UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
☒ QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2023

or

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

For the transition period from __________ to __________

Commission File Number: 001-40611

NAUTICUS ROBOTICS, INC.
(Exact name of registrant as specified in its charter)

Delaware	**85-1699753**
(State or other jurisdiction of incorporation)	(IRS Employer Identification No.)

17146 FEATHERCRAFT LANE, SUITE 450,
WEBSTER, TEXAS 77598
(Address of principal executive offices and zip code)

(281) 942-9069
(Registrant's telephone number, including area code)

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

Title of each class	Trading symbol(s)	Name of each exchange on which registered
Common Stock	KITT	The Nasdaq Stock Market LLC
Redeemable Warrants	KITTW	The Nasdaq Stock Market LLC

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 filing requirements for the past 90 days. Yes ☒ No ☐

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

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

Large accelerated filer ☐	Accelerated filer ☐
Non-accelerated filer ☒	Smaller reporting company ☒
	Emerging growth company ☒

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

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

As of November 14, 2023, the registrant had 50,035,824 shares of common stock outstanding.

TABLE OF CONTENTS

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q ("Form 10-Q") contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements appear in a number of places in this Form 10-Q including, without limitation, in the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations." In addition, any statements that refer to projections, forecasts or other characterizations of future events or circumstances, including any underlying assumptions, are forward-looking statements. Forward-looking statements are typically identified by words such as "plan," "believe," "expect," "anticipate," "intend," "outlook," "estimate," "forecast," "project," "continue," "could," "may," "might," "possible," "potential," "predict," "should," "would" and other similar words and expressions, but the absence of these words does not mean that a statement is not forward-looking.

The forward-looking statements are based on the current expectations of our management and are inherently subject to uncertainties and changes in circumstances and their potential effects and speak only as of the date such statements are made. These forward-looking statements involve a number of risks, uncertainties or other assumptions that may cause actual results or performance to be materially different from those expressed or implied by these forward-looking statements. These risks and uncertainties include, but are not limited to, those described in "Item 1A. Risk Factors" and other sections in the Annual Report on Form 10-K filed by us on March 28, 2023, and Amendment No. 1 to the Quarterly Report on Form 10-Q/A filed by us on August 10, 2023.

These and other factors could cause actual results to differ from those implied by the forward-looking statements. Forward-looking statements are not guarantees of performance and speak only as of the date hereof. There can be no assurance that future developments will be those that have been anticipated or that we will achieve or realize these plans, intentions, or expectations.

All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the foregoing cautionary statements. We undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

In addition, statements of belief and similar statements reflect our beliefs and opinions on the relevant subject. These statements are based upon information available to us as of the date they are made, and while we believe such information forms a reasonable basis for such statements, such information may be limited or incomplete, and statements should not be read to indicate that we have conducted an exhaustive inquiry into, or review of, all potentially available relevant information. These statements are inherently uncertain, and you are cautioned not to unduly rely upon these statements.

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NAUTICUS ROBOTICS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	September 30, 2023	December 31, 2022
	(Unaudited)	
Assets		
Current Assets:		
Cash and cash equivalents	$ 6,771,531	$ 17,787,159
Restricted certificate of deposit	400,375	250,375
Short-term investments	-	4,959,263
Accounts receivable, net	997,400	1,622,434
Inventories	13,960,390	6,666,912
Contract assets	26,712	573,895
Prepaid expenses	5,125,855	5,046,599
Other current assets	584,492	56,410
Total Current Assets	27,866,755	36,963,047
Property and equipment, net	26,275,377	15,167,367
Operating lease right-of-use asset	2,090,859	317,208
Other assets	104,853	155,490
Total Assets	$ 56,337,844	$ 52,603,112
Liabilities and Stockholders' Equity (Deficit)		
Current Liabilities:		
Accounts payable	$ 5,712,946	$ 324,484
Accrued liabilities	6,474,818	3,142,977
Contract liability	152,000	-
Operating lease liabilities - current	616,308	410,158
Total Current Liabilities	12,956,072	3,877,619
Warrant liabilities	14,503,449	32,688,342
Operating lease liabilities - long-term	1,629,516	87,214
Notes payable - long-term, net of discount (related party)	29,925,121	15,922,118
Total Liabilities	59,014,158	52,575,293
Commitments and Contingencies		
Stockholders' Equity (Deficit):		
Common stock, $0.0001 par value; 625,000,000 shares authorized, 49,858,194 and 47,250,771 shares issued, respectively, and 49,858,194 and 47,250,771 shares outstanding, respectively	4,986	4,725
Additional paid-in capital	76,567,814	68,128,196
Accumulated deficit	(79,249,114)	(68,105,102)
Total Stockholders' Equity (Deficit)	(2,676,314)	27,819
Total Liabilities and Stockholders' Equity (Deficit)	$ 56,337,844	$ 52,603,112

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

NAUTICUS ROBOTICS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three months ended September 30,		Nine months ended September 30,	
	2023	**2022**	**2023**	**2022**
Revenue:				
Service	$ 1,593,854	$ 2,964,610	$ 5,542,249	$ 7,996,734
Service - related party	-	17,000	500	210,400
Total revenue	1,593,854	2,981,610	5,542,749	8,207,134
Costs and expenses:				
Cost of revenue (exclusive of items shown separately below)	2,651,380	3,781,224	7,484,249	8,220,447
Depreciation	160,744	141,901	487,052	370,306
Research and development	275,154	242,996	984,882	2,094,278
General and administrative	6,704,890	4,861,319	17,478,099	8,778,498
Total costs and expenses	9,792,168	9,027,440	26,434,282	19,463,529
Operating loss	(8,198,314)	(6,045,830)	(20,891,533)	(11,256,395)
Other (income) expense:				
Other (income) expense, net	(133,311)	(27,980)	1,019,816	(32,692)
Gain on sale of assets	-	-	(3,908)	-
Foreign currency transaction loss (gain)	83,654	(206,617)	56,061	(207,146)
Loss on exchange of warrants	-	-	590,266	-
Change in fair value of warrant liabilities	8,656,392	5,963,238	(18,775,158)	5,963,238
Interest expense, net	873,738	1,402,026	7,365,402	3,057,660
Total other (income) expense, net	9,480,473	7,130,667	(9,747,521)	8,781,060
Net loss	$ (17,678,787)	$ (13,176,497)	$ (11,144,012)	$ (20,037,455)
Basic and diluted loss per share	$ (0.43)	$ (1.10)	$ (0.28)	$ (2.09)
Basic and diluted weighted average shares outstanding	41,155,115	16,535,661	40,453,015	11,983,183

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

NAUTICUS ROBOTICS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES OF STOCKHOLDERS' EQUITY (DEFICIT)
(UNAUDITED)

	Series A Preferred Stock		Series B Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity (Deficit)
	Shares	Amount	Shares	Amount	Shares	Amount			
Balance at December 31, 2021	334,800	$ 3,348	725,426	$ 7,254	9,669,217	$ 967	$ 33,221,505	$ (39,844,531)	$ (6,611,457)
Stock-based compensation	-	-	-	-	-	-	200,157	-	200,157
Net loss	-	-	-	-	-	-	-	(3,504,002)	(3,504,002)
Balance at March 31, 2022	334,800	3,348	725,426	7,254	9,669,217	967	33,421,662	(43,348,533)	(9,915,302)
Stock-based compensation	-	-	-	-	-	-	188,657	-	188,657
Net loss	-	-	-	-	-	-	-	(3,356,956)	(3,356,956)
Balance at June 30, 2022	334,800	$ 3,348	725,426	$ 7,254	9,669,217	967	$ 33,610,319	$ (46,705,489)	$ (13,083,601)
Cancellation and exchange of convertible note in connection with reverse capitalization					5,299,546	530	14,548,384	-	14,548,914
Conversion of Series A preferred stock in connection with reverse recapitalization	(334,800)	(3,348)	-	-	4,756,470	476	2,872	-	-
Conversion of Series B preferred stock in connection with reverse recapitalization	-	-	(725,426)	(7,254)	10,306,055	1,030	6,224	-	-
Reverse recapitalization with Cleantech Acquisition Corp, net	-	-	-	-	6,619,490	662	(669,904)	-	(669,242)
Earnout shares placed in escrow	-	-	-	-	7,499,993	750	(750)	-	-
Issuance of common stock for PIPE Investment	-	-	-	-	3,100,000	310	30,999,690	-	31,000,000
Equity issuance costs	-	-	-	-	-	-	(12,582,000)	-	(12,582,000)
Stock-based compensation	-	-	-	-	-	-	235,593	-	235,593
Net loss	-	-	-	-	-	-	-	(13,176,497)	(13,176,497)
Balance at September 30, 2022	-	$ -	-	$ -	47,250,771	$ 4,725	$ 66,150,428	$ (59,881,986)	$ 6,273,167
Balance at December 31, 2022	-	$ -	-	$ -	47,250,771	$ 4,725	$ 68,128,196	$ (68,105,102)	$ 27,819
Stock-based compensation	-	-	-	-	-	-	1,214,863	-	1,214,863
Exercise of stock options	-	-	-	-	30,504	3	59,186	-	59,189
Net loss	-	-	-	-	-	-	-	(14,138,665)	(14,138,665)
Balance at March 31, 2023	-	$ -	-	$ -	47,281,275	$ 4,728	$ 69,402,245	$ (82,243,767)	$ (12,836,794)
Stock-based compensation	-	-	-	-	-	-	1,862,164	-	1,862,164
Exercise of stock options	-	-	-	-	148,732	15	283,375	-	283,390
Exercise of warrants	-	-	-	-	165,713	16	338,039	-	338,055
Exercise of RSUs	-	-	-	-	298,531	30	(30)	-	-
Net income	-	-	-	-	-	-	-	20,673,440	20,673,440
Balance at June 30, 2023	-	$ -	-	$ -	47,894,251	$ 4,789	$ 71,885,793	$ (61,570,327)	$ 10,320,255
Stock-based compensation	-	-	-	-	-	-	917,993	-	917,993
Settlement of liquidated damages	-	-	-	-	1,890,066	189	3,685,440	-	3,685,629
Exercise of stock options	-	-	-	-	48,601	5	78,591	-	78,596
Exercise of RSUs	-	-	-	-	25,276	3	(3)	-	-
Net loss	-	-	-	-	-	-	-	(17,678,787)	(17,678,787)
Balance at September 30, 2023	-	$ -	-	$ -	49,858,194	$ 4,986	$ 76,567,814	$ (79,249,114)	$ (2,676,314)

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

NAUTICUS ROBOTICS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Nine months ended September 30, 2023	Nine months ended September 30, 2022
Cash flows from operating activities:		
Net loss	$ (11,144,012)	$ (20,037,455)
Adjustments to reconcile net loss to net cash from operating activities:		
Depreciation	487,052	370,306
Accretion of debt discount	2,928,003	464,779
Stock-based compensation	3,995,020	624,407
Loss on exchange of warrants	590,266	-
Change in fair value of warrant liabilities	(18,775,158)	5,963,238
Noncash impact of lease accounting	332,787	145,647
Interest and legal expenses assumed into Bridge Note	528,116	-
Changes in operating assets and liabilities:		
Accounts receivable	625,034	156,786
Inventories	(7,293,478)	(5,558,996)
Contract assets	547,183	409,431
Other assets	(206,702)	(4,817,187)
Accounts payable and accrued liabilities	11,155,980	(9,013,681)
Contract liabilities	152,000	-
Operating lease liabilities	(357,985)	(241,819)
Net cash from operating activities	(16,435,894)	(31,534,544)
Cash flows from investing activities:		
Capital expenditures	(10,745,111)	(6,805,648)
Proceeds from sale of short-term investments	4,959,263	-
Net cash from investing activities	(5,785,848)	(6,805,648)
Cash flows from financing activities:		
Proceeds from notes payable	10,446,884	2,000,000
Proceeds from exercise of stock options	421,175	-
Payments of note payable	-	(17,850,333)
Proceeds from reverse recapitalization with CleanTech Acquisition Corp, net	-	14,947,876
Proceeds from exercise of warrants	338,055	-
Proceeds from issuance of common stock for Pipe Investment	-	31,000,000
Proceeds from issuance of debentures and SPA Warrants, net of discount	-	35,800,000
Payment of transaction costs on equity funding	-	(12,582,000)
Net cash from financing activities	11,206,114	53,315,543
Net change in cash and cash equivalents	(11,015,628)	14,975,351
Cash and cash equivalents, beginning of period	17,787,159	20,952,867
Cash and cash equivalents, end of period	$ 6,771,531	$ 35,928,218
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 1,006,993	$ 2,108,819
Cash paid for taxes	$ -	$ -
Non-cash investing and financing activities:		
Capital expenditures included in accounts payable	$ 849,951	$ 1,773,082
Operating leases at inception	$ 2,016,931	$ -
Settlement of liquidated damages with common stock	$ 3,685,440	$ -
Conversion of convertible debt and interest expense to common stock	$ -	$ 14,548,914
Conversion of Series A preferred stock in connection with reverse recapitalization	$ -	$ 3,348
Conversion of Series B preferred stock in connection with reverse recapitalization	$ -	$ 7,254
Private and Public Warrant Liabilities assumed in reverse recapitalization	$ -	$ 5,278,145

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

NAUTICUS ROBOTICS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Description of the Business

Nauticus Robotics, Inc. ("Nauticus," the "Company," "our," "us," or "we") is a developer of ocean robots, software, and services delivered in a modern business model to the ocean industry. We were initially incorporated as CleanTech Acquisition Corp. ("CLAQ") under the laws of the State of Delaware on June 18, 2020. The Company's principal corporate offices are located in Webster, Texas. Our robotics products and services are delivered to commercial and government-facing customers through a Robotics as a Service ("RaaS") business model and direct product sales for both hardware platforms and software licenses. Besides a standalone service offering and forward-facing products, our approach to ocean robotics has also resulted in the development of a range of technology products for retrofitting/upgrading legacy systems and other 3rd party vehicle platforms. Our services provide customers with the necessary data collection, analytics, and subsea manipulation capabilities to support and maintain assets while reducing their operational footprint, operating cost, and greenhouse gas emissions, and to improve offshore health, safety, and environmental exposure.

