

Heritage-Crystal Clean, Inc.  
Form 10-Q  
October 17, 2018

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 8, 2018

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 001-33987

HERITAGE-CRYSTAL CLEAN, INC.  
(Exact name of registrant as specified in its charter)

Delaware 26-0351454  
State or other jurisdiction of (I.R.S. Employer  
Incorporation Identification No.)

2175 Point Boulevard  
Suite 375  
Elgin, IL 60123  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (847) 836-5670

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required

to submit and post such files). Yes  No  Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated

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filer, smaller reporting company, or an emerging growth company. See 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  (Do not check if a smaller reporting company) 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

On October 15, 2018, there were outstanding 23,050,109 shares of Common Stock, \$0.01 par value, of Heritage-Crystal Clean, Inc.

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## PART I

## ITEM 1. FINANCIAL STATEMENTS

Heritage-Crystal Clean, Inc.  
 Condensed Consolidated Balance Sheets  
 (In Thousands, Except Share and Par Value Amounts)

|   | September 8,<br>2018 | December 30,<br>2017 |
|---|----------------------|----------------------|
|   | (unaudited)          |                      |
| <b>ASSETS</b>   |                      |                      |
| Current Assets:   |                      |                      |
| Cash and cash equivalents   | \$ 46,315            | \$ 41,889            |
| Accounts receivable - net   | 51,051               | 45,491               |
| Inventory - net   | 29,745               | 21,639               |
| Other current assets  | 6,745                | 5,895                |
| Total Current Assets  | 133,856              | 114,914              |
| Property, plant and equipment - net   | 133,753              | 128,119              |
| Equipment at customers - net  | 23,767               | 23,312               |
| Software and intangible assets - net  | 15,211               | 16,732               |
| Goodwill  | 34,125               | 31,580               |
| Total Assets  | \$ 340,712           | \$ 314,657           |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                      |                      |
| Current Liabilities:  |                      |                      |
| Accounts payable  | \$ 31,411            | \$ 25,568            |
| Contract liabilities - net  | 231                  | —                    |
| Accrued salaries, wages, and benefits   | 4,923                | 6,386                |
| Taxes payable   | 6,679                | 5,787                |
| Other current liabilities   | 4,783                | 2,690                |
| Total Current Liabilities   | 48,027               | 40,431               |
| Long-term debt  | 28,953               | 28,744               |
| Deferred income taxes   | 13,554               | 9,556                |
| Total Liabilities   | \$ 90,534            | \$ 78,731            |
| <b>STOCKHOLDERS' EQUITY:</b>  |                      |                      |
| Common stock - 26,000,000 shares authorized at \$0.01 par value, 23,050,109 and 22,891,674 shares issued and outstanding at September 8, 2018 and December 30, 2017, respectively | \$ 231               | \$ 229               |
| Additional paid-in capital  | 196,082              | 193,640              |
| Retained earnings   | 53,315               | 41,359               |
| Total Heritage-Crystal Clean, Inc. Stockholders' Equity   | 249,628              | 235,228              |
| Noncontrolling interest   | 550                  | 698                  |
| Total Equity  | \$ 250,178           | \$ 235,926           |
| Total Liabilities and Stockholders' Equity  | \$ 340,712           | \$ 314,657           |

See accompanying notes to financial statements.



Heritage-Crystal Clean, Inc.  
Condensed Consolidated Statements of Income  
(In Thousands, Except per Share Amounts)  
(Unaudited)

|   | Third Quarter Ended,<br>September 9,<br>2018 |           | First Three Quarters<br>Ended,<br>September 9,<br>2018 |            |
|---|--|-----------|--|------------|
|   | 2018   | 2017      | 2018   | 2017       |
| Revenues  |  |           |  |            |
| Service revenues  | \$58,054                                     | \$ 54,048 | \$172,205  | \$ 162,071 |
| Product revenues  | 41,620                                       | 29,283    | 110,918  | 88,095     |
| Total revenues  | \$99,674                                     | \$ 83,331 | \$283,123  | \$ 250,166 |
| Operating expenses  |  |           |  |            |
| Operating costs   | \$76,045                                     | \$ 63,649 | \$220,702  | \$ 188,210 |
| Selling, general, and administrative expenses                               | 10,641                                       | 10,955    | 33,185   | 33,871     |
| Depreciation and amortization   | 3,776  | 4,186     | 11,078   | 12,501     |
| Other expense (income) - net  | 253  | (3,078)   | 983  | (11,112)   |
| Operating income  | 8,959  | 7,619     | 17,175   | 26,696     |
| Interest expense – net  | 256  | 276       | 742  | 775        |
| Income before income taxes  | 8,703  | 7,343     | 16,433   | 25,921     |
| Provision for income taxes  | 2,284  | 2,586     | 3,996  | 9,361      |
| Net income  | 6,419  | 4,757     | 12,437   | 16,560     |
| Income attributable to noncontrolling interest                              | 74   | 53        | 213  | 158        |
| Net income attributable to Heritage-Crystal Clean, Inc. common stockholders | \$6,345                                      | \$ 4,704  | \$12,224   | \$ 16,402  |
| Net income per share: basic   | \$0.28                                       | \$ 0.21   | \$0.53   | \$ 0.73    |
| Net income per share: diluted   | \$0.27                                       | \$ 0.20   | \$0.52   | \$ 0.72    |
| Number of weighted average shares outstanding: basic                        | 23,048                                       | 22,686    | 23,013   | 22,515     |
| Number of weighted average shares outstanding: diluted                      | 23,404                                       | 22,970    | 23,299   | 22,813     |

See accompanying notes to financial statements.

Heritage-Crystal Clean, Inc.  
Condensed Consolidated Statement of Stockholders' Equity  
(In Thousands, Except Share Amounts)

(Unaudited)

|   | Shares     | Par Value<br>Common | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Total<br>Heritage-Crystal<br>Clean, Inc.<br>Stockholders'<br>Equity | Non-controlling<br>Interest | Total<br>Equity |
|---|------------|---------------------|----------------------------------|----------------------|---|-----------------------------|-----------------|
| Balance at December 30, 2017                                | 22,891,674 | \$ 229              | \$ 193,640                       | \$ 41,359            | \$ 235,228  | \$ 698                      | \$ 235,926      |
| Adjustment from adopting ASC<br>606                         | —          | —                   | —                                | (268 )               | (268 )  | —                           | (268 )          |
| Net income  | —          | —                   | —                                | 12,224               | 12,224  | 213                         | 12,437          |
| Distribution  | —          | —                   | —                                | —                    | —   | (361 )                      | (361 )          |
| Issuance of common stock –<br>ESPP                          | 15,170     | —                   | 311                              | —                    | 311   | —                           | 311             |
| Exercise of stock options                                   | 14,048     | —                   | 103                              | —                    | 103   | —                           | 103             |
| Share-based compensation                                    | 129,217    | 2                   | 3,058                            | —                    | 3,060   | —                           | 3,060           |
| Share repurchases to satisfy tax<br>withholding obligations | —          | —                   | (1,030 )                         | —                    | (1,030 )  | —                           | (1,030 )        |
| Balance at September 8, 2018                                | 23,050,109 | \$ 231              | \$ 196,082                       | \$ 53,315            | \$ 249,628  | \$ 550                      | \$ 250,178      |

See accompanying notes to financial statements.



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Heritage-Crystal Clean, Inc.  
 Condensed Consolidated Statements of Cash Flows  
 (In Thousands)  
 (Unaudited)

|   | For the First Three<br>Quarters Ended,<br>September 9,<br>2018      2017 |              |
|---|--|--------------|
| Cash flows from Operating Activities:   |  |              |
| Net income  | \$ 12,437  | \$ 16,560    |
| Adjustments to reconcile net income to net cash provided by operating activities: |  |              |
| Depreciation and amortization   | 11,078   | 12,501       |
| Net (gain) on disposition of assets   | —  | (2,506 )     |
| Bad debt provision  | 177  | 105          |
| Share-based compensation  | 3,060  | 1,962        |
| Deferred taxes  | 3,998  | 8,904        |
| Other, net  | 215  | 513          |
| Changes in operating assets and liabilities:                                      |  |              |
| (Increase) decrease in accounts receivable  | (4,780 )   | 1,534        |
| Increase in inventory   | (7,845 )   | (2,376 )     |
| Increase in other current assets  | (851 )   | (739 )       |
| Increase (decrease) in accounts payable   | 5,670  | (3,749 )     |
| Decrease in accrued liabilities   | (157 )   | (336 )       |
| Cash provided by operating activities   | \$ 23,002  | \$ 32,373    |
| Cash flows from Investing Activities:   |  |              |
| Capital expenditures  | \$ (12,874)  | \$ (9,465 )  |
| Business acquisitions, net of cash acquired                                       | (4,805 )   | —            |
| Proceeds from the disposal of assets  | 80   | 4,129        |
| Cash used in investing activities   | \$ (17,599)  | \$ (5,336 )  |
| Cash flows from Financing Activities:   |  |              |
| Payments on Term loan   | \$ —   | \$ (64,195 ) |
| Proceeds from new Term Loan   | —  | 30,000       |
| Proceeds under revolving credit facility  | —  | 4,000        |
| Payments of revolving credit facility   | —  | (4,000 )     |
| Proceeds from the exercise of stock options                                       | 103  | 5,412        |
| Share repurchases to satisfy tax withholding obligations                          | (1,030 )   | (354 )       |
| Proceeds from the issuance of common stock  | 311  | 303          |
| Payments of debt issuance costs   | —  | (1,051 )     |
| Distributions to noncontrolling interest  | (361 )   | (310 )       |
| Cash used in financing activities   | \$ (977 )  | \$ (30,195 ) |
| Net increase (decrease) in cash and cash equivalents                              | 4,426  | (3,158 )     |
| Cash and cash equivalents, beginning of period                                    | 41,889   | 36,610       |
| Cash and cash equivalents, end of period  | \$ 46,315  | \$ 33,452    |
| Supplemental disclosure of cash flow information:                                 |  |              |
| Income taxes paid   | \$ 371   | \$ 208       |

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|  |       |        |
|--|-------|--------|
| Cash paid for interest                           | 846   | 970    |
| Supplemental disclosure of non-cash information: |       |        |
| Payables for construction in progress            | \$526 | \$ 386 |
| See accompanying notes to financial statements.  |       |        |

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HERITAGE-CRYSTAL CLEAN, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

September 8, 2018

(1) ORGANIZATION AND NATURE OF OPERATIONS

Heritage-Crystal Clean, Inc., a Delaware corporation and its subsidiaries (collectively the "Company"), provides parts cleaning, hazardous and non-hazardous containerized waste, used oil collection, vacuum, antifreeze recycling and field services primarily to small and mid-sized industrial and vehicle maintenance customers. The Company owns and operates a used oil re-refinery where it re-refines used oils and sells high quality base oil for lubricants as well as other re-refinery products. The Company also has multiple locations where it dehydrates used oil. The oil processed at these locations is sold as recycled fuel oil. The Company also operates multiple wastewater treatment plants and antifreeze recycling facilities at which it produces virgin-quality antifreeze. The Company operates in the United States and Ontario, Canada. The Company conducts its primary business operations through Heritage-Crystal Clean, LLC, its wholly owned subsidiary, and all intercompany balances have been eliminated in consolidation.

