Primo Water Corp
Form 10-Q
November 08, 2018

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2018

OR

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

COMMISSION FILE NUMBER 001-34850

PRIMO WATER CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**82-1161432**
(State of incorporation)	*(I.R.S. Employer Identification No.)*

101 North Cherry Street, Suite 501, Winston-Salem, NC 27101

(Address of principal executive office) (Zip code)

(336) 331-4000

(Registrant's telephone number, including area code)

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, if any, every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

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

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

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

As of November 2, 2018, there were 38,535,113 shares of our Common Stock, par value $0.001 per share, outstanding.

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PRIMO WATER CORPORATION

FORM 10-Q

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2018

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

PRIMO WATER CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except par value information)

	September 30, 2018 (unaudited)	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 5,630	$ 5,586
Accounts receivable, net	23,503	18,015
Inventories	9,602	6,178
Prepaid expenses and other current assets	4,477	3,409
Total current assets	43,212	33,188
Bottles, net	4,611	4,877
Property and equipment, net	92,607	100,692
Intangible assets, net	80,028	144,555
Goodwill	92,069	92,934
Investment in Glacier securities ($0 and $3,881 available-for-sale, at fair value at September 30, 2018 and December 31, 2017, respectively)	–	6,510
Other assets	667	997
Assets held-for-sale at fair value	5,288	–
Total assets	$ 318,482	$ 383,753
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 27,290	$ 18,698
Accrued expenses and other current liabilities	7,663	9,878
Current portion of long-term debt and capital leases	11,088	3,473
Total current liabilities	46,041	32,049
Long-term debt and capital leases, net of current portion and debt issuance costs	178,196	269,793

Deferred tax liability, net	–	8,455
Other long-term liabilities	806	1,985
Liabilities held-for-sale at fair value	1,438	–
Total liabilities	226,481	312,282
Commitments and contingencies		
Stockholders’ equity:		
Preferred stock, $0.001 par value - 10,000 shares authorized, none issued and outstanding	–	–
Common stock, $0.001 par value - 70,000 shares authorized, 38,527 and 30,084 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively	39	30
Additional paid-in capital	423,402	345,963
Accumulated deficit	(330,329)	(273,752)
Accumulated other comprehensive loss	(1,111)	(770)
Total stockholders’ equity	92,001	71,471
Total liabilities and stockholders’ equity	$ 318,482	$ 383,753

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

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PRIMO WATER CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands, except per share amounts)

	Three months ended September 30,		**Nine months ended September 30,**	
	2018	**2017**	**2018**	**2017**
Net sales	$81,770	$82,207	$231,231	$217,762
Operating costs and expenses:				
Cost of sales	58,312	57,273	164,462	154,166
Selling, general and administrative expenses	7,369	7,939	26,169	26,703
Non-recurring and acquisition-related costs	139	158	626	7,583
Depreciation and amortization	6,194	6,358	18,365	19,571
Impairment charges and other	67,940	(72)	68,184	(90)
Total operating costs and expenses	139,954	71,656	277,806	207,933
(Loss) income from operations	(58,184)	10,551	(46,575)	9,829
Interest expense, net	2,465	5,153	18,909	15,177
Change in fair value of warrant liability	–	–	–	3,220
(Loss) income before income taxes	(60,649)	5,398	(65,484)	(8,568)
Income tax (benefit) provision	(2,411)	451	(8,907)	823
Net (loss) income	$(58,238)	$4,947	$(56,577)	$(9,391)
(Loss) earnings per common share:				
Basic	$(1.45)	$0.15	$(1.55)	$(0.28)
Diluted	$(1.45)	$0.14	$(1.55)	$(0.28)
Weighted average shares used in computing (loss) earnings per share:				
Basic	40,072	33,525	36,410	33,086
Diluted	40,072	34,653	36,410	33,086

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

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PRIMO WATER CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

(Unaudited)

(In thousands)

	Three months ended September 30, 2018	Three months ended September 30, 2017	Nine months ended September 30, 2018	Nine months ended September 30, 2017
Net (loss) income	$(58,238)	$4,947	$(56,577)	$(9,391)
Other comprehensive income (loss):				
Reclassification of gain recognized in net income on redemption of Glacier securities	–	–	(86)	–
Unrealized gain on investment in Glacier securities	–	38	14	59
Foreign currency translation adjustments, net	160	386	(269)	723
Total other comprehensive income (loss)	160	424	(341)	782
Comprehensive (loss) income	$(58,078)	$5,371	$(56,918)	$(8,609)

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

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PRIMO WATER CORPORATION

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(Unaudited)

(In thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance, December 31, 2017	**30,084**	**$ 30**	**$ 345,963**	**$ (273,752)**	**$ (770)**	**$ 71,471**
Employee stock compensation plans, net	1,521	2	(5,324)	–	–	(5,322)
Exercise of common stock warrants	1,583	2	12,148	–	–	12,150
Proceeds from equity offering, net of costs	5,339	5	70,786	–	–	70,791
Reclassification of equity issuance costs previously capitalized	–	–	(171)	–	–	(171)
Net loss	–	–	–	(56,577)	–	(56,577)
Other comprehensive loss	–	–	–	–	(341)	(341)
Balance, September 30, 2018	**38,527**	**$ 39**	**$ 423,402**	**$ (330,329)**	**$ (1,111)**	**$ 92,001**