Business Combination – On September 9, 2022 (the "Closing Date"), the Company (prior to the Closing Date, CLAQ) consummated its initial business combination (the "Closing") pursuant to that certain Agreement and Plan of Merger, dated as of December 16, 2021 (as amended, the "Merger Agreement," and together with any other agreements and transactions contemplated by the Merger Agreement, the "Business Combination"), with CleanTech Merger Sub, Inc., a Texas corporation and wholly owned subsidiary of CLAQ ("Merger Sub"), and Nauticus Robotics Holdings, Inc. (prior to the Closing Date, "Nauticus Robotics, Inc."), a Texas corporation ("Nauticus Robotics Holdings"). Pursuant to the terms of the Merger Agreement, a business combination between CLAQ and Nauticus Robotics Holdings was affected through the merger of Merger Sub with and into Nauticus Robotics Holdings, with Nauticus Robotics Holdings surviving the merger as a wholly owned subsidiary of CLAQ. On the Closing Date, CLAQ was renamed "Nauticus Robotics, Inc." and the previous Nauticus Robotics, Inc. was renamed "Nauticus Robotics Holdings, Inc."

At the Closing, among other things, (a) each share of Nauticus Preferred Stock, par value $0.01 per share, that was issued and outstanding immediately prior to the Closing converted into shares of Nauticus Common stock, par value $0.01 per share, ("Nauticus Preferred Stock Conversion"); (b) each of Nauticus Robotic Holdings, Inc.'s unsecured convertible note obligations outstanding was converted into shares of Nauticus Common Stock in accordance with the terms of each such Nauticus Convertible Note ("Nauticus Convertible Notes Conversion"); and (c) each share of Nauticus Common Stock (including shares of Nauticus Common Stock outstanding as a result of the Nauticus Preferred Stock Conversion and Nauticus Convertible Notes Conversion) was converted into the right to receive (i) the per share merger consideration and (ii) Earnout Shares (defined below).

Shares issued at Closing are summarized as follows (i) an aggregate of 36,650,778 shares of Common Stock, par value $0.0001 (the "Common Stock" of CLAQ prior to the Closing, and the Common Stock of Nauticus following the Closing) shares were issued to holders of Nauticus Common Stock in the Business Combination (ii) the right to receive 7,499,993 additional shares of Common Stock held in escrow pursuant to the terms of the Merger Agreement and as further described below (such additional escrowed shares, the "Earnout Shares") and (iii) the issuance of 3,100,000 shares of Common Stock for the Equity Financing (as described below). An aggregate of 47,250,771 shares of Common Stock (inclusive of the Earnout Shares) was issued after the Business Combination.

Former holders of Nauticus Robotics Holdings, Inc. Common Stock are entitled to receive their pro rata share of up to 7,499,993 additional Earnout Shares of Common Stock that were issued and are held in escrow. The Earnout Shares will be released from escrow upon occurrence of the following (each, a "Triggering Event"):

i. one-half of the Earnout Shares will be released if, within a 5-year period from Closing Date, the volume-weighted average price of our Common Stock equals or exceeds $15.00 per share over any 20 trading days within a 30-day trading period;

ii. one-quarter of the Earnout Shares will be released if, within a 5-year period from Closing Date, the volume-weighted average price of our Common Stock equals or exceeds $17.50 per share over any 20 trading days within a 30-day trading period; and

iii. one-quarter of the Earnout Shares will be released if, on or after December 31, 2022, within a 5-year period from Closing Date, the volume-weighted average price of our Common Stock equals or exceeds $20.00 per share over any 20 trading days within a 30-day trading period.

We received proceeds from a private investment in a public entity (“PIPE Investment”), consisting of:

- immediately prior to the Closing, the issuance to certain investors of 3,100,000 shares of Common Stock, for a purchase price of $10.00 per share, and an aggregate purchase price of $31 million (the “Equity Financing”); and

- substantially concurrent with the closing of the Business Combination, the issuance to certain investors (the “SPA Parties”) pursuant to that certain securities purchase agreement, dated as of December 16, 2021, as amended on January 31, 2022, and as further amended and restated on September 9, 2022 (the “Securities Purchase Agreement”), of secured debentures (the “Debentures”) in an aggregate principal amount of $36,530,320 and associated warrants (the “Original SPA Warrants”), for gross proceeds of $35,800,000. The fair value of the Original SPA Warrants was estimated to be $20,949,110 using a Monte Carlo valuation model incorporating future projections of the various potential outcomes and any exercise price adjustments based on future financing events. The Debentures, which were issued with a 2% original issue discount, are convertible into 2,922,425 shares of Common Stock and the Original SPA Warrants, upon issuance, were exercisable for an additional 2,922,425 shares of Common Stock, with an exercise price equal to $20.00 per share, subject to adjustment. As discussed in further detail below, pursuant to the Letter Agreements (defined below), the exercise price of the Original SPA Warrants was lowered to a weighted average of $3.28 per share, with multiple tranches priced between $2.04 and $4.64 per share (such Original SPA Warrants, upon and following the entry to the Letter Agreements, the “Amended SPA Warrants”). In connection with the exercise of 165,713 Amended SPA Warrants by ATW Special Situations I LLC (“ATW”) in June 2023, 165,713 New SPA Warrants (defined below) were issued to ATW pursuant to its Letter Agreement with the Company. As used in this Form 10-Q, unless context otherwise requires, the term “SPA Warrants” means (i) before the entry into the Letter Agreements, the Original SPA Warrants, and (ii) upon and following the entry into the Letter Agreements, (a) the Amended SPA Warrants, and (b) the warrants that have been issued or are issuable pursuant to the Letter Agreements (the “New SPA Warrants”). See Note 12 for additional information regarding the SPA Warrants.

The Business Combination was accounted for as a reverse recapitalization under generally accepted accounting principles in the United States (“GAAP”). Nauticus Robotics Holdings, Inc. was determined to be the accounting acquirer and CLAQ was treated as the acquired company for financial reporting purposes. Accordingly, the financial statements of the combined company represent a continuation of the financial statements of Nauticus Robotics Holdings, Inc.

On September 9, 2022, the Company received from the Business Combination with CLAQ net cash of $14,947,875. The Company also assumed $30,157 in prepaids, $14,796,942 in accounts payable and accrued liabilities, $850,333 in notes payable and net equity of $(669,243).

CLAQ’s net cash at the Closing Date totaled $14,947,875. This amount, together with proceeds of the PIPE Investment, were available to repay certain indebtedness, transaction costs and for general corporate purposes.

The Company incurred $12,582,000 in direct and incremental costs associated with the Business Combination and Equity Financing, which primarily consisted of investment banking, legal, accounting, and other professional fees.

Impact of COVID-19 Pandemic on Business – The global spread of COVID-19 and its variants (e.g., the omicron variant) created significant market volatility, economic uncertainty, and disruption during 2021 and 2022 and continuing into 2023. The Company was adversely affected by the deterioration and increased uncertainty in the macroeconomic outlook as a result of the impact of COVID-19. We have experienced and may continue to experience disruptions in our supply chain, due in part to the global impact of the COVID-19 pandemic. Depending upon the duration, including the extent of any residual or further effects, of COVID-19 pandemic-related business interruptions, our customers, suppliers, manufacturers, and partners may suspend or delay their engagements with us, which could result in a material adverse effect on our financial condition and ability to meet current timelines. In addition, the COVID-19 pandemic has affected and may continue to affect our ability to recruit skilled employees to join our team. The conditions caused by the COVID-19 pandemic have adversely affected and may continue to adversely affect, among other things, demand for our products and the ability to test and assess our robotic systems with potential customers, any of which, in turn, could adversely affect our business, results of operations and financial condition. Any further or future impacts of COVID-19 or of another pandemic, epidemic or outbreak of an infectious disease cannot be accurately predicted at this time, and the ultimate direct and indirect impacts on our business, results of operations, and financial condition will depend on future developments that are highly uncertain.

***Liquidity* –** Total cash and cash equivalents on hand as of September 30, 2023, was $6.8 million. The Company has incurred recurring losses each year since its inception. The Company may seek funding through additional debt or equity financing arrangements, implement incremental expense reduction measures, or a combination thereof to continue financing its operations. The Company implemented a workforce reduction of 22% on September 29, 2023, which increased costs by $.4 million in the current quarter, which is attributable to severance paid to employees. The cost savings that will be realized over the next twelve months is expected to be $2.7 million. During the third quarter of 2023, the Company received net proceeds of $10.4 million from the issuance of debt. Utilizing cost control measures, cash on hand, revenue from operations, and potential future equity and debt funding, the Company anticipates having sufficient funds to meet its obligations for at least one year from the issuance date of this Form 10-Q. See “Financial Statements – Note 7 – Notes Payable” for additional information on debt capital.

2. Summary of Significant Accounting Policies

***Basis of Presentation* –** The accompanying condensed consolidated financial statements have been prepared by the Company without audit pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (“SEC”) and, in the opinion of management, include all adjustments (consisting of normal, recurring adjustments, unless otherwise disclosed) necessary for a fair statement of the condensed consolidated results of operations, financial position, cash flows and changes in stockholders’ equity (deficit) for each period presented. All intercompany balances and transactions have been eliminated in preparation of these condensed consolidated financial statements. The condensed consolidated results for the interim periods are not necessarily indicative of results to be expected for the full year. The 2022 year-end consolidated balance sheet was derived from audited financial statements but does not include all disclosures required by GAAP. These financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2022.

Summary of Significant Accounting Policies – The Company’s significant accounting policies are discussed in Note 1 to Nauticus Robotics, Inc.’s consolidated financial statements included in its Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2022. There have been no significant changes to these policies which have had a material impact on the Company’s interim unaudited condensed consolidated financial statements and related notes during the three and nine months ended September 30, 2023.

***Use of Estimates* –** The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Significant items subject to such estimates and assumptions include the (i) estimates of future costs to complete customer contracts recognized over time, (ii) valuation allowances for deferred income tax assets, (iii) valuation of stock-based compensation awards and (iv) the valuation of conversion options, warrants and earnouts. Actual results could differ from those estimates.

Cash and Cash Equivalents – The Company classifies all highly-liquid instruments with an original maturity of three months or less as cash equivalents. The Company maintains cash and cash equivalents in bank deposit accounts, which at times may exceed federally insured limits of $250,000. Historically, the Company has not experienced any losses in such accounts.

Restricted Certificates of Deposit — The Company has restricted certificate of deposit of $250,375, which is held by a bank on our behalf as of September 30, 2023 and 2022 as a guarantee against corporate credit cards. The Company entered into an agreement in August of 2023 whereby a $150,000 restricted certificate of deposit was required to collateralize a letter of credit.

Short-term Investments **–** Short-term investments on December 31, 2022, include an investment in a US Treasury Bill that matured on March 14, 2023. The original maturity for this investment was more than three months and any change in the investment is recognized in the condensed consolidated balance sheets. On March 14, 2023, the Company received proceeds of $4,959,263 at maturity, which were recognized in the condensed consolidated statements of cash flows under cash flows from investing activities.

Revenue – Our primary sources of revenue are from providing technology, engineering services and products to the offshore industry and governmental entities. Revenue is generated pursuant to contractual arrangements to design and develop subsea robots and software and to provide related engineering, technical, and other services according to the specifications of the customers. These contracts can be service sales (cost plus fixed fee or firm fixed price) or product sales and typically have terms of up to 18 months. The Company had no product sales for the three and nine months ended September 30, 2023 and 2022, respectively.

A performance obligation is a promise in a contract to transfer distinct goods or services to a customer. For all contracts, we assess if there are multiple promises that should be accounted for as separate performance obligations or combined into a single performance obligation. We generally separate multiple promises in a contract as separate performance obligations if those promises are distinct, both individually and in the context of the contract. If multiple promises in a contract are highly interrelated or require significant integration or customization within a group, they are combined and accounted for as a single performance obligation.