The Company has two reportable segments: "Environmental Services" and "Oil Business." The Environmental Services segment consists of the Company's parts cleaning, containerized waste management, vacuum truck services, antifreeze recycling activities, and field services. The Oil Business segment consists of the Company's used oil collection, recycled fuel oil sales, used oil re-refining activities, and used oil filter removal and disposal services. No customer represented greater than 10% of consolidated revenues for any of the periods presented. There were no intersegment revenues. Both segments operate in the United States and in Ontario, Canada.

The Company's fiscal year ends on the Saturday closest to December 31. The most recent fiscal year ended on December 30, 2017. Each of the Company's first three fiscal quarters consists of twelve weeks while the last fiscal quarter consists of sixteen or seventeen weeks.

In the Company's Environmental Services segment, product revenues include sales of solvent, machines, absorbent, accessories, and antifreeze; service revenues include servicing of parts cleaning machines, drum waste removal services, vacuum truck services, field services, and other services. In the Company's Oil Business segment, product revenues include sales of re-refined base oil, recycled fuel oil, used oil, and other products; service revenues include revenues from used oil collection activities, collecting and disposing of waste water and removal and disposal of used oil filters. Due to the Company's integrated business model, it is impracticable to separately present costs of tangible products and costs of services.

## (2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company's significant accounting policies are described in Note 2, "Summary of Significant Accounting Policies," in the Company's Annual Report on Form 10-K for the fiscal year ended December 30, 2017. There have been no material changes in these policies or their application with the exception of revenue recognition. See footnote 4 — Revenue for more information.

## Recently Issued Accounting Pronouncements

| Standard  | Issuance Date    | Description   | Our Effective Date   | Effect on the Financial Statements   |
|---|------------------|---|----------------------|--|
| ASU 2016-02<br>Leases<br>(Topic 842),<br>and<br>subsequent<br>updates | February<br>2016 | This update was issued to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. Early application of the amendments in this update is permitted for all entities. | December<br>30, 2018 | The Company is currently evaluating the effect that implementation of this update will have on its consolidated financial position and results of operations. The Company anticipates that implementation of this standard will result in an increase to assets and an increase to liabilities. To date, certain personnel have attended technical training concerning this new lease accounting standard. The Company has engaged a third party to assist in implementing the standard and to provide a software solution to aid in accounting for leases. Contract review and software configuration are currently underway in preparation for our adoption of the requirements of Topic 842. The Company is also continuing to evaluate transition considerations such as whether to elect practical expedients, use of hindsight, and comparative reporting periods. |

Recently Issued Accounting Standards Adopted

| Standard   | Issuance Date           | Description  | Effective Date    | Effect on the Financial Statements   |
|--|-------------------------|--|-------------------|--|
| ASU 2014-09 "Revenue from Contracts with Customers (Topic 606)," ASU 2014-15 "Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date," ASU 2016-08 "Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)," ASU 2016-10 "Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing," and ASU 2016-12 "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients" | May 2014 and subsequent | These standards outline a single comprehensive model for entities to use in accounting for revenue using a five-step process that supersedes virtually all existing revenue guidance. The underlying principle is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Entities have the option of using either a full retrospective approach or a modified retrospective approach to adopt the guidance. Early adoption is permitted. | December 31, 2017 | On December 31, 2017, we adopted the new accounting standard ASC 606, "Revenue from Contracts with Customers" using the modified retrospective method. We recognized the cumulative effect as an adjustment to our opening balance of retained earnings. |

Effective December 31, 2017, we adopted the requirements of Topic 606. The cumulative effects of the changes made to our statement of income and balance sheet were as follows:

| (thousands)   | For the Third Quarter Ended, September 8, 2018 |  |                                 | For the First Three Quarters Ended, September 8, 2018 |  |                                 |
|---|--|--|---------------------------------|---|--|---------------------------------|
|   | As Reported                                    | Balances Without Adoption of Topic 606 | Effect of Change Higher/(Lower) | As Reported   | Balances Without Adoption of Topic 606 | Effect of Change Higher/(Lower) |
| Statement of Income   |  |  |                                 |   |  |                                 |
| Service revenues  | \$58,054                                       | \$58,077                               | \$ (23 )                        | \$172,205   | \$172,168                              | \$ 37                           |
| Total revenues  | 99,674   | 99,697                                 | (23 )                           | 283,123   | 283,086                                | 37                              |
| Operating income  | 8,959  | 8,982                                  | (23 )                           | 17,175  | 17,138                                 | 37                              |
| Income before income taxes  | 8,703  | 8,726                                  | (23 )                           | 16,433  | 16,396                                 | 37                              |
| Provision for income taxes  | 2,284  | 2,290                                  | (6 )                            | 3,996   | 3,987                                  | 9                               |
| Net income  | 6,419  | 6,436                                  | (17 )                           | 12,437  | 12,409                                 | 28                              |
| Net income attributable to Heritage-Crystal Clean, Inc. common stockholders | \$6,345  | \$6,362                                | \$ (17 )                        | \$12,224  | \$12,196                               | \$ 28                           |

| (thousands)   | September 8, 2018 |  |                                 |
|---|-------------------|--|---------------------------------|
|   | As Reported       | Balances Without Adoption of Topic 606 | Effect of Change Higher/(Lower) |
| <b>Balance Sheet</b>                                    |                   |  |                                 |
| Contract liabilities - net                              | \$231             | \$—                                    | \$ 231                          |
| Total Current Liabilities                               | 48,027            | 47,796                                 | 231                             |
| Deferred income taxes                                   | 13,554            | 13,545                                 | 9                               |
| Total Liabilities                                       | 90,534            | 90,294                                 | 240                             |
| Retained earnings                                       | 53,315            | 53,555                                 | (240 )                          |
| Total Heritage-Crystal Clean, Inc. Stockholders' Equity | 249,628           | 249,868                                | (240 )                          |
| Total Equity  | \$250,178         | \$250,418                              | \$ (240 )                       |

## (3) BUSINESS COMBINATIONS

On May 3, 2018, the Company purchased the assets of Products Plus, Inc. and AO Holding Company-Kansas City, LLC (collectively "PPI") pursuant to an Asset Purchase Agreement. The Company purchased the assets of PPI to expand the Company's market share in the collection, recycling, and sales of a full line of antifreeze products. The purchase price was set at \$5.9 million subject to certain adjustments, including a working capital adjustment and a contingent consideration provision, and is preliminarily allocated based on our estimates and assumptions of the approximate fair values of assets acquired on the acquisition date. We are still in the process of completing our valuation, and accordingly our estimates and assumptions are subject to change within the measurement period. The Company is continuing to examine facts and circumstances that existed at the acquisition date and how those affect the estimated fair value of contingent consideration, working capital, and the allocation of the estimated purchase price to other tangible and intangible assets. The results of PPI are consolidated into the Company's Environmental Services segment.

On June 11, 2018, the Company purchased the assets of Kurt Lanse d/b/a Hot Tank Supply Company ("HTSC") pursuant to an Asset Purchase Agreement. The Company purchased the assets of HTSC to expand the Company's market share in California. The purchase price was set at \$0.7 million subject to certain adjustments, including a working capital adjustment and a deferred and contingent consideration provision, and is preliminarily allocated based on our estimates and assumptions of the approximate fair values of assets acquired on the acquisition date. We are still in the process of completing our valuation, and accordingly our estimates and assumptions are subject to change within the measurement period. The Company is continuing to examine facts and circumstances that existed at the acquisition date and how those affect the estimated fair value of contingent consideration, working capital, and the allocation of the estimated purchase price to other tangible and intangible assets. The results of HTSC are consolidated into the Company's Environmental Services segment.

The following table summarizes the preliminary estimated fair values of the assets acquired, net of cash acquired, related to each acquisition:

|  | As of                |       |
|--|----------------------|-------|
|  | September 8,<br>2018 |       |
| (thousands)                                | PPI                  | HTSC  |
| Accounts receivable                        | \$909                | \$48  |
| Inventory                                  | 259                  | 3     |
| Property, plant, & equipment               | 1,969                | 47    |
| Equipment at customers                     | —                    | 104   |
| Intangible assets                          | 528                  | 100   |
| Goodwill                                   | 2,172                | 377   |
| Total purchase price, net of cash acquired | \$5,837              | \$679 |
| Less: working Capital adjustment           | (62 )                | (2 )  |
| Less: deferred consideration               | —                    | 225   |
| Less: contingent consideration             | 1,450                | 100   |
| Net cash paid                              | \$4,449              | \$356 |

(4) REVENUE

We account for a contract when it has approval and commitment from both parties, the rights of the parties are identified, payment terms are identified, the contract has commercial substance and collectability of consideration is probable. Revenue is recognized when our performance obligations under the terms of a contract with our customers are satisfied. Recognition occurs when the Company transfers control by completing the specified services at the point in time the customer benefits from the services performed or once our products are delivered. The Company measures progress toward complete satisfaction of a performance obligation satisfied over time using a cost-based input method. This method of measuring progress provides a faithful depiction of the transfer of goods or services because the costs incurred are expected to be substantially proportionate to the Company's satisfaction of the performance obligation. Revenue is measured as the amount of consideration we expect to receive in exchange for completing our performance obligations. Sales tax and other taxes we collect with revenue-producing activities are excluded from revenue. In the case of contracts with multiple performance obligations, the Company allocates the transaction price to each performance obligation based on the relative stand-alone selling prices of the various goods and/or services encompassed by the contract. We do not have any material significant payment terms as payment is generally due within 30 days after the performance obligation has been satisfactorily completed. The Company has elected the practical expedient to recognize the incremental costs of obtaining a contract as an expense when incurred if the amortization period of the asset that we otherwise would have recognized is one year or less. In applying the guidance in Topic 606, there were no judgments or estimates made that the Company deems significant.

Accounts Receivable — Net, includes amounts billed and currently due from customers. The amounts due are stated at their net estimated realizable value. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company determines the allowance based on analysis of customer credit worthiness and historical losses. Accounts receivable are written off once the Company determines the account to be uncollectible. The Company does not have any off-balance-sheet credit exposure related to its customers.

Contract Balances — Contract assets primarily relate to the Company's rights to consideration for work completed in relation to its services performed but not billed at the reporting date. Contract liabilities primarily consist of advance payments of performance obligations yet to be fully satisfied in the period reported. Our contract liabilities and contract assets are reported in a net position at the end of each reporting period.

