

Recology Western Oregon - North Coast Collections Inc.

(A Wholly - Owned Subsidiary of Recology Inc.)

Financial Statements

December 31, 2019

(With Independent Accountant's Review Report)



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INDEPENDENT ACCOUNTANT'S REVIEW REPORT

To the Board of Directors of
Recology Western Oregon - North Coast Collections Inc.
McMinnville, Oregon

We have reviewed the accompanying financial statements of Recology Western Oregon - North Coast Collections Inc., which comprise the balance sheet as of December 31, 2019 and the related statements of earnings and stockholder's investment, and cash flows for the year then ended, and the related notes to the financial statements. A review includes primarily applying analytical procedures to management's financial data and making inquiries of company management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement whether due to fraud or error.

Accountant's Responsibility

Our responsibility is to conduct the review engagement in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the AICPA. Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. We believe that the results of our procedures provide a reasonable basis for our conclusion.

Accountant's Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

Supplementary Information

The supplementary information included in the Schedule of Expenses is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the financial statements. The supplementary information has been subjected to the review procedures applied in our review of the basic financial statements. We are not aware of any material modifications that should be made to the supplementary information. We have not audited the supplementary information and do not express an opinion on such information.

Change in Accounting Principle

As described in Note 1 in the financial statements, the Company adopted Accounting Standards Codification Topic 606 as of January 1, 2019. Our opinion is not expressed on this matter.

Armanino LLP
Armanino^{LLP}
San Ramon, California

March 31, 2020



An independent firm
associated with Moore
Global Network Limited

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.

(A Wholly - Owned Subsidiary of Recology Inc.)

Balance Sheet

December 31, 2019

ASSETS

Current assets:

Accounts receivable, net of allowance for doubtful accounts of \$25,069	\$ 1,038,772
Prepaid expenses	64,374
Due from parent	367,018
Total current assets	<u>1,470,164</u>

Property and equipment:

Building and improvements	2,642
Machinery and equipment	6,437
Less accumulated depreciation	<u>(8,705)</u>
Property and equipment, net	<u>374</u>
Total assets	<u>\$ 1,470,538</u>

LIABILITIES AND STOCKHOLDER'S INVESTMENT

Current liabilities:

Accounts payable	\$ 22,716
Accrued liabilities	168,842
Deferred revenues	<u>230,880</u>
Total current liabilities	<u>422,438</u>

Stockholder's investment, net

Stockholder's investment, net	<u>1,048,100</u>
Total liabilities and stockholder's investment	<u>\$ 1,470,538</u>

See accompanying notes to financial statements and independent accountant's review report.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
(A Wholly - Owned Subsidiary of Recology Inc.)
Statement of Earnings and Stockholder's Investment
For the Year Ended December 31, 2019

Revenues	<u>\$ 11,533,639</u>
Cost of operations	
Disposal costs	2,831,079
Labor costs	2,045,291
Operational expenses	<u>3,519,970</u>
Total cost of operations	<u>8,396,340</u>
Gross profit	3,137,299
General and administrative expenses	<u>1,782,844</u>
Earnings from operations	<u>1,354,455</u>
Other income	
Interest income	<u>7,782</u>
Net earnings	<u>7,782</u>
	1,362,237
Stockholder's investment, net, beginning of year	975,510
Net distributions to parent and affiliates	<u>(1,289,647)</u>
Stockholder's investment, net, end of year	<u>\$ 1,048,100</u>

See accompanying notes to financial statements and independent accountant's review report.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
(A Wholly - Owned Subsidiary of Recology Inc.)
Statement of Cash Flows
For the Year Ended December 31, 2019

Cash flows from operating activities:	
Net earnings	\$ 1,362,237
Adjustments to reconcile net earnings to net cash provided by operating activities:	
Depreciation	264
Changes in assets and liabilities:	
Accounts receivable	(35,407)
Prepaid expenses	(1,683)
Due from parent	(36,457)
Accounts payable	(19,015)
Accrued liabilities	16,467
Deferred revenues	<u>3,241</u>
Net cash provided by operating activities	<u>1,289,647</u>
Cash flows from financing activities:	
Net distribution to parent and affiliates	<u>(1,289,647)</u>
Net change in cash	-
Cash, beginning of year	<u>-</u>
Cash, end of year	<u>\$ -</u>

See accompanying notes to financial statements and independent accountant's review report.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
(A Wholly - Owned Subsidiary of Recology Inc.)
Notes to Financial Statements
December 31, 2019

1. ACCOUNTING POLICIES

Organization

Recology Western Oregon - North Coast Collections Inc. (the "Company"), is a wholly - owned subsidiary of Recology Oregon Inc., which is a wholly - owned subsidiary of Recology Inc. (the "Parent" or "Recology"), which in turn is wholly - owned by the Recology Employee Stock Ownership Plan (the "Recology ESOP" or the "ESOP").

