

Heritage-Crystal Clean, Inc.
Form 10-K
March 06, 2019

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

FORM 10-K

(Mark One)

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

For the fiscal year
ended December 29,
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

Securities registered pursuant to Section 12(b) of the Securities Exchange Act of 1934:

Edgar Filing: Heritage-Crystal Clean, Inc. - Form 10-K

Title of Class	Name of each exchange on which registered
Common Stock, \$0.01 par value	NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Securities Exchange Act of 1934:

None

1

Edgar Filing: Heritage-Crystal Clean, Inc. - Form 10-K

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

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

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

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

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Emerging growth Company

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

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

On June 15, 2018 (the last business day of the registrant's most recently completed second fiscal quarter), the aggregate market value of the common stock of the registrant held by non-affiliates of the registrant was approximately \$276.6 million, based on the closing price of such common stock as of that date on the NASDAQ Global Select Market.

On March 1, 2019, there were outstanding 23,118,007 shares of Common Stock, \$0.01 par value, of Heritage-Crystal Clean, Inc.

Table of Contents

PART I

<u>ITEM 1. BUSINESS</u>	<u>4</u>
<u>ITEM 1A. RISK FACTORS</u>	<u>16</u>
<u>ITEM 1B. UNRESOLVED STAFF COMMENTS</u>	<u>28</u>
<u>ITEM 2. PROPERTIES</u>	<u>28</u>
<u>ITEM 3. LEGAL PROCEEDINGS</u>	<u>29</u>
<u>ITEM 4. MINE SAFETY DISCLOSURES</u>	<u>29</u>

PART II

<u>ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	<u>30</u>
<u>ITEM 6. SELECTED FINANCIAL DATA</u>	<u>31</u>
<u>ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	<u>33</u>
<u>ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	<u>45</u>
<u>ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	<u>46</u>
<u>ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>	<u>82</u>
<u>ITEM 9 A. CONTROL AND PROCEDURES</u>	<u>82</u>
<u>ITEM 9 B. OTHER INFORMATION</u>	<u>82</u>

PART III

<u>ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE</u>	<u>83</u>
<u>ITEM 11. EXECUTIVE COMPENSATION</u>	<u>83</u>
<u>ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	<u>83</u>
<u>ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE</u>	<u>84</u>
<u>ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES</u>	<u>84</u>

PART IV

<u>ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES</u>	<u>84</u>
<u>SIGNATURES</u>	<u>86</u>

Disclosure Regarding Forward-Looking Statements

In addition to historical information, this annual report contains forward-looking statements that are based on current management expectations and that involve substantial risks and uncertainties, which could cause actual results to differ materially from the results expressed in, or implied by, these forward-looking statements. 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,” “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.

The factors listed under “Risk Factors,” as well as any cautionary language in this annual report, provide examples of risks, uncertainties, and events that may cause our actual results to differ materially from the expectations or estimates we describe in our forward-looking statements. Although we believe that our expectations are based on reasonable assumptions, actual results may differ materially from those in the forward-looking statements as a result of various factors, including, but not limited to, those described under the heading “Risk Factors” and elsewhere in this annual report.

Forward-looking statements speak only as of the date of this annual report. We do not have any intention, and do not undertake, to update any forward-looking statements. As a result of these risks and uncertainties, readers are cautioned not to place undue reliance on the forward-looking statements included in this annual 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.

PART I

ITEM 1. BUSINESS

Overview

Heritage-Crystal Clean, LLC (herein collectively referred to as “we,” “us,” “our,” “HCC” or “the Company”) is a wholly owned subsidiary of Heritage-Crystal Clean, Inc. (herein referred to as “HCCI”). HCC provides full-service parts cleaning, containerized waste management, used oil collection, vacuum truck services, antifreeze recycling, field services, and owns and operates a used oil re-refinery. We believe that we are the second largest provider of full-service parts cleaning, hazardous and non-hazardous waste services and used oil collection services to small and mid-sized customers in both the industrial and vehicle maintenance sectors in North America, and we are the second largest used oil re-refiner by capacity in North America. We operate our business through our Environmental Services and Oil Business segments.

Environmental Services Segment

Our Environmental Services segment consists of our full-service parts cleaning, containerized waste management, vacuum truck, antifreeze, and field services. These services allow our customers to outsource their handling and disposal of parts cleaning solvents as well as other hazardous and non-hazardous waste. Many of these substances are subject to extensive and complex regulations, and mismanagement can result in citations, penalties, and substantial direct costs both to the service provider and to the generator. We allow our customers to focus more on their core business and devote fewer resources to industrial and hazardous waste management and its related administrative burdens.