Our performance obligations under service agreements generally are satisfied over time as the service is provided. Revenue under these contracts is recognized over time using an input measure of progress (typically costs incurred to date relative to total estimated costs at completion). This requires management to make significant estimates and assumptions to estimate contract sales and costs associated with its contracts with customers. At the outset of a long-term contract, the Company identifies risks to the achievement of the technical, schedule and cost aspects of the contract. Throughout the contract term, on at least a quarterly basis, we monitor and assess the effects of those risks on its estimates of sales and total costs to complete the contract. Changes in these estimates could have a material effect on our results of operations.

Firm-fixed price contracts present the risk of unreimbursed cost overruns, potentially resulting in lower-than-expected contract profits and margins. This risk is generally lower for cost plus fixed fee contracts which, as a result, generally have a lower margin.

Performance obligations for product sales are typically satisfied at a point in time. This occurs when control of the products is transferred to the customer, which generally is when title and risk of loss have passed to the customer.

Inventories **–** Inventories include raw materials and work in progress used in the construction and installation of a portfolio of ocean robotics systems technology products that include the Aquanaut and Olympic Arm. Raw materials consist of composite marine structures, commercial off-the-shelf or COTS, batteries, and hardware and electrical components. Work in progress inventories consist of raw materials and labor for construction of projects. Inventories are stated at the lower of cost or net realizable value. Cost is determined using the first-in, first-out method. The Company periodically reviews inventories for specifically identifiable items that are unusable or obsolete based on assumptions about future demand and market conditions. Based on this evaluation, we make provisions for unusable and obsolete inventories in order to write inventories down to their net realizable value.

Inventories consisted of the following:

	September 30, 2023	December 31, 2022
Raw material and supplies	$ 936,623	$ 1,499,030
Work in progress	13,023,767	5,167,882
Finished goods	-	-
Total inventories	$ 13,960,390	$ 6,666,912

Leases – The Company's lease arrangements are operating leases which are capitalized on the balance sheet as right-of-use ("ROU") assets and obligations. ROU assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. These are recognized at the lease commencement date based on the present value of payments over the lease term. If leases do not provide for an implicit rate, we use our incremental borrowing rate based on the estimated rate of interest for collateralized borrowing over a similar term as the lease payments. Lease expense for operating leases is recognized on a straight-line basis over the lease term.

Stock-Based Compensation – The Company accounts for employee stock-based compensation using the fair value method. Compensation cost for equity incentive awards is based on the fair value of the equity instrument generally on the date of grant and is recognized over the requisite service period. The Company's policy is to issue new shares upon the exercise or conversion of options and recognize option forfeitures as they occur.

Income Taxes – Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. In assessing the realizability of deferred tax assets, management considers whether it is more-likely-than-not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax asset (including the impact of available carryback and carryforward periods), projected future taxable income, and tax-planning strategies in making this assessment. A valuation allowance for deferred tax assets is recorded when it is more likely than not that the benefit from the deferred tax asset will not be realized.

The Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which a change in judgment occurs. The Company had no material uncertain tax positions as of September 30, 2023, and December 31, 2022.

Foreign Currency Gains and Losses – Nauticus purchases certain materials and equipment from foreign companies, and these transactions are generally denominated in the vendors' local currency. The Company recorded a foreign currency loss of $83,654 and $56,061 for the three and nine months ended September 30, 2023, respectively, and a foreign currency gain of $206,617 and $207,146 for the three and nine months ended September 30, 2022, respectively, which amounts are included in other (income) expense.

Common Stock Warrants – We account for common stock warrants as either equity-classified or liability-classified instruments based on an assessment of the warrant's specific terms and applicable authoritative guidance. This assessment considers whether the warrants are freestanding financial instruments, meet the definition of a liability or requirements for equity classification, including whether the warrants are indexed to the Company's Common Stock, among other conditions for equity classification. This assessment, which requires the use of professional judgment, is conducted at the time of warrant issuance and as of each subsequent quarterly period end date while the warrants are outstanding.

We have determined that the private warrants sold in a private placement to CLAQ's co-sponsors in connection with CLAQ's initial public offering (the "Private Warrants") and warrants sold to the public in CLAQ's initial public offering (the "Public Warrants") should be accounted for as liabilities. The Private Warrants and Public Warrants were initially recorded at their estimated fair value on the Closing Date. They are then revalued at each reporting date thereafter, with changes in the fair value reported in the condensed consolidated statements of operations. Derivative warrant liabilities are classified in the balance sheet as current or non-current based on whether or not net-cash settlement or conversion of the instrument could be required within 12 months of the balance sheet date. The fair value of the Private Warrants was estimated using a Black-Scholes option pricing model (a Level 3 measurement). The Public Warrants are valued using their publicly-traded price at each measurement date (a Level 1 measurement).

We have determined that the SPA Warrants should be accounted for as liabilities. The SPA Warrants were initially recorded at their estimated fair value on the Closing Date and are then revalued at each reporting date thereafter, with changes in the fair value reported in the Company's statements of operations. Derivative warrant liabilities are classified in our balance sheets as current or non-current based on whether or not net-cash settlement or conversion of the instrument could be required within 12 months of the balance sheet date. At the Closing Date, the fair value of the Original SPA Warrants upon issuance was estimated using a Monte Carlo valuation model (a Level 3 measurement).

Earnout Shares – Earnout Shares, issuable to former holders of Nauticus Robotics Holdings, Inc.'s Common Stock, are held in escrow. The Earnout Shares will be released upon the occurrence of a Triggering Event within five years of the Closing Date. The Earnout Shares are considered legally issued and outstanding shares of Common Stock subject to restrictions on transfer and potential forfeiture pending the achievement of the earnout targets. The Company evaluated the Earnout Shares and concluded that they meet the criteria for equity classification. The Earnout Shares were classified in stockholders' equity, recognized at fair value upon the closing of the Business Combination, and will not be subsequently remeasured. A Monte Carlo valuation model (a Level 3 measurement) determined their estimated fair value upon issuance.

Capitalized Interest – The Company capitalizes interest costs incurred to work in progress during the related construction periods. Capitalized interest is charged to cost of revenue when the related completed project is delivered to the buyer. During the nine months ended September 30, 2023, the Company capitalized interest totaling $873,816, of which $354,162 and $519,654 related to inventory and property and equipment, respectively. During the nine months ended September 30, 2022, the Company capitalized interest totaling $615,507, of which $265,650 and $350,857 related to inventory and property and equipment, respectively.

Major Customer and Concentration of Credit Risk – We have a limited number of customers. During the three and nine months ended September 30, 2023, sales to two customers accounted for 100% and 99% of total revenue, respectively. The total balance due from these customers as of September 30, 2023, comprised 99% of accounts receivable. During the three and nine months ended September 30, 2022, sales to two customers accounted for 99% and 96% of total revenue, respectively. The total balances due from these customers as of December 31, 2022, made up 96% of accounts receivable. No other customer represented more than 10% of our revenue. Loss of these customers could have a material adverse impact on the Company.

Reclassifications – Financial statements presented for prior periods include reclassifications that were made to conform to the current-period presentation.

Recent Accounting Pronouncements – In September 2022, the FASB issued ASU 2022-04, Liabilities – Supplier Finance Programs (Subtopic 405-60): Disclosure of Supplier Finance Program Obligations, which requires companies to disclose the use and impact of such programs on a company's working capital, liquidity, and cash flow. We adopted this standard on January 1, 2023. We do not utilize Supplier Finance Programs and therefore no further disclosure is required.

In June 2016, the FASB issued ASU No. 2016-13, an amendment to ASC 326, *Financial Instruments - Credit Losses*, which changes the impairment model for certain financial assets that have a contractual right to receive cash, including trade and loan receivables. The new model requires recognition based upon an estimation of expected credit losses rather than recognition of losses when it is probable that they have been incurred. An entity will apply the amendment through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective. The Company has adopted this standard as of January 1, 2023, and there was no impact on its financial position, results of operations and cash flows upon adoption.

In March 2022, the FASB issued ASU No. 2022-02, an amendment to ASC 326, *Financial Instruments-Credit Losses*, which eliminates the accounting guidance for creditors in troubled debt restructuring. It also aligns conflicting disclosure requirement guidance in ASC 326 by requiring disclosure of current-period gross write-offs by year of origination. The amendment also adds new disclosures for creditors with loan refinancing and restructuring for borrowers experiencing financial difficulty. The Company has adopted this standard as of January 1, 2023, and there was no impact on its financial position, results of operations and cash flows upon adoption.

There are no other new accounting pronouncements that are expected to have a material impact on our condensed consolidated financial statements.

3. Revenue

The following table presents the components of our revenue:

	Three months ended September 30,		Nine months ended September 30,	
	2023	2022	2023	2022
Cost plus fixed fee	$ 1,075,603	$ 1,847,250	$ 3,652,771	$ 5,482,569
Firm fixed-price	518,251	756,027	1,889,978	1,589,565
Firm fixed-price-vehicle lease	-	378,333	-	1,135,000
Total	$ 1,593,854	$ 2,981,610	$ 5,542,749	$ 8,207,134

Our performance obligations under service agreements are generally satisfied over time as the service is provided and, therefore, all revenue above has been recognized over time.

Contract Balances **–** Accounts receivable, net as of September 30, 2023, totaled $997,400 due from customers for contract billings and is expected to be collected within the next three to nine months. As of December 31, 2022, accounts receivable, net totaled $1,622,434. The decrease in accounts receivable as of September 30, 2023, as compared with December 31, 2022, corresponds to the timing of the collections between periods. As of September 30, 2023, and December 31, 2022, allowances for doubtful accounts included in accounts receivable totaled $9,963. Bad debt expense was $0 for the three and nine months ended September 30, 2023. Bad debt expense was $0 and $17,827, respectively, for the three and nine months ended September 30, 2022.

Contract assets include unbilled amounts typically resulting from sales under contracts when the cost-to-cost method of revenue recognition is utilized, and revenue recognized exceeds the amount billed to the customer. Contract assets are recorded at the net amount expected to be billed and collected. The Company had $26,712 of contract assets as of September 30, 2023 and $573,895 as of December 31, 2022. Contract assets decreased $547,183 in the first nine months of 2023, primarily due to the timing of the billing for the recognition of revenue related to the satisfaction or partial satisfaction of performance obligations.

Contract liabilities include billings in excess of revenue recognized and accrual of certain contract obligations. The Company had $152,000 of contract liabilities as of September 30, 2023, and $0 as of December 31, 2022, respectively.

Unfulfilled Performance Obligations – As of September 30, 2023, we expect to recognize approximately $1.9 million of revenue in future periods from unfulfilled performance obligations from existing contracts with customers.

The following table summarizes the expected revenue from our unfilled performance obligations as of September 30, 2023:

($ in millions)	Expected Revenue from Unfulfilled Performance Obligations by Period: Total	2023	2024
Unfulfilled performance obligations:			
Performance obligations	$ 1.9	$ 1.3	$ 0.6
Total unfulfilled performance obligations	$ 1.9	$ 1.3	$ 0.6

If any of our contracts were to be modified or terminated, the expected value of the unfulfilled performance obligations of such contracts would be reduced.

4. Prepaid Expenses

Prepaid expenses consisted of the following:

	September 30, 2023	December 31, 2022
Prepaid material purchases	$ 2,862,337	$ 2,454,298
Prepaid insurance	1,917,191	2,392,978
Other prepayments	346,327	199,323
Total other current assets	$ 5,125,855	$ 5,046,599

5. Property and Equipment

Property and equipment consisted of the following:

	Useful Life (years)	September 30, 2023	December 31, 2022
Leasehold improvements	5.1	$ 789,839	$ 789,839
Property & equipment	5	2,372,339	2,206,004
Technology hardware equipment	5	1,392,507	1,200,504
Total		4,554,685	4,196,347
Less accumulated depreciation		(2,480,962)	(2,003,341)
Construction in progress		24,201,653	12,974,361
Total property and equipment, net		$ 26,275,377	$ 15,167,367

6. Accrued Liabilities

Accrued liabilities consisted of the following:

	September 30, 2023	December 31, 2022
Accrued compensation	$ 1,740,458	$ 1,501,736
Accrued professional fees	1,261,385	794,021
Accrued insurance	1,629,731	590,936
Accrued sales and property taxes	1,196,468	171,660
Accrued royalties	250,000	-
Other accrued expenses	396,777	84,624
Total accrued expenses	$ 6,474,818	$ 3,142,977

In April 2023, the Company received correspondence from the State of Texas assessing a sale and use tax liability of $1.2 million. The accrual is recorded under accrued liabilities of the condensed consolidated balance sheet.

7. Notes Payable

Notes payable consisted of the following:

	September 30, 2023	December 31, 2022
Convertible secured debentures	$ 36,530,320	$ 36,530,320
Convertible senior secured term loan	11,600,000	-
Total	48,130,320	36,530,320
Less: debt discount, net	(18,205,199)	(20,608,202)
Less: current portion	-	-
Total notes payable – long-term	$ 29,925,121	$ 15,922,118

Convertible Secured Debentures –

Upon closing of the Business Combination, we issued to the SPA Parties the Debentures, which featured a 2% original issue discount, in an aggregate principal amount of $36,530,320, together with 2,922,425 Original SPA Warrants, for gross proceeds of $35,800,000. The fair value of the Original SPA Warrants was estimated to be $20,949,110 using a Monte Carlo valuation model incorporating future projections of the various potential outcomes and any exercise price adjustments based on future financing events. This amount was recorded as a warrant liability and, together with the original issue discount, was recognized as a debt discount upon issuance totaling $21,679,716.