Revenue recognition and accounts receivable

The Company recognizes revenue on an accrual basis when services are performed. Deferred revenues primarily consist of revenues billed in advance that are recorded as revenue in the period in which the related services are rendered. The majority of the Company's revenue is subject to rate regulation by the municipalities in which it operates.

The Company's receivables are recorded when billed and represent claims against third parties that will be settled in cash. The carrying value of the Company's receivables, net of the allowance for doubtful accounts, represents their estimated net realizable value. The Company estimates its allowance for doubtful accounts based on several factors, including historical collection trends, type of customer, existing economic conditions and other factors.

Effective January 1, 2019, the Company adopted ASU 2014-09, Revenue from Customers (Topic 606) and Other Assets and Deferred Cost-Contracts with Customers (Subtopic 340-40) noting the timing and pattern of revenue recognition has not significantly changed under the new revenue recognition standard, nor has there been any change to the Company's net income.

Under ASU 2014-09, the Company records revenue when control is transferred to the customer, generally at the time the Company provides a service. While the timing and pattern of revenue recognition remains unchanged, the Company identified certain consideration payable to its customers that is now recorded as a reduction of revenue in accordance with the new revenue recognition standard. These costs were historically recorded as a component of cost of operations and include:

- Payments issued to the Company's municipal customers in accordance with their commercial contracts.

In accordance with the Company's adoption of the new revenue recognition standard, municipal franchise fees were presented as a reduction to revenue for the year ended December 31, 2019.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
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 Notes to Financial Statements
 December 31, 2019

1. ACCOUNTING POLICIES (continued)

Property and equipment

Property and equipment, including major renewals and betterments, are stated at cost. It is the Company's policy to periodically review the estimated useful lives of its property and equipment. Depreciation is calculated on a straight-line basis over the estimated useful lives of assets as follows:

	Estimated useful lives
Buildings	20-40 years
Leasehold improvements	Shorter of lease or useful life
Machinery and equipment	6-8 years
Furniture and fixtures	8 years
Vehicles	9 years
Containers	10 years

Depreciation expense on the above amounted to \$264 for the year ended December 31, 2019. The cost of maintenance and repairs is charged to operations as incurred; significant renewals and betterments are capitalized.

Environmental remediation liabilities

The Company accrues for environmental remediation costs when they become probable and based on its best estimate within a range. If no amount within the range appears to be a better estimate than any other, the low end of such ranges is used. Remediation costs are estimated by environmental remediation professionals based upon site remediation plans they develop and on their experience working with regulatory agencies and the Company's environmental staff and legal counsel. All estimates require assumptions about future events due to a number of uncertainties, including the nature and extent of any contamination, the appropriate remedy or remedies, the final apportionment of responsibility among the potentially responsible parties, if any are identified, the financial viability of other potentially responsible parties, and regulatory agency requirements. Thus, actual costs incurred may differ from the Company's initial estimate. These estimates do not take into account discounts for the present value of total estimated future costs, as the timing of cash payments is not reliably determinable. The Company regularly evaluates the recorded liabilities when additional information becomes available or regulatory changes occur to ascertain whether the accrued amounts are accurate. The Company does not recognize recoverable amounts from other responsible parties or insurance carriers until receipt is deemed probable. No environmental liabilities were accrued at December 31, 2019.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
(A Wholly - Owned Subsidiary of Recology Inc.)
Notes to Financial Statements
December 31, 2019

1. ACCOUNTING POLICIES (continued)

Impairment of long-lived assets

The Company's policy is to review estimated undiscounted future cash flows and other measures of asset value for its operations when events or changes in circumstances indicate the carrying value of an asset may not be fully recoverable. If an asset is deemed impaired, a loss is recognized.

During the year ended December 31, 2019, there were no events or changes in circumstances that indicated the carrying value of an asset was not fully recoverable.