We have adopted innovative approaches in our Environmental Services segment to minimize the regulatory burdens for our customers and have made “ease of use” of our services and products a priority. Our company has pioneered a program whereby our customers' used parts cleaning solvent may be excluded from the U.S. Environmental Protection Agency's ("EPA") definition of hazardous waste. These two programs not only simplify the management of used solvent generated by our customers, but also reduce the total volume of hazardous waste generated at many of our customers' locations. This can allow the customer to achieve a lower “generator status” with the EPA and thereby reduce their overall regulatory burden, including reduced reporting obligations and inspections.

Our focus on providing ease of use for our customers is also part of our containerized waste management, vacuum services, antifreeze services, and field services offerings. As part of our containerized waste and vacuum service programs, we assist our customers in identifying and characterizing their regulated wastes as well as providing the proper labeling and shipping documentation for their regulated materials. Our antifreeze recycling service offers our customers a fully-compliant

method to safely manage their used antifreeze while providing a high quality, environmentally friendly, remanufactured product which allows them to further their sustainability goals. Similarly, our field services allow our customers to focus on their core business activities while we manage non-core activities such as tank cleanings and spill clean-up.

Oil Business Segment

The Oil Business segment consists of used oil collection activities, re-refining activities, oil filter removal and disposal services, and the sale of recycled fuel oil. Through our re-refining process, we recycle used oil into high quality lubricant base oil and other products, and we are a supplier to firms that produce and market finished lubricants. We operate a used oil re-refinery with an annual nameplate capacity of 75 million gallons. We are currently feeding the re-refinery with a combination of used oil collected from our customers and used oil that we purchase from third parties.

Industry

We operate within markets for industrial and hazardous waste services in the U.S. and a portion of Ontario, Canada. Specifically, we focus on the parts cleaning, containerized waste management, used oil collection and re-refining, vacuum truck services, antifreeze recycling, and field services areas of the industrial and hazardous waste services markets mainly for small to mid-sized establishments. These establishments have a need to remove grease and dirt from machine and engine parts and include businesses involved in vehicle maintenance operations, such as car dealerships, automotive repair shops, and trucking firms, as well as small manufacturers, such as metal product fabricators and printers. These businesses also generate waste materials such as used oil, waste paint, or antifreeze that generally cannot be legally discarded as municipal trash or poured down standard drains.

Environmental Services Segment

Parts cleaning machines and the related cleaning chemicals and solutions are used by operators and maintenance personnel in industrial plants and technicians in automotive service locations to clean dirty machine parts. Through use, the cleaning chemicals and solutions become contaminated with oil and sediment and must be replaced regularly. This replacement of used cleaning chemicals and solutions is subject to environmental regulations prohibiting disposal with municipal trash or by pouring down drains. Vehicle maintenance facilities as well as small to medium sized industrial businesses generate other regulated materials which may not be legally disposed of in the municipal trash or poured down drains, such as used oil, waste paint, antifreeze, used oil filters, discarded fluorescent light tubes, spent batteries, etc. Because the management of these wastes is subject to changing regulatory requirements, most businesses need specialized knowledge to prepare required paperwork, maintain records, and ensure compliance with environmental laws. Large businesses, which generate substantial volumes of industrial and hazardous wastes, may find it more efficient to employ highly trained employees to manage these wastes. Small and mid-sized businesses that generate lesser quantities of waste often cannot justify such personnel investments and typically prefer to outsource these services to providers that can assist them in their disposal of used cleaning chemicals and solutions as well as other wastes subject to environmental regulations.

Oil Business Segment

Through our used oil collection services, we compete in the used oil collection market. Automotive shops generate used oil as a result of performing oil changes on passenger cars and trucks. Industrial plants also generate used oil,

often as a result of changing lubricants used in heavy machinery. Environmental regulations prohibit the disposal of used oil into sewers or landfills, so most commercial generators arrange to have their used oil picked up periodically by a used oil collector.

Since fiscal 2012, we have produced and sold lubricating base oil from our re-refinery. Most lubricating base oil is produced at refineries that process crude oil, and lubricating base oil is just one of the many products of the refining process along with gasoline, diesel fuel, jet fuel, asphalt, and other hydrocarbon products. Major refining companies such as Chevron, ExxonMobil, and Motiva produce a significant share of the total U.S. base oil output. These refiners who produce base oil from crude oil, typically set the market price for base oil and re-refiners such as HCC, who produce base oil from used oil, are price takers. Some of the major refining companies use base oil to produce their own branded lubricant products and also sell some of their produced material to other firms that focus on the blending and packaging of lubricants. The market price of base oil is primarily driven by the market price of crude oil feedstock and the balance between the supply and demand for base oil.