The Debentures may be converted at each holder's option at 120% of the principal amount at a conversion price of $15.00 or 2,922,425 shares of Common Stock, subject to certain adjustments including full ratchet anti-dilution price protections. Interest accrues on the outstanding principal amount of the Debentures at 5% per annum, payable quarterly. The Debentures are secured by first priority interests, and liens on, all our assets, and mature on the fourth anniversary of the date of issuance, September 9, 2026.

The Original SPA Warrants, upon issuance, were initially exercisable, at the holder's option, at $20.00 per share over their 10-year term and featured the same anti-dilution provisions as those included in the Debentures. On September 18, 2023, the Company entered into a convertible senior secured term loan agreement convertible at $6.00 per share. Based on the letter agreement, SPA warrants holders who exchange through March 1, 2024, the exercise price reset from $20.00 to $6.00 a warrant pursuant to the full-ratchet provision. The exchange warrants were reset to $6.00 with a factor of 3.3333, increasing the number of warrants to 552,377. The remaining SPA warrant holders will reset from $20.00 to $6.00 a warrant subsequent from March 1, 2024, pursuant to the full-ratchet provision. See Note 12 for more information regarding the SPA Warrants.

The debt discount is being accreted to interest expense over the four-year term of the Debentures. We recorded $1,037,971 and $2,916,347 of debt discount accretion for the three and nine months ended September 30, 2023, and is included as part of interest expense in the condensed consolidated statements of operations. The Debentures effective interest rate is approximately 22.7%.

RCB Equities #1, LLC –

On July 14, 2023, the Company issued a secured promissory note to RCB Equities #1, LLC, a related party for $5,000,000. The promissory note included a 2.5% original issue discount or $125,000, bears interest at 15% per annum, and matures on September 9, 2026. The promissory note provides for an exit fee of $125,000 if paid off in full between October 12, 2023, and the maturity date, with no other considerations triggered for premiums or penalties. Further, the promissory note provides for an automatic rollover into the structure of certain future debt-financing transactions. On September 18, 2023, the RCB Equities #1, LLC promissory note was rolled into the convertible senior secured term loan discussed below bearing interest at 12.5% per annum including the $125,000 exit fee.

Convertible Senior Secured Term Loan –

On September 18, 2023, the Company entered into a convertible senior secured term loan agreement with ATW Special Situations II LLC as collateral agent (in such capacity, the “Collateral Agent”) and lender, and Transocean Finance Limited, ATW Special Situations I LLC, Material Impact Fund II, L.P., and RCB Equities #1, LLC, as lenders, are related parties.

The Convertible Senior Secured Term Loan Agreement provides the Company with up to $20.0 million of secured term loans, of which $11.6 million has already been funded and deemed issued under the Convertible Senior Secured Term Loan Agreement. Any portion of the outstanding principal amount of the Loans is prepayable at the Company’s option pro rata to each Lender upon at least five days’ prior written notice to each Lender.

The Convertible Senior Secured Term Loan Agreement included a 2.5% exit fee or $290,000, bearing interest at 12.50% per annum, payable quarterly in arrears on the first day of each calendar quarter commencing April 1, 2024. The loan agreement included a 2.5% original issue discount or $125,000 from the RCB Equities #1, LLC promissory note. The loan includes assumed legal fees of $150,000, deemed interest from convertible debentures of $378,116, and $500,000 held in escrow, recorded under other current assets of the condensed consolidated balance sheet. The escrow balance will be held for at least thirty days or until the collateral agent determines no obligation of expense greater than $150,000 incurred by the lender. The Loans will mature on the earliest of (a) the third anniversary of the date of the Term Loan Agreement of September 17, 2026., (b) 91 days prior to the maturity of the 5% Original Issue Discount Senior Secured Convertible Debentures, dated as of September 9, 2022.

Subject to the terms and conditions of the Term Loan Agreement, the Company may, upon at least two trading days’ written notice to the Lenders, elect to redeem some or all of the then outstanding principal amount of the Loans. In connection with any such election, which shall be irrevocable, the Company shall pay each Lender, on a pro rata basis, an amount in cash equal to the greater of (x) the sum of (i) 100% of the then outstanding principal amount of the Loans, (ii) accrued but unpaid interest and (iii) all liquidated damages and other amounts due in respect of the Loans (including, without limitation, the Exit Fee (as defined in the Term Loan Agreement)) (the “Optional Redemption Amount”) and (y) the product of (i) the aggregate number of shares of the Company’s common stock, par value $0.0001 per share (“Common Stock”), then issuable upon conversion of the applicable Optional Redemption Amount (without regard to any limitations on conversion set forth in the Term Loan Agreement) multiplied by (ii) the highest closing sale price of the Common Stock on any trading day during the period commencing on the date immediately preceding the date that the applicable notice of redemption is delivered to the Lenders and ending on the trading day immediately prior to the date the Company makes the entire payment required to be made in connection with such redemption.

The Loans are convertible, in whole or in part, at the option of each Lender into shares of Common Stock until the date that the Loans are no longer outstanding, at a conversion rate equal to the outstanding principal amount of the Loans to be converted divided by a conversion price of $6.00 per share of Common Stock (the "Conversion Price"), subject to certain customary anti-dilution adjustments as described in the Term Loan Agreement.

8. Leases

The Company determines if an arrangement is a lease at inception based on whether the Company has the right to control the use of an identified asset, the right to obtain substantially all of the economic benefits from the use of the asset and the right to direct the use of the asset. After the criteria are satisfied, the Company accounts for these arrangements as leases in accordance with ASC 842, Leases. Right-of-use assets represent the Company's right to use the underlying asset for the lease term and lease liabilities represent the Company's obligation to make lease payments arising from the lease. Right-of-use assets and liabilities are recognized at the lease commencement date based on the present value of lease payments over the lease term, including payments at commencement that depend on an index or rate. For leases in which the Company is the lessee do not have a readily determinable implicit rate, an incremental borrowing rate, based on the information available at the lease commencement date, is utilized to determine the present value of lease payments. When a secured borrowing rate is not readily available, unsecured borrowing rates are adjusted for the effects of collateral to determine the incremental borrowing rate. The Company uses the implicit rate for agreements in which it is a lessor. The Company has not entered into any material agreements in which it is a lessor. Lease expense and lease income are recognized on a straight-line basis over the lease term for operating leases.

In April of 2023, the Company entered into an operating lease for office space. The lease has a 10-year lease term with an additional abatement period of 23 months. The Company's secured borrowing rate of 15% was used to determine the present value of lease payments and establish the right-of-use asset and lease liability at lease inception for this lease.

In July of 2023, the Company entered into an operating lease for office space in Scotland. The lease has a term of 5 years with two options to extend. Management is reasonably certain to exercise the first option to extend the lease. The Company's secured borrowing rate of 15% was used to determine the present value of the lease payments and establish the right-of-use asset and lease liability at lease inception for this lease.

In August of 2023, the Company entered into an operating lease for office space in Norway. The lease has a term of 5 years. The Company's secured borrowing rate of 15% was used to determine the present value of the lease payments and establish the right-of-use asset and lease liability at lease inception for this lease.

The Company's other operating leases include its current office and manufacturing facility and leases for certain office equipment.

The following table presents the Company's lease costs which are included in general and administrative expenses in the unaudited condensed consolidated statements of operations:

	Three months ended September 30,		Nine months ended September 30,	
	2023	2022	2023	2022
Fixed lease expense	$ 129,822	$ 139,315	$ 382,662	$ 69,191
Variable lease expense	136,785	89,016	192,547	44,508
Total operating lease expense	$ 266,607	$ 228,331	$ 575,209	$ 113,699

Cash paid for operating leases was $357,985 and $241,819 for the nine months ended September 30, 2023, and September 30, 2022, respectively.

The following table presents the balance and classifications of the Company's right-of-use assets and lease liabilities included in the unaudited condensed balance sheets:

	Balance Sheet Location	September 30, 2023	December 31, 2022
Assets			
Noncurrent			
Operating lease assets	Operating lease right-of-use asset	$ 2,090,859	$ 317,208
Liabilities			
Current			
Operating lease liabilities	Operating lease liabilities - current	616,308	410,158
Noncurrent			
Operating lease liabitlies	Operating lease liabilities - long-term	1,629,516	87,214
Total lease liabilities		$ 2,245,824	$ 497,372

For operating lease assets and liabilities, the weighted average remaining lease term was 10.5years and 2.2 years as of September 30, 2023, and December 31, 2022, respectively. The weighted average discount rate used in the valuation over the remaining lease terms was 14.2% as of September 30, 2023, and 7.9% as of December 31, 2022.

The following table presents the Company's maturities of lease liabilities as of September 30, 2023:

2023	$ 199,850
2024	194,982
2025	394,811
2026	455,125
2027	477,610
2028 onward	2,940,247
Total lease payments	4,662,625
Total present value discount	(2,416,801)
Operating lease liabilities	$ 2,245,824

9. Commitments and Contingencies

Litigation – From time to time, we may be subject to litigation and other claims in the normal course of business. No amounts have been accrued in the condensed consolidated financial statements with respect to any matters.

10. Income Taxes

Income tax provisions for interim periods are generally based on an estimated annual effective income tax rate calculated separately from the effect of significant, infrequent, or unusual items related specifically to interim periods. No income tax expense was recognized for the nine months ended September 30, 2023, or 2022. The Company has a full valuation allowance against its deferred tax assets as of September 30, 2023, and December 31, 2022, respectively.

11. Equity

Common Stock – A total of 49,858,194 shares of Common Stock were outstanding as of September 30, 2023.

Earnout Shares - Following the closing of the Business Combination, former holders of shares of Nauticus Robotics Holdings' Common Stock (including shares received as a result of the Nauticus Preferred Stock Conversion and the Nauticus Convertible Notes Conversion) are entitled to receive their pro rata share of up to 7,499,993 Earnout Shares which are held in escrow. The Earnout Shares will be released from escrow upon the occurrence of certain Triggering Events. As of September 30, 2023, the earnout targets have not been achieved, and the Earnout Shares remain in escrow.

12. Warrants

Public Warrants – We assumed 8,624,991 Public Warrants in the Business Combination which remained outstanding as of September 30, 2023. Each whole Public Warrant entitles the holder to purchase one share of Common Stock at a price of $11.50, subject to adjustment. However, no Public Warrants will be exercisable for cash unless we have an effective and current registration statement covering the shares of Common Stock issuable upon exercise of the Public Warrants and a current prospectus relating to such shares of Common Stock. During any period when we shall have failed to maintain an effective registration statement, warrant holders may exercise, subject to the terms of the governing warrant agreement, Public Warrants on a cashless basis pursuant to an available exemption from registration under the Securities Act. The Public Warrants expire on the fifth anniversary of our completion of the Business Combination, or earlier upon redemption or liquidation. Our Public Warrants are listed on Nasdaq under the symbol "KITTW".

We may redeem the outstanding Public Warrants, in whole and not in part, at a price of $0.01 per warrant:

- at any time after the Public Warrants become exercisable,
- upon not less than 30 days' prior written notice of redemption to each warrant holder,
- if, and only if, the reported last sale price of the shares of Common Stock equals or exceeds $16.50 per share (subject to adjustment for splits, dividends, recapitalizations and other similar events), for any 20 trading days within a 30-day trading period ending on the third business day prior to the notice of redemption to warrant holders, and
- if, and only if, there is a current registration statement in effect with respect to the shares of Common Stock underlying such warrants at the time of redemption and for the entire 30-day trading period referred to above and continuing each day thereafter until the date of redemption.

If we call the Public Warrants for redemption as described above, we have the option to require all holders that wish to exercise warrants to do so on a "cashless basis."

The exercise price and number of shares of Common Stock issuable on exercise of the Public Warrants may be adjusted in certain circumstances including in the event of a share dividend, extraordinary dividend or our recapitalization, reorganization, merger or consolidation.

The Public Warrants, which are accounted for as liabilities in our condensed consolidated balance sheets, were valued as of September 30, 2023, at $1,897,500 based on their publicly-traded price. The change in the value of the Public Warrants during the three and nine months ended September 30, 2023, totaled $(24,150) and $378,638, respectively, and was reported with other (income) expense in our condensed consolidated statements of operations.

Private Warrants – We assumed 7,175,000 Private Warrants in the Business Combination, which remained outstanding as of September 30, 2023. Each whole Private Warrant is exercisable for one share of Common Stock at an exercise price of $11.50 and is identical in all material respects to the Public Warrants except that the Private Warrants are exercisable for cash (even if a registration statement covering the shares of Common Stock issuable upon exercise of such warrants is not effective) or on a cashless basis, at the holder's option, and will not be redeemable by us, in each case so long as the initial purchasers or their affiliates still hold them. The Private Warrants purchased by CleanTech Investments, LLC are not exercisable after July14, 2026, as long as Chardan Capital Markets, LLC or any of its related persons beneficially own these Private Warrants.