Income taxes

Effective October 1, 1998, the Parent elected to become an S corporation with the Company electing to be treated as a Qualified Subchapter S corporation subsidiary. Under S corporation rules, the Parent's taxable income and losses are passed through to the ESOP, the Parent's sole stockholder, which is exempt from income tax, and the Company is treated as a division of the Parent having no separate income tax obligations. The Parent has not allocated any income tax expense to the Company.

The Company recognizes income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that has a greater than 50% likelihood of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company's accounting policy for evaluating uncertain tax positions is to accrue estimated benefits or obligations relating to those positions.

The Company records interest related to unrecognized tax benefits as interest expense and penalties as an administrative expense. For the year ended December 31, 2019, there was no interest or penalties recorded because the Company has no uncertain tax positions that meet the more likely than not threshold.

Cash concentration account

The Company's bank account is linked to the Parent's concentration account. Cash balances (or deficits) at the end of each day are automatically transferred to (or from) the concentration account, so that at the end of any particular day, as well as at year-end, the Company's bank account has a zero balance, with related amounts debited or credited to the underlying intercompany account.

Allocations

The Company includes allocated charges from the Parent and affiliates in operating expenses. The charges are allocated by applying activity appropriate factors to direct and indirect costs of the Parent and affiliates or based upon established fees.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
(A Wholly - Owned Subsidiary of Recology Inc.)
Notes to Financial Statements
December 31, 2019

1. ACCOUNTING POLICIES (continued)

Use of estimates

Management of the Company has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. The more significant estimates requiring the judgment of management include the valuation of the allowance for doubtful accounts and accrued franchise fees. Actual results could differ from those estimates.

Stockholder's investment

The Company has 100,000 shares of common stock authorized and 1,000 shares issued and outstanding with no par value as of December 31, 2019. Stockholder's investment, net is comprised of the legal capital plus cumulative contributions net of distributions.

Fair value of financial instruments

The carrying amounts reported in the balance sheet of the assets and liabilities, which are considered to be financial instruments (such as receivables, accounts payable, and accrued liabilities), approximate their fair value based upon current market indicators.

Concentration of credit risk

Cash and accounts receivable are financial instruments that potentially expose the Company to credit risk. The Company's bank account is linked to the Parent's concentration account. Cash balances (or deficits) at the end of each day are automatically transferred to (or from) the concentration account. Management believes that the Company is not exposed to any significant risk on cash. During the year ended December 31, 2019, three jurisdictions accounted for 76% of accounts receivable.

2. OPERATIONS

The Company collects refuse and recyclables in Northwest Oregon and along the Northern Oregon coast. The Company's refuse collection rates are set by these municipalities. The rate setting process may result in the disallowance of certain costs and/or delays in cost recovery, as well as differences in the timing of when revenues and expenses are recognized.

During the year ended December 31, 2019, the Company disposed of the yard debris collected by its operations at both a transfer station owned and operated by an affiliate and an independent third party. All refuse was disposed at an affiliate and an independent third party.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
(A Wholly - Owned Subsidiary of Recology Inc.)
Notes to Financial Statements
December 31, 2019

3. COMMITMENTS AND CONTINGENCIES

Substantially all of the assets of the Company are pledged to secure the obligations of the Parent. The Company, along with the Parent and the Parent's wholly - owned subsidiaries, has guaranteed the repayment, on a joint and several basis, of any and all obligations under the Parent's Revolving Credit Agreement. The Company could be required to honor the guarantee upon an uncured default event, as defined in the Parent's Revolving Credit Agreement. The Parent's Revolving Credit Agreement expires on April 21, 2022. At September 30, 2019, there was an outstanding balance of \$142.5 million on the Parent's Revolving Credit Agreement and there were standby letters of credit issued for \$254.9 million. The Parent has represented to the Company that it is in compliance with all covenants of the Revolving Credit agreement.

The Company, along with the Parent and the Parent's wholly - owned subsidiaries, has guaranteed the payment of amounts owed to unrelated third parties, which provided the equipment financing to affiliates of the Company. The affiliates are obligated to the unrelated third parties with various expiration dates through August 2025. At September 30, 2019, the outstanding principal on the financed equipment recorded by the affiliates was \$49.2 million.

The Company and the Parent are involved in various legal actions arising in the normal course of business. It is the Company's opinion that these matters are adequately provided for or that the resolution of such matters will not have a material adverse impact on the financial position or results of operations of the Company or the Parent.

