Heritage-Crystal Clean, Inc.
Form 10-Q
October 20, 2016

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

FORM 10-Q
(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 10, 2016
OR
o 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 Incorporation	(I.R.S. Employer 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 x No o

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 x No o

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 o	Accelerated filer x
Non-accelerated filer o	Smaller reporting company o

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

On October 17, 2016, there were outstanding 22,410,470 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 10, 2016 (unaudited)	January 2, 2016
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 29,767	$ 23,608
Accounts receivable - net	47,370	41,592
Inventory - net	20,723	24,774
Other current assets	6,563	4,810
Total Current Assets	104,423	94,784
Property, plant and equipment - net	131,400	131,365
Equipment at customers - net	23,277	23,172
Software and intangible assets - net	20,786	22,202
Goodwill	31,510	30,325
Total Assets	$ 311,396	$ 301,848
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$ 31,612	$ 25,129
Current maturities of long-term debt	6,659	6,700
Accrued salaries, wages, and benefits	4,875	4,330
Taxes payable	7,209	6,735
Other current liabilities	3,965	3,617
Total Current Liabilities	54,320	46,511
Long term debt, less current maturities	59,917	62,778
Deferred income taxes	3,699	2,726
Total Liabilities	$ 117,936	$ 112,015
STOCKHOLDERS' EQUITY:		
Common stock - 26,000,000 shares authorized at $0.01 par value, 22,272,941 and 22,213,364 shares issued and outstanding at September 10, 2016 and January 2, 2016, respectively	$ 223	$ 222
Additional paid-in capital	183,788	182,558
Retained earnings	8,784	6,385
Total Heritage-Crystal Clean, Inc. Stockholders' Equity	192,795	189,165
Noncontrolling interest	665	668
Total Equity	$ 193,460	$ 189,833
Total Liabilities and Stockholders' Equity	$ 311,396	$ 301,848

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,		First Three Quarters Ended,	
	September 30, 2016	September 12, 2015	September 30, 2016	September 12, 2015
Revenues				
Product revenues	$27,182	$ 32,888	$75,582	$ 99,509
Service revenues	54,690	49,797	165,295	150,154
Total revenues	$81,872	$ 82,685	$240,877	$ 249,663
Operating expenses				
Operating costs	$61,695	$ 63,499	$187,654	$ 197,576
Selling, general, and administrative expenses	10,726	9,872	34,455	31,553
Depreciation and amortization	4,196	4,419	12,442	13,050
Other expense (income) - net	1,439	99	1,238	(153)
Operating income	3,816	4,796	5,088	7,637
Interest expense – net	463	404	1,432	1,366
Income before income taxes	3,353	4,392	3,656	6,271
Provision for income taxes	942	1,637	1,140	2,418
Net income	2,411	2,755	2,516	3,853
Income attributable to noncontrolling interest	76	46	117	115
Net income attributable to Heritage-Crystal Clean, Inc. common stockholders	$2,335	$ 2,709	$2,399	$ 3,738
Net income per share: basic	$0.10	$ 0.12	$0.11	$ 0.17
Net income per share: diluted	$0.10	$ 0.12	$0.11	$ 0.17
Number of weighted average shares outstanding: basic	22,267	22,153	22,246	22,136
Number of weighted average shares outstanding: diluted	22,550	22,438	22,417	22,405

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 Common	Additional Paid–in Capital	Retained Earnings	Total Heritage-Crystal Clean, Inc. Stockholders' Equity	Noncontrolling Interest	Total Equity
Balance at January 2, 2016	22,213,364	$ 222	$ 182,558	$ 6,385	$ 189,165	$ 668	$ 189,833
Net income	—	—	—	2,399	2,399	117	2,516
Distribution	—	—	—	—	—	(120)	(120)
Issuance of common stock – ESPP	32,036	1	324	—	325	—	325
Exercise of stock options	2,202	—	16	—	16		16
Share-based compensation	25,339	—	890	—	890	—	890
Balance at September 10, 2016	22,272,941	$ 223	$ 183,788	$ 8,784	$ 192,795	$ 665	$ 193,460

See accompanying notes to financial statements.

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

	For the First Three Quarters Ended,	
	September 30, 2016	September 12, 2015
Cash flows from Operating Activities:		
Net income	$2,516	$ 3,853
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	12,442	13,050
Non-cash inventory impairment	1,651	6,846
Bad debt provision	714	1,081
Share-based compensation	890	815
Deferred taxes	973	2,250
Amortization of deferred gain on lease conversion	(201)	(245)
Other, net	383	914
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	(6,131)	3,031
Decrease (increase) in inventory	2,428	(3,163)
(Increase) decrease in other current assets	(1,753)	3,403
Increase (decrease) increase in accounts payable	8,890	(11,106)
Increase (decrease) in accrued expenses	1,197	(3,704)
Cash provided by operating activities	$23,999	$ 17,025
Cash flows from Investing Activities:		
Capital expenditures	$(12,594)	$ (12,526)
Business acquisitions, net of cash acquired	(2,400)	—
Proceeds from the sale of property, plant, and equipment	$304	$ 106
Cash used in investing activities	$(14,690)	$ (12,420)
Cash flows from Financing Activities:		
Payments on term loan	$(3,371)	$ (5,303)
Payments of notes payable	—	(241)
Payments of contingent consideration	—	(95)
Proceeds from the issuance of common stock	341	345
Distributions to noncontrolling interest	(120)	(410)
Cash used in financing activities	$(3,150)	$ (5,704)
Net increase (decrease) in cash and cash equivalents	6,159	(1,099)
Cash and cash equivalents, beginning of period	23,608	21,555
Cash and cash equivalents, end of period	$29,767	$ 20,456
Supplemental disclosure of cash flow information:		
Income taxes paid	$315	$ 263
Cash paid for interest, net of capitalized interest of $100 and $439, respectively	1,473	1,161
Supplemental disclosure of non-cash information:		
Payables for construction in progress	$287	$ 1,026

See accompanying notes to financial statements.

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

September 10, 2016

(1) ORGANIZATION AND NATURE OF OPERATIONS

Heritage-Crystal Clean, Inc., a Delaware corporation and its subsidiaries (collectively the “Company”), provides parts cleaning and hazardous and non-hazardous waste services primarily to small and mid-sized customers in both the manufacturing and vehicle maintenance sectors. The Company's service programs include parts cleaning, containerized waste management, used oil collection, vacuum truck services, waste antifreeze collection and recycling, and field services. The Company also owns and operates a used oil re-refinery through which it recycles used oil into high quality base oil for lubricants as well as other re-refinery byproducts. The Company also has multiple locations where it dehydrates used oil to be sold as recycled fuel oil. The Company's locations are 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’s fiscal year ends on the Saturday closest to December 31. The most recent fiscal year ended on January 2, 2016. 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, antifreeze, and accessories; and service revenues include drum waste removal services, servicing of parts cleaning machines, vacuum truck services, field services, and other services. In the Company's Oil Business segment, product revenues include sales of re-refined base oil, byproducts, recycled fuel oil, and used oil; and service revenues include revenues from collecting used oil, collecting and recycling of oil filters and collecting and disposing of waste water. 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 January 2, 2016. There have been no material changes in these policies or their application.