As of December 29, 2018, we operated 12 oil processing operations. Certain locations remove excess water from the used oil and separate oil from oily water mixtures using thermal treatment, gravity separation, and mechanical filtration. The finished product from this process is called Recycled Fuel Oil ("RFO"). The RFO we produce is sold to industrial burners and

used oil processors, such as Vacuum Gas Oil ("VGO") producers and used oil re-refiners, or sold as a blend or cutter stock. We also operate four commercial wastewater treatment operations that service our Environmental Services segment. These facilities allow us to remove oil from wastewater, treat the wastewater, and then discharge it according to the standards in the applicable discharge permits. Some of the oil removed in the wastewater treatment process may become RFO.

The Crystal Clean Solution

Through our network of 89 branches, as of December 29, 2018, we provided parts cleaning, used oil collection, industrial waste removal, vacuum services, antifreeze recycling services, and field services to over 90,000 active customer locations.

Environmental Services Segment

During fiscal 2018, we performed more than 615,000 environmental services, of which over 305,000 were parts cleaning services. We believe our services are highly attractive to our customers, who value features such as assistance in preparing waste manifests and drum labels, regularly-scheduled service visits to check inventories and remove accumulated waste, and minimizing the number of vendors they must deal with related to the management of these materials. Our focus is to meet the service requirements of small and mid-sized clients, which we define as firms that generally spend less than \$50,000 per year on industrial and hazardous waste services. Small and mid-sized clients have needs that are often highly differentiated from the needs of larger accounts. We believe that our company is structured to meet these particular needs. Revenues in our Environmental Services segment accounted for approximately 66% of our revenues for fiscal 2018 and are generated primarily from providing parts cleaning services, industrial waste removal, and vacuum services for our clients.

Oil Business Segment

Through our used oil collection service, we collect the used oil generated by our customers when they replace used lubricating oil in vehicles and machinery. Most customers store used oil they generate in tanks, which must be emptied regularly to mitigate the risk of overflow or termination of their oil change activities. As a result, these customers have a strong need for timely used oil service. We have designed our services to deliver regularly-scheduled pickups, as well as the capability to respond to unscheduled requests on short notice. The used oil we collect is either transported to our used oil re-refinery or processed into RFO. When we re-refine or recycle their used oil, we are able to provide our customers with the satisfaction that their used oil is re-refined into high quality lubricants, using the approach cited as preferred by the EPA, or recycled by being used in the production of RFO.

We operate our used oil re-refinery in Indianapolis, Indiana where we re-refine used oil, collected from our customers or purchased from other oil collection service providers, into lubricating base oil that we sell to firms who then blend, package, and market finished lubricants. The nameplate capacity is 75 million gallons of annual input of used oil feedstock including the impact of periodic shutdowns to perform routine maintenance. In fiscal 2018, we collected over 64 million gallons of used oil from our customers. Revenues in our Oil Business segment accounted for approximately 34% of our total revenues in fiscal 2018.

Services

Across our full range of services, we focus on reducing our customers' burdens associated with their generation of hazardous and non-hazardous wastes. Many of these wastes are subject to extensive and complex regulations, and

mismanagement can result in citations, penalties, and substantial direct costs, both to the service provider and the generator. Many customers are familiar with “Superfund liability” and the possibility that they will be required to pay for future cleanups if their waste is mismanaged in a way that leads to environmental damage. Our services allow customers to focus more on their core business and devote fewer resources to industrial and hazardous waste management. A majority of our customers use a combination of our parts cleaning, waste management, and/or used oil collection services which are offered at most of our branches.

Environmental Services Segment

In our full-service parts cleaning business, we provide customers with parts cleaning equipment and chemicals to remove oil, grease, and other contaminants from engine parts and machine parts. Most commonly, we provide a parts cleaning machine that contains either a petroleum or aqueous-based solvent in a reservoir. The customer activates a pump that circulates the cleaning solvent through a nozzle where it is used to enable our customers to remove contaminants from their parts. The solvent can be reused until the contamination level is too high to allow for proper cleaning and requires replacement. We