We disaggregate our revenue from contracts with customers by major lines of business for each of our segments, as we believe it best depicts how the nature, amount, timing and uncertainty of our revenue and cash flows are affected by economic factors.

The following table disaggregates our revenue by major lines:

|             | For the Third Quarter    |       | For the First Three Quarters |           |
|-------------|--------------------------|-------|------------------------------|-----------|
|             | Ended, September 8, 2018 |       | Ended, September 8, 2018     |           |
| Total       |                          |       |                              |           |
| Net         |                          |       |                              |           |
| Sales       |                          |       |                              |           |
| by          |                          |       |                              |           |
| Major       | Environmental            | Total | Environmental                | Total     |
| Lines       | Services Business        |       | Services Business            |           |
| of          |                          |       |                              |           |
| Business    |                          |       |                              |           |
| (thousands) |                          |       |                              |           |
|             | \$40,767                 | \$—   | \$40,767                     | \$121,875 |
|             |                          |       | \$—                          | \$121,875 |



|  |          |          |          |           |          |           |
|--|----------|----------|----------|-----------|----------|-----------|
| Parts<br>cleaning,<br>containerized<br>waste,<br>&<br>related<br>products/services |          |          |          |           |          |           |
| Vacuum<br>Services<br>&  | 12,565   | —        | 12,565   | 36,872    | —        | 36,872    |
| Wastewater<br>Treatment  |          |          |          |           |          |           |
| Antifreeze<br>Business   | 4,531    | —        | 4,531    | 11,993    | —        | 11,993    |
| Field<br>Services  | 4,931    | —        | 4,931    | 13,153    | —        | 13,153    |
| Environmental<br>Services  | 513      | —        | 513      | 1,333     | —        | 1,333     |
| Other<br>Re-refinery<br>Product<br>Sales   | 29,357   | 29,357   | —        | —         | 79,254   | 79,254    |
| Oil<br>Collection<br>Services<br>&<br>RFO  | 5,941    | 5,941    | —        | —         | 15,054   | 15,054    |
| Oil<br>Filter<br>Business<br>Revenues<br>from<br>Contract<br>with<br>Customers     | 1,025    | 1,025    | —        | —         | 3,333    | 3,333     |
| Other<br>Revenue   | 44       | 44       | —        | —         | 256      | 256       |
| Total<br>Revenues  | \$63,307 | \$36,367 | \$99,674 | \$185,226 | \$97,897 | \$283,123 |

The following table provides information about contract assets and contract liabilities from contracts with customers:

| September 8,<br>(thousands)<br>2018 | December<br>31, 2017 |
|-------------------------------------|----------------------|
| Contract<br>assets<br>\$ 58         | \$ 59                |
| Contract<br>liabilities<br>289      | 327                  |
| Contract<br>liabilities<br>\$ 231   | \$ 268               |
| -                                   |                      |
| net                                 |                      |

During the quarter ended September 8, 2018, the Company recognized zero revenue that was included in the contract liabilities balance as of December 31, 2017. During the first three quarters ended September 8, 2018, the Company recognized \$0.3 million of revenue that was included in the contract liabilities balance as of December 31, 2017. The Company has no assets recognized from costs to obtain or fulfill a contract with a customer. We do not disclose the value of unsatisfied performance obligations for contracts with an original expected length of one year or less.

## (5) ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following:

| (thousands)                           | September 8,<br>2018 | December 30,<br>2017 |
|---------------------------------------|----------------------|----------------------|
| Trade                                 | \$ 50,000            | \$ 43,301            |
| Less: allowance for doubtful accounts | 1,494                | 1,881                |
| Trade - net                           | 48,506               | 41,420               |
| Related parties                       | 1,758                | 1,906                |
| Other                                 | 787                  | 2,165                |
| Total accounts receivable - net       | \$ 51,051            | \$ 45,491            |

The following table provides the changes in the Company's allowance for doubtful accounts for the first three quarters ended September 8, 2018, and the fiscal year ended December 30, 2017:

| (thousands)                             | For the First<br>Three<br>Quarters<br>Ended,<br>September 8,<br>2018 | For the Fiscal<br>Year Ended,<br>December 30,<br>2017 |
|---|--|---|
| Balance at beginning of period          | \$ 1,881   | \$ 2,176  |
| Provision for bad debts                 | 177  | 402   |
| Accounts written off, net of recoveries | (564 )   | (697 )  |
| Balance at end of period                | \$ 1,494   | \$ 1,881  |

## (6) INVENTORY

The carrying value of inventory consisted of the following:

| (thousands)                        | September 8,<br>2018 | December 30,<br>2017 |
|------------------------------------|----------------------|----------------------|
| Used oil and processed oil         | \$ 10,436            | \$ 5,788             |
| Solvents and solutions             | 7,534                | 6,201                |
| Machines                           | 5,244                | 3,679                |
| Drums and supplies                 | 4,734                | 4,430                |
| Other                              | 2,154                | 1,936                |
| Total inventory                    | 30,102               | 22,034               |
| Less: machine refurbishing reserve | 357                  | 395                  |
| Total inventory - net              | \$ 29,745            | \$ 21,639            |

Inventory consists primarily of used oil, processed oil, solvents and solutions, new and refurbished parts cleaning machines, drums and supplies, and other items. Inventories are valued at the lower of first-in, first-out (FIFO) cost or net realizable value, net of any reserves for excess, obsolete, or unsalable inventory. The Company routinely monitors its inventory levels at each of its locations and evaluates inventories for excess or slow-moving items. If circumstances indicate the cost of inventories exceed their recoverable value, inventories are reduced to net realizable value. The Company had no inventory write downs during the first three quarters of fiscal 2018 or fiscal 2017.



## (7) PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment consisted of the following:

| (thousands)                         | September 8,<br>2018 | December 30,<br>2017 |
|-------------------------------------|----------------------|----------------------|
| Machinery, vehicles, and equipment  | \$ 88,846            | \$ 85,427            |
| Buildings and storage tanks         | 69,363               | 69,009               |
| Land                                | 9,553                | 9,562                |
| Leasehold improvements              | 5,664                | 5,427                |
| Construction in progress            | 16,689               | 9,378                |
| Assets held for sale                | 45                   | 53                   |
| Total property, plant and equipment | 190,160              | 178,856              |
| Less: accumulated depreciation      | 56,407               | 50,737               |
| Property, plant and equipment - net | \$ 133,753           | \$ 128,119           |

| (thousands)                    | September 8,<br>2018 | December 30,<br>2017 |
|--------------------------------|----------------------|----------------------|
| Equipment at customers         | \$ 71,695            | \$ 68,234            |
| Less: accumulated depreciation | 47,928               | 44,922               |
| Equipment at customers - net   | \$ 23,767            | \$ 23,312            |

Depreciation expense for the third quarters ended September 8, 2018 and September 9, 2017 was \$3.1 million and \$3.4 million, respectively. Depreciation expense for the first three quarters ended September 8, 2018 and September 9, 2017 was \$8.9 million and \$10.2 million, respectively.

## (8) GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill is measured as a residual amount as of the acquisition date, which in most cases results in measuring goodwill as an excess of the purchase consideration transferred plus the fair value of any noncontrolling interest in the acquiree over the fair value of the net assets acquired, including any contingent consideration. The Company tests goodwill for impairment annually in the fourth quarter and in interim periods if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The Company's determination of fair value requires certain assumptions and estimates, such as margin expectations, market conditions, growth expectations, expected changes in working capital, etc., regarding expected future profitability and expected future cash flows. The Company tests goodwill for impairment at each of its two reporting units, Environmental Services and Oil Business.

The following table shows changes to our goodwill balances by segment from December 31, 2016, to September 8, 2018:

| (thousands)                         | Oil<br>Business | Environmental<br>Services | Total    |
|-------------------------------------|-----------------|---------------------------|----------|
| Goodwill at December 31, 2016       |                 |                           |          |
| Gross carrying amount               | \$ 3,952        | \$ 31,483                 | \$35,435 |
| Accumulated impairment loss         | (3,952 )        | —                         | (3,952 ) |
| Net book value at December 31, 2016 | \$—             | \$ 31,483                 | \$31,483 |
| Measurement period adjustments      | —               | 97                        | 97       |
| Goodwill at December 30, 2017       |                 |                           |          |
| Gross carrying amount               | 3,952           | 31,580                    | 35,532   |
| Accumulated impairment loss         | (3,952 )        | —                         | (3,952 ) |
| Net book value at December 30, 2017 | \$—             | \$ 31,580                 | \$31,580 |
| Acquisitions                        | —               | 2,545                     | 2,545    |
| Goodwill at September 8, 2018       |                 |                           |          |
| Gross carrying amount               | 3,952           | 34,125                    | 38,077   |
| Accumulated impairment loss         | (3,952 )        | —                         | (3,952 ) |
| Net book value at September 8, 2018 | \$—             | \$ 34,125                 | \$34,125 |

The following is a summary of software and other intangible assets:

| (thousands)                          | September 8, 2018           |                             |                           | December 30, 2017           |                             |                           |
|--------------------------------------|-----------------------------|-----------------------------|---------------------------|-----------------------------|-----------------------------|---------------------------|
|                                      | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Carrying<br>Amount | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Carrying<br>Amount |
| Customer & supplier relationships    | \$23,694                    | \$ 10,688                   | \$ 13,006                 | \$23,077                    | \$ 9,027                    | \$ 14,050                 |
| Software                             | 4,753                       | 4,045                       | 708                       | 4,724                       | 3,899                       | 825                       |
| Non-compete agreements               | 2,942                       | 2,862                       | 80                        | 2,949                       | 2,617                       | 332                       |
| Patents, formulae, and licenses      | 1,769                       | 688                         | 1,081                     | 1,769                       | 642                         | 1,127                     |
| Other                                | 1,348                       | 1,012                       | 336                       | 1,348                       | 950                         | 398                       |
| Total software and intangible assets | \$34,506                    | \$ 19,295                   | \$ 15,211                 | \$33,867                    | \$ 17,135                   | \$ 16,732                 |

Amortization expense was \$0.7 million for the third quarter ended September 8, 2018, and \$0.8 million for the third quarter ended September 9, 2017. Amortization expense was \$2.2 million for the first three quarters ended September 8, 2018, and \$2.3 million for the first three quarters ended September 9, 2017. The weighted average useful

lives of software; customer & supplier relationships; patents, formulae, and licenses; non-compete agreements, and other intangibles were 9 years, 10 years, 15 years, 5 years, and 6 years, respectively.

The expected amortization expense for the remainder of fiscal 2018 and for fiscal years 2019, 2020, 2021, and 2022 is \$0.9 million, \$2.8 million, \$2.6 million, \$2.5 million, and \$2.3 million, respectively. The preceding expected amortization expense is an estimate. Actual amounts of amortization expense may differ from estimated amounts due to additional intangible asset acquisitions, the finalization of the fair value of intangible assets that have been acquired from business combinations, disposal of intangible assets, accelerated amortization of intangible assets, and other events.