Recently Issued Accounting Pronouncements
Accounting standards not yet adopted

Standard	Issuance Date	Description	Our Effective Date	Effect on the Financial Statements
ASU 2016-09 Compensation - Stock Compensation: Improvements to Employee Share-Based Payment Accounting. (Topic 718)	March 2016	This update addresses the simplification of accounting for employee share-based payment transactions as it pertains to income taxes, the classification of awards as equity or liabilities, accounting for forfeitures, statutory tax withholding requirements, and certain classifications on the statement of cash flows. Early adoption is permitted.	January 1, 2017	The Company is currently evaluating the effect that implementation of this update will have on its consolidated financial position and results of operations.
ASU 2016-02 Leases (Topic 842)	February 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.	January 4, 2019	The Company is currently evaluating the effect that implementation of this update will have on its consolidated financial position and results of operations.
ASU 2014-15 Presentation of Financial Statements - Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern. (Subtopic 205-40)	August 2014	This update provides guidance about management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. Early adoption is permitted.	December 31, 2016	The adoption of ASU 2014-15 is not expected to have an impact on the Company’s consolidated financial statements.
ASU 2014-09 Revenue from Contracts with Customers, and ASU 2015-14 Revenue from Contracts with Customers: Deferral of the Effective Date (Topic 606)	May 2014	The underlying principle of this update 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 or a modified approach to adopt the guidance. Early adoption is	December 31, 2017	This update could impact the timing and amounts of revenue recognized. The Company is currently evaluating the effect that implementation of this update will have on its consolidated financial position and results of operations upon adoption.

not permitted.

Recently issued accounting standards adopted

Standard	Issuance Date	Description	Effective Date	Effect on the Financial Statements
2015-03 Interest—Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs, and 2015-15 Interest—Imputation of Interest (Subtopic 835-30)	April 2015	These updates require debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying value of the associated debt, and allows for the presentation of debt issuance costs as an asset regardless of whether or not there is an outstanding balance on the line-of-credit arrangement.	January 3, 2016	The adoption of ASU 2015-03 resulted in the reclassification of $1.4 million of unamortized debt issuance costs from "Other current assets" to "Term loan, less current maturities" as of January 2, 2016.

(3) BUSINESS COMBINATIONS

On March 24, 2016, the Company purchased the assets of Phoenix Environmental Services, Inc. and Pipeline Video and Cleaning North Corporation (together "Phoenix Environmental"). The purchase price for the acquisition was $2.7 million, including $0.3 million placed into escrow and including contingent consideration of up to $0.3 million based on subsequent business performance.

The Company is continuing to evaluate the purchase price allocations. Preliminary purchase price allocations are tentative and subject to revision as the Company finalizes appraisals and other analyses. Measurement period adjustments reflect new information obtained about facts and circumstances that existed as of the acquisition date. Final determination of the fair values may result in further adjustments to the values presented. The Company believes that the preliminary allocations provide a reasonable basis for estimating the fair values of assets acquired based on the information available. The Phoenix Environmental purchase price allocation is preliminary as the Company is still in the process of obtaining information to finalize the purchase price, net cash paid, and estimated fair values of the assets presented below. The Company expects to finalize the purchase price allocation no later than one year from the purchase date.

The following table summarizes the estimated fair values of the assets acquired related to the acquisition:

(Thousands)	Phoenix Environmental Services
Accounts receivable	$ 361
Inventory	27
Property, plant, & equipment	374
Equipment at customers	55
Intangible assets	710
Goodwill[(a)]	1,173
Total purchase price	2,700
Less: contingent consideration	(300)
Net cash paid	$ 2,400

[(a)]Goodwill recognized from the acquisition of Phoenix Environmental represents the excess of the fair value of the net assets acquired over the purchase price, and is based upon the Company's expectations of synergies from combining the operations of Phoenix Environmental and the Company, and the value of intangible assets that are not separately recognized, such as the assembled workforce. All of the goodwill was assigned to the Environmental

Services reporting unit. All goodwill is expected to be deductible for income tax purposes.

Unaudited Pro Forma Financial Information

The pro forma financial information in the table below presents the combined results of the Company as if the Phoenix Environmental acquisition that occurred in fiscal 2016 had occurred January 3, 2015. The pro forma information is shown for illustrative purposes only and is not necessarily indicative of future results of operations of the Company or results of operations of the Company that would have actually occurred had the transactions been in effect for the period presented.

(In thousands, except per share data)	Third Quarter Ended, September 10, 2016	Third Quarter Ended September 12, 2015
Total revenues	$ 81,872	$ 83,600
Net income	2,335	2,892
Income per share		
Basic	$ 0.10	$ 0.13
Diluted	0.10	0.13

(In thousands, except per share data)	First Three Quarters Ended, September 10, 2016	First Three Quarters Ended, September 12, 2015
Total revenues	$ 241,602	$ 252,121
Net income	2,357	4,107
Income per share		
Basic	$ 0.11	$ 0.19
Diluted	0.11	0.18

(4) ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following:

(Thousands)	September 10, 2016	January 2, 2016
Trade	$ 42,597	$ 38,379
Less: allowance for doubtful accounts	2,394	2,207
Trade - net	40,203	36,172
Related parties	1,378	1,250
Other	5,789	4,170
Total accounts receivable - net	$ 47,370	$ 41,592

The following table provides the changes in the Company’s allowance for doubtful accounts for the three quarters ended September 10, 2016 and the fiscal year ended January 2, 2016:

(Thousands)	For the First Three Quarters Ended, September 10, 2016	For the Fiscal Year Ended, January 2, 2016
Balance at beginning of period	$ 2,207	$ 3,927
Balance acquired from FCC Environmental, including measurement period adjustments	—	2,701
Provision for bad debts	714	1,009
Accounts written off, net of recoveries	(527)	(5,430)
Balance at end of period	$ 2,394	$ 2,207

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(5) INVENTORY

The carrying value of inventory consisted of the following:

(Thousands)	September 10, 2016	January 2, 2016
Used oil and processed oil	$ 7,254	$ 9,045
Solvents and solutions	4,543	6,285
Machines	3,127	3,827
Drums and supplies	4,417	4,226
Other	1,630	1,681
Total inventory	20,971	25,064
Less: machine refurbishing reserve	248	290
Total inventory - net	$ 20,723	$ 24,774

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 market, net of any reserves for excess, obsolete, or unsalable inventory. The Company continually 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 third quarter of 2016, compared to a write down of $2.4 million in the third quarter of 2015. Total inventory write-downs for the first three quarters of fiscal 2016 and the first three quarters of fiscal 2015 were $1.7 million and $6.8 million, respectively. Write-downs in 2015 and the first half of fiscal 2016 pertain to used oil and processed oil inventory as well as solvents and solutions inventory.

(6) PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment consisted of the following:

(Thousands)	September 10, 2016	January 2, 2016
Machinery, vehicles, and equipment [(a)]	$ 77,775	$75,129
Buildings and storage tanks	69,723	69,317
Land	10,368	9,295
Leasehold improvements [(a)]	4,758	4,523
Construction in progress	7,076	4,474
Assets held for sale	178	189
Total property, plant and equipment	169,878	162,927
Less: accumulated depreciation	(38,478)	(31,562)
Property, plant and equipment - net	$ 131,400	$131,365

(Thousands)	September 10, 2016	January 2, 2016
Equipment at customers [(a)]	$ 62,380	$59,216
Less: accumulated depreciation	(39,103)	(36,044)
Equipment at customers - net	$ 23,277	$23,172

[(a)] Numbers include preliminary fair values of assets acquired in the acquisition described in Note 3 that may be adjusted as additional information becomes known.