typically visit our customers every 4 to 12 weeks to remove the used solvent and replace it with clean solvent, while at the same time cleaning and inspecting the parts cleaning equipment to ensure that it is functioning properly and assisting our customers with relevant regulatory paperwork. We believe there are still quite a few parts cleaning services performed in the U.S. which are structured as hazardous waste services, meaning that when the solvent has been used, it is managed as a regulated hazardous waste subject to numerous laws and regulatory filings. We reduce this burden for our customers by offering three alternative parts cleaning programs (our non-hazardous and reuse programs for mineral spirits parts cleaning and our aqueous parts cleaning program) that do not subject the customer to the same hazardous waste regulations. These low-burden approaches help certain customers to achieve regulatory compliance while minimizing the paperwork and bureaucracy associated with hazardous waste management - ultimately saving them time and money. For example, these programs currently enable many of our customers to reduce their generation of hazardous wastes below the 220 pounds per month maximum threshold for retaining the EPA generator status of Very Small Quantity Generator ("VSQG"). For our customers, maintaining a VSQG status provides significant savings associated with not having to maintain an EPA identification number; prepare, track, and file transportation manifests; or produce other reports related to the use, storage, and disposal of used solvents. We offer a wide variety of different models of parts cleaning machines from which our customers may choose the machine that best fits their specific parts cleaning needs. While the majority of our customers are provided or sold machines directly from us, we also offer parts cleaning services for customers who purchase their parts cleaning machines from other sources. We offer a variety of petroleum solvents and aqueous chemicals for use in parts cleaning machines. We also have a wide range of service schedules from weekly service visits to triannual service visits.

In our containerized waste services, we collect drums, pails, boxes, and other containers of hazardous and non-hazardous waste materials from our customers. Typical wastes from vehicle maintenance include used antifreeze, used oil filters, waste paint, and used absorbent material. Typical wastes from manufacturing operations include waste paint and solvents, oily water wastes, used absorbents, and discarded fluorescent lighting tubes. We endeavor to find the lowest burden regulatory approach for managing each of these materials for our clients. In some cases, we can develop lower burden alternatives based on recycling materials for component recovery, such as with oil filters, or by following the less onerous universal waste regulations, such as with fluorescent tubes and waste paint. In other cases, the hazardous waste regulations may apply, in which case we assist customers with the complete hazardous waste disposal process, including performing analysis to characterize their waste, preparing manifests and drum labels, and selecting the appropriate destination facility. As part of our full-service approach, we visit our customers periodically to check their inventory of used or waste materials and remove full containers as appropriate. Because there are statutory limits on the amount of time that customers can store these waste materials, these service visits are valuable to help customers stay in compliance. To the extent that we can coordinate these service visits together with a regularly scheduled parts cleaning service, we are able to perform both tasks during the same visit, with the same truck and service employee.

In a majority of our branch locations, we provide vacuum truck services for the removal of mixtures of oil, water, and sediment from wastewater pretreatment devices and other sources. Many shops and plants have floor drain systems that lead to pits, sumps, or separators that are designed to separate and retain oil and dirt, but allow clear water to flow out to a municipal sewer. Periodically, these drains and collection points accumulate excess oil or sediment needing removal. Because some of the material is very thick, a specialized vacuum truck is utilized for efficient removal of the material. Our vacuum truck service includes the removal of the oil, water, and sediment so that the customer's equipment operates as intended. We also offer bulk oily water removal. These services are scheduled on a regular basis. We currently offer vacuum truck service at 60 of our branches. We believe we have the opportunity to grow this business by adding vacuum truck service to almost all of our remaining branches. We operate four commercial wastewater treatment facilities that allow us to remove oil from wastewater, treat the wastewater, and discharge it according to the standards in the applicable discharge permits.

Through our antifreeze recycling service, we offer customers a legally-compliant method to safely manage their used antifreeze while providing a high quality, environmentally friendly, remanufactured product. We offer responsive, on-time scheduled or on-demand collection and transportation of used antifreeze to our six antifreeze recycling facilities, where it is recycled into high quality clean antifreeze. We then sell a variety of formulations of this antifreeze to our vehicle maintenance customers.

We also offer a variety of field services to assist customers with on-site equipment cleaning and the removal and proper management of various types of waste. Typical projects include lab pack services, soil remediation services, the cleaning of above ground storage tanks, sumps, separators, ship-to-shore fluid transfers, and other environmental remediation services. We typically serve as a contractor and engage contract labor or outsourced labor to provide our field services.