#### (9) ACCOUNTS PAYABLE

Accounts payable consisted of the following:

|                                    | September | December  |
|------------------------------------|-----------|-----------|
| (thousands)                        | 8,        | 30,       |
|                                    | 2018      | 2017      |
| Accounts payable                   | \$ 31,051 | \$ 25,540 |
| Accounts payable - related parties | 360       | 28        |
| Total accounts payable             | \$ 31,411 | \$ 25,568 |

#### (10) DEBT AND FINANCING ARRANGEMENTS

##### Bank Credit Facility

The Company's Credit Agreement as amended ("Credit Agreement"), provides for borrowings of up to \$95.0 million, subject to the satisfaction of certain terms and conditions, comprised of a term loan of \$30.0 million and up to \$65.0 million of borrowings under the revolving loan portion. The actual amount of borrowings available under the revolving loan portion of the Credit Agreement is limited by the Company's total leverage ratio. The amount available to draw at any point in time would be further reduced by any standby letters of credit issued.

Loans made under the Credit Agreement may be Base Rate Loans or LIBOR Rate Loans, at the election of the Company subject to certain exceptions. Base Rate Loans have an interest rate equal to (i) the higher of (a) the federal funds rate plus 0.5%, (b) the London Interbank Offering Rate ("LIBOR") plus 1%, or (c) Bank of America's prime rate, plus (ii) a variable margin of between 0.75% and 1.75% depending on the Company's total leverage ratio, calculated on a consolidated basis. LIBOR rate loans have an interest rate equal to (i) the LIBOR rate plus (ii) a variable margin of between 1.75% and 2.75% depending on the Company's total leverage ratio. Amounts borrowed under the Credit Agreement are secured by a security interest in substantially all of the Company's tangible and intangible assets.

The Credit Agreement contains customary terms and provisions (including representations, covenants, and conditions) for transactions of this type. Certain covenants, among other things, restrict the Company's and its subsidiaries' ability to incur indebtedness, grant liens, make investments and sell assets. The Credit Agreement also contains customary events of default, covenants and representations and warranties. Financial covenants include:

• An interest coverage ratio (based on interest expense and EBITDA) of at least 3.5 to 1.0;

A total leverage ratio no greater than 3.0 to 1.0, provided that in the event of a permitted acquisition having an aggregate consideration equal to \$10.0 million or more, at the Borrower's election, the total leverage ratio shall be deemed to be 3.25 to 1.00 for the fiscal quarter in which such permitted acquisition occurs and the three immediately following fiscal quarters and thereafter will revert to 3.00 to 1.00; and



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- A capital expenditures covenant limiting capital expenditures to \$100.0 million plus, if the capital expenditures permitted have been fully utilized, an additional amount for the remaining term of the Credit Agreement equal to 35% of EBITDA for the thirteen “four-week” periods most recently ended immediately prior to the full utilization of such \$100.0 million basket.

The Credit Agreement places certain limitations on acquisitions and the payment of dividends.

Debt at September 8, 2018 and December 30, 2017 consisted of the following:

| (thousands)                               | September 8,<br>2018 | December<br>30, 2017 |
|---|----------------------|----------------------|
| Principal amount                          | \$ 30,000            | \$ 30,000            |
| Less: unamortized debt issuance costs     | 1,047                | 1,256                |
| Debt less unamortized debt issuance costs | \$ 28,953            | \$ 28,744            |

The Company recorded interest expense of \$0.4 million, of which \$0.3 million is on our term loan, and \$0.1 million which is amortization of debt issuance costs, for the third quarter ended September 8, 2018. The Company recorded interest expense of \$0.3 million which was primarily on our term loan for the third quarter ended September 9, 2017. During the first three quarters of fiscal 2018, the Company recorded interest expense of \$1.0 million, of which \$0.8 million of interest expense is on our term loan, and \$0.2 million which is amortization of debt issuance costs. During the first three quarters of fiscal 2017, the Company recorded \$1.2 million of interest expense during the first three quarters of fiscal 2017. No interest was capitalized during the first three quarters of fiscal 2018 or 2017.

The Company's weighted average interest rate for all debt as of September 8, 2018, and September 9, 2017 was 3.8% and 3.6%, respectively.

As of September 8, 2018 and December 30, 2017, the Company was in compliance with all covenants under its Credit Agreement. As of September 8, 2018 and December 30, 2017, the Company had \$1.5 million and \$0.9 million of standby letters of credit issued, respectively, and \$63.5 million and \$64.1 million was available for borrowing under the bank credit facility, respectively. We believe that the carrying value of our debt balance at September 8, 2018 approximates fair value.

## (11) SEGMENT INFORMATION

The Company has two reportable segments: "Environmental Services" and "Oil Business." The Environmental Services segment consists of the Company's parts cleaning, containerized waste management, vacuum truck service, antifreeze recycling activities, and field services. The Oil Business segment consists primarily of the Company's used oil collection, used oil re-refining activities, and the dehydration of used oil to be sold as recycled fuel oil.

No single customer in either segment accounted for more than 10.0% of consolidated revenues in any of the periods presented. There were no intersegment revenues. Both the Environmental Services and Oil Business segment operate in the United States and, to an immaterial degree, in Ontario, Canada. As such, the Company is not disclosing operating results by geographic segment.

Segment results for the third quarters ended September 8, 2018, and September 9, 2017 were as follows:

Third Quarter Ended,

September 8, 2018

| (thousands)   | Environmental Services | Oil Business | Corporate and Eliminations | Consolidated |
|---|------------------------|--------------|----------------------------|--------------|
| Revenues  |                        |              |                            |              |
| Service revenues  | \$ 55,473              | \$ 2,581     | \$ —                       | \$ 58,054    |
| Product revenues  | 7,834                  | 33,786       | —                          | 41,620       |
| Total revenues  | \$ 63,307              | \$ 36,367    | \$ —                       | \$ 99,674    |
| Operating expenses  |                        |              |                            |              |
| Operating costs   | 45,460                 | 30,585       | —                          | 76,045       |
| Operating depreciation and amortization                               | 1,599                  | 1,410        | —                          | 3,009        |
| Profit before corporate selling, general, and administrative expenses | \$ 16,248              | \$ 4,372     | \$ —                       | \$ 20,620    |
| Selling, general, and administrative expenses                         |                        |              | 10,641                     | 10,641       |
| Depreciation and amortization from SG&A                               |                        |              | 767                        | 767          |
| Total selling, general, and administrative expenses                   |                        |              | \$ 11,408                  | \$ 11,408    |
| Other expense - net   |                        |              | 253                        | 253          |
| Operating income  |                        |              |                            | 8,959        |
| Interest expense – net  |                        |              | 256                        | 256          |
| Income before income taxes  |                        |              |                            | \$ 8,703     |



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Third Quarter Ended,  
September 9, 2017

| (thousands)  | Environmental<br>Services | Oil<br>Business | Corporate<br>and<br>Eliminations | Consolidated |
|--|---------------------------|-----------------|----------------------------------|--------------|
| Revenues   |                           |                 |                                  |              |
| Service revenues   | \$ 49,419                 | \$ 4,629        | \$ —                             | \$ 54,048    |
| Product revenues   | 5,623                     | 23,660          | —                                | 29,283       |
| Total revenues   | \$ 55,042                 | \$ 28,289       | \$ —                             | \$ 83,331    |
| Operating expenses   |                           |                 |                                  |              |
| Operating costs  | 38,298                    | 25,351          | —                                | 63,649       |
| Operating depreciation and amortization                                  | 1,794                     | 1,555           | —                                | 3,349        |
| Profit before corporate selling, general,<br>and administrative expenses | \$ 14,950                 | \$ 1,383        | \$ —                             | \$ 16,333    |
| Selling, general, and administrative<br>expenses                         |                           |                 | 10,955                           | 10,955       |
| Depreciation and amortization from<br>SG&A                               |                           |                 | 837                              | 837          |
| Total selling, general, and administrative<br>expenses                   |                           |                 | \$ 11,792                        | \$ 11,792    |
| Other (income) - net   |                           |                 | (3,078)                          | (3,078)      |
| Operating income   |                           |                 |                                  | 7,619        |
| Interest expense – net   |                           |                 | 276                              | 276          |
| Income before income taxes   |                           |                 |                                  | \$ 7,343     |

Segment results for the first three quarters ended September 8, 2018, and September 9, 2017 were as follows:

First Three Quarters Ended,  
September 8, 2018

| (thousands)  | Environmental<br>Services | Oil<br>Business | Corporate<br>and<br>Eliminations | Consolidated |
|--|---------------------------|-----------------|----------------------------------|--------------|
| Revenues   |                           |                 |                                  |              |
| Service revenues   | \$ 163,428                | \$ 8,777        | \$ —                             | \$ 172,205   |
| Product revenues   | 21,798                    | 89,120          | —                                | 110,918      |
| Total revenues   | \$ 185,226                | \$ 97,897       | \$ —                             | \$ 283,123   |
| Operating expenses   |                           |                 |                                  |              |
| Operating costs  | 134,640                   | 86,062          | —                                | 220,702      |
| Operating depreciation and amortization                                  | 4,590                     | 4,188           | —                                | 8,778        |
| Profit before corporate selling, general,<br>and administrative expenses | \$ 45,996                 | \$ 7,647        | \$ —                             | \$ 53,643    |
| Selling, general, and administrative<br>expenses                         |                           |                 | 33,185                           | 33,185       |
| Depreciation and amortization from<br>SG&A                               |                           |                 | 2,300                            | 2,300        |
| Total selling, general, and administrative<br>expenses                   |                           |                 | \$ 35,485                        | \$ 35,485    |

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|                            |     |           |
|----------------------------|-----|-----------|
| Other expense - net        | 983 | 983       |
| Operating income           |     | 17,175    |
| Interest expense – net     | 742 | 742       |
| Income before income taxes |     | \$ 16,433 |

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First Three Quarters Ended,  
September 9, 2017

| (thousands)  | Environmental<br>Services | Oil<br>Business | Corporate<br>and<br>Eliminations | Consolidated |
|--|---------------------------|-----------------|----------------------------------|--------------|
| Revenues   |                           |                 |                                  |              |
| Service revenues   | \$ 146,135                | \$ 15,936       | \$ —                             | \$ 162,071   |
| Product revenues   | 17,215                    | 70,880          | —                                | 88,095       |
| Total revenues   | \$ 163,350                | \$ 86,816       | \$ —                             | \$ 250,166   |
| Operating expenses   |                           |                 |                                  |              |
| Operating costs  | 111,419                   | 76,791          | —                                | 188,210      |
| Operating depreciation and amortization                                  | 5,341                     | 4,624           | —                                | 9,965        |
| Profit before corporate selling, general,<br>and administrative expenses | \$ 46,590                 | \$ 5,401        | \$ —                             | \$ 51,991    |
| Selling, general, and administrative<br>expenses                         |                           |                 | 33,871                           | 33,871       |
| Depreciation and amortization from<br>SG&A                               |                           |                 | 2,536                            | 2,536        |
| Total selling, general, and administrative<br>expenses                   |                           |                 | \$ 36,407                        | \$ 36,407    |
| Other (income) - net   |                           |                 | (11,112)                         | (11,112)     |
| Operating income   |                           |                 |                                  | 26,696       |
| Interest expense – net   |                           |                 | 775                              | 775          |
| Income before income taxes   |                           |                 |                                  | \$ 25,921    |

Total assets by segment as of September 8, 2018, and December 30, 2017 were as follows:

| (thousands)                        | September 8,<br>2018 | December 30,<br>2017 |
|------------------------------------|----------------------|----------------------|
| Total Assets:                      |                      |                      |
| Environmental<br>Services          | \$ 141,414           | \$ 131,457           |
| Oil Business                       | 141,250              | 129,936              |
| Unallocated<br>Corporate<br>Assets | 58,048               | 53,264               |
| Total                              | \$ 340,712           | \$ 314,657           |

Segment assets for the Environmental Services and Oil Business segments consist of property, plant, and equipment, intangible assets, accounts receivable, goodwill, and inventories. Assets for the corporate unallocated amounts consist of property, plant, and equipment used at the corporate headquarters as well as cash and net deferred tax assets.