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Depreciation expense for the third quarters ended September 10, 2016 and September 12, 2015 was $3.4 million and $3.7 million, respectively. Depreciation expense for the first three quarters ended September 10, 2016 and the first three quarters ended September 12, 2015 was $10.2 million and $11.1 million, respectively.

(7) 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, and the Company does not aggregate reporting units for purposes of impairment testing.

The following table shows changes to our goodwill balances by segment from January 2, 2016, to September 10, 2016:

(Thousands)	Oil Business	Environmental Services	Total
Balance at January 2, 2016	$ —	$ 30,325	$30,325
Phoenix Environmental acquisition	—	1,173	1,173
Adjustments	—	12	12
Balance at September 10, 2016	$ —	$ 31,510	$31,510

Following is a summary of software and other intangible assets:

	September 10, 2016			January 2, 2016		
(Thousands)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer & supplier relationships	$22,930	$ 5,927	$ 17,003	$22,202	$ 4,369	$ 17,833
Software	4,573	3,557	1,016	4,455	3,382	1,073
Non-compete agreements	2,939	2,043	896	2,930	1,713	1,217
Patents, formulae, and licenses	1,769	556	1,213	1,769	510	1,259
Other	1,348	690	658	1,354	534	820
Total software and intangible assets	$33,559	$ 12,773	$ 20,786	$32,710	$ 10,508	$ 22,202

Amortization expense was $0.7 million for the third quarter ended September 10, 2016 and $0.7 million for third quarter ended September 12, 2015. Amortization expense was $2.3 million for the first three quarters ended September 10, 2016 and $1.9 million for first three quarters ended September 12, 2015. The weighted average useful lives of software; customer & supplier relationships; patents, formulae, and licenses; non-compete agreements, and other intangibles were 9 years, 11 years, 15 years, 5 years, and 6 years, respectively.

The expected amortization expense for the remainder of fiscal 2016 and for fiscal years 2017, 2018, 2019, and 2020 is $1.0 million, $3.2 million, $2.9 million, $2.6 million, and $2.5 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, disposal of intangible assets, accelerated amortization of intangible assets, and other events.

(8) DEBT AND FINANCING ARRANGEMENTS

Bank Credit Facility

On October 16, 2014, the Company amended its Amended and Restated Credit Agreement ("Credit Agreement", or "Credit Facility"). The Credit Agreement, as amended, allows for up to $140.0 million in borrowings. As of September 10, 2016 and January 2, 2016, the Company's total borrowings were $67.5 million and $70.9 million, respectively, under the term loan which has a maturity date of February 5, 2018. The remaining portion of the Credit Facility is a revolving loan which expires on February 5, 2018. There were no amounts outstanding under the revolver at September 10, 2016 and January 2, 2016. Unamortized debt issuance costs were $0.9 million and $1.4 million as of September 10, 2016 and January 2, 2016, respectively.

During the third quarter of fiscal 2016, the Company recorded interest of $0.5 million on the term loan and capitalized less than $0.1 million for various capital projects. During the first three quarters of fiscal 2016, the Company recorded interest of $1.5 million on the term loan, of which less than $0.1 million was capitalized for various capital projects. During the third quarter of fiscal 2015, the Company recorded interest of $0.4 million on the term loan and capitalized $0.1 million for various capital projects. During the first three quarters of fiscal 2015, the Company recorded interest of $1.4 million on the term loan and capitalized $0.4 million for various capital projects.

As of September 10, 2016 and January 2, 2016, the Company was in compliance with all covenants under the Credit Agreement. As of September 10, 2016 and January 2, 2016, the Company had $3.0 million and $4.4 million of standby letters of credit issued, respectively, and $8.6 million and $34.5 million was available for borrowing under the Credit Facility. 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 10, 2016 and September 12, 2015 was 3.2% and 3.1%, respectively.

(9) SEGMENT INFORMATION

The Company reports in two 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 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.

Operating segment results for the third quarters and first three quarters ended September 10, 2016, and September 12, 2015 were as follows:

Third Quarter Ended,
September 10, 2016

(Thousands)	Environmental Services	Oil Business	Corporate and Eliminations	Consolidated
Revenues				
Product revenues	$ 4,691	$ 22,491	$ —	$ 27,182
Service revenues	46,591	8,099	—	54,690
Total revenues	$ 51,282	$ 30,590	$ —	$ 81,872
Operating expenses				
Operating costs	34,456	27,239	—	61,695
Operating depreciation and amortization	1,742	1,618	—	3,360
Profit before corporate selling, general, and administrative expenses	$ 15,084	$ 1,733	$ —	$ 16,817
Selling, general, and administrative expenses			10,726	10,726
Depreciation and amortization from SG&A			836	836
Total selling, general, and administrative expenses			$ 11,562	$ 11,562
Other expense - net			1,439	1,439
Operating income				3,816
Interest expense – net			463	463
Income before income taxes				$ 3,353

Third Quarter Ended,
September 12, 2015

(Thousands)	Environmental Services	Oil Business	Corporate and Eliminations	Consolidated
Revenues				
Product revenues	$ 4,923	$ 27,965	$ —	$ 32,888
Service revenues	47,199	2,598	—	49,797
Total revenues	$ 52,122	$ 30,563	$ —	$ 82,685
Operating expenses				
Operating costs	35,532	27,967	—	63,499
Operating depreciation and amortization	1,647	1,949	—	3,596
Profit before corporate selling, general, and administrative expenses	$ 14,943	$ 647	$ —	$ 15,590
Selling, general, and administrative expenses			9,872	9,872
Depreciation and amortization from SG&A			823	823
Total selling, general, and administrative expenses			$ 10,695	$ 10,695
Other expense - net			99	99
Operating income				4,796
Interest expense – net			404	404
Income before income taxes				$ 4,392

First Three Quarters Ended,
September 10, 2016

(Thousands)	Environmental Services	Oil Business	Corporate and Eliminations	Consolidated
Revenues				
Product revenues	$ 14,826	$ 60,756	$ —	$ 75,582
Service revenues	141,254	24,041	$ —	165,295
Total revenues	$ 156,080	$ 84,797	$ —	$ 240,877
Operating expenses				
Operating costs	106,892	80,762	—	187,654
Operating depreciation and amortization	5,166	4,789	—	9,955
Profit (loss) before corporate selling, general, and administrative expenses	$ 44,022	$ (754)	$ —	$ 43,268
Selling, general, and administrative expenses			34,455	34,455
Depreciation and amortization from SG&A			2,487	2,487
Total selling, general, and administrative expenses			$ 36,942	$ 36,942
Other expense - net			1,238	1,238
Operating income				5,088