The Private Warrants, which are accounted for as liabilities in our condensed consolidated balance sheets, were valued as of September 30, 2023, at $1,636,052 based on their using a Black-Scholes model. The fair value of the Private Warrants was estimated using a Black-Scholes option pricing model using the following assumptions: stock price of $1.77, no assumed dividends, a risk-free rate of 4.59%, and implied volatility of 67.0%. The change in the value of the Private Warrants during the three and nine months ended September 30, 2023, totaled $40,973 and $298,536, respectively, and was reported with other (income) expense in our condensed consolidated statements of operations.

SPA Warrants – Substantially concurrent with the Closing and pursuant to the Securities Purchase Agreement, we issued an aggregate 2,922,425 Original SPA Warrants to the SPA Parties. Upon issuance, each whole Original SPA Warrant was exercisable over its 10-year term for one share of Common Stock at a price of $20.00 per share, subject to certain adjustments including full ratchet anti-dilution price protections.

In connection with the Securities Purchase Agreement, the Company and the SPA Parties entered into that certain Registration Rights Agreement, dated as of September 9, 2022 (the "RRA"), pursuant to which the Company and the SPA Parties agreed to certain requirements and conditions covering the resale by the SPA Parties of the shares of Common Stock underlying the Debentures and Original SPA Warrants. Under the terms of the RRA, the Company was required to (i) file a registration statement (the "Initial Registration Statement") covering such underlying shares within 15 business days of the Closing and (ii) use its best efforts to cause the Initial Registration Statement to be declared effective as promptly as possible after the filing thereof, but in any event no later than the applicable Effectiveness Date (as defined in the RRA) (the "Registration Requirements"). The RRA additionally provided for liquidated damages if the Registration Requirements were not met.

On June 22, 2023, the Company and the SPA Parties entered into the first amendment to the RRA (the "RRA Amendment"), pursuant to which the Company agreed to deliver to the SPA Parties an aggregate 1,890,066 shares of Common Stock at an agreed upon price of $2.286 (the "RRA Amendment Shares") in exchange for the waiver and release by the SPA Parties of any and all claims, remedies, causes of action and any other Initial Effectiveness Date Claims (as defined in the RRA Amendment) under any of the Transaction Documents (as defined in the RRA), including all past and future claims for liquidated damages under the RRA with respect to, and any other amounts that may be payable by reason of or otherwise relating to, the Effectiveness Date (as defined in the RRA) of the Initial Registration Statement.

During the third quarter of 2023, the Company issued 1,890,066 shares of Common Stock as payment for liquidated damages and interest of $4,320,690, and the damages and interest are recorded under interest expense in the condensed consolidated statements of operations. The settlement date of the liquidated damages occurred August 3, 2023, with a closing price of $1.95, with the change in the agreed upon price of $2.286 to settlement resulting in a gain of $635,061, which is also included in interest expense in the condensed consolidated statements of operations.

Pursuant to the RRA Amendment, the Company also agreed to file a registration statement on Form S-3 (or other appropriate form) for the registration and resale of the RRA Amendment Shares by the SPA Parties and to cause such registration statement to become effective as soon as practicable thereafter in accordance with the terms of the RRA, as amended by the RRA Amendment.

On June 22, 2023, we entered into the Letter Agreements with the SPA Parties (the "Letter Agreements"), pursuant to which the SPA Parties (also being the holders of the Original SPA Warrants) agreed to amend the exercise price of the Original SPA Warrants, which, since issuance, had been exercisable to purchase an aggregate 2,922,425 shares of Common Stock, in exchange for the Company's agreement to (i) lower the exercise price of the Original SPA Warrants to a weighted average of $3.28 per share, with multiple tranches priced between $2.04 and $4.64 per share, and (ii) upon the SPA Parties' exercise of the Amended SPA Warrants, issue New SPA Warrants to the SPA Parties to purchase, in the aggregate, up to 2,922,425 shares of Common Stock.

The Letter Agreements will terminate in accordance with their terms on March 1, 2024 (the "Letter Agreement Termination Date"). Upon the Letter Agreement Termination Date, any Amended SPA Warrants then-outstanding will revert to having the terms associated with the Original SPA Warrants, as described herein.

During any period when we shall have failed to maintain an effective registration statement covering the shares of Common Stock issuable upon exercise of the Amended SPA Warrants, the registered holder may exercise its Amended SPA Warrants on a cashless basis pursuant to an available exemption from registration under the Securities Act.

On June 23, 2023, pursuant to its Letter Agreement with the Company, ATW exercised 165,713 Amended SPA Warrants, pursuant to which 165,713 shares of Common Stock and 165,713 New SPA Warrants were issued to ATW by the Company in accordance with the terms of the Letter Agreement. The Company received proceeds of $338,055 from the warrants exercised by ATW.

On September 18, 2023, the Company entered into a convertible senior secured term loan agreement convertible at $6.00 per share. Based on the letter agreement, SPA warrants holders who exchange through March 1. 2024, the exercise price was reset from $20.00 to $6.00 a warrant pursuant to the full-ratchet provision. The exchange warrants were reset to $6.00 with a factor of 3.3333, increasing the number of warrants to 552,377.

The New SPA Warrants will be (and, with respect to those already issued, are) substantially in the form of the Amended SPA Warrants as described above except that the New SPA Warrants (i) have an exercise price of $20.00 per share (including, for purposes of clarification, full-ratchet anti-dilution on the exercise price and number of underlying shares issuable based on the aggregate exercise price using $20.00 as the base exercise price), (ii) are immediately exercisable upon issuance, and (iii) are exercisable until September 9, 2032.

If a registration statement covering the shares of Common Stock issuable upon exercise of the New SPA Warrants is not effective 60 days after March 1, 2024 (or, in the event of a "full review" by the SEC, 120 days after March 1, 2024), upon the registered holder's election to exercise its New SPA Warrants, the registered holder may, until such time as there is an effective registration statement and during any period when we shall have failed to maintain an effective registration statement, exercise its New SPA Warrants on a cashless basis pursuant to an available exemption from registration under the Securities Act.

As indicated in Note 1 above, unless context otherwise requires, the term "SPA Warrants" means (i) before the entry into the Letter Agreements, the Original SPA Warrants, and (ii) upon and following the entry into the Letter Agreements, (a) the Amended SPA Warrants, and (b) the New SPA Warrants.

The SPA Warrants, which are accounted for as liabilities in our condensed consolidated balance sheets, were valued as of September 30, 2023, at $10,969,897 and were estimated using a Monte Carlo valuation model incorporating future projections of the various potential outcomes and any exercise price adjustments based on future financing events. Management's future assumptions to raise enough debt capital in the near term to become cash-flow positive have eliminated reset events and have affected the valuation's variability from the prior quarter. The change in the value of the SPA Warrants during the three and nine months ended September 30, 2023, totaled $(8,721,515) and $18,097,987, respectively, and was reported with other (income) expense in our condensed consolidated statements of operations. Due to entering into the Letter Agreements, the warrants were accounted for and treated as warrant repricing, resulting in a loss of $590,266, which was reported with other (income) expense in our condensed consolidated statements of operations. Proceeds from the exercise of SPA Warrants for the nine months ended September 30, 2023, were $338,055.

13. Stock-Based Compensation

On September 6, 2022, shareholders approved our 2022 Omnibus Incentive Plan (the "Omnibus Incentive Plan") and on September 9, 2022, our board of directors ratified the Omnibus Incentive Plan. The Omnibus Incentive Plan provides for the grant of options, stock appreciation rights, restricted stock units ("RSUs"), restricted stock and other stock-based awards, any of which may be performance-based, and for incentive bonuses, which may be paid in cash, Common Stock or a combination thereof. As of September 30, 2023, 7,789,663 equity units were available for future issuance under the Omnibus Incentive Plan.

At the Closing Date of the Business Combination, Nauticus Robotics Holdings, Inc. had 279,464 options outstanding for the purchase of its Common Stock. Such options were originally issued under the 2015 Equity Incentive Plan (the "2015 Plan") historically maintained by Nauticus Robotics Holdings, Inc. The outstanding options were converted into 3,970,266 options to purchase shares of our Common Stock. Outstanding options vest assuming continuous service to the Company, with 25% of the options vesting one year after grant and the balance vesting in a series of 36 successive equal monthly installments measured from the first anniversary of grant. During the vesting period, holders have no rights of a stockholder with respect to the shares of Common Stock subject to an option, and the options may not be sold, assigned, transferred, pledged, or otherwise encumbered. Unvested options are forfeited upon termination of employment. As of September 30, 2023, 3,084,601 options (originally issued under the 2015 Plan) remained available to purchase shares of our Common Stock.

Compensation expense for stock option grants is recognized based on the fair value at the date of grant using the Black-Scholes option pricing model.

Stock-based compensation expense, which relates to options originally issued under the 2015 Plan, totaled $131,098 and $406,679 for the three and nine months of 2023, respectively, and was recorded in general and administrative expense. Stock-based compensation expense, which relates to options originally issued under the 2015 Plan, totaled $235,593 and $624,407 for the three and nine months of 2022, respectively, and was recorded in general and administrative expense. As of September 30, 2023, $948,451 of total unrecognized compensation costs related to the options will be recognized as an expense over a remaining weighted average period of 1.91 years.

The following table summarizes options outstanding, as well as activity for the periods presented (prior year amounts have been converted using the conversion ratio of 14.2069 applied in the Business Combination):

	Options	Weighted Average Exercise Price	Aggregate Intrinsic Value
Outstanding as of December 31, 2021	3,949,158	$ 1.84	$ 2,992,895
Granted	166,927	$ 2.50	
Forfeited	(174,817)	$ 2.25	
Cancelled	(7,103)	$ 1.28	
Outstanding as of September 30, 2022	3,934,165	$ 1.86	$ 6,901,057
Outstanding as of December 31, 2022	3,503,601	$ 1.87	$ 6,554,541
Exercised	(227,837)	$ 1.85	
Forfeited	(66,964)	$ 2.00	
Cancelled	(124,199)	$ 2.28	
Outstanding as of September 30, 2023	3,084,601	$ 1.85	$ 525,465

The remaining weighted average contractual life of exercisable options as of September 30, 2023, was 5.71 years.

The total intrinsic value of all options exercised during the nine months ended September 30, 2023 and 2022, was $104,985 and $0, respectively. The intrinsic value of all options outstanding as of September 30, 2023 and 2022, was $525,465 and $6,901,057, respectively. The intrinsic value of all exercisable options as of September 30, 2023 and 2022, was $507,471 and $4,458,862, respectively.

Proceeds from exercises of options issued under the 2015 Plan for the nine months ended September 30, 2023 and 2022, were $421,175 and $0, respectively. The tax benefit realized from stock-based compensation was $196,711 and $0 for the nine months ended September 30, 2023 and 2022, respectively. Realization of this amount is dependent on the generation of future taxable income.

Incentive Plans – During 2022, RSUs were granted to certain of our key executives, employees, and non-employee directors. Each RSU is a notional amount that represents the right to receive one share of Common Stock of the Company if and when the RSU vests. RSUs were issued to the following recipients and vest as follows:

Employee RSU grants are time-based and vest equally over a three-year period on December 31 of 2023, 2024, and 2025, conditional upon continued employment.

Non-employee director RSU grants are time-based and vest fully on the earlier of the one-year anniversary of the grant date or the next Annual Meeting of Stockholders of the Company if a grantee is not on the election ballot, conditional upon continued service as a director.

Executive RSU grants issued as executive sign-on bonuses are time-based and vest 50% on the one-year anniversary of the new hire date and 50% on the two-year anniversary of the new-hire date.

In addition, during 2022, an aggregate target grant of 1,214,580 performance-based restricted stock units ("PRSUs") were made to members of the senior executive management team. Each PRSU is a notional amount that represents the right to receive one share of Common Stock if and when the applicable PRSU performance period is measured and the settled PRSU vests. PRSU participants may earn between 0% and 150% of the target PRSUs granted based on the attainment of performance conditions connected to the Company's 2022 revenues. The PRSUs earned will vest 50% on December 31, 2023, and 50% on December 31, 2024.

In March 2023, the Company's board of directors determined that 51% of the performance target was satisfied and an aggregate 619,438 PRSUs were settled to members of the senior executive management team and will vest in accordance with the terms of the applicable award agreements.

The Compensation Committee has a policy that the Company will not provide U.S. federal income tax gross-up payments to any of its directors or executive officers in connection with future awards of restricted stock or stock units.

The following is a summary of our RSU and PRSU activity for the first nine months of 2023:

	Shares	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value
Outstanding as of December 31, 2022	3,134,677	$ 4.73	
Awarded	271,399	$ 2.68	
Released	(323,807)	$ 4.08	
Forfeited	(670,667)	$ 4.48	
Outstanding as of September 30, 2023	2,411,602	$ 4.65	$ 4,268,535

The remaining weighted average contractual life of RSUs granted as of September 30, 2023, was 1.37 years.