## (12) COMMITMENTS AND CONTINGENCIES

The Company may enter into purchase obligations with certain vendors. They represent expected payments to third party service providers and other commitments entered into during the normal course of our business. These purchase obligations are generally cancelable with or without notice, without penalty, although certain vendor agreements provide for cancellation fees or penalties depending on the terms of the contract.

The Company has purchase obligations in the form of open purchase orders of \$24.1 million as of September 8, 2018, and \$15.6 million as of December 30, 2017, primarily for used oil, solvent, machine purchases, disposal and transportation expenses, and capital expenditures.

The Company may be subject to investigations, claims or lawsuits as a result of operating its business, including matters governed by environmental laws and regulations. The Company may also be subject to tax audits in a variety of jurisdictions. When claims are asserted, the Company evaluates the likelihood that a loss will occur and records a liability for those instances when the likelihood is deemed probable and the exposure is reasonably estimable. The Company carries insurance at levels it believes are adequate to cover loss contingencies based on historical claims activity. When the potential loss exposure is limited to the insurance deductible and the likelihood of loss is determined to be probable, the Company accrues for the amount of the required deductible, unless a lower amount of exposure is estimated. As of September 8, 2018 and December 30, 2017, the Company had accrued \$4.6 million and \$4.5 million related to loss contingencies and other contingent liabilities, respectively.

## (13) INCOME TAXES

On December 22, 2017, the Tax Cuts and Jobs Act (the "Act") was enacted into law and introduced significant changes to U.S. tax law. The Act reduces the U.S. federal corporate tax rate from 35% to 21%. The new legislation also sets forth a variety of other changes, including a limitation on the tax deductibility of interest expense, the acceleration of business asset expensing, a limitation on the use of net operating losses generated in future years, the repeal of the alternative minimum tax (AMT), and a reduction in the amount of executive pay that could qualify as a tax deduction.

On December 22, 2017, the SEC issued Staff Accounting Bulletin No. 118 (SAB 118) which addresses income tax accounting implications of the Tax Act. The purpose of SAB 118 was to address any uncertainty or diversity of view in applying ASC 740 Income Taxes in the reporting period in which the Tax Act was enacted. SAB 118 allows for a measurement period to finalize the impacts of the Tax Act, not to extend beyond one year from the date of enactment. As of September 8, 2018 the Company has not finalized its SAB 118 tax reform estimates.

The Internal Revenue Service has issued guidance with respect to the one time deemed income inclusion under IRC 965 and the Company has determined there was no income inclusion related to its controlled foreign corporation under IRC 965 for the year ended December 30, 2017.

The Company deducted for federal income tax purposes accelerated "bonus" depreciation on the majority of its capital expenditures for assets placed in service in fiscal 2011 through fiscal 2017. Therefore, the Company recorded a deferred tax liability related to the difference between the book basis and the tax basis of those assets. In addition, as a result of the federal bonus depreciation, the Company recorded a Net Operating Loss ("NOL"). The balance on the federal NOL at September 8, 2018 was \$12.6 million. There are also state NOLs of varying amounts, dependent on each state's conformity with bonus depreciation. The remaining deferred tax asset related to the Company's state and federal NOL was a tax effected balance of \$3.4 million.



The Company's effective tax rate for the third quarter of fiscal 2018 was 26.2% compared to 35.2% in the third quarter of fiscal 2017. The Company's effective rate for the first three quarters of fiscal 2018 was 24.3% compared to 36.1% in the first three quarters of fiscal 2017. The rate difference is principally attributable to the decrease in the federal corporate tax rate.

The Company establishes reserves when it is more likely than not that the Company will not realize the full tax benefit of a position. The Company had a reserve of \$2.5 million for uncertain tax positions as of September 8, 2018 and December 30, 2017. The gross unrecognized tax benefits would, if recognized, decrease the Company's effective tax rate.

## (14) SHARE-BASED COMPENSATION

The aggregate number of shares of common stock which may be issued under the Company's 2008 Omnibus Plan ("Plan") is 2,602,077 plus any common stock that becomes available for issuance pursuant to the reusage provision of the Plan. As of September 8, 2018, the number of shares available for issuance under the Plan was 181,723 shares.

## Stock Option Awards

A summary of stock option activity under this Plan is as follows:

| Outstanding Stock Options                | Number of<br>Options<br>Outstanding | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term<br>(in years) | Aggregate<br>Intrinsic<br>Value as of<br>Date Listed<br>(in<br>thousands) |
|--|-------------------------------------|--|---|---|
| Options outstanding at December 30, 2017 | 19,435                              | \$ 7.33                                  | 1.23  | \$ 280  |
| Exercised                                | (14,048 )                           | 7.33                                     | —   | —   |
| Options outstanding at September 8, 2018 | 5,387                               | \$ 7.33                                  | 0.54  | \$ 81   |

## Restricted Stock Compensation/Awards

Annually, the Company grants restricted shares to its Board of Directors. The shares become fully vested one year from their grant date. The fair value of each restricted stock grant is based on the closing price of the Company's common stock on the date of grant. The Company amortizes the expense over the service period, which is the fiscal year in which the award is granted. In addition, the Company may grant restricted shares to certain members of management based on their services and contingent upon continued service with the Company. The restricted shares vest over a period of approximately three years from the grant date. The fair value of each restricted stock grant is based on the closing price of the Company's common stock on the date of grant.

Pursuant to the Heritage-Crystal Clean, Inc. Omnibus Incentive Plan of 2008, on April 13, 2018, the Company granted 350,000 shares of restricted stock to certain members of Management as part of a Special Incentive Program. The number of shares granted may be increased up to 612,500 shares depending on the Company's level of performance with regard to certain market conditions. Up to 612,500 shares will vest on April 13, 2022, depending on the satisfaction of certain service and market conditions.

The following table shows a summary of restricted share grants and expense resulting from the awards:

| (thousands, except share amounts) | Grant Date     | Restricted<br>Shares | Compensation<br>Expense                                   |                      | Unrecognized<br>Expense as of, |                       |
|-----------------------------------|----------------|----------------------|---|----------------------|--------------------------------|-----------------------|
|                                   |                |                      | First Three Quarters<br>Ended,<br>September<br>8,<br>2018 | September 9,<br>2017 | September<br>8,<br>2018        | September<br>30, 2017 |
| Members of Management             | January, 2016  | 43,208               | \$ 67   | \$ 72                | \$ 30                          | \$ 101                |
| Members of Management             | February, 2017 | 146,564              | 318   | 307                  | 507                            | 841                   |
| Chief Executive Officer           | February, 2017 | 500,000              | 921   | 737                  | 1,502                          | 2,423                 |

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|                         |                |         |     |     |       |       |
|-------------------------|----------------|---------|-----|-----|-------|-------|
| Board of Directors      | April, 2017    | 14,980  | —   | 168 | —     | —     |
| Members of Management   | February, 2018 | 116,958 | 374 | 601 | 1,359 | 1,770 |
| Special Incentive Grant | April, 2018    | 350,000 | 817 | —   | 7,251 | —     |
| Board of Directors      | May, 2018      | 13,800  | 197 | —   | 88    | —     |

In February 2017, as part of Mr. Recatto's employment agreement, the Company granted a restricted stock award of 500,000 shares of common stock, which vests through January 2021 in an amount based on the vesting table below, with the common stock price increase to be determined based on the increase in the price of the Company's common stock (if any) from the closing price

of the common stock as reported by Nasdaq on the employment commencement date (\$15.00) and the common stock price on the potential vesting date (determined by using the weighted average closing price of a share of the Company's common stock for the 90-day period ending on the vesting date). If the stock price does not increase by \$5.00, then no shares shall vest. During the first three quarters of fiscal 2018, the Company recorded approximately \$0.9 million of compensation expense, which includes \$0.2 million of expense from the recognition of an accelerated vesting, related to this award. In the future, the Company expects to recognize compensation expense of approximately \$1.5 million over the remaining requisite service period, which ends January 31, 2021. The fair value of this restricted stock award as of the grant date was estimated using a Monte Carlo simulation model. Key assumptions used in the Monte Carlo simulation to estimate the grant date fair value of this award are a risk-free rate of 1.70%, expected dividend yield of zero, and an expected volatility assumption of 41.73%.

#### Vesting Table

| Increase in Stock Price From the Employment Commencement Date to the Vesting Date | Total percentage of Restricted Stock Shares to Be Vested |
|---|--|
| Less than \$5 per share increase  | —%   |
| \$5 per share increase  | 25%  |
| \$10 per share increase   | 50%  |
| \$15 per share increase   | 75%  |
| \$20 or more per share increase   | 100%   |

#### Provision for possible accelerated vesting of award

If the average closing price of the Company's common stock increases by the marginal levels set forth in the above vesting table for any consecutive 180 day period between the award date and final vesting date, Mr. Recatto shall become vested in 50% of the corresponding total percentage of restricted shares earned on the last day of the 180 day period. On March 14, 2018, the average closing price of the Company's common stock met the 25% marginal level and Mr. Recatto became fully vested in half of the 125,000 vested shares.