Interest expense – net	1,432	1,432
Income before income taxes		$ 3,656

First Three Quarters Ended, September 12, 2015

(Thousands)	Environmental Services	Oil Business	Corporate and Eliminations	Consolidated
Revenues				
Product revenues	$ 15,634	$83,875	$ —	$ 99,509
Service revenues	142,344	7,810	—	150,154
Total revenues	$ 157,978	$91,685	$ —	$ 249,663
Operating expenses				
Operating costs	109,836	87,740	—	197,576
Operating depreciation and amortization	5,045	5,653	—	10,698
Profit (loss) before corporate selling, general, and administrative expenses	$ 43,097	$(1,708)	$ —	$ 41,389
Selling, general, and administrative expenses			31,553	31,553
Depreciation and amortization from SG&A			2,352	2,352
Total selling, general, and administrative expenses			$ 33,905	$ 33,905
Other (income) - net			(153)	(153)
Operating income				7,637
Interest expense – net			1,366	1,366
Income before income taxes				$ 6,271

Total assets by segment as of September 10, 2016 and January 2, 2016 were as follows:

(Thousands)	September 10, 2016	January 2, 2016
Total Assets:		
Environmental Services	$ 130,384	$133,718
Oil Business	137,377	132,556
Unallocated Corporate Assets	43,635	35,574
Total	$ 311,396	$301,848

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.

(10) 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 $7.8 million as of September 10, 2016, and $9.8 million as of January 2, 2016, 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 10, 2016 and January 2, 2016, the Company had accrued $5.4 million and $6.0 million related to loss contingencies and other contingent liabilities, respectively.

(11) INCOME TAXES

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 2015. Therefore, the Company recorded a noncurrent deferred tax liability to reflect 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") of $44.7 million, which will begin to expire in 2031. The NOL as of September 10, 2016 was $51.9 million, and the remaining deferred tax asset related to the Company’s state and federal NOL was a tax effected balance of $20.0 million.

The Company recognizes windfall tax benefits associated with the exercise of stock options directly to stockholders' equity only when realized. Consequently, deferred tax assets are not recognized for NOLs resulting from windfall tax benefits. At September 10, 2016, deferred tax assets do not include $2.5 million of excess tax benefits from share-based compensation.

The Company's effective tax rate for the third quarter of fiscal 2016 was 28.1% compared to 37.3% in the third quarter of fiscal 2015. The Company's effective tax rate for the first three quarters of fiscal 2016 was 31.2% compared to 38.6% in the first three quarters of fiscal 2015. The rate difference is principally attributable to the differing treatment for financial reporting and income tax reporting for certain income and expenditures items. The rate decrease attributable to expenditures reported net of anticipated reimbursement from an unrelated third party for financial reporting purposes, but deducted on a gross basis for income tax purposes, is partially offset by expenditures which are expensed for financial reporting purposes but not deductible for income tax purposes.

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 10, 2016 and January 2, 2016. The gross unrecognized tax benefits would, if recognized, decrease the Company's effective tax rate.

(12) SHARE-BASED COMPENSATION

The aggregate number of shares of common stock which may be issued under the Company's 2008 Omnibus Plan ("Plan") is 1,902,077 plus any common stock that becomes available for issuance pursuant to the reusage provision of the Plan. As of September 10, 2016, the number of shares available for issuance under the Plan was 553,970 shares.

Stock Option Awards

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

Outstanding Stock Options	Number of Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value as of Date Listed (in thousands)
Options outstanding at January 2, 2016	534,428	$ 10.97	2.34	$ 224
Exercised	(2,202)	12.35		
Options outstanding at September 10, 2016	532,226	$ 10.98	1.64	$ 942

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 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. On May 8, 2015, the Company granted 22,638 restricted shares for service in fiscal 2015, which vested in the second quarter of fiscal 2016. On May 5, 2016, the Company granted 28,674 restricted shares to the Board of Directors for service in fiscal 2016. As of September 10, 2016, there was less than $0.1 million of unrecognized expense associated with these grants, which will be recorded throughout the remainder fiscal 2016. Expense related to the Board of Directors' restricted stock in both the first three quarters of fiscal 2016, and the first three quarters of fiscal 2015 was $0.2 million.

In February 2014, the Company granted certain members of management 132,107 restricted shares based on the Company's performance in fiscal 2013. These restricted shares are subject to a graded vesting schedule over a three year period which started January 1, 2015. There was approximately $0.2 million and $0.5 million in unrecognized compensation expense remaining related to these awards as of September 10, 2016 and January 2, 2016, respectively. In both the first three quarters of fiscal 2016, and the first three quarters of fiscal 2015, compensation expense related to these awards was $0.4 million.

In February 2015, the Company granted certain members of management 38,372 restricted shares based on their services in fiscal 2014 and contingent upon continued service. The restricted shares vest over a three year period which started January 1, 2016. There was approximately $0.1 million and $0.2 million in unrecognized compensation expense remaining related to these awards as of September 10, 2016 and January 2, 2016, respectively. In both the first three quarters of fiscal 2016, and the first three quarters of fiscal 2015, compensation expense related to these awards was approximately $0.1 million.

In January 2016, the Company granted certain members of management 43,208 restricted shares based on their services in fiscal 2015 and contingent upon the employees' continued employment with the Company. The restricted shares vest over a period of approximately three years, beginning with the grant date in January 2016 and ending with the final vesting in January 2019. There was approximately $0.2 million and $0.3 million in unrecognized

compensation expense remaining related to these awards as of September 10, 2016 and January 2, 2016, respectively. In the first three quarters of fiscal 2016 and the first three quarters of fiscal 2015, approximately $0.1 million and $0.2 million was recorded as compensation expense related to these awards, respectively.

The following table summarizes the restricted stock activity for the period ended September 10, 2016:

Restricted Stock (Nonvested Shares)	Number of Shares	Weighted Average Grant-Date Fair Value Per Share
Nonvested shares outstanding at January 2, 2016	91,529	$ 14.47
Granted	71,882	9.92
Vested	(25,882)	12.59
Nonvested shares outstanding at September 10, 2016	137,529	$ 12.44

Employee Stock Purchase Plan

As of September 10, 2016, the Company had reserved 63,948 shares of common stock available for purchase under the Employee Stock Purchase Plan of 2008. In the first three quarters of fiscal 2016, employees purchased 32,036 shares of the Company's common stock with a weighted average fair market value of $10.65 per share.

(13) EARNINGS PER SHARE

The following table reconciles the number of shares outstanding for the third quarters of fiscal 2016 and 2015, 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:

	Third Quarter Ended,		First Three Quarters Ended,	
(Thousands)	September 10, 2016	September 12, 2015	September 10, 2016	September 12, 2015
Net income	$2,411	$ 2,755	$2,516	$ 3,853
Less: Income attributable to noncontrolling interest	76	46	117	115
Net income attributable to Heritage-Crystal Clean, Inc. available to common stockholders	$2,335	$ 2,709	$2,399	$ 3,738
Weighted average basic shares outstanding	22,267	22,153	22,246	22,136
Dilutive shares from share–based compensation plans	283	285	171	269
Weighted average diluted shares outstanding	22,550	22,438	22,417	22,405
Net income per share: basic	$0.10	$ 0.12	$0.11	$ 0.17
Net income per share: diluted	$0.10	$ 0.12	$0.11	$ 0.17

(14) OTHER EXPENSE (INCOME)

Other expense for the third quarter of fiscal 2016 includes expenses pertaining to a fine and restitution to be paid by International Petroleum Corp. of Delaware (“IPC”). The net charge to other expense in the third quarter of fiscal 2016 pertaining to this matter was approximately $1.6 million.