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

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PRIMO WATER CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

	Nine Months Ended September 30,	
	2018	**2017**
Cash flows from operating activities:		
Net loss	$(56,577)	$(9,391)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	18,365	19,571
Impairment charges and other	68,184	(90)
Stock-based compensation expense	2,710	4,611
Non-cash interest expense (income)	2,547	(51)
Change in fair value of warrant liability	–	3,220
Bad debt expense	170	180
Deferred income tax (benefit) expense	(8,907)	823
Realized foreign currency exchange loss and other, net	338	(11)
Changes in operating assets and liabilities:		
Accounts receivable	(5,724)	(8,480)
Inventories	(3,431)	(351)
Prepaid expenses and other current assets	(618)	(956)
Accounts payable	6,523	7,611
Accrued expenses and other current liabilities	(796)	(6,036)
Net cash provided by operating activities	22,784	10,650
Cash flows from investing activities:		
Purchases of property and equipment	(14,200)	(13,434)
Purchases of bottles, net of disposals	(1,596)	(2,120)
Proceeds from the sale of property and equipment	227	167
Proceeds from redemption of investment in Glacier securities	6,277	–
Additions to intangible assets and other	(975)	(113)
Net cash used in investing activities	(10,267)	(15,500)
Cash flows from financing activities:		
Borrowings under Revolving Credit Facility	15,000	–
Payments under Revolving Credit Facility	(15,000)	–
Borrowings under prior Revolving Credit Facility	14,000	2,500
Payments under prior Revolving Credit Facility	(14,000)	(2,500)
Borrowings under Term loan	190,000	–
Payments under Term loan	(2,375)	–

Payments under prior Term loan	(184,140)	(1,395)
Payments upon redemption of Junior Subordinated Debentures	(87,629)	–
Proceeds from common stock issuance, net of costs	70,791	–
Proceeds from warrant exercises, net	12,150	–
Capital lease payments	(1,190)	(1,712)
Bank overdraft	1,023	–
Stock option and employee stock purchase activity and other, net	(9,424)	(3,088)
Debt issuance costs and other	(1,671)	(261)
Net cash used in financing activities	(12,465)	(6,456)
Effect of exchange rate changes on cash and cash equivalents	(8)	(30)
Net increase (decrease) in cash and cash equivalents	44	(11,336)
Cash and cash equivalents, beginning of year	5,586	15,586
Cash and cash equivalents, end of period	$5,630	$4,250

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

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PRIMO WATER CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(In thousands, except per share amounts)

1. Description of Business and Significant Accounting Policies

Business

Primo Water Corporation (together with its consolidated subsidiaries, “Primo,” “we,” “our,” or “us”) is North America’s leading single source provider of multi-gallon purified bottled water, self-service refill drinking water and water dispensers sold through major retailers in the United States and Canada.

Follow-on Equity Offering

On May 22, 2018, we completed a follow-on offering of 5,339 shares of our common stock at a price of $14.00 per share to the public, which included the exercise in full by the underwriters of their option to purchase 696 additional shares of our common stock on the same terms and conditions. All of the shares were offered and sold by Primo. Net proceeds were approximately $70,791, after deducting the underwriting discounts and commissions and estimated offering expenses payable by us of approximately $4,132. We used the net proceeds from the offering to pay down existing indebtedness and subsequently refinance our remaining outstanding indebtedness (see Note 4 – Debt and Capital Leases, net of Debt Issuance Costs).

Unaudited Interim Financial Information

The accompanying interim condensed consolidated financial statements and notes have been prepared in accordance with our accounting practices described in our audited consolidated financial statements as of and for the year ended December 31, 2017. In the opinion of management, the unaudited interim condensed consolidated financial statements included herein contain all adjustments necessary to present fairly our financial position, results of operations and cash flows for the periods indicated. Such adjustments, other than nonrecurring adjustments that have been separately disclosed, are of a normal, recurring nature. The operating results for interim periods are not necessarily indicative of results to be expected for a full year or future interim periods. The unaudited interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes as of and for the year ended December 31, 2017 as filed on Form 10-K (the “2017 Form 10-K”). The accompanying interim condensed consolidated financial statements are presented in accordance with the rules and regulations of the Securities and Exchange Commission (the “SEC”) and, accordingly, do not include all the disclosures required by generally accepted accounting principles in the United States (“U.S. GAAP”) with respect to annual audited financial statements. Significant accounting policies are summarized in our 2017 Form 10-K.

Reclassifications

Certain amounts reported previously have been reclassified to conform to the current year presentation, with no effect on stockholders’ equity or net (loss) income as previously reported. These reclassifications relate to the following: presentation of common stock warrants which are included within additional paid-in capital on the condensed consolidated balance sheets and the condensed consolidated statement of stockholders’ equity, and (gain) loss on disposal of property and equipment which is included in impairment charges and other on the condensed consolidated statements of operations.