The following table summarizes the restricted stock activity for the first three quarters ended September 8, 2018:

| Restricted Stock (Nonvested Shares)               | Number of Shares | Weighted Average Grant-Date Fair Value Per Share |
|---|------------------|--|
| Nonvested shares outstanding at December 30, 2017 | 685,999          | \$ 14.52   |
| Granted   | 480,755          | 21.81  |
| Vested  | (149,710 )       | 14.57  |
| Forfeited   | (3,181 )         | 17.75  |
| Nonvested shares outstanding at September 8, 2018 | 1,013,863        | \$ 18.20   |

#### Employee Stock Purchase Plan

As of September 8, 2018, the Company had reserved 134,856 shares of common stock available for purchase under the Employee Stock Purchase Plan of 2008. In the first three quarters of fiscal 2018, employees purchased 15,170 shares of the Company's common stock with a weighted average fair market value of \$21.61 per share.



## (15) EARNINGS PER SHARE

The following table reconciles the number of shares outstanding for the third quarters and the first three quarters of fiscal 2018 and 2017, respectively, to the number of weighted average basic shares outstanding and the number of weighted average diluted shares outstanding for the purposes of calculating basic and diluted earnings per share:

| (thousands, except share amounts)  | Third Quarter Ended, |                    | First Three Quarters Ended, |                    |
|--|----------------------|--------------------|-----------------------------|--------------------|
|  | September 30, 2018   | September 30, 2017 | September 30, 2018          | September 30, 2017 |
| Net income   | \$6,419              | \$ 4,757           | \$12,437                    | \$ 16,560          |
| Less: income attributable to noncontrolling interest                                     | 74                   | 53                 | 213                         | 158                |
| Net income attributable to Heritage-Crystal Clean, Inc. available to common stockholders | \$6,345              | \$ 4,704           | \$12,224                    | \$ 16,402          |
| Weighted average basic shares outstanding  | 23,048               | 22,686             | 23,013                      | 22,515             |
| Dilutive shares for share-based compensation plans                                       | 356                  | 284                | 286                         | 298                |
| Weighted average diluted shares outstanding  | 23,404               | 22,970             | 23,299                      | 22,813             |
| Net income per share: basic  | \$0.28               | \$ 0.21            | \$0.53                      | \$ 0.73            |
| Net income per share: diluted  | \$0.27               | \$ 0.20            | \$0.52                      | \$ 0.72            |

## (16) OTHER EXPENSE (INCOME) - NET

Other expense of \$1.0 million for the first three quarters of fiscal 2018 primarily consists of \$0.7 million of site closure costs. Other (income) of \$11.1 million for the first three quarters of fiscal 2017 includes a gain of \$5.1 million received in the first quarter of fiscal 2017 as a partial award for an arbitration claim and a gain of \$3.6 million received during the third quarter of fiscal 2017 from a settlement agreement, both of which were related to our acquisition of FCC Environmental, LLC and International Petroleum Corp. of Delaware in 2014. Additionally, during third quarter of 2017, the Company recorded a gain of \$3.1 million from having sold the Company's facility located in Pompano Beach, Florida.

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

### Disclosure Regarding Forward-Looking Statements

You should read the following discussion in conjunction with our consolidated financial statements and related notes in our Annual Report on Form 10-K filed with the SEC on March 1, 2018. In addition to historical information, this discussion contains forward-looking statements that involve risks, uncertainties and assumptions that could cause actual results to differ materially from our expectations. These statements can be identified by the fact that they do not relate strictly to historical or current facts. They use words such as "aim," "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "project," "should," "will be," "will continue," "will likely result," "would" and other words and terms of similar meaning in conjunction with a discussion of future or estimated operating or financial performance. You should read statements that contain these words carefully, because they discuss our future expectations, contain projections of our future results of operations or of our financial position or state other "forward-looking" information. Forward-looking statements speak only as of the date of this quarterly report. Factors that could cause such differences include those described in the section titled "Risk Factors" and elsewhere in our Annual Report on Form 10-K for fiscal 2017 filed with the SEC on March 1, 2018. Except as required under federal securities laws and the rules and regulations of the SEC, we do not have any intention, and do not undertake, to update any forward-looking statements to reflect events or circumstances arising after the date of this quarterly report, whether as a result of new information, future events or otherwise. As a result of these risks and uncertainties, readers are cautioned not to place undue reliance on the forward-looking statements included in this quarterly report or that may be made elsewhere from time to time by, or on behalf of, us. All forward-looking statements attributable to us are expressly qualified by these cautionary statements. Certain tabular information may not foot due to rounding. Our fiscal year ends on the Saturday closest to December 31. Interim results are presented for the twelve weeks ("third quarter" or "quarter") and thirty-six weeks (first three quarters) ended September 8, 2018 and September 9, 2017, respectively. "Fiscal 2017" represents the 52-week period ended December 30, 2017 and "Fiscal 2018" represents the 52-week period ending December 29, 2018.

### Overview

We provide parts cleaning, containerized waste management, used oil collection, vacuum truck services, antifreeze recycling, and field services primarily to small and medium sized industrial customers as well as vehicle maintenance customers. We own and operate a used oil re-refinery, several wastewater treatment plants and multiple antifreeze recycling facilities. We believe we are the second largest provider of industrial and hazardous waste services to small and mid-sized customers in both the vehicle maintenance and manufacturing services sector in North America, and we have the second largest used oil re-refining capacity in North America. Our services help our customers manage their used chemicals and liquid and solid wastes while also helping to minimize their regulatory burdens. We operate from a network of 89 branch facilities providing services to customers in 45 states and parts of Canada. We conduct business through two segments: Environmental Services and Oil Business.

Our Environmental Services segment revenues are generated primarily from providing parts cleaning services, containerized waste management, vacuum truck services, antifreeze recycling, and field services. Revenues from this segment accounted for approximately 65% of our total Company revenues for the first three quarters of fiscal 2018. In the Environmental Services segment, we define and measure same-branch revenues for a given period as the subset of all our branches that have been open and operating throughout and between the periods being compared, and we refer to these as established branches. We calculate average revenues per working day by dividing our revenues by the number of non-holiday weekdays in the applicable fiscal year or fiscal quarter.

Our Oil Business segment consists primarily of our used oil collection, used oil re-refining activities, and recycled fuel oil ("RFO") sales which accounted for approximately 35% of our total Company revenues in the first three quarters of fiscal 2018.

Our operating costs include the costs of the materials we use in our products and services, such as used oil collected from customers or purchased from third party collectors, solvent, and other chemicals. The used solvent that we retrieve from customers in our product reuse program is accounted for as a reduction in our net cost of solvent under operating costs, whether placed in inventory or sold to a purchaser for reuse. Changes in the price of crude oil can impact operating costs indirectly as it may impact the price we pay for solvent or used oil, although we attempt to offset volatility in the oil markets by managing the spread between the costs we pay for our materials and the prices we charge for our products and services. Operating costs also include transportation of solvents and waste, payments to third parties to recycle or dispose of the waste materials that we collect, and the costs of operating our re-refinery, recycling centers, waste water treatment facilities, hubs, and branch system including personnel costs (including commissions), facility rent, truck leases, fuel, and maintenance. Our operating costs as a



percentage of sales generally increase in relation to the number of new branch openings. As new branches achieve route density and scale efficiencies, our operating costs as a percentage of sales generally decrease.

We use profit before corporate selling, general, and administrative expenses ("SG&A") as a key measure of segment profitability. We define profit before corporate SG&A expense as revenue less operating costs and depreciation and amortization from operations.

Our corporate selling, general, and administrative expenses include the costs of performing centralized business functions, including sales management at or above the regional level, business management, billing, receivables management, accounting and finance, information technology, environmental health and safety, human resources and legal.

We operate a used oil re-refinery located in Indianapolis, Indiana, through which we recycle used oil into high quality lubricant base oil and other products. We supply the base oil to firms that produce and market finished lubricants. Our re-refinery has an annual nameplate capacity of approximately 75 million gallons of used oil feedstock, allowing it to produce approximately 47 million gallons of lubricating base oil per year when operating at full capacity.

#### Critical Accounting Policies

Critical accounting policies are those that are both important to the accurate portrayal of a company's financial condition and results and require subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

In order to prepare financial statements that conform to accounting principles generally accepted in the United States, commonly referred to as GAAP, we make estimates and assumptions that affect the amounts reported in our financial statements and accompanying notes. Certain estimates are particularly sensitive due to their significance to the financial statements and the possibility that future events may be significantly different from our expectations.

There were no material changes during the first three quarters of fiscal 2018 to the information provided under the heading "Critical Accounting Policies" included in our Annual Report on Form 10-K for the fiscal year ended December 30, 2017 with the exception of revenue recognition. See footnote 4 — Revenue for more information.

## RESULTS OF OPERATIONS

## General

The following table sets forth certain operating data as a percentage of revenues for the periods indicated:

| (thousands)   | For the Third Quarter Ended, |                      | For the First Three Quarters Ended, |                      |           |        |           |        |
|---|------------------------------|----------------------|-------------------------------------|----------------------|-----------|--------|-----------|--------|
|   | September 8,<br>2018         | September 9,<br>2017 | September 8,<br>2018                | September 9,<br>2017 |           |        |           |        |
| <b>Revenues</b>   |                              |                      |                                     |                      |           |        |           |        |
| Service revenues  | \$58,054                     | 58.2%                | \$54,048                            | 64.9%                | \$172,205 | 60.8%  | \$162,071 | 64.8%  |
| Product revenues  | 41,620                       | 41.8%                | 29,283                              | 35.1%                | 110,918   | 39.2%  | 88,095    | 35.2%  |
| Total revenues  | \$99,674                     | 100.0%               | \$83,331                            | 100.0%               | \$283,123 | 100.0% | \$250,166 | 100.0% |
| <b>Operating expenses</b>   |                              |                      |                                     |                      |           |        |           |        |
| Operating costs   | \$76,045                     | 76.3%                | \$63,649                            | 76.4%                | \$220,702 | 78.0%  | \$188,210 | 75.2%  |
| Selling, general and administrative expenses                                | 10,641                       | 10.7%                | 10,955                              | 13.1%                | 33,185    | 11.7%  | 33,871    | 13.5%  |
| Depreciation and amortization   | 3,776                        | 3.8%                 | 4,186                               | 5.0%                 | 11,078    | 3.9%   | 12,501    | 5.0%   |
| Other expense (income) - net  | 253                          | 0.3%                 | (3,078)                             | (3.7)%               | 983       | 0.3%   | (11,112)  | (4.4)% |
| Operating income  | 8,959                        | 9.0%                 | 7,619                               | 9.1%                 | 17,175    | 6.1%   | 26,696    | 10.7%  |
| Interest expense – net  | 256                          | 0.3%                 | 276                                 | 0.3%                 | 742       | 0.3%   | 775       | 0.3%   |
| Income before income taxes  | 8,703                        | 8.7%                 | 7,343                               | 8.8%                 | 16,433    | 5.8%   | 25,921    | 10.4%  |
| Provision for income taxes  | 2,284                        | 2.3%                 | 2,586                               | 3.1%                 | 3,996     | 1.4%   | 9,361     | 3.7%   |
| Net income  | 6,419                        | 6.4%                 | 4,757                               | 5.7%                 | 12,437    | 4.4%   | 16,560    | 6.6%   |
| Income attributable to noncontrolling interest                              | 74                           | 0.1%                 | 53                                  | 0.1%                 | 213       | 0.1%   | 158       | 0.1%   |
| Net income attributable to Heritage-Crystal Clean, Inc. common stockholders | \$6,345                      | 6.4%                 | \$4,704                             | 5.6%                 | \$12,224  | 4.3%   | \$16,402  | 6.6%   |

## Revenues

For the third quarter of fiscal 2018, revenues increased \$16.3 million, or 19.6%, from \$83.3 million in the third quarter of fiscal 2017 to \$99.7 million in the third quarter of fiscal 2018. The increase in revenue was driven by growth in all Environmental Services segment product and service lines of business, along with a 28.6% increase in revenue from our Oil Business segment. For the first three quarters of fiscal 2018, revenues increased \$33.0 million, or 13.2%, from \$250.2 million in the first three quarters of fiscal 2017 to \$283.1 million. The growth in revenue was mainly driven by a 13.4% year over year increase in our Environmental Services segment and a 12.8% year over year increase in our Oil Business segment.