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 16, 2016. 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 2015 filed with the SEC on March 16, 2016. 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 10, 2016 and September 12, 2015, respectively. "Fiscal 2015" represents the 52-week period ended January 2, 2016 and "Fiscal 2016" represents the 52-week period ended December 31, 2016.

Overview

We provide parts cleaning, containerized waste management, used oil collection, vacuum truck services, antifreeze recycling, and field services, and we own and operate a used oil re-refinery. 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 83 branch facilities providing services to customers in 45 states and parts of Canada. We conduct business through two operating 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 three quarters of fiscal 2016. 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 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 2016.

Our operating costs include the costs of the materials we use in our products and services, such as used oil 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, 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 SG&A expense as revenues less operating costs and depreciation and amortization from operations.

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

Our 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, and legal.

On March 24, 2016, we purchased the assets of Phoenix Environmental. Services, Inc. and Pipeline Video and Cleaning North Corporation (together "Phoenix Environmental"). The purchase price for the acquisition was $2.7 million including $0.3 million placed into escrow, plus contingent consideration of up to $0.3 million based on subsequent business performance.

For further discussion on these acquisitions, see Note 3 in our consolidated financial statements included elsewhere in this document.

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 in the first three quarters of fiscal 2016 to the information provided under the heading "Critical Accounting Policies" included in our Annual Report on Form 10-K for the fiscal year ended January 2, 2016.

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 10, 2016		September 12, 2015		September 10, 2016		September 12, 2015	
Revenues								
Product revenues	$27,182	33.2%	$32,888	39.8%	$75,582	31.4%	$99,509	39.9%
Service revenues	54,690	66.8%	49,797	60.2%	165,295	68.6%	150,154	60.1%
Total Revenues	$81,872	100.0%	$82,685	100.0%	$240,877	100.0%	$249,663	100.0%
Operating expenses -								
Operating costs	$61,695	75.4%	$63,499	76.8%	$187,654	77.9%	$197,576	79.1%
Selling, general and administrative expenses	10,726	13.1%	9,872	11.9%	34,455	14.3%	31,553	12.6%
Depreciation and amortization	4,196	5.1%	4,419	5.3%	12,442	5.2%	13,050	5.2%
Other expense (income) - net	1,439	1.8%	99	0.1%	1,238	0.5%	(153)	(0.1)%
Operating income	3,816	4.7%	4,796	5.8%	5,088	2.1%	7,637	3.1%
Interest expense – net	463	0.6%	404	0.5%	1,432	0.6%	1,366	0.5%
Income before income taxes	3,353	4.1%	4,392	5.3%	3,656	1.5%	6,271	2.5%
Provision for income taxes	942	1.2%	1,637	2.0%	1,140	0.5%	2,418	1.0%
Net income	2,411	2.9%	2,755	3.3%	2,516	1.0%	3,853	1.5%
Income attributable to noncontrolling interest	76	0.1%	46	0.1%	117	—%	115	—%
Net income attributable to Heritage-Crystal Clean, Inc. common stockholders	$2,335	2.9%	$2,709	3.3%	$2,399	1.0%	$3,738	1.5%

Revenues

For the third quarter of fiscal 2016, revenues decreased $0.8 million, or 1.0%, from $82.7 million in the third quarter of fiscal 2015 to $81.9 million in the third quarter of fiscal 2016. For the three quarters of fiscal 2016, revenues decreased $8.8 million, or 3.5%, from $249.7 million in the three quarters of fiscal 2015 to $240.9 million in the first three quarters of fiscal 2016. The declines in revenues in our Environmental Services segment were mainly due to the downturn in activity at customers directly involved in and related to the energy sector, as well as lower energy surcharge revenues. The declines in revenues in our Oil Business segment were mainly due to lower selling prices for our base oil and RFO products, partially offset by higher base oil volume sales and higher used oil collection charges.

Operating expenses

Operating costs

Operating costs decreased $1.8 million, or 2.8%, from the third quarter of fiscal 2015 to the third quarter of fiscal 2016, and $9.9 million, or 5.0%, from the three quarters of fiscal 2015 to the three quarters of fiscal 2016. The decrease in operating costs was primarily a result of lower costs for oil-based inventory due to decreases in crude oil prices year over year. Additionally, lower crude oil prices resulted in lower solvent costs 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 crude oil price could cause a decline in the price we pay for parts cleaning solvent and diesel fuel. In the Oil Business, we expect our operating costs will also increase in the future if our throughput

capacity increases at our re-refinery. We also expect that a change in the price for crude oil could impact our used oil collection costs and processing costs at our re-refinery either favorably or unfavorably.

Selling, general, and administrative expenses

Selling, general, and administrative expenses increased $0.9 million, or 8.7%, from the third quarter of fiscal 2015 to the third quarter of fiscal 2016. Selling, general, and administrative expenses increased $2.9 million, or 9.2%, from the first three quarters of fiscal 2015 to the first three quarters of fiscal 2016. The increases in expense was mainly driven by increased legal fees, partially offset by lower outsourcing costs pertaining to information technology. Legal fees were $2.1 million and $5.5 million in the third quarter of 2016 and the first three quarters of 2016, respectively, compared to $0.1 million and $1.1 million in the third quarter of 2015 and the first three quarters of 2015, respectively. The higher legal expenses in fiscal 2016 pertain primarily to arbitration proceedings and environmental matters described in Part II, Item 1 "Legal Proceedings."

Other expense (income) - net

Other expense (income) - net was $1.4 million of expense for the third quarter of fiscal 2016 compared to $0.1 million of expense for the third quarter of fiscal 2015. Other expense (income) - net was $1.2 million of expense for the first three quarters of fiscal 2016 compared to $0.2 million of income for the first three quarters of fiscal 2015. Other expense for the third quarter of fiscal 2016 includes expenses pertaining to the Company's portion of a fine and restitution to be paid by International Petroleum Corp. of Delaware (“IPC”). The net charge to other expense in the third quarter of fiscal 2016 pertaining to this matter was approximately $1.6 million. Additional information regarding this matter can be found in Part II, Item 1 “Legal Proceedings".

Interest expense

Interest expense for the third quarter of fiscal 2016 was $0.5 million compared to interest expense of $0.4 million in the third quarter of fiscal 2015. In both the first three quarters of fiscal 2016 and the first three quarters of fiscal 2015, interest expense was $1.4 million. In the first three quarters of fiscal 2016 we capitalized less than $0.1 million in interest compared to the first three quarters of 2015 when we capitalized $0.4 million in interest.

Provision for income taxes

Our effective tax rate for the first three quarters of fiscal 2016 was 31.2% compared to 38.6% in the first three quarters of fiscal 2015. The rate difference is principally attributable to the differing treatment for financial reporting and income tax reporting for certain income and expenditures items. The rate decrease attributable to expenditures reported net of anticipated reimbursement from an unrelated third party for financial reporting purposes, but deducted on a gross basis for income tax purposes, is partially offset by expenditures which are expensed for financial reporting purposes but not deductible for income tax purposes.