Oil Business Segment

As of the end of fiscal year 2018, we offered bulk used oil collection services in 81 of our branch locations. Although we manage some used oil through our containerized waste program, most customers who generate used oil (typically from vehicle engine oil changes) produce large quantities that are stored in bulk tanks. These volumes are handled more efficiently via bulk tank trucks, such as the type we utilize, where we pump the customer's material into our tank truck for proper handling. We transfer a majority of the used oil we collect to our re-refinery to be recycled into lubricating base oil. We recycle the remaining used oil into RFO, some of which is sold to industrial burners, such as asphalt plants that use the RFO as a less expensive substitute for other fuels, and some of which is sold to used oil processors such as VGO producers and used oil re-refiners and some of it is sold for use as blend or cutter stock. As with our other services, we offer to visit customers on a regularly scheduled basis to arrange for the removal of their accumulated oil.

Competitive Strengths

We believe that we are the second largest provider of full-service parts cleaning services and used oil collection services in the U.S., and a leading provider of containerized waste and antifreeze recycling services to small and medium sized customers. From our base of 89 branch locations, we employ an organized and disciplined approach to increasing our market share by taking advantage of the following competitive strengths:

Excellent Customer Service. Since our founding, we have followed a standardized, sales-oriented approach to our customers across our branch network. Our branch personnel are focused on local sales and service delivery, and a significant portion of their compensation is linked to revenue growth and new business development. In order to achieve this revenue growth, our personnel understand that they must retain existing business, which is best achieved by providing a very high level of customer service which can lead to cross-selling opportunities and referrals to new prospects. During fiscal 2018, approximately 97% of our Environmental Services revenues were generated from customers that we also served during fiscal 2017.

Cost-Efficient Branch Rollout Model. Our branch model allows us to consolidate operational and administrative functions not critical to sales and service at a regional hub, treatment or processing facility, or at our headquarters. This model has been the foundation for our new branch rollout as we have expanded from 14 branches in 1999, and we expect to extend this model to new locations. Furthermore, as we grow within each branch, we improve our route density, which is an important contribution to profitability in our business.

Large Branch Network. We have spent over nineteen years building and developing a large network of branches that has enabled us to rapidly grow our environmental services and used oil collection services efficiently and cost effectively. Our investments in this network help us to rapidly open new branches and cross sell products and services through existing branches.

Large and Highly Diverse Customer Base. Our focus on small and mid-sized businesses has enabled us to attract a variety of customers engaged in a wide range of industrial businesses (such as manufacturing, transportation and distribution) and vehicle service. This diversification helps insulate us from disruption caused by the possible loss of a single large account. Our customer base consists of approximately 90,000 active customer locations. In fiscal 2018, our largest single customer in our Environmental Services segment represented 1.3% of our consolidated revenues, and our largest ten customers represented approximately 4.7% of our consolidated revenues. In the Oil Business segment, revenues from our largest single customer accounted for 6.1% of our consolidated revenues for fiscal 2018, and our largest ten customers represented 19.7% of our consolidated revenues for fiscal 2018.

Experience in Re-Refining Technology. Our management team has substantial experience in the development and operation of used oil re-refineries and is able to design and construct re-refining capacity for a comparatively low capital cost due to this experience. In 2012, we began operating our re-refinery which had an original nameplate capacity of 50 million gallons of used oil. We were able to construct the original re-refining capacity for approximately \$54 million, or approximately \$1 per gallon of capacity. In 2015, we completed the re-refinery expansion from 50 million to 75 million gallons of annual capacity for approximately \$1 of capital cost per gallon of annual capacity. We believe other re-refineries recently constructed in the United States have had a capital cost of substantially more than \$1 per gallon of capacity.

Innovative Services that Reduce Customers' Regulatory Burdens. We have designed our service programs to meet the needs of our target customers. In particular, these customers desire to minimize their regulatory compliance burdens, and we

8

have developed innovative methods to help our customers achieve this objective. For example, we have created parts-cleaning service programs which exempt our customers from certain hazardous waste regulations and filing requirements:

Non-hazardous Program for Parts Cleaning. In our non-hazardous program for parts cleaning, we provide our customers with a solvent that is not included in the EPA's definition of hazardous waste due to its increased flashpoint, and we educate each participating customer to prevent harmful contaminants from being added to the solvent during use. Because of the reduced solvent flammability, as long as the customer does not add toxic or flammable contaminants during use, neither the clean solvent that we supply nor the resulting used solvent generated by customers participating in the program is classified as hazardous waste by the EPA, and as a result can be managed as non-hazardous waste. To participate in this program, our customers must provide certification that no hazardous wastes have been added to the parts cleaning solvent. After we collect the used solvent from customers participating in our non-hazardous program for parts cleaning, we recycle it via distillation for re-delivery to our parts cleaning customers. The recycling process removes oil, water, and other impurities, resulting in solvent suitable to be re-used by our customers for parts cleaning. At the same time, this process minimizes the burdensome hazardous waste regulations faced by our customers and allows us to minimize our virgin solvent purchases. Our solvent recycling system located in Indianapolis, Indiana is capable of recycling up to six million gallons per year of used solvent generated by customers participating in our non-hazardous program. This provides adequate capacity in excess of our current requirements.