The RSUs and PSRUs granted in 2022 do not have voting rights or dividend rights unless the subject RSU or PRSU has vested and the share of common stock underlying it has been distributed to the participant.

Grants of RSUs are valued at their estimated fair values as of their respective grant dates. The RSU grants in 2022 were subject only to vesting conditioned on continued employment or service as a nonemployee director; therefore, these grants were valued at the grant date fair market value using the closing price of our stock on the Nasdaq Stock Market.

Stock-based compensation expense attributable to PRSUs under the Omnibus Incentive Plan for the three and nine months ended of 2023 was $102,127 and $613,661, respectively and recorded in general and administrative expense. Stock-based compensation expense attributable to RSUs under the Omnibus Incentive Plan for the three and nine months ended of 2023, respectively, was $725,879 and $2,974,680 and recorded in general and administrative expense. As of September 30, 2023, we had $855,793 of future expense related to PRSUs to be recognized and $4,037,399 of future expense related to RSUs over a weighted average remaining life of 1.37 years. Total stock-based compensation expense for the three and nine months of 2023, including options, PRSUs, and RSUs, totaled $959,104 and $3,995,020, respectively. Total stock-based compensation expense for the three and nine months of 2022 for options totaled $235,593 and $624,407, respectively.

14. Employee Benefit Plan

Nauticus offers a 401(k) plan which permits eligible employees to contribute portions of their compensation to an investment trust. The Company makes contributions to the plan totaling 3% of employees' gross salaries and such contributions vest immediately. The 401(k) plan provides several investment options, for which the employee has sole investment discretion. The Company's cost for the 401(k) plan was $103,446 and $262,952 for the three and nine months ended September 30, 2023, respectively. The Company's cost for the 401(k) plan was $89,854 and $252,166 for the three and nine months ended September 30, 2022, respectively.

15. Related Party Transactions

PIPE Investment and Securities Purchase Agreement – Concurrent with the closing of the Business Combination, the Company received (i) $2,500,000 from related party Material Impact Fund II, L.P. ("Material Impact") as their contribution to the PIPE Investment, (ii) $7,500,000 from related party Schlumberger Technology Corporation as their contribution to the PIPE Investment, (iii) $7,500,000 from related party Transocean Ltd. as their contribution to the PIPE Investment, (iv) $5,000,000 from related party RCB Equities #4, LLC, as their contribution to the PIPE Investment and (v) $1,836,720 from related party SLS Family Irrevocable Trust, $29,591,600 from related party ATW and $5,102,000 from related party Material Impact pursuant to the Securities Purchase Agreement.

ATW, Material Impact and SLS Family Irrevocable Trust currently hold $29,591,600, $5,102,000 and $1,836,720 respectively, of the outstanding Debentures, which bear interest at a rate of 5% per annum, payable quarterly, and mature on September 9, 2026. During the three and nine months ended September 30, 2023, ATW Material Impact, and SLS Family Irrevocable Trust received $88,661 and $1,006,993, respectively, in interest payments on the Debentures from the Company.

Convertible Senior Secured Term Loan – The Company entered into a convertible senior secured term loan agreement with ATW Special Situations II LLC as collateral agent (in such capacity, the "Collateral Agent") and lender, and Transocean Finance Limited, ATW Special Situations I LLC, Material Impact Fund II, L.P., and RCB Equities #1, LLC, as lenders, are related parties. See "Financial Statements – Note 7 Notes Payable for additional information.

RRA Amendment – On June 22, 2023, the Company and the SPA Parties entered into the RRA Amendment, pursuant to which, among other things, the Company agreed to issue 1,531,059, 263,976 and 95,031 RRA Amendment Shares to ATW , Material Impact and SLS Family Irrevocable Trust, respectively, in exchange for their waiver and release of any and all claims, remedies, causes of action and any other Initial Effectiveness Date Claims (as defined in the RRA Amendment) under any of the Transaction Documents (as defined in the RRA), including all past and future claims for liquidated damages under the RRA with respect to, and any other amounts that may be payable by reason of or otherwise relating to, the Effectiveness Date (as defined in the RRA) of the Initial Registration Statement. See Note 12 for more information.

Letter Agreements – On June 22, 2023, the Company entered into Letter Agreements with ATW, Material Impact and SLS Family Irrevocable Trust, pursuant to which such, among other things, the Company agreed to (i) lower the exercise price of the Original SPA Warrants from $20.00 per share to a weighted average of $3.28 per share, with multiple tranches priced between $2.04 and $4.64 per share, and (ii) upon the exercise of Amended SPA Warrants, issue to the exercising party New SPA Warrants to purchase up to a number of shares of Common Stock equal to the number of Original SPA Warrants initially issued to such party.

On June 23, 2023, pursuant to its Letter Agreement with the Company, ATW exercised 165,713 Amended SPA Warrants, pursuant to which 165,713 shares of Common Stock and 165,713 New SPA Warrants were issued to ATW by the Company in accordance with the terms of the Letter Agreement. The Company received proceeds of $338,039 from the warrants exercised by ATW.

On September 18, 2023, the Company entered into a convertible senior secured term loan agreement convertible at $6.00 per share. Based on the Letter Agreement, SPA warrants holders who exchange through March 1. 2024, the exercise price was reset from $20.00 to $6.00 a warrant pursuant to the full-ratchet provision. The exchange warrants were reset to $6.00 with a factor of 3.3334, increasing the number of warrants to 552,377.

Revenue and Accounts Receivable – Revenue from Transocean Ltd. for contract services totaled $17,000 and $210,400 for the three months and nine months ended September 30, 2022, respectively. Accounts receivable included $0 and $21,000 outstanding from Transocean Ltd. at September 30, 2023, and December 31, 2022, respectively.

16. Earnings (Loss) Per Share

Following is the computation of earnings (loss) per basic and diluted share:

	Three months ended September 30,		Nine months ended September 30,	
	2023	**2022**	**2023**	**2022**
Numerator:				
Net earnings (loss)	$ (17,678,787)	$ (13,176,497)	$ (11,144,012)	$ (20,037,455)
Less: deemed dividend for Earnout Shares		(4,957,366)		(4,957,366)
Net earnings (loss) attributable to common stockholders	$ (17,678,787)	$ (18,133,863)	$ (11,144,012)	$ (24,994,821)
Denominator:				
Weighted average shares used to compute basic EPS	41,155,115	16,535,661	40,453,015	11,983,183
Basic and diluted earnings (loss) per share	$ (0.43)	$ (1.10)	$ (0.28)	$ (2.09)
Anti-dilutive securities excluded from shares outstanding:				
Stock options	3,084,601	3,934,165	3,084,601	3,934,165
Restricted and performance stock units	2,411,602	-	2,411,602	-
Warrants	19,109,090	18,722,425	19,109,090	18,722,425
Earnout shares	7,499,993	7,499,993	7,499,993	7,499,993
Convertible debt	4,855,758	2,922,425	4,855,758	2,922,425
Total	36,961,044	33,079,008	36,961,044	33,079,008

17. Fair Value Measurements

The Company measures and reports certain financial and non-financial assets and liabilities on a fair value basis. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three levels related to fair value measurements are as follows:

Level 1 – Observable inputs such as quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active or other inputs that are observable or can be corroborated by observable market data.

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. This includes certain pricing models, discounted cash flow methodologies, and similar techniques that use significant unobservable inputs.

The estimated fair values of accounts receivable, contract assets, accounts payable, accrued expenses, and indebtedness with unrelated parties approximate their carrying amounts due to the relatively short maturity or time to maturity of these instruments. Notes payable with related parties may not be arms-length transactions and therefore may not reflect fair value. The estimated fair value of the Debentures approximates their carrying amount due to their recent issuance.

The Company's non-financial assets measured at fair value on a recurring basis include SPA Warrants and Private Warrants. These are considered Level 3 measurements as they involve significant unobservable inputs.

In accordance with the fair value hierarchy described above, the following tables show the fair value of the Company's financial liabilities that are required to be measured at fair value on a recurring basis and the related activity for the periods presented:

	Fair Value as of September 30, 2023			
	Carrying Value	**Level 1**	**Level 2**	**Level 3**
Financial liabilities:				
Warrant liability - Public Warrants	$ 1,897,500	$ 1,897,500	$ -	$ -
Warrant liability - Private Warrants	1,636,052	-	-	1,636,052
Warrant liability - SPA Warrants	10,969,897	-	-	10,969,897
Total	$ 14,503,449	$ 1,897,500	$ -	$ 12,605,949

The following table sets forth a summary of the changes in fair value of the Company's financial liabilities:

	Warrant Liability
Balance, December 31, 2022	$ 32,688,341
Loss on exchange of warrants	590,266
Change in fair value of warrant liabilities	(18,775,158)
Balance, September 30, 2023	$ 14,503,449

18. Subsequent Events

Merger Agreement with 3D at Depth

On October 2, 2023, Nauticus entered into an Agreement and Plan of Merger (the "Merger Agreement") with 3D Merger Sub, Inc., a Delaware corporation and a direct, wholly owned subsidiary of Nauticus ("Merger Sub"), and 3D at Depth, Inc., a Delaware corporation ("3DAD", and together with Nauticus and Merger Sub, each a "Party" and collectively the "Parties"). Pursuant to the Merger Agreement, and upon the terms and subject to the conditions thereof, a merger between Nauticus and 3DAD will be effected through the merger of Merger Sub with and into 3DAD, with 3DAD surviving the merger as a wholly owned subsidiary of Nauticus (the "Merger", and together with the other transactions contemplated by the Merger Agreement and the other agreements contemplated thereby, the "Transactions"). The board of directors of Nauticus (the "Board") has unanimously (i) approved the Merger Agreement and the Transactions and (ii) resolved to recommend the approval and adoption of the Merger Agreement and the Transactions to the stockholders of Nauticus ("Nauticus Stockholders").

The Base Equity Value for the 3DAD Merger is $34M. The consideration of payment will be 100% equity transaction of Nauticus common stock. The "Per Share Equity Consideration" means, with respect to any share of 3DAD Common Stock held by a 3DAD stockholder which is issued and outstanding immediately prior to the Effective Time, a number of shares of Nauticus Common Stock equal to (a) the Per Share Equity Consideration Value (as defined below) divided by (b) the 20-day VWAP (as defined in the Merger Agreement) calculated pursuant to Annex II of the Merger Agreement, which is stipulated by the Parties to be $2.04.

The "Per Share Equity Consideration Value" means (a) the Base Equity Value (as adjusted, if applicable, as set forth above) divided by (b) the total number of shares of 3DAD Common Stock issued and outstanding as of immediately prior to the Effective Time.

Closing of the transaction contemplated by the Merger Agreement is subject to the satisfaction or waiver of usual and customary conditions, including the effectiveness of a Registration Statement on Form S-4 and the approval of the stockholders of both Nauticus and 3DAD.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto included in Part I, Item 1, "Financial Statements" of this Quarterly Report on Form 10-Q.

Explanatory Note

On the Closing Date, we consummated the Business Combination with Merger Sub, and Nauticus Robotics Holdings, Inc. Pursuant to the terms of the Merger Agreement, a business combination between CLAQ and Nauticus Robotics Holdings was affected through the merger of Merger Sub with and into Nauticus Robotics Holdings, with Nauticus Robotics Holdings surviving the merger as a wholly owned subsidiary of CLAQ. On the Closing Date, CLAQ was renamed "Nauticus Robotics, Inc." and the Nauticus Robotics Holdings' predecessor was renamed "Nauticus Robotics Holdings, Inc."

The Business Combination was accounted for as a reverse recapitalization under generally accepted accounting principles in the United States ("GAAP"). Nauticus Robotics Holdings, Inc. was determined to be the accounting acquirer and CLAQ was treated as the acquired company for financial reporting purposes. Accordingly, the financial statements of Nauticus represent a continuation of the financial statements of Nauticus Robotics Holdings, Inc.

Overview

Nauticus Robotics, Inc. (the "Company," "our," "us," or "we") is a developer of ocean vehicles and robots, autonomy software, intervention and data services delivered to the offshore industries. We were initially incorporated as CleanTech Acquisition Corp. ("CLAQ") under the laws of the State of Delaware on June 18, 2020. The Company's principal corporate offices are located in Webster, Texas. Our offshore services provide customers with the necessary inspection, intervention, data collection, and analytics, ~~a~~ to support and maintain assets while reducing their operational footprint, operating cost, and greenhouse gas emissions, as well ~~as to~~ improving offshore health, safety, and environmental exposure.

Nauticus' mission is to be the most impactful ocean robotics company through the deployment of autonomous systems. To that end, Nauticus is a technology company, tooled accordingly. Our core staff were principals in the spaceflight robotics community from NASA. In addition, we have continued to augment our staff with data scientists, roboticists, and engineers to create and deploy intelligent machines into the ocean domain with significant self-sufficient and self-directed behaviors, to robustly handle the uncertainty of real-time events underwater.

The opportunity we saw was to remove the operational requirement for tethers and high-speed communication, central to how current undersea operations are performed using Remotely Operated Vehicles (ROVs). These lengthy and constraining tethers require large and expensive surface vessels to operate the ROVs, which in turn drive the cost of accessing the underwater environment. Nauticus has clean slate developed and deployed an ecosystem of autonomy software and novel vehicle architectures to render obsolete current operational paradigms that necessitate the usage of these tethers and therefore, our service could potentially reduce the subsequent operational costs.