Recent Accounting Pronouncements

In August 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2018-15, *Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40)*. This update aligns the requirements for capitalizing implementation costs incurred in a cloud computing arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The update is effective for fiscal years beginning after December 15, 2019, and interim periods within that reporting period. Early adoption is permitted. We are currently in the process of evaluating the impact of adopting this guidance on our consolidated financial statements.

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In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*, which modifies the disclosure requirements on fair value measurements. The update is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2019 and early adoption is permitted. We are currently in the process of evaluating the impact of adopting this guidance on our consolidated financial statements.

In June 2018, the FASB issued ASU 2018-07, *Compensation - Stock Compensation (Topic 718), Improvements to Nonemployee Share-Based Payment Accounting*. This ASU is intended to simplify aspects of share-based compensation issued to non-employees by making the guidance consistent with the accounting for employee share-based compensation. The update is effective for fiscal years beginning after December 15, 2018, and interim periods within that reporting period. Early adoption is permitted, but no earlier than an entity's adoption date of Topic 606. We are currently in the process of evaluating the impact of adopting this guidance on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, *Intangibles – Goodwill and Other (Topic* 350*): Simplifying the Test for Goodwill Impairment*. The updated guidance eliminates step two of the goodwill impairment test and specifies that goodwill impairment should be measured by comparing the fair value of a reporting unit with its carrying amount. Additionally, the amount of goodwill allocated to each reporting unit with a zero or negative carrying amount of net assets should be disclosed. The update is effective for annual or interim goodwill impairment tests performed in fiscal years beginning after December 15, 2019; early adoption is permitted. We currently anticipate that adoption of the guidance will not have a material impact on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-01, *Business Combinations (Topic* 805*): Clarifying the Definition of a Business* to clarify the definition of a business, which is fundamental in the determination of whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses combinations. The updated guidance requires that in order to be considered a business the integrated set of assets and activities acquired must include, at a minimum, an input and process that contribute to the ability to create output. If substantially all of the fair value of the assets acquired are concentrated in a single identifiable asset or group of similar assets, it is not considered a business, and therefore would not be considered a business combination. We adopted this standard on January 1, 2018 with no impact on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic* 842) along with subsequent amendments to the initial guidance in ASU 2017-13, ASU 2018-10 and ASU 2018-11 (collectively, Topic 842) requiring lessees to recognize for all leases (with the exception of short-term leases) at the commencement date: (1) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis, and (2) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. The update is effective for fiscal years beginning after December 15, 2018, and interim periods within that reporting period. We have selected a leasing software solution and are in the process of identifying changes to our business processes, systems and controls to support the adoption of this standard. While we are still evaluating the impact of this new guidance on our consolidated financial statements, we expect it will result in a significant increase in total assets and total liabilities on our balance sheet due to the addition of our leased assets and related liabilities. We do not believe the adoption of this ASU will have a significant effect on our results of operations.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers* (Topic 606) which supersedes existing revenue recognition requirements in U.S. GAAP. The updated guidance requires that an entity 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. To achieve that core principle, the guidance establishes a five-step approach for the recognition of revenue. In each of March, April, May and December 2016, the FASB issued further guidance to provide clarity regarding principal versus agent considerations, the identification of performance obligations and certain other matters. The updates are currently effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Financial statement disclosures required under the guidance will enable users to understand the nature, amount, timing, judgments and uncertainty of revenue and cash flows relating to contracts with customers. Based on the analysis of our contracts with customers, the timing, measurement, and presentation of revenues based on Topic 606 is consistent with our revenues under Topic 605. We adopted the above standard utilizing the modified retrospective method beginning January 1, 2018, with no adjustment to the opening balance of retained earnings. Based on our analysis of disclosure requirements within the standard, we have included additional disclosures of disaggregated net sales included in Note 2 – Revenue Recognition below.

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2. Revenue Recognition

Sales of Products

We earn revenue from contracts with customers, primarily through the sale of our purified, multi-gallon bottled water, self-service filtered drinking water, or through the sale of water dispensers. All revenue recognized in the current period is derived from contracts with customers. We account for these revenues under Topic 606 which we adopted January 1, 2018, using the modified retrospective approach, which resulted in no adjustment to the opening balance of retained earnings.

In certain arrangements, depending on the nature and scope of the contract, our customer may be identified as the end consumer as we are interacting directly with the consumer via an implied contract upon the dispensing of self-service purified water. In other arrangements, our customer may be identified as the retailer, as we enter into contracts with retailers to resell purified multi-gallon bottled water or self-service filtered drinking water to the end consumer on our behalf. Our arrangements may also include standalone purchase orders from retailers to sell water dispensers. In such arrangements, the retailer is our customer.

Our performance obligations vary by business segment. Our performance obligations may include the delivery of purified water, the sale of the related bottle, or the sale of a water dispenser. In some instances, our sales arrangements may include multiple of the aforementioned performance obligations.

Our arrangements may include the shipping of products to our customers after the performance obligation related to that product has been satisfied. For such arrangements when shipping and handling activities are performed subsequent to the performance obligation being satisfied, we have elected to account for shipping and handling as activities to fulfill the promise to transfer goods. In such instances, we recognize shipping and handling costs at the same time as we recognize revenue.

We have no contractual obligation to accept returns nor do we guarantee sales. We may accept returns or issue credits for manufacturer defects or for items that were damaged in transit. We recognize revenue net of an estimated allowance for returns based on historical average return rates.