Product Reuse Program for Parts Cleaning. Rather than managing used solvent as a waste, we have developed a program that uses the solvent as an ingredient in the manufacture of asphalt roofing materials. Used solvent generated by customers participating in our product reuse program for parts cleaning is sold as a direct substitute for virgin solvent that is otherwise used in the manufacturing process for asphalt roofing materials. Because the used solvent is destined for reuse, it is not deemed a waste, and therefore it is not subject to hazardous waste regulations. To enhance the marketing of these programs, in the past 20 plus years we and our predecessor, Heritage Environmental Services, have voluntarily obtained concurrence letters from more than 30 state environmental agencies to validate this approach.

Aqueous Program. In addition to our petroleum-based solvent, we offer a full suite of proprietary aqueous-based parts cleaning solutions, including our patented aqueous parts cleaning equipment and patented filtration technology for water-based fluids, which we believe is the most comprehensive aqueous-based solutions offering in the industry. After our customer is finished using the solution, we remove the used solution and almost exclusively manage it as non-hazardous waste. Similar to the two solvent-based programs described above, our customers' used cleaning material will not be included in the EPA's definition of a hazardous waste, which helps reduce our customers' regulatory burdens. In addition, our patented Aqua Filtration Unit provides our customers with an innovative method to remove contaminants from their water-based fluids.

Experienced Management Team. Our management team has substantial experience in the industry and possesses particular expertise in the small to mid-sized customer segment. As of December 29, 2018, our senior managers had on average more than 25 years of industry experience and our middle managers have on average more than 15 years of industry experience.

Growth Strategies

We intend to grow by providing environmental solutions that meet the needs of our customers. We have several different strategies to accomplish this which include:

Same-Branch Sales Growth. We seek to generate year-over-year growth in existing markets by obtaining new customers and by cross-selling multiple services to existing customers. Our sales and marketing strategy includes providing significant incentives to our field sales and service personnel to find and secure new business. These incentives include commission compensation for individuals and managers as well as prize awards and contests at the individual and team level. Our company culture is designed to consistently emphasize the importance of sales and service excellence and to build and maintain enthusiasm that supports continued sales success. Additionally, we intend to drive profitability by leveraging fixed costs against incremental sales growth at our existing branches.

Expanded Service Offerings. Of our 89 branches, all branches currently offer parts cleaning and containerized waste management services, 81 offer used oil collection services, and 60 offer vacuum truck services. As our business grows and we achieve sufficient market penetration, we have the opportunity to expand our used oil collection and vacuum truck services to each branch location. We also have other new business programs in various stages of development which have the potential to be offered through our branch locations in the future.

Geographic Expansion. We currently operate from 89 branch locations that offer all or portions of our service menu to customers in the vast majority of the United States, the District of Columbia, and parts of Ontario, Canada. We have historically been able to install new branches at a relatively low cost, although installation of branches in the Western U.S. is relatively more costly. Within the contiguous United States, we believe that there are opportunities to open more branches and provide convenient local service to additional markets.

Selectively Pursue Acquisition Opportunities. Our management team has significant experience in identifying and integrating acquisition targets. Given the number of small competitors in our business, there are generally multiple acquisition opportunities available to us at any given time. In fiscal 2016, we acquired the assets of Phoenix Environmental Services, Inc. and Recycled Engine Coolant, Inc. in order to expand our operations into the Pacific Northwest and to increase our used antifreeze recycling capabilities, respectively. In fiscal 2018, the Company purchased the assets of Products Plus, Inc. and AO Holding Company-Kansas City, LLC to expand the Company's market share in the collection, recycling, and sales of a full line of antifreeze products. We also purchased the assets of a small business based in Fresno, CA focused primarily on providing parts cleaning related services during 2018. In January 2019, we purchased the assets of the antifreeze collection and recycling business of GlyEco, Inc. to both increase our route density in our current service area and further expand our antifreeze business in other areas. On February 1, 2019, we completed the acquisition of certain assets of W. S. Supplies, Inc., a subsidiary of Merrill's Inc. W.S. Supplies, Inc., which provided chemical sales and service to auto dealerships and auto body-shops in Iowa, Nebraska, Minnesota, Missouri and South Dakota to expand geographically while potentially providing new services and products for this market. As the markets for some of our services mature, we will increasingly consider making acquisitions which are adjacent to the businesses we currently operate in. Specifically, we will explore opportunities to leverage our core strengths which include our branch network and our customer relationships. Our growth plan is not dependent on acquisitions, but we will continue to pursue acquisitions that leverage our established infrastructure.