## Operating expenses

## Operating costs

Operating costs increased \$12.4 million, or 19.5%, from the third quarter of fiscal 2017 compared to the third quarter of fiscal 2018. Operating costs increased \$32.5 million, or 17.3%, from the first three quarters of fiscal 2017 to the first three quarters of fiscal 2018. The main drivers of the increase were increases in disposal costs, used oil collection and processing costs, transportation costs and labor costs. Higher expenses for disposal were due to an outage at one of our main third-party disposal vendors during the first quarter of fiscal 2018, along with higher disposal costs associated with a special project in our field services line of business during the second and third quarters of fiscal 2018. Higher labor costs were primarily due to additional resources to support revenue growth initiatives in our

Environmental Services segment.

We expect that in the future our operating costs in the Environmental Services business will continue to increase as our service volume increases; however, a decrease in crude oil prices could partially offset this cost increase because a decrease in price could cause a decline in the price we pay for parts cleaning solvent and diesel fuel. Likewise, an increase in crude oil prices could cause an increase in the price we pay for parts cleaning solvent and diesel fuel. In the Oil Business segment, our

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operating costs could increase or decrease in the future depending on changes in the price for crude oil which could indirectly impact our used oil collection costs and processing costs at our re-refinery.

#### Selling, general, and administrative expenses

Selling, general, and administrative expenses decreased \$0.3 million, or 2.9%, from the third quarter of fiscal 2017 to the third quarter of fiscal 2018. Selling, general, and administrative expenses decreased \$0.7 million, or 2.0%, from the first three quarters of fiscal 2017 to the first three quarters of fiscal 2018. The decrease in expense was mainly driven by lower severance and bank fees, partially offset by higher share-based compensation expense year over year.

#### Other expense (income) - net

Other expense (income) - net was \$0.3 million of expense for the third quarter of fiscal 2018 compared to income of \$3.1 million for the third quarter of fiscal 2017. Other income for the third quarter of fiscal 2017 was mainly driven by a gain of \$3.1 million from having sold the Company's facility located in Pompano Beach, Florida.

Other expense (income) - net was \$1.0 million of expense for the first three quarters of fiscal 2018 compared to approximately \$11.1 million of income for the first three quarters of fiscal 2017. Other expense for the first three quarters of fiscal 2018 was mainly driven by \$0.7 million of site closure costs for a facility in Wilmington, DE. The first three quarters of fiscal 2017 included a gain of \$5.1 million received in the first quarter of fiscal 2017 as a result of having received a partial award for a claim made in arbitration, and a gain of \$3.6 million received during the third quarter of fiscal 2017 from a settlement agreement, both of which were related to our acquisition of FCC Environmental, LLC and International Petroleum Corp. of Delaware in 2014, along with the aforementioned \$3.1 million gain from the sale of the Company's Pompano Beach, Florida facility.

#### Interest expense - net

Net interest expense for the third quarters of fiscal 2018 and fiscal 2017 was \$0.3 million. Net interest expense for the first three quarters of fiscal 2018 was \$0.7 million compared to \$0.8 million for the first three quarters of fiscal 2017.

#### Provision for income taxes

The Company's effective tax rate for the third quarter of fiscal 2018 was 26.2% compared to 35.2% in the third quarter of fiscal 2017. The Company's effective rate for the first three quarters of fiscal 2018 was 24.3% compared to 36.1% in the first three quarters of fiscal 2017. The rate difference is principally attributable to the decrease in the federal corporate tax rate.

#### Segment Information

The following table presents revenues by reportable segment:

|                        | For the Third Quarter<br>Ended, |                      | Change   |       |
|------------------------|---------------------------------|----------------------|----------|-------|
| (thousands)            | September<br>2018               | September 9,<br>2017 | \$       | %     |
| Revenues:              |                                 |                      |          |       |
| Environmental Services | \$63,307                        | \$ 55,042            | \$ 8,265 | 15.0% |
| Oil Business           | 36,367                          | 28,289               | 8,078    | 28.6% |

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|               |                     |              |           |       |
|---------------|---------------------|--------------|-----------|-------|
| Total         | \$99,674            | \$ 83,331    | \$ 16,343 | 19.6% |
|               | For the First Three |              | Change    |       |
|               | Quarters Ended,     |              |           |       |
|               | September           | September 9, | \$        | %     |
|               | 2018                | 2017         |           |       |
| Revenues:     |                     |              |           |       |
| Environmental | \$185,226           | \$ 163,350   | \$ 21,876 | 13.4% |
| Services      |                     |              |           |       |
| Oil Business  | 97,897              | 86,816       | 11,081    | 12.8% |
| Total         | \$283,123           | \$ 250,166   | \$ 32,957 | 13.2% |

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In the third quarter of fiscal 2018, Environmental Services revenue increased by \$8.3 million, or 15.0%, from \$55.0 million in the third quarter of fiscal 2017 to \$63.3 million in the third quarter of fiscal 2018. The increase in revenue was driven by growth in all of our product and service lines with the strongest growth in our field services, containerized waste, and antifreeze businesses. Our growth in field services was achieved in part due to one large project, that commenced during the second quarter of fiscal 2018, which contributed approximately \$2.0 million in revenue during the third quarter of fiscal 2018. In the first three quarters of fiscal 2018, Environmental Services revenues increased by \$21.9 million, or 13.4%, from \$163.4 million in the first three quarters of fiscal 2017 to \$185.2 million in the first three quarters of fiscal 2018. Approximately \$5.2 million, or 3.2%, of our increased revenue for the first three quarters of 2018 in our Environmental Services segment was attributed to the large field services project mentioned above.

In the third quarter of fiscal 2018, Oil Business revenues were up \$8.1 million, or 28.6%, compared to the third quarter of fiscal 2017. In the first three quarters of fiscal 2018, Oil Business revenues increased \$11.1 million, or 12.8%, compared to the first three quarters of fiscal 2017. The increase in revenue was primarily due to stronger base oil pricing and higher volumes of base oil gallons sold, due in part to strong base oil production at our re-refinery during the second and third quarters of fiscal 2018. During the third quarter of fiscal 2018, we produced 11.2 million gallons of base oil compared to 9.5 million gallons during the third quarter of fiscal of 2017. During the third quarter of fiscal 2018, we sold approximately 10.5 million gallons of base oil compared to 8.9 million gallons during the third quarter of fiscal 2017. For the first three quarters of 2018 we sold 29.3 million gallons of base oil compared to 28.2 million for the first three quarters of 2017.

Segment Profit Before Corporate Selling, General and Administrative Expenses ("SG&A")

The following table presents profit by reportable segment before corporate SG&A expense:

|                               | For the Third Quarter Ended,        |                | Change  |        |
|-------------------------------|-------------------------------------|----------------|---------|--------|
| (thousands)                   | September 2018                      | September 2017 | \$      | %      |
| Profit before corporate SG&A* |                                     |                |         |        |
| Environmental Services        | \$16,248                            | \$14,950       | \$1,298 | 8.7%   |
| Oil Business                  | 4,372                               | 1,383          | 2,989   | 216.1% |
| Total                         | \$20,620                            | \$16,333       | \$4,287 | 26.2%  |
|                               | For the First Three Quarters Ended, |                | Change  |        |
| (thousands)                   | September 2018                      | September 2017 | \$      | %      |
| Profit before corporate SG&A* |                                     |                |         |        |
| Environmental Services        | \$45,996                            | \$46,590       | \$(594) | (1.3)% |
| Oil Business                  | 7,647                               | 5,401          | 2,246   | 41.6%  |
| Total                         | \$53,643                            | \$51,991       | \$1,652 | 3.2%   |

\*Includes depreciation and amortization related to operating activity but not depreciation and amortization related to corporate selling, general, and administrative activity. For further discussion see Note 11 in our consolidated financial statements included elsewhere in this document.

Environmental Services profit before corporate SG&A expense increased \$1.3 million in the third quarter of fiscal 2018 compared to the third quarter of fiscal 2017. The \$1.3 million increase was mainly driven by higher revenue, partially offset by higher disposal and disposal related transportation costs. Environmental Services profit before corporate SG&A expense decreased \$0.6 million, or 1.3%, in the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017. The decrease in profit before corporate SG&A is primarily due to higher disposal and disposal freight costs and the addition of sales and service resources partially offset by the increase in revenue for the first three quarters of fiscal 2018 compared to fiscal 2017.

Oil Business profit before corporate SG&A expense increased \$3.0 million in the third quarter of fiscal 2018 compared to the third quarter of fiscal 2017. Oil Business profit before corporate SG&A expense increased \$2.2 million in the first three quarters of fiscal 2018, compared to the first three quarters of fiscal 2017. The improvement of profit before corporate SG&A expense was mainly due to higher revenues as a result of higher product prices, improved oil collection route efficiency, and lower maintenance cost due to a shutdown occurring during the third quarter of fiscal 2017 with no shutdown during the third quarter of fiscal 2018.

## FINANCIAL CONDITION

### Liquidity and Capital Resources

#### Cash and Cash Equivalents

As of September 8, 2018 and December 30, 2017, cash and cash equivalents were \$46.3 million and \$41.9 million, respectively. Our primary sources of liquidity are cash flows from operations and funds available to borrow under our term loan and revolving bank credit facility.

#### Debt and Financing Arrangements

The Company's Credit Agreement as amended ("Credit Agreement"), provides for borrowings of up to \$95.0 million, subject to the satisfaction of certain terms and conditions, comprised of a term loan of \$30.0 million and up to \$65.0 million of borrowings under the revolving loan portion. The actual amount available under the revolving loan portion of the Credit Agreement is limited by the Company's total leverage ratio. The amount available to draw at any point in time would be further reduced by any standby letters of credit issued.