Typically, the transaction price of our products is fixed as agreed upon in our contracts with customers. Our arrangements may include variable consideration in the form of volume incentive agreements or coupon programs.

We provide sales incentives to certain retailers in the form of a volume rebate to promote the sale of our products. Generally, the rebates are tiered, such that as sales increase, the rebate percentage increases. We estimate the expected amount of these rebates based on historical sales volume at the time of the original sale. We update our assessment of the amount of rebates that will be earned either quarterly or annually based on our best estimate of the volume levels the customer will reach during the measurement period. We also may include a redeemable coupon for the purchase of purified, multi-gallon bottled water upon the purchase of one of our products. We account for the coupons based on historical redemption rates. The customer's right to redeem the coupon for a free purified, multi-gallon bottle of water is exercised at or near the purchase of our products such that it does not create a material timing difference in the recognition of revenue.

Our sales arrangements may involve collecting revenue directly from the end consumer. Tax on filtered water dispensed from a vended machine is exempt in several jurisdictions. For those remaining jurisdictions in which taxes are not exempt, we have analyzed our contracts with customers, concluding that we are the primary obligor to the respective taxing authority, and as such present sales tax charged to the end consumer utilizing the gross method.

We recognize revenue on the products we sell at a point in time. The delivery of purified water and sale of the related bottle are completed via a point-of-sale transaction at which time the customer obtains control and remits payment for the product. The shipment of a water dispenser to our customer reflects the transfer of control. We may grant credit limits and terms to customers based upon traditional practices and competitive conditions. In such instances, the terms may vary, but payments are generally due in 30 days or less from the invoicing date. Due to the point-of-sale nature of our products, we have not recognized revenue in the current period for performance obligations satisfied in previous reporting periods and have no unsatisfied performance obligations as of the end of the current period.

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Multiple Performance Obligations

Our sales arrangements may include multiple performance obligations. We identify each of the performance obligations in these arrangements and allocate the total transaction price to each performance obligation based on its identified relative selling price. In such arrangements, all of the performance obligations are met simultaneously as our products are concurrently delivered and have the same pattern of transfer to the customer. Thus, revenue is recognized simultaneously for each performance obligation when the customer obtains control of the product.

Presentation of Revenue

Our arrangements may involve another party selling products to our customers. We partner with retailers to place our self-service filtered water dispensing machines in their stores. We pay retailers a commission on the amount of sales generated from our products. We evaluate whether we control the products before they are transferred to the customer. In such instances where we control our products prior to transferring them to the customer, we are the principal in the transaction and record revenue at the gross amount and record commission paid to retailers as cost of sales. If we conclude that we do not control the products, we are the agent in the transaction and record revenue net of commissions paid to retailers.

Accounts Receivable Net of Allowances

Trade accounts receivable represent amounts billed to customers and not yet collected, and are presented net of allowances. The allowance for doubtful accounts is based on a review of specifically identified accounts in addition to an overall aging analysis and is our best estimate of the amount of probable credit losses in our existing accounts receivable. Judgements are made with respect to the collectability of accounts receivable based on historical experience and current economic trends. We also maintain an allowance for sales discounts, rebates and promotions based on our arrangements with customers. Account balances are charged off against the allowance in the period in which we determine that it is probable the receivable will not be recovered. These allowances totaled $2,282 and $1,509 at September 30, 2018 and December 31, 2017, respectively. Bad debt write-offs for the three and nine months ended September 30, 2018 and 2017 were immaterial.

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Disaggregation of Revenue

The tables below present our consolidated net sales by geographic area.

	Three months ended September 30, 2018			
	Refill	**Exchange**	**Dispensers**	**Total**
Geographical area				
United States	$46,884	$ 20,658	$ 11,053	$78,595
Canada	1,446	855	874	3,175
	$48,330	$ 21,513	$ 11,927	$81,770

	Three months ended September 30, 2017			
	Refill	**Exchange**	**Dispensers**	**Total**
Geographical area				
United States	$49,795	$ 19,600	$ 10,419	$79,814
Canada	1,492	835	66	2,393
	$51,287	$ 20,435	$ 10,485	$82,207

	Nine months ended September 30, 2018			
	Refill	**Exchange**	**Dispensers**	**Total**
Geographical area				
United States	$130,526	$ 57,273	$ 33,522	$221,321
Canada	4,016	2,504	3,390	9,910
	$134,542	$ 59,777	$ 36,912	$231,231

	Nine months ended September 30, 2017			
	Refill	**Exchange**	**Dispensers**	**Total**
Geographical area				
United States	$128,127	$ 53,005	$ 30,412	$211,544
Canada	3,687	2,296	235	6,218
	$131,814	$ 55,301	$ 30,647	$217,762

3. Impairment Charges and Other

	Three months ended September 30, 2018	Three months ended September 30, 2017	Nine months ended September 30, 2018	Nine months ended September 30, 2017
Impairment of Glacier trade name intangible	$60,750	$–	$60,750	$–
Impairment of property and equipment	2,363	–	2,363	–
Impairment of Ice assets held-for-sale	4,586	–	4,586	–
Loss (gain) on disposal of property and equipment and other	241	(72)	485	(90)
Total	$67,940	$(72)	$68,184	$(90)