Segment Information

The following table presents revenues by operating segment:

	For the Third Quarter Ended,		Change	
(Thousands)	September 10, 2016	September 12, 2015	$	%
Revenues:				
Environmental Services	$51,282	$ 52,122	$(840)	(1.6)%

Oil Business	30,590	30,563	27	0.1 %
Total	$81,872	$ 82,685	$(813)	(1.0)%

(Thousands)	For the First Three Quarters Ended, September 10, 2016	September 12, 2015	Change $	%
Revenues:				
Environmental Services	$156,080	$ 157,978	$(1,898)	(1.2)%
Oil Business	84,797	91,685	(6,888)	(7.5)%
Total	$240,877	$ 249,663	$(8,786)	(3.5)%

In the third quarter of fiscal 2016, Environmental Services revenues decreased by approximately $0.8 million, or 1.6%, from $52.1 million in the third quarter of fiscal 2015 to $51.3 million in the third quarter of fiscal 2016. In the first three quarters of fiscal 2016, Environmental Services revenues decreased $1.9 million, or 1.2%, from $158.0 million in the first three quarters of fiscal 2015 to $156.1 million in the first three quarters of fiscal 2016. The decline in revenue was mainly due to a downturn in activity of customers directly involved in, or related to, the energy sector, the loss of certain customers, and lower energy surcharge revenue.

At the end of the third quarter of fiscal 2016, the Environmental Services segment was operating in 83 branch locations compared with 83 at the end of the third quarter of fiscal 2015. There were 82 branches that were in operation throughout both the third quarters of fiscal 2016 and fiscal 2015.

In the third quarter of fiscal 2016, Oil Business revenues were flat compared to the third quarter of fiscal 2015. In the first three quarters of fiscal 2016, Oil Business revenues decreased $6.9 million compared to the first three quarters of fiscal 2015. The revenue decrease was mainly due to lower selling prices for our base oil and RFO products, which was partially offset by higher base oil sales volume. The decline in revenue was further offset by increased revenue from used oil collection charges and stop fees of $4.6 million in the third quarter of fiscal 2016 compared to the third quarter of fiscal 2015, and an approximate increase of $12.9 million in the first three quarters of fiscal 2016 compared to the first three quarters of 2015. During the third quarter of fiscal 2016, we produced base oil at a rate of 92% of the nameplate capacity of our re-refinery which was a slightly lower rate compared to the two prior quarters in fiscal 2016. The decreased production rate was mainly due to a planned, extended shutdown during the fiscal third quarter.

During the third quarter of fiscal 2016, the average spot market price for the type of lubricating base oil we produce declined over 11% compared to the third quarter of fiscal 2015. However, the average spot market price during the third quarter was up approximately 10% compared to the second quarter of fiscal 2016.

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

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

	For the Third Quarter Ended,		Change	
(Thousands)	September 10, 2016	September 12, 2015	$	%
Profit (loss) before corporate SG&A*				
Environmental Services	$15,084	$ 14,943	$141	0.9 %
Oil Business	1,733	647	1,086	167.9%
Total	$16,817	$ 15,590	$1,227	7.9 %

	For the First Three Quarters Ended,		Change	
(Thousands)	September 10, 2016	September 12, 2015	$	%

Profit (loss) before corporate SG&A*				
Environmental Services	$44,022	$ 43,097	$925	2.1 %
Oil Business	(754)	(1,708)	954	55.9%
Total	$43,268	$ 41,389	$1,879	4.5 %

*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 9 in our consolidated financial statements included elsewhere in this document.

Environmental Services profit before corporate SG&A expense increased 0.9% in the third quarter of fiscal 2016 compared to the third quarter of fiscal 2015. This increase was mainly due to lower disposal costs, partially offset by lower revenues, in the fiscal third quarter 2016, compared to the fiscal third quarter of 2015. Environmental Services profit before corporate SG&A expense increased 2.1% in the first three quarters of fiscal 2016 compared to the first three quarters of fiscal 2015 mainly due to $2.7 million in lower disposal charges, partially offset by a $1.9 million decrease in revenue.

The recovery of used solvent from customers participating in our product reuse program for parts cleaning is not accounted for as revenues, but rather as a reduction in our net cost of solvent under operating costs. As a result of falling solvent prices, sales of reuse solvent provided a negative impact on profit before corporate SG&A expense during the first three quarters of fiscal 2016 of $0.3 million, compared to a negative impact of $1.3 million in the first three quarters of fiscal 2015. Sales of reuse solvent did not provide a material impact during the third quarter of fiscal 2016 or in the third quarter of fiscal 2015.

Oil Business income before corporate SG&A expense increased $1.1 million in the third quarter of fiscal 2016, from income of $0.6 million in the third quarter of fiscal 2015, to income of $1.7 million in the third quarter of fiscal 2016. This improvement was primarily driven by the increase in used oil collection related charges of $4.6 million in the third quarter of fiscal 2016 compared to the third quarter of fiscal 2015.

Oil Business loss before corporate SG&A expense was $0.8 million in the first three quarters of fiscal 2016, compared to a loss of $1.7 million in the first three quarters of fiscal 2015. Oil Business margins improved due to higher used oil collection-related revenues, partially offset by lower base oil and Recycled Fuel Oil ("RFO") pricing.

FINANCIAL CONDITION

Liquidity and Capital Resources

Cash and Cash Equivalents

As of September 10, 2016 and January 2, 2016, cash and cash equivalents were $29.8 million and $23.6 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. In the future, the Company will have a cash outlay of $3.5 million in conjunction with the settlement described in Part II, Item 1 “Legal Proceedings.”

Debt and Financing Arrangements

On October 16, 2014, in connection with our acquisition of FCC Environmental, we amended our Amended and Restated Credit Agreement ("Credit Agreement", or "Credit Facility") to allow for up to $140.0 million in borrowings. As of September 10, 2016 and January 2, 2016, our total borrowings were $67.5 million and $70.9 million, respectively, under the term loan portion of our Credit Facility which has a maturity date of February 5, 2018. The remaining portion of the Credit Facility is a revolving loan which expires on February 5, 2018. There were no amounts outstanding under the revolver at September 10, 2016 and January 2, 2016.

During the third quarter of fiscal 2016, we recorded interest of $0.5 million on the term loan and capitalized less than $0.1 million of recorded interest for various capital projects. During the first three quarters of fiscal 2016, we recorded interest of $1.5 million on the term loan, of which less than $0.1 million was capitalized for various capital projects. During the third quarter of fiscal 2015, we recorded interest of $0.4 million on the term loan and capitalized $0.1 million for various capital projects. During the first three quarters of fiscal 2015, we recorded interest of $1.4 million on the term loan and capitalized $0.4 million for various capital projects.

Certain covenants of the Credit Agreement, among other things, restrict our ability to incur indebtedness, grant liens, make investments, and sell assets. The Credit Agreement, as amended, 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; and
- A capital expenditures covenant limiting certain capital expenditures to $15.0 million annually

As of September 10, 2016 and January 2, 2016, we were in compliance with all covenants under the Credit Agreement. As of September 10, 2016 and January 2, 2016, we had $3.0 million and $4.4 million of standby letters of credit issued, respectively, and $8.6 million and $34.5 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 our total leverage ratio.