The industries affected by this shift in offshore operations are numerous. These include oil & gas, offshore renewables like wind, and tidal, telecommunications, national security & defense, aquaculture, ports, and mining to name a few. To address these markets, Nauticus is commercializing the *Nauticus Fleet*, which is the cornerstone of our offshore offering. The *Nauticus Fleet* tandem pair is comprised of both an unmanned underwater vehicle (Aquanaut), and a small optionally crewed surface vessel (Hydronaut). Hydronaut, an 18-meter optionally crewed autonomous surface vessel (ASV) that supports the launch, recovery and real-time operations of Aquanaut, its undersea robotic counterpart. Hydronaut ferries Aquanaut to and from the worksite and supports battery recharges and the communications link from the local remote operations center for supervised autonomous operations.

Aquanaut is a fully electric, free-swimming subsea robot, controlled through acoustic communication networking and can perform a wide range of data collection, inspection, and intervention tasks. Covered under US Patent, Aquanaut's defining capability is operating in two distinct modes: actively transforming itself between the excursion and intervention configurations. Excursion mode involves the usage of data collection and perception sensors during transit, while intervention mode uses two electric work-class manipulators (Nauticus' Olympic Arms) to perform work in the subsea environment.

Nauticus has spent several years developing the latest generation of Aquanaut and Hydronaut capabilities and we are now entering the commercialization phase. Much time and attention has been paid to the manufacturability of the designs and we anticipate we can potentially scale the business beyond the initial production run. This includes a data and drawing build package that can be bid out to vehicle manufactures to help drive down long-term production costs.

Commercializing offshore technology is a lengthy and expensive process. Extensive functional acceptance testing (FATs) has been performed, at the subsystem level, to catch any production quality issues during assembly. After the unit build is complete, in water commissioning exercises will be performed to ensure the system is functioning properly. Finally, initial production units must be qualified for offshore work in the energy sector. This work is currently ongoing to support our initial contracts with Shell, Petrobras, and Equinor.

We expect to have each *Nauticus Fleet* tandem pair utilized at 200 working days per year, with our service contract commercial ramp beginning in the first quarter of 2024.

Basis of Presentation – The accompanying condensed consolidated financial statements have been prepared by the Company without audit pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the "SEC") and, in the opinion of management, include all adjustments (consisting of normal, recurring adjustments, unless otherwise disclosed) necessary for a fair statement of the condensed consolidated results of operations, financial position, cash flows, and changes in stockholders' equity (deficit) for each period presented. All intercompany balances and transactions have been eliminated in preparation of these condensed consolidated financial statements. The condensed consolidated results for the interim periods are not necessarily indicative of results to be expected for the full year. The 2022 year-end consolidated balance sheet was derived from audited financial statements but does not include all disclosures required by GAAP. These financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2022.

Impact of COVID-19 Pandemic on Business **–** The global spread of COVID-19 and its variants (e.g., the omicron variant) created significant market volatility, economic uncertainty, and disruption during 2021 and 2022 and continuing into 2023. The Company was adversely affected by the deterioration and increased uncertainty in the macroeconomic outlook as a result of the impact of COVID-19. We have experienced and may continue to experience disruptions in our supply chain, due in part to the global impact of the COVID-19 pandemic. Depending upon the duration, including the extent of any residual or further effects, of COVID-19 pandemic-related business interruptions, our customers, suppliers, manufacturers, and partners may suspend or delay their engagements with us, which could result in a material adverse effect on our financial condition and ability to meet current timelines. In addition, the COVID-19 pandemic has affected and may continue to affect our ability to recruit skilled employees to join our team. The conditions caused by the COVID-19 pandemic have adversely affected and may continue to adversely affect, among other things, demand for our products and the ability to test and assess our robotic systems with potential customers, any of which, in turn, could adversely affect our business, results of operations and financial condition. Any further or future impacts of COVID-19 or of another pandemic, epidemic or outbreak of an infectious disease cannot be accurately predicted at this time, and the ultimate direct and indirect impacts on our business, results of operations, and financial condition will depend on future developments that are highly uncertain.

Liquidity **–** Total cash and cash equivalents on hand as of September 30, 2023, was $6.8 million. The Company has incurred recurring losses each year since its inception. The Company may seek funding through additional debt or equity financing arrangements, implement incremental expense reduction measures, or a combination thereof to continue financing its operations. The Company implemented a workforce reduction of 22% on September 29, 2023, which increased costs by $.4 million in the current quarter, which is attributable to severance paid to employees. The cost savings that will be realized over the next twelve months is expected to be $2.7 million. During the third quarter of 2023, the Company received net proceeds of $10.4 million from the issuance of debt. Utilizing cost control measures, cash on hand, revenue from operations, and potential future equity and debt funding, the Company anticipates having sufficient funds to meet its obligations for at least one year from the issuance date of this Form 10-Q. See "Financial Statements – Note 7– Notes Payable" for additional information on debt capital.

Results of Operations

Three and Nine Months Ended September 30, 2023, Compared to Three and Nine Months Ended September 30, 2022

The following table sets forth summarized condensed consolidated financial information:

	Three months ended		Change		Nine months ended		Change	
	2023	**2022**	**$**	**%**	**2023**	**2022**	**$**	**%**
Revenue								
Service	$ 1,593,854	$ 2,964,610	$ (1,370,756)	-46%	$ 5,542,249	$ 7,996,734	$ (2,454,485)	-31%
Service - related party	-	17,000	(17,000)	-100%	500	210,400	(209,900)	-100%
Total revenue	1,593,854	2,981,610	(1,387,756)	-47%	5,542,749	8,207,134	(2,664,385)	-32%
Costs and Expenses								
Cost of revenue	2,651,380	3,781,224	(1,129,844)	-30%	7,484,249	8,220,447	(736,198)	-9%
Depreciation	160,744	141,901	18,843	13%	487,052	370,306	116,746	32%
Research and development	275,154	242,996	32,158	13%	984,882	2,094,278	(1,109,396)	-53%
General and administrative	6,704,890	4,861,319	1,843,571	38%	17,478,099	8,778,498	8,699,601	99%
Total costs and expenses	9,792,168	9,027,440	764,728	8%	26,434,282	19,463,529	6,970,753	36%
Operating loss	(8,198,314)	(6,045,830)	(2,152,484)	36%	(20,891,533)	(11,256,395)	(9,635,138)	86%
Other (income) expense:								
Other (income) expense, net	(133,311)	(27,980)	(105,331)	376%	1,019,816	(32,692)	1,052,508	-3219%
(Gain) on sale of assets	-	-	-	0%	(3,908)	-	(3,908)	-100%
Foreign currency transaction loss (gain)	83,654	(206,617)	290,271	100%	56,061	(207,146)	263,207	100%
Loss on exchange of warrants	-	-	-	0%	590,266	-	590,266	100%
Change in fair value of warrant liabilities	8,656,392	5,963,238	2,693,154	45%	(18,775,158)	5,963,238	(24,738,396)	-415%
Interest expense, net	873,738	1,402,026	(528,288)	-38%	7,365,402	3,057,660	4,307,742	141%
Net income (loss)	$ (17,678,787)	$ (13,176,497)	$ (4,502,290)	34%	$ (11,144,012)	$ (20,037,455)	$ 8,893,443	-44%

Revenue. For the three months ended September 30, 2023, total revenue decreased by $1.4 million, or 47%, to $1.6 million for 2023, as compared to $3.0 million for 2022. The decrease in total revenue is primarily attributable to delays in contract authorizations with government entities and completion of several contracts during the quarter.

For the nine months ended September 30, 2023, total revenue decreased by $2.7 million, or 32%, to $5.5 million for 2023, as compared to $8.2 million for 2022. The decrease in total revenue is primarily attributable to delays in contract authorizations with government entities and completion of several contracts during the quarter.

Cost of revenue. For the three months ended September 30, 2023, cost of revenue decreased by $1.1 million, or 30%, to $2.7 million for 2023, as compared to $3.8 million for 2022. The decrease in the cost of revenue is primarily attributable to decreased revenue as discussed above.

For the nine months ended September 30, 2023, cost of revenue decreased by $0.7 million, or 9%, to $7.5 million for 2023, as compared to $8.2 million for 2022. The decrease in the cost of revenue is primarily attributable to decreased revenue as discussed above.

Depreciation. For the three months ended September 30, 2023, depreciation increased by $19 thousand, or 13%, to $161 thousand for 2023, as compared to $142 thousand for 2022 primarily due to primarily due to increased investment in operational assets.

For the nine months ended September 30, 2023, depreciation increased by $117 thousand, or 32%, to $487 thousand for 2023, as compared to $370 thousand for 2022 primarily due to increased investment in operational assets.

Research and development. For the three months ended September 30, 2023, total research and development expenses increased by $0.1 million, or 13%, to $0.3 million for 2023, as compared to $0.2 million for 2022. The nominal increase was due primarily to the Company achieving technological feasibility in both hardware and software development and focusing on bringing its products to market.

For the nine months ended September 30, 2023, total research and development expenses decreased by $1.1 million, or 53%, to $1.0 million for 2023, as compared to $2.1 million for 2022. The decrease was due primarily to the Company achieving technological feasibility in both hardware and software development and focusing on bringing its products to market.

General and administrative. For the three months ended September 30, 2023, total general and administrative expenses increased by $1.8 million, or 38%, to $6.7 million for 2023, as compared to $4.9 million for 2022. General and administrative expenses increased primarily due to sales and marketing expenses, professional fees, and other costs to support the Company's continued growth. The Company also implemented a workforce reduction of 22% on September 30, 2023, which increased costs of $.4 million attributable to severance paid to employees.

For the nine months ended September 30, 2023, total general and administrative expenses increased by $8.7 million, or 99%, to $17.5 million for 2023, as compared to $8.8 million for 2022. General and administrative expenses increased primarily due to an increase in stock–based compensation expense, sales and marketing expenses, professional fees, and other costs to support the continued growth of the Company. The Company also implemented a workforce reduction of 22% on September 30, 2023, which increased costs of $.4 million attributable to severance paid to employees.

Other expense, net. For the three months ended September 30, 2023, other expense, net was nominal for the quarter.

For the nine months ended September 30, 2023, other expense, net increased by $1.3 million to $1.0 million for 2023 as compared to $(.3) million, net in 2022. The increase was due primarily to a state sales tax assessment of $1.2 million that the Company plans to vigorously mitigate, by contesting the preliminary estimate from the governmental entity, Texas Comptroller of Public Accounts.

Change in fair value of warrant liabilities. For the three months ended September 30, 2023, the change in the fair value of warrant liabilities increased by $2.7 million to $8.7 million of other (income) expense in 2023 as compared to $6.0 million as of September 30, 2022. This increase was due to the reset of the warrants price from $20.00 to $6.00 warrants from financing that occurred during the quarter.

For the nine months ended September 30, 2023, the change in the fair value of warrant liabilities decreased by $(24.7) million to $(18.8) million of other (income) expense in 2023 as compared to $6.0 as of September 30, 2022. This decrease was due to management's expectation to raise debt capital that would limit the triggering of future reset events.

Interest expense, net. For the three months ended September 30, 2023, interest expense, net decreased by $0.5 million to $.9 million for 2023 as compared to $1.4 million in 2022. Interest expense, net decreased is primarily due to the gain on settlement of liquidated damages. For the three months ended September 30, 2023 and 2022, cash paid for interest was $0.1 million and 1.5 million, respectively.

For the nine months ended September 30, 2023, interest expense, net increased by $4.3 million to $7.4 million for 2023 as compared to $3.1 million in 2022. Interest expense, net increased due to the amortization of debt discount of $2.9 million associated with the Debentures and approximately net $3.7 million associated with liquidated damages and interest arising out of the RRA. Please see Note 6 to the accompanying condensed consolidated financial statements included herein for additional information. For the nine months ended September 30, 2023, cash paid for interest decreased by $1.1 million to $1.0 million for 2023 as compared to $2.1 million in 2022 due primarily to interest paid on settling prior year debt services in 2022.

Liquidity and Capital Resources

As of September 30, 2023, we had $6,771,531 of cash and cash equivalents. The cash equivalents consist of money market funds.

Significant sources and uses of cash during the first nine months of 2023.

Sources of cash:

- The Company received net proceeds of $10.4 million from the issuance of debt. We received net proceeds of $421 thousand from the exercise of stock options, representing the strike price of such options. The Company received $338 thousand from the exercise of warrants.

Uses of cash:

- Cash used in operating activities was $16.4 million, which included $4.6 million invested in working capital.

- Cash used in investing activities for capital expenditures was $10.7 million.

Future sources and uses of cash. Our capital requirements will depend on many factors, including sales volumes, the timing and extent of spending to support research and development efforts, investments in technology, the expansion of sales and marketing activities, and market adoption of new and enhanced products and features. To date, our principal sources of liquidity have been proceeds received from the issuance of debt and equity funding and cash flows from our operations.