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During the third quarter ended September 30, 2018, we decided to discontinue the use of the Glacier Water Services, Inc. (“Glacier”) trade name acquired as part of the acquisition of Glacier (the “Acquisition”) in December 2016, in order to more effectively and efficiently focus our brand building and marketing efforts in Refill around the Primo brand (the “Re-branding Strategy”). In connection with the initial accounting for the Acquisition, $62,900 of the purchase price was allocated to the indefinite-lived trade name related to the Refill segment. As a result of the Re-branding Strategy, during the three and nine months ended September 30, 2018, we recorded a pre-tax, non-cash intangible asset impairment charge of $60,750 to reduce the carrying value of the trade name to its estimated fair value, which is recorded in impairment charges and other on the condensed consolidated statements of operations. The fair value of the trade name was estimated based on the future discounted cash flows expected to be generated under the trade name prior to its complete phase-out. Based on the change in circumstances, the trade name was determined to have a finite life and will be amortized straight line over 2019 and 2020, in-line with the expected roll-out of the Re-Branding Strategy. The following table provides a rollforward of the discontinued Glacier trade name:

	Glacier Trade Name Intangible
Balance at December 31, 2017	$ 62,900
Impairment charge	(60,750)
Balance at September 30, 2018	$ 2,150

In addition, as a result of the Re-branding Strategy, during the third quarter ended September 30, 2018, we recorded a pre-tax, non-cash asset impairment charge of $2,363 to reduce the carrying value of property and equipment to its estimated fair value associated with certain Glacier-branded Refill equipment that is not expected to generate future cash flows sufficient to recover the net book value of the equipment. The fair value was estimated based on the undiscounted cash flows expected to be produced by the property and equipment. The impairment charge is recorded in impairment charges and other on the condensed consolidated statements of operations.

During the third quarter ended September 30, 2018, we concluded that a sale of certain assets of our Refill segment (the “Ice Assets”) was probable to take place within one year, which meets the criteria for assets held-for-sale treatment in accordance with FASB ASC No. 360, *Property, Plant, and Equipment.* Accordingly, during the three and nine months ended September 30, 2018, we recorded a pre-tax, non-cash asset impairment charge of $4,586, consisting of $3,786 related to property and equipment and $800 related to goodwill allocated to the Ice Assets. These impairment charges reduced the carrying value of the Ice Assets to their estimated fair value less costs to sell at September 30, 2018 as follows:

	September 30, 2018
Property and equipment, net	$ 4,688
Identifiable intangible assets	600

Assets held-for-sale at fair value	$ 5,288
Contingent consideration	$ 1,438
Liabilities held-for-sale at fair value	$ 1,438
Ice Assets, net	$ 3,850

The estimated fair value of the assets held-for-sale does not include accounts receivable for which we anticipate retaining the rights.

4. Debt and Capital Leases, net of Debt Issuance Costs

Debt and capital leases, net of debt issuance costs are summarized as follows:

	September 30, 2018	**December 31, 2017**
Revolving facilities	$ –	$ –
Term loans	187,625	184,140
Debt issuance costs, net	(1,346)	(3,011)
Total Credit Facilities	186,279	181,129
Junior Subordinated Debentures	–	88,579
Capital leases	3,005	3,558
	189,284	273,266
Less current portion	(11,088)	(3,473)
Long-term debt and capital leases, net of current portion and debt issuance costs	$ 178,196	$ 269,793

SunTrust Credit Facility

On June 22, 2018, we entered into a new senior secured credit facility (the “SunTrust Credit Facility”) that provides for a $190,000 senior term loan facility (the “Term Loan”) and a $30,000 senior revolving loan facility (the “Revolving Facility”). SunTrust Bank serves as the Administrative Agent, Swingline Lender and Issuing Bank under the SunTrust Credit Facility. The SunTrust Credit Facility matures on June 22, 2023. The Term Loan requires annual principal payments (payable in quarterly installments) equal to 5% per annum, or $9,500, with the remaining indebtedness due at maturity. The SunTrust Credit Facility is secured by a first priority security interest in and lien on substantially all of our assets. The SunTrust Credit Facility and related obligations are guaranteed by certain of our domestic subsidiaries.

Interest on outstanding borrowings under the SunTrust Credit Facility is calculated at our option at either (1) a base rate (which is derived from the Administrative Agent's prime lending rate, the federal funds effective rate plus 0.5%, or a London Interbank Offered Rate ("LIBOR") plus 1.0%) or (2) LIBOR plus, in each case of the foregoing (1) and (2), a margin, initially set at 2.50% per annum with respect to LIBOR loans and 1.50% per annum for base rate loans. A commitment fee, initially set at 0.30% per annum, ranging from 0.15% to 0.30% per annum, is payable quarterly on the average undrawn portion of the Revolving Facility. The margins and commitment fee fluctuate based on our consolidated leverage ratio as specified in the SunTrust Credit Facility. Total issuance costs associated with the SunTrust Credit Facility were $1,662, which have been presented either as a direct deduction from the carrying amount of the debt within long-term debt and capital leases, net of current portion and debt issuance costs, with respect to costs attributable to the Term Loan, or within other assets, with respect to costs attributable to the Revolving Facility. The costs are being amortized as part of interest expense over the term of the SunTrust Credit Facility. As of September 30, 2018, we had no outstanding borrowings and $30,000 of availability under the Revolving Facility.