Our weighted average interest rate for all debt outstanding as of September 10, 2016 and September 12, 2015 was 3.2% and 3.1%, respectively.

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, including 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 Quarters Ended, September 30, 2016	September 12, 2015
Net cash provided by (used in):		
Operating activities	$23,999	$ 17,025
Investing activities	(14,690)	(12,420)
Financing activities	(3,150)	(5,704)
Net increase (decrease) in cash and cash equivalents	$6,159	$ (1,099)

The most significant items affecting the comparison of our operating activities for the first three quarters of fiscal 2016 and the first three quarters of fiscal 2015 are summarized below:

Net Cash Provided by Operating Activities —

- Accounts Payable — The increase in accounts payable favorably affected cash flows from operations by $20.0 million in the first three quarters of fiscal 2016 compared to the first three quarters of fiscal 2015. The increase in accounts payable in the first three quarters of fiscal 2016 was mainly driven by higher legal fees and amounts payable in conjunction with the settlement described in Part II, Item 1 "Legal Proceedings." In the first three quarters of fiscal 2015, accounts payable decreased significantly due to the lower unit cost of raw materials such as used oil and solvent.

- Accrued expenses — In the first three quarters of fiscal 2016, accrued expenses increased $4.9 million compared to the first three quarters of fiscal 2015 driven mainly by higher legal fee accruals year over year. In the first three quarters of fiscal 2015, accrued expenses decreased due to reductions in accrued severance and lower accrued wages and benefits.

- Accounts Receivable — The increase in accounts receivable had a negative impact on cash provided by operating activities of $9.2 million in the first three quarters of fiscal 2016 compared to the first three quarters of fiscal 2015 primarily due to a net increase in the selling price of oil products and used oil collection services during the first three quarters of fiscal 2016 compared to a net decrease in the selling price of oil products during the first three quarters of fiscal 2015.

Net Cash Used in Investing Activities —

- Capital expenditures — We used $12.6 million and $12.5 million for capital expenditures during the first three quarters of fiscal 2016 and fiscal 2015, respectively. During the first three quarters of fiscal 2016, we spent $6.3 million for capital improvements to the re-refinery, compared to $4.2 million on capital improvements at the re-refinery in the first three quarters of fiscal 2015. Additionally, in the first three quarters of fiscal 2016, approximately $3.2 million of the capital expenditures were for purchases of parts cleaning machines compared to $3.8 million in the first three quarters of fiscal 2015. The remaining $3.1 million in the first three quarters of fiscal 2016 was for other items including leasehold improvements and intangible assets compared to approximately $4.4 million spent in the first three quarters of fiscal 2015.

- Acquisitions — In the first three quarters of fiscal 2016, we used $2.4 million for the purchase of the assets of Phoenix Environmental.

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 third quarter of fiscal 2016 were $70.1 million, and the annual effective interest rate for the Credit Facility for the third quarter of fiscal 2016 was 3.2%. 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 $0.7 million to our interest expense in the third quarter of fiscal 2016.

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.

There was no change in the Company's internal controls over financial reporting that occurred during the third fiscal quarter of 2016 that has materially affected or is reasonably likely to materially affect, the Company's internal controls over financial reporting.

PART II
ITEM 1. LEGAL PROCEEDINGS

On July 1, 2015, we received a grand jury subpoena from the U.S. Department of Justice ("DOJ"), along with the U.S. Environmental Protection Agency ("EPA"), requesting certain materials related to the transportation and disposal of wastewater by International Petroleum Corp. of Delaware ("IPC"), a company acquired along with the acquisition of FCC Environmental, LLC (FCCE), and the due diligence documents provided to us in connection with our acquisition of IPC. Earlier this year we received indirect communication that the City of Wilmington, Delaware was also seeking to recover amounts related to municipal services allegedly incurred prior to our acquisition of IPC. The portion of the IPC operation that was the subject of the investigation was not operating at the time of our acquisition of IPC.

In October 2016 we reached a settlement, subject to final documentation, with the DOJ, EPA and the City of Wilmington, Delaware to settle the above referenced investigation. As part of the settlement IPC will plead guilty to two criminal counts related to activity which occurred prior to our acquisition of IPC and pay a fine of $1.3 million. The two counts include conspiracy to violate the Clean Water Act, 33 U.S.C. § 1319(c)(2) and violation of the Resource Conservation and Recovery Act, 42 U.S.C. § 6928(d)(5). The settlement also includes payment of an additional $2.2 million by IPC to the City of Wilmington, Delaware for restitution related to underpayment of sewer fees which occurred prior to our acquisition of IPC. Our acquisition of the IPC business is governed by a Stock Purchase Agreement which obligates the Seller to indemnify us for certain costs that may arise in connection with the above matter. Approximately $1.6 million was charged to other expense (income) - net in our 2016 fiscal third quarter results pertaining to this matter.

We are involved in an arbitration with the sellers of FCCE and IPC in order to enforce our rights under the Stock Purchase Agreement. The arbitration includes the matter described above as well as other routine post-closing items related to our acquisition of FCCE and IPC. It is the Company's position in the arbitration that the sellers of IPC are obligated to indemnify us for the full amount of the fine and restitution. We expect the arbitration process to be completed by the end of fiscal 2016.

ITEM 1A. RISK FACTORS

Investing in our common stock involves a high degree of risk. You should carefully consider the following factors, as well as other information contained or incorporated by reference in this report, before deciding to invest in shares of our common stock. The risks and uncertainties described below are not the only risks and uncertainties we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business operations. If any of those risks actually occurs, our business, financial condition and results of operations would suffer. In that event, the trading price of our common stock could decline, and you may lose all or part of your investment. The risks discussed below also include forward-looking statements and our actual results may differ substantially from those discussed in these forward-looking statements. Risks facing our business have not changed substantively from those discussed in our Annual Report on Form 10-K for the year ended January 2, 2016, except those set forth below.

Our operations are subject to numerous environmental, transportation, and other laws and regulations and, to the extent we are found to be in violation of any such laws and regulations, we may be subject to involuntary shutdowns and/or significant financial penalties.

Our operations are subject to extensive federal, state, and local laws and regulations relating to the protection of the environment which, among other things:

- regulate the collection, sale, transportation, handling, processing, and disposal of the hazardous and non-hazardous wastes that we collect from our customers;
- regulate the treatment and processing of waste material that we collect from our customers and the discharge of treated material;
- impose liability on persons involved in generating, handling, processing, transporting, or disposing hazardous materials; and
- impose joint and several liability for the remediation and clean-up of environmental contamination

We are also subject to various transportation rules and regulations enforced by the DOT, Federal Railroad Administration (FRA), the Federal Motor Carrier Safety Administration, and the Department of Homeland Security. The breadth and complexity of these laws and regulations affecting our business make consistent compliance extremely difficult and often result in increased operating and compliance costs. Even with these programs, we and other companies in the industry are routinely faced with legal and administrative proceedings which can result in civil and criminal penalties (including the loss of certain licenses and permits that are required for our business), interruption of business operations, fines or other sanctions, and require expenditures for remedial work at our and third-party facilities. Under current law, we may be held liable for damage caused by conditions that existed before we acquired the assets or operations involved or if we arrange for the transportation, disposal, or treatment of hazardous substances that cause environmental contamination. We may also be held liable for the mishandling of waste streams resulting from the misrepresentations by a customer as to the nature of such waste streams. We may be subject to monetary fines, civil or criminal penalties, remediation, clean-up or stop orders, injunctions, orders to cease or suspend certain practices, or denial of permits we require to operate our facilities.