Sales and Marketing

Our mission and culture emphasize sales and service excellence and entrepreneurship, and our sales philosophy starts with the principle of “sales through service.” We assign a territory to each of our Sales & Service Representatives (“SSRs”), and require and encourage them to grow their business on their routes by delivering excellent service to existing customers. This helps our SSRs retain business, sell more services to satisfied customers, and obtain valued referrals to potential new customers. In addition to the efforts of our SSRs, we employ a branch manager at each of our branches, and we also employ branch sales managers at approximately two-thirds of our branches, all of whom have dedicated sales territories and responsibilities.

Suppliers and Recycling/Disposal Facilities

We purchase goods such as parts cleaning machines, solvent (petroleum naphtha mineral spirits), cleaning chemicals, bulk used oil, bulk antifreeze (ethylene glycol) and used antifreeze, and absorbent from a limited group of suppliers. We also have arrangements with various firms that can recycle, burn, or dispose of the waste materials we collect from customers. These suppliers and disposal facilities are important to our business, and we have identified backup suppliers in the event that our current suppliers and disposal facilities cannot satisfy our supply or disposal needs. Heritage Environmental Services, an affiliate of The Heritage Group, Fred Fehsenfeld and the Fehsenfeld family trusts, which collectively beneficially owned 31.5% of our common stock as of December 29, 2018, operates one of the largest privately-owned hazardous waste treatment businesses in the U.S. We have used their hazardous waste services in the past, and it is likely that we will continue some level of use in the future.

We operate four commercial waste water treatment facilities. These facilities allow us to remove oil from wastewater, treat the waste water, and then discharge it according to the standards in the applicable discharge permits. These facilities allow us the flexibility to dispose of our oily water and vacuum services waste water collected from certain branches internally as well as accepting wastewater from our customers directly at most of these facilities.

Competition

The markets for parts cleaning, containerized waste management, used oil collection, vacuum truck services, antifreeze recycling, and field services in which we participate are intensely competitive. While numerous small companies provide these services, our largest competitor, Safety-Kleen (a wholly-owned subsidiary of Clean Harbors, Inc.), has held substantial market share in the full-service parts cleaning industry for the last five decades and has developed significant market share in used oil collection and containerized waste management. We believe that Safety-Kleen has greater financial and other resources and greater name recognition than us. We estimate that in the full-service portion of the parts cleaning market, Safety-Kleen is significantly larger than us, and that we are substantially larger than the next largest competitor.

Many of our smaller competitors tend to be regional firms or parts cleaning companies that operate in a single city. Although many of these smaller competitors lack the resources to offer clients a full menu of services, they generally offer parts cleaning services ancillary to a primary line of business, such as used oil collection, in order to present a more complete menu to customers. In addition, companies involved in the waste management industry, including waste hauling, separation, recovery, and recycling, may have the expertise, access to customers, and financial resources that would encourage them to develop and market services and products competitive with those offered by us. We also face competition from alternative services that provide similar benefits to our customers as those provided by us.

Price, service quality and timeliness, breadth of service offering, reputation, financial strength, and compliance history are the principal competitive factors in the markets in which we compete. While we feel that most market competitors compete primarily on price, we believe that our competitive strength comes from our focus on customer service and our broad menu of services. Although we employ a pricing structure that controls discounts, we are able to deliver a sound value proposition through the reduced regulatory burden achieved through our programs. We could lose a significant number of customers if Safety-Kleen or other competitors materially lower their prices, improve service quality, develop more competitive product and service offerings, or offer a non-hazardous, reuse or aqueous program for parts cleaning more appealing to customers than ours.

We have the second largest used oil re-refinery, by capacity, in North America. We believe that our largest competitor, Safety-Kleen, currently controls a majority of the used oil re-refining capacity in North America.

Seasonality

Our operations may be affected by seasonal fluctuations due to weather cycles influencing the timing of customers' need for products and services. Typically during the first quarter and the end of the fourth quarter of each year there is less demand

for most of our products and services due to the lower levels of activities by our customers as a result of the cold weather, particularly in the Northern and Midwestern regions of the United States. This lower level of activity also results in lower volumes of used oil generated for collection by us in the first quarter. In the winter months there is less construction activity, which reduces demand for certain re-refinery products. In addition, factory closings for the year-end holidays reduce the volume of industrial waste generated, which results in lower volumes of waste handled by us during the first quarter of the following year. However, we generally experience the opposite seasonality impact (higher levels of activity in the first quarter and end of the fourth quarter) in our antifreeze business.

