10,000 plus interest using a 20 year amortization schedule with a balloon payment of $1,667,992 in February 2015. The loan is collateralized by certain real property and personally guaranteed by Don Cohen. Interest is payable monthly at the rate per annum equal to one-month LIBOR plus 1.7% (1.97% at December 31, 2011). | 1,986,411 | 2,073,631 |
| Other | | |
| $200,000 note, payable in annual installments of $40,000 on the anniversary of the closing date of the Fairtide Shellfish, Ltd. acquisition (Note 7); due December 2015. | 170,000 | 200,000 |
| Other | | |
| $533,461 note, payable in monthly installments of $5,990 with a final payment due September, 2019 including interest at 1.88%. The note is unsecured. | 517,975 | - |
| Bank of America | | |
| $47,699 note, payable in 60 installments of $896 with final due April 2016, including interest at 4.9%; collateralized by a vehicle. | 41,898 | - |
| GMAC | | |
| $26,084 note, payable in 60 installments of $573 with final made in 2011, including interest at 11.25%; collateralized by a vehicle. | - | 7,719 |
| | 21,429,403 | 11,328,169 |
| Less: current portion | 3,493,738 | 2,068,851 |
| | $ 17,935,665 | $ 9,259,318 |

### Note 9. Notes Payable (Continued)

Principal payments on long-term debt as follows:

| Years Ending December 31, | |
|---|---|
| 2012 | $ 3,493,738 |
| 2013 | 3,664,935 |
| 2014 | 3,791,417 |
| 2015 | 3,415,747 |
| 2016 and thereafter | 7,063,566 |
| | $ 21,429,403 |

Interest expense on long-term debt for the years ended December 31, 2011 and 2010, was $900,675 and $795,474, respectively.

The Wells Fargo term notes contain various covenants, which require, among other restrictions, the maintenance of certain financial ratios. During the year ended December 31, 2010 and during 2011, the Company was in violation of certain covenants. The Company received a waiver of such violations.

### Note 10. Commitments and Contingencies

Litigation: The Company is party to various claims arising in the ordinary course of business. Although the ultimate outcome of the matters is presently not determinable, management, after consultation with legal counsel, does not believe that the outcome of these matters will have a material adverse effect on the Company's financial position or results of operations.

Crewmembers Insurance: During 2011 and 2010, the Company was a limited self-insurer with respect to medical expenses for personal injuries for all eligible crew members employed by SHI. For the 2011 and 2010 plan years, the Company was liable for the first $10,000 per incident for each eligible participant up to an aggregate maximum amount of approximately $100,000. The insurance company covers claims in excess of the above limits. The Company records a monthly accrual for expected claims. The amounts charged to expense for such claims were approximately $196,076 and $162,640 for the years ended December 31, 2011 and 2010, respectively.

Lease Commitments: The Company leases an office located in New Bedford, Massachusetts under a month-to-month operating lease with an unrelated third-party. Rental expense was approximately $42,000 for the years ended December 31, 2011 and 2010, respectively.

## Note 11. Stockholders' Equity as of December 31, 2011 and 2010

| | | Common Stock Shares | | |
|---|---|---|---|---|
| Reporting Entity | Par Value | Authorized | Issued | Outstanding |
| Operating Companies | | | | |
| Food Processors and Dock Services | | | | |
| Atlantic Capes Fisheries, Inc. | - | 1,000 | 100 | 100 |
| Pt. Pleasant Packing, Inc. | $10 | 1,000 | 100 | 100 |
| Vessel Operators | | | | |
| Sea Harvest, Inc. | - | 300 | 100 | 100 |
| Aquaculture | | | | |
| Dalian Atlantic Capes Fisheries, Ltd. (Partnership) | N/A | N/A | N/A | N/A |
| Qingdao Laodong Seafood Godd Varieties Cultivated Co., Ltd. (Partnership) | N/A | N/A | N/A | N/A |
| Leasing Companies | | | | |
| Vessel Lessors | | | | |
| Fishing Vessel Enterprises, Inc. | - | 1,000 | 100 | 100 |
| Sea Products, Inc. | - | 1,000 | 100 | 100 |
| Edgar Seafood Products, Inc. | - | 200 | 10 | 10 |
| Real Estate Lessors | | | | |
| Oceanside Realty, Inc. | - | 1,000 | 1,000 | 1,000 |
| Dan Cohen Properties (Proprietorship) | N/A | N/A | N/A | N/A |
| SHIP, Ltd. (Limited Liability Company) | N/A | N/A | N/A | N/A |
| Maxie, Inc. | - | 2,500 | 300 | 300 |

## Note 12. Major Customers

One customer represented $16,806,063 or 9% and $17,164,230 or 12% of aggregate sales for the years ended December 31, 2011 and 2010, respectively. The amounts due from this customer at December 31, 2011 and 2010 were $3,326,580 and $2,277,511, respectively.