The SunTrust Credit Facility contains a number of affirmative and negative covenants that use consolidated adjusted EBITDA ("Adjusted EBITDA"). Adjusted EBITDA is a non-U.S. GAAP financial measure that is calculated as net income (loss) before depreciation and amortization; interest expense, net; income taxes; change in fair value of warrant liability; non-cash stock-based compensation expense; non-recurring and acquisition-related costs; and loss (gain) on disposal of property and equipment and other assets, and other.

The primary operational covenants included in the SunTrust Credit Facility are as follows: (i) a minimum consolidated fixed charge coverage ratio of 1.10:1.00 beginning with the fiscal quarter ended June 30, 2018 and (ii) a maximum consolidated leverage ratio of 4.50:1.00 beginning with the fiscal quarter ended June 30, 2018 with the financial ratios tested as of the last day of each fiscal quarter. The leverage ratio steps down to 4.25:1.00 with respect to each fiscal quarter ending after June 30, 2019 and on or prior to June 30, 2020 and to 4.00:1.00 with respect to each fiscal quarter ending after June 30, 2020. At September 30, 2018, we were in compliance with all operational covenants, including (i) a consolidated fixed charge coverage ratio of 1.39:1.00 and (ii) a consolidated leverage ratio of 3.37:1.00.

The proceeds of entering into the SunTrust Credit Facility, together with the approximately $70,791 in net proceeds from our recent follow-on equity offering, were used to pay off the Goldman Credit Facility and Junior Subordinated Debentures, as described more fully below.

Goldman Credit Facility

On December 12, 2016, to complete the Acquisition, we entered into a senior secured credit facility with Goldman Sachs Bank USA (the "Goldman Credit Facility") that provided for an $186,000 term loan facility and a $10,000 revolving loan facility. We repaid all outstanding borrowings and accrued interest under the Goldman Credit Facility with the proceeds from our recent follow-on equity offering and the proceeds from the SunTrust Credit Facility during the second quarter of 2018. In connection with the repayment and termination of the Goldman Credit Facility during the second quarter of 2018, we immediately charged to interest expense, net on the condensed consolidated statements of operations the remaining $2,960 in unamortized debt issuance costs related to the Goldman Credit Facility and $3,904 related to early payment penalties.

Junior Subordinated Debentures and Investments

In connection with the Acquisition, we assumed $89,529 of 9-1/16% Junior Subordinated Deferrable Interest Debentures due 2028 (the “Subordinated Debentures”) issued to Glacier Water Trust I (“the Trust”), a wholly owned subsidiary of Primo following the Acquisition. On June 29, 2018, in connection with the closing of the SunTrust Credit Facility, we paid $87,938, including accrued interest of $309, to redeem the Subordinated Debentures. In connection with the redemption of the Subordinated Debentures, we recorded a gain of $475 in interest expense, net on the condensed consolidated statements of operations for the nine months ended September 30, 2018 resulting from the accretion of the remaining fair value adjustment allocated to the Subordinated Debentures as part of the purchase price allocation of the Acquisition.

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In connection with the redemption of the Subordinated Debentures described above, the Trust issued a revocable notice of redemption of all outstanding capital securities of the Trust, and all outstanding capital securities of the Trust were redeemed on June 29, 2018. We owned a portion of such securities and received $6,277 in proceeds upon their redemption, resulting in a $161 loss on the redemption of the Glacier securities which is included in impairment charges and other on the condensed consolidated statements of operations for the nine months ended September 30, 2018.

Subsequent to the redemption of the Subordinated Debentures and the redemption of all outstanding capital securities of the Trust, the Trust and all related agreements were terminated and effectively dissolved.

5. Glacier Warrants

On December 12, 2016, we issued warrants to purchase approximately 2,000 shares of our common stock in connection with the Acquisition (the “Glacier Warrants”). The Glacier Warrants became exercisable as follows: 33% on June 10, 2017, 33% on September 8, 2017 and the final 34% on December 12, 2017. The Glacier Warrants are exercisable at an exercise price of $11.88 per share of Primo common stock and expire on December 12, 2021. The Glacier Warrants’ fair value at the date of issuance of $8,420 was initially recorded as a liability on our condensed consolidated balance sheets as part of consideration for the Acquisition. Prior to the Amendment (as defined below), subsequent changes in the estimated fair value of the Glacier Warrants were recorded in our consolidated statements of operations.

On March 13, 2017, we entered into Amendment No. 1 to the Glacier Warrant Agreement (the “Amendment”). The Amendment provides, among other things, that under no circumstances may a Glacier Warrant holder exercise any Glacier Warrants and receive a cash payment as a net cash settlement. Thus, effective March 13, 2017, the Glacier Warrants were no longer reported as a liability on the consolidated balance sheets with changes in the fair value of the warrant liability reported within the consolidated statements of operations. Instead, following the Amendment, the Glacier Warrants were reported as equity instruments on the consolidated statements of stockholders’ equity. The change in the estimated fair value of the warrant liability for the period of January 1, 2017 through March 13, 2017 resulted in non-cash expense of $3,220 as presented on the condensed consolidated statements of operations for the nine months ended September 30, 2017.