We are also required to obtain and maintain permits, licenses, and approvals to conduct our operations in compliance with such laws and regulations. If we are unable to maintain our currently held permits, licenses, and approvals, we may not be able to continue certain of our operations. If we are unable to obtain additional permits, licenses, and

approvals which may be required as we expand our operations, we may not be able to grow our business.

We have in the past been subject to penalties and fines for noncompliance with environmental regulations and could be subject to penalties and fines in the future. For example, as described in “Legal Proceedings,” on July 1, 2015, we received a grand jury subpoena from the U.S. Department of Justice ("DOJ"), along with the U.S. Environmental Protection Agency ("EPA"), requesting certain materials related to the transportation and disposal of wastewater by International Petroleum Corp. of Delaware ("IPC"), a company acquired along with the acquisition of FCC Environmental, LLC (FCCE), and the due diligence documents provided to us in connection with our acquisition of IPC. In 2016 we received indirect communication that the City of Wilmington, Delaware was also seeking to recover amounts related to municipal services allegedly incurred prior to our acquisition of IPC. The portion of the IPC operation that was the subject of the investigation was not operating at the time of our acquisition of IPC. In October 2016 we reached a settlement, subject to final documentation, with the DOJ, EPA and the City of Wilmington, Delaware to settle the above referenced investigation. As part of the settlement IPC will plead guilty to two criminal counts related to activity which occurred prior to our acquisition of IPC and pay a fine of $1.3 million. The two counts include conspiracy to violate the Clean Water Act, 33 U.S.C. § 1319(c)(2) and violation of the Resource Conservation and Recovery Act, 42 U.S.C. § 6928(d)(5). The settlement also includes payment of an additional $2.2 million by IPC to the City of Wilmington, Delaware for restitution related to underpayment of sewer fees which occurred prior to our acquisition of IPC. The consequences from this investigation could have a material effect on our business, financial condition, and results of operations, including the potential loss of permits, licenses, and approvals to conduct our business and the potential inability to obtain additional permits, licenses, and approvals which may be required as we expand our operations.

In addition, the operation of our used oil re-refinery exposes us to risks related to the potential loss of permits, contamination of feedstock, adverse environmental impact of a spill or other release, the risk of explosion or fire or other hazards, the risk of injury to our employees or others, as well as the negative publicity due to public concerns regarding our operation. The occurrence of any of these events could result in reduced production rates, loss of inventory, operational inefficiencies, clean-up costs, or other items that might negatively affect the operating results of the Company. While these risks are in some respects similar to risks that we have experienced in our traditional service businesses, the magnitude of exposure may be greater due to the nature of the used oil re-refining industry and the greater volumes, temperatures, and pressures involved. While we may maintain some insurance that covers portions of these exposures, in many cases the risks are uninsurable or we will not choose to procure insurance at levels that will cover all potential exposure.

CERCLA and similar state laws impose strict liability on current or former owners and operators of facilities that release hazardous substances into the environment, as well as on the businesses that generate those substances or transport them to the facilities. As a potentially responsible party, or PRP, we may be liable under CERCLA for substantial investigation and cleanup costs even if we operate our business properly and comply with applicable federal and state laws and regulations. Liability under CERCLA may be joint and several, which means that if we were found to be a business with responsibility for a particular CERCLA site, we could be required to pay the entire cost of the investigation and cleanup, even though we were not the party responsible for the release of the hazardous substance and even though other companies might also be liable. Even if we were able to identify who the other responsible parties might be, we may not be able to compel them to contribute to the remediation costs, or they might be insolvent or unable to contribute due to lack of financial resources. Our facilities and the facilities of our customers and third party contractors may have generated, used, handled and/or disposed of hazardous substances and other regulated wastes. Environmental liabilities could exist, including cleanup obligations at these facilities or at off-site locations where materials from our operations were disposed of, which could result in future expenditures that cannot

be currently quantified and which could materially reduce our profits. It is also possible that government officials responsible for enforcing environmental laws may view an environmental liability as more significant than we then currently estimate, or that we will fail to identify or fully appreciate an existing liability before we become legally responsible to address it.

Our pollution liability insurance excludes certain liabilities under CERCLA. Thus, if we were to incur liability under CERCLA that was not covered by our insurance, and if we could not identify other parties responsible under the law whom we are able to compel to contribute to the liabilities, the cost to us could be substantial and could impair our profitability, reduce our liquidity, and have a material adverse effect on our business. Although our customer service agreements typically provide that the customer is responsible for ensuring that only appropriate materials are disposed of, we could be exposed to third party claims if customers dispose of improper waste, and we might not be successful in recovering our damages from those customers. In addition, new services or products offered by us could expose us to further environmental liabilities for which we have no historical experience and cannot estimate our potential exposure to liabilities.

In addition, there currently exists a high level of public concern over hazardous waste operations, including with respect to the siting and operation of transfer, processing, storage, and disposal facilities. For example, under the DOT's Compliance, Safety, Accountability (CSA) initiative, a compliance and enforcement initiative designed to monitor commercial motor vehicle safety, the fleets and drivers in our network are evaluated and ranked based on certain safety-related standards. A poor fleet ranking or a reduction in eligible drivers could impact our ability to service our customers and could cause our customers to use a competitor with higher fleet rankings than ours, which could have a material adverse effect on our business, financial condition and results of operations.

Part of our business strategy is to increase our re-refining capacity through the operation of our facility and by adding new branch operations. Each of these efforts requires us to undergo an intensive regulatory approval process that could be time consuming and impact the success of our business strategy. Zoning, permit, and licensing applications and proceedings, as well as regulatory enforcement proceedings, are all matters open to public scrutiny and comment. Accordingly, from time to time we have been, and may in the future be, subject to public opposition and publicity which may damage our reputation and delay or limit the expansion and development of our operating properties or impair our ability to renew existing permits which could prevent us from implementing our growth strategy and have a material adverse effect on our business, financial condition or results of operations.

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

In August 2016, in connection with the vesting of restricted stock awards held by retiring employees, the Company purchased from these employees a total of 543 shares of its common stock for a purchase price of $13.01 per share for the sole purposes of satisfying the minimum tax withholding obligations of the employees upon the vesting of a portion of certain restricted stock award grants to them by the Company. No shares were repurchased in the open market.

The following table shows the Company's stock repurchase activity during the three months ended September 10, 2016:

Period	Total Number of Shares Purchased[(a)]	Average Price Paid per Share	Total Number of Shares Purchased as part of	Maximum Number (or Approximate Dollar Value) of Shares that

			Publicly Announced Plans or Programs	May Yet be Purchased Under the Plans or Programs
August 2016	543	$ 13.01	—	—

[a] Shares withheld for income tax liabilities upon equity award vestings

ITEM 6. EXHIBITS

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 20, 2016 By: /s/ Mark DeVita

Mark DeVita
Chief Financial Officer