Information Technology

We believe that automation and technology can enhance customer convenience, lower labor costs, improve cash management, and increase overall profitability. We are constantly evaluating opportunities to develop technologies that can improve our sales and service processes. Our commitment to the application of technology has resulted in the creation of a custom web-based application for scheduling, tracking, and management of customer services, billing, and collections. This system has been used as an integral part of our business operations since 2003. We believe that our standardized processes and controls enhance our ability to successfully add new branches and expand our operations into new markets. Mobile devices are used by our employees in the field to access customer service information, capture substantially all service transactions and certain inventory movements. Statistics are gathered and reported on a daily and weekly basis. These capabilities provide timely, automated data measurement and control for service activities to accelerate response to market and operational change.

Employees

As of December 29, 2018, we employed 1,270 full time and 68 part time employees. None of our employees are represented by a labor union or covered by a collective bargaining agreement. We believe that our employee relations are good.

Intellectual Property

We regard our intellectual property as important to our success and we rely on trademark, copyright, and other intellectual property laws in the United States to protect our proprietary rights. We have, in the past, successfully defended our patents against infringement, and we intend to continue to defend our intellectual property rights. In addition, we seek to protect our proprietary rights through the use of confidentiality agreements with employees, consultants, vendors, advisors, and others.

Our intellectual property includes the Crystal Clean brand and logo as well as our patented aqueous parts cleaning equipment, chemistry formulae, and filtration technology. Our patents expire at various times through 2034. Although we do not regard any single trade secret or component of our proprietary know-how to be material to our operations as a whole, if one or more of our competitors were to use or independently develop such know-how or trade secrets, our market share, sales volumes and profit margins could be adversely affected.

Regulation

Substantially all of our services and products involve the collection, transportation, storage, recycling and/or disposal of industrial and hazardous waste or hazardous materials, including solvents used in parts cleaners; containerized waste including waste paint, inks, adhesives, used antifreeze, used oil, and used oil filters; and bulk waste including used oil, oily water, and antifreeze. Our services are highly regulated by various governmental agencies at the federal, state, and local levels, as described in more detail below. Regulations govern matters such as the disposal of residual

chemical wastes, operating procedures, storm water and wastewater discharges, fire protection, worker and community right-to-know, and emergency response plans.

Our services and products require us to comply with these laws and regulations and to obtain federal, state, and local environmental permits or approvals for some of our operations. Some of these permits must be renewed periodically, and governmental authorities have the ability to revoke, deny, or modify these permits. Zoning and land use restrictions also apply to all of our facilities. Siting and other state-operating approvals also apply in some states.

We are subject to federal and state regulations governing hazardous and solid wastes. The Resource Conservation and Recovery Act ("RCRA") is the principal federal statute governing hazardous waste generation, treatment, transportation, storage, and disposal. Under RCRA, the EPA has established comprehensive "cradle-to-grave" regulations for the management of a wide range of materials identified as hazardous or solid waste. The regulations impose technical and operating requirements that must be met by facilities that generate, store, treat, transport, and dispose of these wastes. A number of states

have regulatory programs governing the operations and permitting of hazardous and solid waste facilities. In addition, some states classify some wastes as hazardous that are not regulated under RCRA. Accordingly, we must comply with the state requirements for handling state regulated wastes.

On June 30th, 2018 the EPA implemented an e-Manifest system for the capture of manifest documents electronically. This functionality included full electronic manifests, scanned image upload, scanned image plus document data, and mailing of physical manifests to the EPA for processing. The EPA assesses a different fee depending on which of the above approaches is used. Functionality for paper/electronic hybrid documents, and transporter/broker features have not been made available by the EPA. Expectations are this functionality will become available in the first half of 2019. EPA development may be materially impacted by the December 2018 government shutdown.

Disposal partners utilized by the Company are at various stages of implementation of the available features with partners passing their costs incurred to the Company. The Company has mailed physical manifests it terminates to the EPA for state regulated wastes which require manifesting. Once the EPA enables the broker and transporter functionality, this should enable intermediaries like the Company to implement more direct e-Manifest features into its handling and systems. The Company intends to pass along the direct costs imposed by the EPA, or indirectly from disposal partners, to its customers. As partners and the Company are able to implement costs saving measures provided by e-Manifesting, regulatory costs which are currently passed on to customers could be reduced.