The estimated fair value of the Glacier Warrants was determined using Level 3 inputs and assumptions within the Black- Scholes pricing model. The key assumptions used in the Black-Scholes model were as follows:

	March 13,

	2017
Expected life in years	4.75
Risk-free interest rate	2.08 %
Expected volatility	33.0 %
Dividend yield	0.0 %

The risk-free interest rate was based on the U.S. Treasury rate for the expected remaining life of common stock warrants. Our expected volatility was based on the average long-term historical volatilities of peer companies. The dividend yield assumption was based on our current intent not to issue dividends.

During the nine months ended September 30, 2018, we issued 1,136 shares of common stock upon the exercise of Glacier Warrants, including 116 shares of common stock upon the cashless exercise of 349 Glacier Warrants exercised for common stock. At September 30, 2018, there were Glacier Warrants outstanding to purchase 631 shares of common stock.

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6. Stock-Based Compensation

Overview

Total non-cash stock-based compensation expense by award type for all of our plans, all of which is included in selling, general and administrative expenses on our condensed consolidated statements of operations, was as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2018	**2017**	**2018**	**2017**
Stock options	$85	$142	$361	$441
Restricted stock	(12)	641	1,709	2,089
Value Creation Plan	–	–	–	1,482
Long-Term Performance Plan	(67)	124	565	526
Employee Stock Purchase Plan	25	26	75	73
	$31	$933	$2,710	$4,611

Value Creation Plan

On May 7, 2012, we established the Value Creation Plan (the “VCP”), which was subsequently amended on May 14, 2013 and amended and restated on March 3, 2016. The VCP provided awards comprised of cash or equity grants for eligible employees as determined by the Compensation Committee, based on the attainment of certain performance-based targets. The VCP provided for the issuance of up to three separate awards to eligible employees based on our attainment of financial targets of at least $15,000, $24,000 and $28,000 in Adjusted EBITDA for any fiscal year between 2014 and 2019. On December 22, 2016, the Compensation Committee of our Board of Directors approved the termination of the VCP, effective December 31, 2016, eliminating the third award related to the $28,000 Adjusted EBITDA target.

The award pool for the second issuance based on the achievement of the $24,000 Adjusted EBITDA target equaled 17.5% of the market capital appreciation of our stock from March 11, 2016 to March 20, 2017, the market close on the third full trading day after public announcement of financial results for 2016. On March 20, 2017, 1,370 shares were issued or deferred into the Primo Water Corporation Executive Deferred Compensation Plan (the “Deferred Compensation Plan”) as a result of the achievement of the $24,000 Adjusted EBITDA target. The deferral of certain shares did not alter the existing vesting conditions, number of awards vested or the form of the awards issued under the VCP. Additional non-cash expense of $1,482 related to the VCP was recorded in the nine months ended September 30, 2017. $10,111 of common stock was purchased by us during the nine months ended September 30, 2018 to settle the tax liability generated from the issuance of 1,706 shares from the Deferred Compensation Plan.

Long-Term Performance Plan

On February 28, 2017, we established the Long-Term Performance Plan (the “LTPP”). The LTPP provides equity grants for eligible employees based on the attainment of certain performance-based targets. Our intention is that all awards under the LTPP will be in the form of equity grants.

On March 20, 2017, we granted performance based equity awards under the LTPP with vesting terms based on our attainment of certain financial targets for the period of January 1, 2017 through December 31, 2019 (the “March 2017 Grant”). The number of shares earnable under the March 2017 Grant awards vary based on achievement of the established financial targets of Adjusted EBITDA and free cash flow on a cumulative basis for fiscal years 2017 through 2019. In the third quarter of 2018, we determined that the attainment of certain financial targets for the March 2017 Grant was not probable which resulted in the reversal of expense during the three and nine months ended September 30, 2018.

On March 9, 2018, we granted performance based equity awards under the LTPP with vesting terms based on our attainment of certain financial targets for the period of January 1, 2018 through December 31, 2020 (the “March 2018 Grant”). The number of shares earnable under the March 2018 Grant awards vary based on achievement of the established financial targets of Adjusted EBITDA and free cash flow on a cumulative basis for fiscal years 2018 through 2020.

7. Commitments and Contingencies

Omnifrio Single-Serve Beverage Business

We previously accrued deferred purchase price payments totaling $1,901 on the condensed consolidated balance sheets as of December 31, 2016 related to the April 11, 2011 acquisition of certain intellectual property and other assets from the seller, Omnifrio Beverage Company LLC (“Omnifrio”). On March 31, 2017, we entered into a settlement and release agreement with Omnifrio in which we agreed to a cash payment of $710 to Omnifrio and to transfer all intellectual property and other assets purchased from Omnifrio in April 2011 back to Omnifrio. The settlement resulted in a gain of $1,191, reported within non-recurring and acquisition-related costs on the condensed consolidated statements of operations for the nine months ended September 30, 2017.