Loans made under the Credit Agreement may be Base Rate Loans or LIBOR Rate Loans, at the election of the Company subject to certain exceptions. Base Rate Loans have an interest rate equal to (i) the higher of (a) the federal funds rate plus 0.5%, (b) the London Interbank Offering Rate ("LIBOR") plus 1%, or (c) Bank of America's prime rate, plus (ii) a variable margin of between 0.75% and 1.75% depending on the Company's total leverage ratio, calculated on a consolidated basis. LIBOR rate loans have an interest rate equal to (i) the LIBOR rate plus (ii) a variable margin of between 1.75% and 2.75% depending on the Company's total leverage ratio. Amounts borrowed under the Credit Agreement are secured by a security interest in substantially all of the Company's tangible and intangible assets. In June 2017, the Company entered into a First Amendment to the Credit Agreement that expands the Company's ability to make dispositions without bank group approval.

The Credit Agreement contains customary terms and provisions (including representations, covenants, and conditions) for transactions of this type. Certain covenants, among other things, restrict the Company's and its subsidiaries' ability to incur indebtedness, grant liens, make investments and sell assets. The Credit Agreement contains customary events of default, covenants and representations and warranties. Financial covenants include:

• An interest coverage ratio (based on interest expense and EBITDA) of at least 3.5 to 1.0;

A total leverage ratio no greater than 3.0 to 1.0, provided that in the event of a permitted acquisition having an aggregate consideration equal to \$10.0 million or more, at the Borrower's election, the total leverage ratio shall be deemed to be 3.25 to 1.00 for the fiscal quarter in which such permitted acquisition occurs and the three immediately following fiscal quarters and thereafter will revert to 3.00 to 1.00;

• A capital expenditures covenant limiting capital expenditures to \$100.0 million plus, if the capital expenditures permitted have been fully utilized, an additional amount for the remaining term of the Agreement equal to 35% of EBITDA for the thirteen "four-week" periods most recently ended immediately prior to the full utilization of such \$100.0 million basket.

As of September 8, 2018 and December 30, 2017, the Company was in compliance with all covenants under the Credit Agreement. As of September 8, 2018 and December 30, 2017, the Company had \$1.5 million and \$0.9 million of standby letters of credit issued, respectively, and \$63.5 million and \$64.1 million was available for borrowing under the bank credit facility, respectively. The actual amount available under the revolving loan portion of the Credit



Agreement is limited by the Company's total leverage ratio.

The Company's weighted average interest rate for all debt as of September 8, 2018 and September 9, 2017 was 3.8% and 3.6%, respectively. As of September 8, 2018, the Company had \$30.0 million outstanding under the term loan, and no amount outstanding under the revolving credit facility.

We believe that our existing cash, cash equivalents, available borrowings, and other sources of financings will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for at least the next 12 months. We cannot assure you that this will be the case or that our assumptions regarding revenues and expenses underlying this belief will be accurate. If, in the future, we require more liquidity than is available to us under our credit facility, we may need to raise additional funds through debt or equity offerings. Adequate funds may not be available when needed or may not be available on

terms favorable to us. If additional funds are raised by issuing equity securities, dilution to existing stockholders may result. If we raise additional funds by obtaining loans from third parties, the terms of those financing arrangements may include negative covenants or other restrictions on our business that could impair our operational flexibility, and would also require us to fund additional interest expense. If funding is insufficient at any time in the future, we may be unable to develop or enhance our products or services, take advantage of business opportunities, or respond to competitive pressures, any of which could have a material adverse effect on our business, financial condition and results of operations.

#### Summary of Cash Flow Activity

| (thousands)  | For the First Three<br>Quarters Ended, |                      |
|--|--|----------------------|
|  | September<br>2018                      | September 9,<br>2017 |
| Net cash provided by (used in):                      |  |                      |
| Operating activities                                 | \$23,002                               | \$ 32,373            |
| Investing activities                                 | (17,599 )                              | (5,336 )             |
| Financing activities                                 | (977 )                                 | (30,195 )            |
| Net increase (decrease) in cash and cash equivalents | \$4,426                                | \$ (3,158 )          |

The most significant items affecting the comparison of our operating activities for the first three quarters of fiscal 2018 and the first three quarters of fiscal 2017 are summarized below:

#### Net Cash Provided by Operating Activities —

**Earnings** — Our decrease in net income for the first three quarters of fiscal 2018 negatively impacted our net cash provided by operating activities by \$4.1 million compared to the first three quarters fiscal 2017.

**Accounts Receivable** — The increase in accounts receivable had an unfavorable impact on cash provided by operating activities of \$6.3 million in the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017 mainly due to higher sales in the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017, along with a one-time receipt of \$4.3 million related to a settlement agreement with the sellers of FCC Environmental in the first quarter of 2017.

**Accounts Payable** — The increase in accounts payable favorably affected cash flows from operating activities by \$9.4 million in the first three quarters of fiscal 2018 compared to the first three quarters of fiscal 2017. The increase in accounts payable was mainly driven by an increase in higher transportation and disposal cost related charges during the first three quarters of fiscal 2018.

**Inventory** — In the first three quarters of fiscal 2018, the increase in inventory unfavorably affected cash flows from operating activities by \$5.5 million compared to the first three quarters of fiscal 2017 driven mainly by higher carrying value of inventory.

#### Net Cash Used in Investing Activities —

**Capital expenditures** — We used \$12.9 million and \$9.5 million for capital expenditures during the first three quarters of fiscal 2018 and the first three quarters of fiscal 2017, respectively. During the first three quarters of fiscal 2018 and the first three quarters of fiscal 2017, we spent \$4.9 million for capital improvements to the re-refinery. Additionally,

in the first three quarters of fiscal 2018, we spent approximately \$3.5 million for purchases of parts cleaning machines compared to \$3.1 million in the first three quarters of fiscal 2017. The remaining \$4.5 million of capital expenditures in the first three quarters of fiscal 2018 included \$2.0 million of IT related projects and \$2.5 million on other various items compared to approximately \$2.4 million spent in the first three quarters of fiscal 2017 for other items.

Business acquisitions, net of cash acquired — We used \$4.8 million of cash outflows for the acquisitions of Products Plus, Inc. and AO Holding-Kansas City, LLC, and Hot Tank Supply Company in fiscal 2018. See footnote 3 — Business Combinations. We did not make any acquisitions during the first three quarters of fiscal 2017.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to interest rate risks primarily through borrowings under our bank Credit Facility. Interest on this facility is based upon variable interest rates. Our weighted average borrowings under our Credit Facility during the first three quarters of fiscal 2018 was \$30.0 million, and the annual effective interest rate for the Credit Facility for the first three quarters of fiscal 2018 was 3.8%. We currently do not hedge against interest rate risk. Based on the foregoing, a hypothetical 1% increase or decrease in interest rates would have resulted in a change of \$0.3 million to our interest expense in the first three quarters of fiscal 2018.

### ITEM 4. CONTROLS AND PROCEDURES

The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by this report, that the Company's disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) and 15d-15(e)) are effective to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's 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 financial disclosures.

#### Changes in Internal Control Over Financial Reporting

There have been no changes in the Company's internal control over financial reporting during the quarter ended September 8, 2018 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II

ITEM 1. LEGAL PROCEEDINGS

In February 2016 the Company received an information request from the U.S. EPA ("EPA") regarding the operation of our Indianapolis, Indiana re-refinery in relation to our Clean Air Act permit for the facility. During 2016 we responded fully to the EPA's information request. On April 7, 2017 we received a notice of violation and finding of violation of the Clean Air Act related to our operation of the re-refinery. We continue to cooperate with the EPA in order to address the notice and finding of violation. No liability was accrued as of the end the third quarter of fiscal 2018 related to this situation.

In October 2016, the United States Environmental Protection Agency ("USEPA") issued a Notice of Intent to file an administrative complaint against the Company for certain alleged violations of the Emergency Planning and Community Right to Know Act ("EPCRA") and regulations under the Clean Water Act (involving Spill Prevention, Control and Countermeasure plans). We have reached a settlement with USEPA involving the alleged EPCRA violations for an immaterial amount. We expect the settlement to be executed by the end of 2018. We are also providing USEPA additional information it has requested with regard to the alleged Clean Water Act matter and expect to have this matter resolved by the end of 2018.

In March 2017, the Delaware Department of Natural Resources and Environmental Control (DNREC) issued a Cease and Desist Order (Order) related to the Company's activities at our facility located in Wilmington, DE ("Facility") which we acquired as part of our acquisition of FCC Environmental and International Petroleum Corporation . We satisfied the terms of the Order and signed a settlement agreement with DNREC in the third quarter which includes a \$350,000 payment to settle the Order and all known disputes occurring on or before March 23, 2018 at the Facility. We fully accrued the cost of the above payment prior to the third quarter of fiscal 2018.

The Company is currently defending a putative class action lawsuit, Adelphia, Inc. d/b/a/ Village Auto and Dan's One Stop Shop, LLC v. Heritage-Crystal Clean, Inc. and Heritage-Crystal Clean, LLC, Case No. 15-L-386, in the Circuit Court for the Sixteenth Judicial Circuit in Kane County, Illinois, alleging that the Company charged fees in violation of both its contracts and applicable state laws. The case involves claims brought under the Illinois Consumer Fraud and Deceptive Business Practices Act, 815 ILCS 505/1 et seq., as well as claims for breach of contract and unjust enrichment. The case has been brought as a putative class action on behalf of all customers of HCC who entered into a written contract and have paid a fuel surcharge from 2005 to present. The Circuit Court granted Plaintiffs' request for class certification on August 28, 2018. We have petitioned the Illinois Court of Appeals for an interlocutory appeal of this order. As of September 9, 2018, no liability was accrued related to this lawsuit.

On August 2, 2018, we received a request for information from the Indiana Department of Environmental Management ("IDEM") seeking information related to the past and present use of our site located in Franklin, IN. We are cooperating with IDEM by providing the requested information.

ITEM 6. EXHIBITS

- 10.1 First Amendment to the Credit Agreement
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 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
- 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
- 101.INS\* XBRL Instance Document
- 101.SCH\* XBRL Taxonomy Extension Schema Document
- 101.CAL\* XBRL Taxonomy Extension Calculation Linkbase Document
- 101.LAB\* XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE\* XBRL Taxonomy Extension Presentation Linkbase Document
- 101.DEF\* XBRL Taxonomy Extension Definition Linkbase Document

\*In accordance with Regulation S-T, the XBRL-related information in Exhibits 101 to this Quarterly Report on Form 10-Q shall be deemed to be "furnished" and not "filed."

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

HERITAGE-CRYSTAL CLEAN, INC.

Date: October 18, 2018 By: /s/ Mark DeVita

Mark DeVita  
Chief Financial Officer