## Note 13. Related Party Transactions

Related party transactions consist of:

| | 2011 | 2010 |
|---|---|---|
| Notes receivable, officer | | |
| Daniel Cohen | | |
| $10,000,000 revolving credit and loan agreement with informal repayment terms expiring December 2015. The note receivable bears interest but no interest has been charged since inception. | $ 5,702,963 | $ 5,168,360 |
| Notes receivable, related parties | | |
| Advances to other related parties for fishing vessel purchases and other operating expenses (net) informal repayment terms interest accrues at various rates. | 478,677 | 608,650 |

The Company purchases inventory from related parties and also provides dock services. Related party transactions consisted of the following for the years ended December 31, 2011 and 2010:

| | 2011 | 2010 |
|---|---|---|
| Accounts receivable | $ 7,019 | $ 97,644 |
| Accounts payable and accrued expenses | 521,610 | 27,784 |

Dock services provided to related parties for the years ended December 31, 2011 and 2010 were $145,700 and $82,697. Purchases from related parties for the years ended December 31, 2011 and 2010 were $2,284,593 and $1,352,214.

## Note 14. Retirement Plan

Atlantic Capes Fisheries, Inc. and Pt. Pleasant Packing, Inc., sponsor a profit sharing and salary reduction 401(k) plan covering all eligible full-time employees. Contributions to the profit sharing plan component of the plan are made at the Company's discretion. The 401(k) component includes an employer matching contribution of 25% of the first 6% of participant contributions.

Employer matching contributions of $30,562 and $111,139 are included in cost of sales and in operating expenses for 2011 and 2010, respectively. No profit sharing contributions were made for either 2011 or 2010.

## Note 15. Fair Value of Financial Instruments

The methods and significant assumptions used to estimate the fair values of the Company's financial instruments are as follows:

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | Carrying Value | Estimated Fair Value | Carrying Value | Estimated Fair Value |
| Financial assets | | | | |
| Equity securities | $ 1,948,391 | $ 1,948,391 | $ 464,914 | $ 464,914 |
| Financial liabilities | | | | |
| Interest rate swaps | $ 607,080 | $ 607,080 | $ 801,084 | $ 801,084 |

The fair value of the equity securities is based upon quoted market prices in active markets. The fair value of the interest rate swaps (used for purposes other than trading) is the estimated amount the Company would pay to terminate the swap agreements at the reporting date, taking into account current interest rates. The Company also considers the creditworthiness of the swap counterparty for assets and creditworthiness of the Company for liabilities.

In accordance with FASB ASC Topic 820 "Fair Value Measurements and Disclosures," the Company utilizes a hierarchy that prioritizes fair value measurements based on the types of inputs used for the various valuation techniques (market approach, income approach and cost approach that relates to its financial asset and financial liabilities). The levels of hierarchy are described as follows:

*Level 1*: Quoted market prices in active markets for identical assets or liabilities.

*Level 2*: Observable market based inputs or unobservable inputs that are corroborated by market data.

*Level 3*: Unobservable inputs that are not corroborated by market data.

In determining the appropriate levels, the Company performs a detailed analysis of the assets and liabilities that are subject to ASC 820-10. At each reporting period, all assets and liabilities for which the fair value measurement is based on significant unobservable inputs are classified as Level 3.

The tables below presents the balances of assets and liabilities measured at fair value on a recurring basis by level within the hierarchy:

| | December 31, 2011 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| Equity securities | $ 1,948,391 | $ 1,948,391 | $ - | $ - |
| Interest rate swaps | $ 607,080 | $ - | $ 607,080 | $ - |

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| Equity securities | $ 464,914 | $ 464,914 | $ - | $ - |
| Interest rate swaps | $ 801,084 | $ - | $ 801,084 | $ - |

## Note 16. Subsequent Events

On January 14, 2011, Atlantic Capes Fisheries, Inc. signed a letter of intent which was memorialized by definitive agreements on April 19, 2011 with Ocean Smart, Inc. for the exclusive option to purchase Island Scallop, Ltd. In exchange for the Company agreeing to lend Island Scallop, Ltd. up to $2,000,000, over time and upon achieving certain milestones, the Company has been granted the absolute and exclusive option to purchase Island Scallop, Ltd and all of its assets. This option is for 24 months into 2013. The loans are fully secured by the all the assets of Island Scallop, Ltd including receivables, inventory, vessels, plants, real estate, and grow-out leases. On April 25, 2012, the Company executed amendments to the agreements dated April 19, 2011 that allowed the Company to exercise its option to purchase Island Scallops for $885,000. Effective April 30, 2012, the Company through its newly formed affiliates Ocean Smart Seafood, LLC and Ocean Smart Organic Seafood Corp. acquired all of the assets of Island Scallops, Ltd. The amended agreements also increased the maximum loan amount to $3,000,000. As of December 31, 2011, the Company has advanced $2,203,629 to Island Scallop, Ltd. Island Scallop, Ltd. operates a full scale shellfish hatchery and aquaculture farm on Vancouver Island, British Columbia, Canada.