Texas Regional Operator Litigation/Arbitration

On August 8, 2014, a lawsuit was commenced against us by our regional operators Artesia Springs, LLC, HOD Enterprises, L.P., and BBB Water, Inc. (the “ROs”) in Texas. DS Services of America, Inc. was also named as a defendant in the lawsuit. The claims alleged against us in the lawsuit were breach of contract, conspiracy and fraud, and the ROs sought unspecified monetary damages as well as injunctive relief. On April 10, 2015, the ROs initiated an arbitration proceeding with the American Arbitration Association (the “AAA”). We resolved the claims asserted by BBB Water, Inc. as of December 31, 2015, and BBB Water, Inc. was no longer a party to the arbitration proceedings.

We entered into a settlement and mutual release agreement with Artesia Springs, LLC and HOD Enterprises, L.P. on April 5, 2017, pursuant to which we agreed to make payments including interest in each of April, July and September 2017 totaling $3,783. The settlement resulted in other expense of $3,701, reported within non-recurring and acquisition-related costs on the condensed consolidated statements of operations for the nine months ended September 30, 2017. The settlement also resulted in interest expense of $21 and $82 for the three and nine months ended September 30, 2017, respectively.

Prism Arbitration

On August 5, 2014, Primo Distribution, LLC (“Prism Distribution”) initiated an arbitration proceeding against us, claiming less than $1,000 in damages for alleged breach of contract. The arbitration was filed with the AAA, and was amended on December 19, 2014 to include additional claims for conversion, unfair and deceptive trade practices, fraud, and unjust enrichment.

On July 24, 2017, we entered into a settlement and mutual release agreement with Prism Distribution pursuant to which we agreed to make a payment to Prism Distribution of $825. The settlement resulted in expense of $825, reported within non-recurring and acquisition-related costs on the condensed consolidated statements of operations for the nine months ended September 30, 2017.

Sales Tax

We routinely purchase equipment for use in operations from various vendors. These purchases are subject to sales tax depending on the equipment type and local sales tax regulations; however, we believe certain vendors have not assessed the appropriate sales tax. For purchases that are subject to sales tax in which we believe the vendor did not assess the appropriate amount, we accrue an estimate of the sales tax liability we ultimately expect to pay.

Other Contingencies

From time to time, we are involved in various claims and legal actions that arise in the normal course of business. Management believes that the outcome of such claims and legal actions will not have a significant adverse effect on our financial position, results of operations or cash flows.

8. Income Tax (Benefit) Provision

On December 22, 2017, the Tax Cuts and Jobs Act (the “2017 Tax Act”) was signed into law and made broad and complex changes to the U.S. tax code. The 2017 Tax Act reduced the U.S. federal corporate income tax rate from 35% to 21%. The 2017 Tax Act also established new tax laws that went into effect in 2018. ASC 740 requires a company to record the effects of a tax law change in the period of enactment, however, shortly after the enactment of the 2017 Tax Act, the SEC staff issued SAB 118, which allows a company to record a provisional amount when it does not have the necessary information available, prepared, or analyzed in reasonable detail to complete its accounting for the changes in the tax laws. The measurement period ends when we have obtained, prepared and analyzed the information necessary to finalize its accounting, but cannot extend beyond one year. We are continuing to gather additional information related to estimates surrounding the remeasurement of deferred taxes to more precisely compute the remeasurement of deferred taxes and the impact of the transition tax.

Although we have incurred operating losses since inception, during the first and second quarters of 2018, we recorded income tax benefits related to the federal net operating loss and interest expense limitation, which can be carried forward indefinitely as a result of the 2017 Tax Act.

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During the third quarter of 2018, as described in Note 3 – Impairment Charges and Other, we recorded a $60,750 impairment for the Glacier trade name as a result of the Re-branding Strategy. We recorded an income tax benefit of $4.1 million in the third quarter of 2018 associated with this impairment, noting that our tax benefit is limited to the amount of previously recorded tax expense.

During the third quarter of 2018, we completed our assessment regarding the deductibility of certain performance-based compensation plans under the 2017 Tax Act, resulting in the reversal of $1.7 million of tax benefit recorded in the second quarter of 2018. As noted in our Form 10-Q for the second quarter of 2018, the tax benefit recorded in that quarter was provisional and subject to adjustment during the measurement period.

For the three and nine months ended September 30, 2017, there was $451 and $823, respectively, of income tax expense recognized related to goodwill and intangibles.

Section 382 of the U.S. Internal Revenue Code imposes an annual limitation on the amount of net operating loss carryforwards that might be used to offset taxable income when a corporation has undergone significant changes in stock ownership. We believe our prior ownership changes have created an annual limit, imposed by Section 382, on the amount of net operating loss we can utilize in a given year. Realization of the loss carryforwards is dependent upon generating sufficient taxable income prior to the expiration of the loss carryforwards, subject to the Section 382 limitation.

9. Fair Value Measurements

Fair value rules currently apply to all financial assets and liabilities and for certain nonfinancial assets and liabilities that are required to be recognized or disclosed at fair value. For this purpose, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs.

U.S. GAAP establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include:

- Level 1 — quoted prices in active markets for identical assets and liabilities.

- Level 2 — observable inputs other than quoted prices in active markets for identical assets and liabilities.

- Level