We anticipate needing additional capital to continue expanding our business operations, which may include acquisitions and capital expenditures. Currently, the Company does not generate sufficient revenue to cover operating expenses, working capital, and capital expenditures. We have historically financed our operations through equity and debt financing. We do not have any commitments for equity funding at this time, and additional funding may not be available to us on favorable terms, if at all. We are considering reducing discretionary spending and other cost-cutting measures, which may be implemented in the near-term to the extent additional financing is not raised. The Company implemented a workforce reduction of 22% on September 29, 2023, which increased costs by $.4 million in the current quarter, which is attributable to severance paid to employees. The cost savings that will be realized over the next twelve months is expected to be $2.7 million. During the third quarter of 2023, the Company received net proceeds of $10.4 million from the issuance of debt. There are no assurances that we can raise sufficient additional capital from external sources or implement material cost-cutting measures. The inability to successfully effectuate either measure could force us to curtail or discontinue our operations. However, utilizing cost control measures, cash on hand, revenue from operations, and potential future equity and debt funding, the Company anticipates having sufficient funds to meet its obligations for at least one year from the issuance date of this Form 10-Q.

Indebtedness. The Company's indebtedness as of September 30, 2023, is presented in Item 1, "Financial Statements – Note 7 – Notes Payable" and our lease obligations are presented in Item 1, "Financial Statements – Note 8 – Leases."

Critical Accounting Policies and Estimates

Please refer to "Critical Accounting Policies and Estimates" contained in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2022 for a complete discussion of our critical accounting estimates.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not required for smaller reporting companies.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures. Our disclosure controls and procedures are designed to ensure that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934, as amended (the "Exchange Act") is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Our management, with the participation and under the supervision of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Form 10-Q. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2023, as a result of the continuation of the previously disclosed material weakness discussed below, our disclosure controls and procedures were not effective because of a material weakness in our internal control over financial reporting described below. . In light of this fact, our management, including our Chief Executive Officer and Chief Financial Officer, has performed additional analyses, reconciliations, and other post-closing procedures in order to conclude that, notwithstanding such material weakness, the unaudited condensed consolidated financial statements included in this Form 10-Q fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with GAAP as of the dates and for the periods presented in this Form 10-Q.

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) under the Exchange Act, as amended. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

Continuation of material weakness. We previously identified a material weakness in controls over the financial reporting and the accounting for complex warrant issuances and the classification of certain issued warrants. This material weakness resulted in the failure to prevent material errors in accounting for the warrants as equity classification when the warrants should have been classified as liabilities, and marked to market each reporting period, resulting in the restatement of our financial statements as of and for the nine months ended September 30, 2022.

Further, the continuation of the abovementioned material weakness, specifically in relation to the accounting for complex transactions and contracts of the Company, resulted in the untimely recognition of an accrued liability and expense arising out of the RRA, which resulted in the restatement of our financial statements as of and for the three months ended March 31, 2023.

Remediation Plan and Status

Management is working to remediate the material weakness described above and to enhance our overall control environment. Our remediation plan includes enhancing our contract review process, particularly in the context of complex agreements and transactions, as well as internal communications in connection therewith, in addition to continuing our engagement of third-party specialists to assist with accounting, valuation, and financial reporting functions in relation to significant contracts, agreements and complex transactions. Our ongoing remediation activities are subject to continued management review supported by ongoing design and evaluation of our internal control over financial reporting framework. The Audit Committee of our board of directors is monitoring, and receives regular reports on the progress of, management's remediation efforts. Due to the nature of the remediation process and the need for sufficient time after implementation to evaluate and test the design and effectiveness of the controls, no assurance can be given as to the timing for completion of remediation We will not consider the material weakness remediated until our enhanced controls are operational for a sufficient period of time and evaluated, enabling management to conclude that the enhanced controls are operating effectively.

Changes in internal control over financial reporting. During the third quarter of 2023, except as described above in "Remediation Plan and Status," there were no other changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

The Company's management has expended, and will continue to expend, a substantial amount of effort and resources in connection with the remediation of previously identified material weaknesses, including the material weakness discussed above, and the ongoing improvement of our internal control over financial reporting.

Inherent limitation on the effectiveness of internal control. The effectiveness of any system of internal control over financial reporting, including ours, is subject to inherent limitations, including the exercise of judgment in designing, implementing, operating, and evaluating the controls and procedures, and the inability to eliminate misconduct completely. Accordingly, in designing and evaluating the disclosure controls and procedures, management recognizes that any system of internal control over financial reporting, including ours, no matter how well designed and operated, can only provide reasonable, not absolute assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints, and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs. Moreover, 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. We intend to continue to monitor and upgrade our internal controls as necessary or appropriate for our business but cannot assure you that such improvements will be sufficient to provide us with effective internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Although we may, from time to time, we may be subject to litigation and other claims in the normal course of business, we are currently not a party to any material legal proceeding. No amounts have been accrued in the condensed consolidated financial statements with respect to any matters.

ITEM 1A. RISK FACTORS

During the three months ended September 30, 2023, there have been no material changes in the “Risk Factors” as set forth in “Item 1A. Risk Factors” of the Company’s Annual Report on Form 10-K for the year ended December 31, 2022, and Amendment No. 1 to the Quarterly Report on 10-Q/A for the period ended March 31, 2023, filed by the Company with the SEC. The risks described therein are not the only risks facing the Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Convertible Senior Secured Term Loan –

On September 18, 2023, the Company entered into a convertible senior secured term loan agreement with ATW Special Situations II LLC as collateral agent (in such capacity, the “Collateral Agent”) and lender, and Transocean Finance Limited, ATW Special Situations I LLC, Material Impact Fund II, L.P., and RCB Equities #1, LLC, as lenders, are related parties.

The Convertible Senior Secured Term Loan Agreement provides the Company with up to $20.0 million of secured term loans, of which $11.6 million has already been funded and deemed issued under the Convertible Senior Secured Term Loan Agreement. Any portion of the outstanding principal amount of the Loans is prepayable at the Company’s option pro rata to each Lender upon at least five days’ prior written notice to each Lender.

The Convertible Senior Secured Term Loan Agreement included a 2.5% exit fee or $290,000, bearing interest at 12.50% per annum, payable quarterly in arrears on the first day of each calendar quarter commencing April 1, 2024. The loan agreement included a 2.5% original issue discount or $125,000 from the RCB Equities #1, LLC promissory note. The loan includes assumed legal fees of $150,000, deemed interest from convertible debentures of $378,116, and $500,000 held in escrow, recorded under other current assets of the condensed consolidated balance sheet. The escrow balance will be held for at least thirty days or until the collateral agent determines no obligation of expense greater than $150,000 incurred by the lender. The Loans will mature on the earliest of (a) the third anniversary of the date of the Term Loan Agreement of September 17, 2026., (b) 91 days prior to the maturity of the 5% Original Issue Discount Senior Secured Convertible Debentures, dated as of September 9, 2022.

Subject to the terms and conditions of the Term Loan Agreement, the Company may, upon at least two trading days’ written notice to the Lenders, elect to redeem some or all of the then outstanding principal amount of the Loans. In connection with any such election, which shall be irrevocable, the Company shall pay each Lender, on a pro rata basis, an amount in cash equal to the greater of (x) the sum of (i) 100% of the then outstanding principal amount of the Loans, (ii) accrued but unpaid interest and (iii) all liquidated damages and other amounts due in respect of the Loans (including, without limitation, the Exit Fee (as defined in the Term Loan Agreement)) (the “Optional Redemption Amount”) and (y) the product of (i) the aggregate number of shares of the Company’s common stock, par value $0.0001 per share (“Common Stock”), then issuable upon conversion of the applicable Optional Redemption Amount (without regard to any limitations on conversion set forth in the Term Loan Agreement) multiplied by (ii) the highest closing sale price of the Common Stock on any trading day during the period commencing on the date immediately preceding the date that the applicable notice of redemption is delivered to the Lenders and ending on the trading day immediately prior to the date the Company makes the entire payment required to be made in connection with such redemption.

The Loans are convertible, in whole or in part, at the option of each Lender into shares of Common Stock until the date that the Loans are no longer outstanding, at a conversion rate equal to the outstanding principal amount of the Loans to be converted divided by a conversion price of $6.00 per share of Common Stock (the “Conversion Price”), subject to certain customary anti-dilution adjustments as described in the Term Loan Agreement.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

		Incorporated by Reference			
Exhibit	**Description**	**Schedule/ Form**	**File Number**	**Exhibits**	**Filing Date**
2.1	Agreement and Plan of Merger, dated as of October 2, 2023, by and among Nauticus Robotics, Inc., 3D Merger Sub, Inc. and 3D at Depth, Inc.	Form 8-K	001-40611	2.1	October 6, 2023
3.1	Second Amended and Restated Certificate of Nauticus Robotics, Inc.	Form 8-K	001-40611	3.5	September 15, 2022
3.2	Amended and Restated Bylaws of Nauticus Robotics, Inc (as of May 11, 2023).	Form 8-K	001-40611	3.1	May 15, 2023
10.1†	Senior Secured Term Loan Agreement, dated as of September 18, 2023, by and among Nauticus Robotics, Inc., ATW Special Situations II LLC, as collateral agent and lender, and the lenders party thereto.	Form 8-K	001-40611	10.1	September 21, 2023
10.2†	Pledge and Security Agreement, dated as of September 18, 2023, by and among Nauticus Robotics, Inc., Nauticus Robotics Holdings, Inc., ATW Special Situations II LLC, as collateral agent.	Form 8-K	001-40611	10.2	September 21, 2023
10.3†	Intellectual Property Security Agreement, dated as of September 18, 2023, by and among Nauticus Robotics, Inc., Nauticus Robotics Holdings, Inc. and ATW Special Situations II LLC, as collateral agent.	Form 8-K	001-40611	10.3	September 21, 2023
10.4	Subsidiary Guarantee, dated as of September 18, 2023, by Nauticus Robotics Holdings, Inc. and acknowledged and agreed to by Nauticus Robotics, Inc.	Form 8-K	001-40611	10.4	September 21, 2023
10.5	Intercreditor Agreement, dated as of September 18, 2023, by and between ATW Special Situations II LLC, as first lien collateral agent, and ATW Special Situations I LLC, as second lien collateral agent, and acknowledged and agreed by Nauticus Robotics, Inc. and Nauticus Robotics Holdings, Inc.	Form 8-K	001-40611	10.5	September 21, 2023
10.6†	Amendment to Securities Purchase Agreement, Senior Secured Convertible Debentures and Pledge and Security Agreement, dated as of September 18, 2023, by and among Nauticus Robotics, Inc., Nauticus Robotics Holdings, Inc. and ATW Special Situations I LLC, as agent and the Required Creditors.	Form 8-K	001-40611	10.6	September 21, 2023
10.7†	Pledge and Security Agreement, dated as of September 9, 2022, by and among Nauticus Robotics, Inc., Nauticus Robotics Holdings, Inc. and ATW Special Situations I LLC, as agent and creditor, and the other creditors party thereto.	Form 8-K	001-40611	10.7	September 21, 2023
10.8	Offer Letter, dated September 27, 2023.	Form 8-K	001-40611	10.1	October 2, 2023
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.				
32.1*	Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				
32.2*	Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.				
101.INS	Inline XBRL Instance Document.				
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document.				
101.SCH	Inline XBRL Taxonomy Extension Schema Document.				
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document.				
101.LAB	Inline XBRL Taxonomy Extension Labels Linkbase Document.				
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document.				
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101).				

* Furnished herewith

† Schedules and similar attachments to this Exhibit have been omitted pursuant to Item 601(a)(5) of Regulation S-K. The Company agrees to furnish supplementally a copy of any omitted schedule or exhibit to the SEC upon request.

SIGNATURES

Pursuant to the requirements of the Exchange Act, the registrant has caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

NAUTICUS ROBOTICS, INC.

By: /s/ Nicolaus Radford
Nicolaus Radford
Chief Executive Officer

Date: November 14, 2023

By: /s/ Rangan Padmanabhan
Rangan Padmanabhan
Chief Financial Officer

Date: November 14, 2023

Exhibit 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT

I, Nicolaus Radford, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Nauticus Robotics, Inc. (“registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision 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;
    c. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    d. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

November 14, 2023

/s/ Nicolaus Radford

Nicolaus Radford
Chief Executive Officer

Exhibit 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT

I, Rangan Padmanabhan, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Nauticus Robotics, Inc. (“registrant”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision 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;

    c. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

November 14, 2023

/s/ Rangan Padmanabhan
Rangan Padmanabhan
Chief Financial Officer

Exhibit 32.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. Section 1350, the undersigned Officer of Nauticus Robotics, Inc. (the "Company"), hereby certifies, that the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2023 (the "Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 14, 2023

/s/ Nicolaus Radford

Nicolaus Radford
Chief Executive Officer

Exhibit 32.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. Section 1350, the undersigned Officer of Nauticus Robotics, Inc. (the "Company"), hereby certifies, that the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2023 (the "Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 14, 2023

/s/ Rangan Padmanabhan

Rangan Padmanabhan
Chief Financial Officer