4. PROPERTY AND EQUIPMENT OBLIGATIONS

The Company has cancelable agreements with an affiliate whereby it pays for the use of certain operating equipment. Future annual payments for continued use of the property and equipment, and in aggregate, as of December 31, 2019 are as follows:

Year ending December 31:	<u>Property</u>	Vehicles and <u>Equipment</u>	<u>Total</u>
2020	\$ 50,125	\$ 819,989	\$ 870,114
2021	50,125	812,885	863,010
2022	50,125	660,268	710,393
2023	50,125	562,523	612,648
2024	8,544	454,270	462,814
Thereafter	<u>-</u>	<u>382,735</u>	<u>382,735</u>
Total payments	<u>\$209,044</u>	<u>\$3,692,670</u>	<u>\$3,901,714</u>

Rental expense for the year ended December 31, 2019 was \$844,521 including amounts under short-term rental agreements with third parties and affiliates.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
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Notes to Financial Statements
December 31, 2019

4. PROPERTY AND EQUIPMENT OBLIGATIONS (continued)

Under the terms of the equipment lease agreement with an affiliate, and in accordance with existing rate policies, the Company may continue to use certain equipment under operating leases without a related payment once the affiliate's equipment cost and related interest have been funded through operating lease payments.

5. TRANSACTIONS WITH RELATED PARTIES

During the year ended December 31, 2019, operating and other expenses of the Company included allocated charges from the Parent and affiliates. Such charges are based upon the direct and indirect costs of the Parent and affiliates, or established fees, and allocated based on specific activities. The allocated charges are as follows:

Parent:	
Health insurance	\$ 450,180
Worker's compensation	42,066
401(k) employer portion	59,376
General and vehicle insurance	<u>137,227</u>
	<u>688,849</u>
Affiliates:	
Collection revenue	(828,947)
Rental of equipment	740,091
Disposal costs	2,315,780
Processing fees	490,410
General administration allocation	1,072,852
Truck and garage	846,664
Regional management and accounting fees	<u>372,257</u>
	<u>5,009,107</u>
Total	<u>\$5,697,956</u>

During the year ended December 31, 2018, amounts due from or payable to Parent and affiliates were accumulated by the Company and as of the Parent's fiscal year-end, September 30, 2019, the net amount was settled by way of capital contributions or distributions. Changes in amounts due from or payable to Parent or affiliates are presented as an operating activity in the statement of cash flows, except as related to expenditures attributable to property and equipment. For the three months from October 1, 2019 to December 31, 2019, the net amount was not settled by way of capital contributions or distributions.

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.
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Notes to Financial Statements
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6. EMPLOYEE STOCK OWNERSHIP PLAN

In 1986, the Parent established an employee stock ownership plan and trust, which purchased all of the Parent's outstanding stock. The ESOP is a noncontributory plan that covers substantially all of the employees of the Company and other Recology subsidiaries. Employees, except under certain conditions, become fully vested after a requirement of three years of service. No vesting occurs until the full service requirement is satisfied.

The Parent's common stock is not traded on an established market. Presently, all shares are held by the ESOP. All distributions will be made from the ESOP in cash, which is received from Recology, or shares, subject to immediate repurchase by Recology. A participant who is vested is entitled to begin receiving a distribution from his or her ESOP account at a future date following his or her termination of employment. Distributions may be made in a lump-sum, equal annual installments over a period generally not to exceed five years, or a combination of the foregoing, generally as determined by the ESOP Administrative Committee (the Committee). The Committee also generally determines the timing and manner of distributions, subject to the following limitations: (i) in the event of a participant's retirement, disability, or death, distribution must begin prior to September 30 of the plan year following the plan year in which employment terminates; and (ii) if a participant's employment terminates for any other reason, distribution must begin prior to September 30 of the sixth plan year following the plan year in which employment terminates, although the Committee may further defer distributions that are not attributable to post-1986 shares until the participant reaches the age that he or she would be required to reach in order to qualify for retirement under the ESOP. Each participant who has attained age 55 and has participated in the ESOP for at least 10 years may elect to receive cash distributions for in-service withdrawals attributable to post-1986 shares allocated to his or her account. An eligible participant is entitled to elect payment attributable to as much as 25% of his or her eligible shares during the first five years of election and up to 50% of eligible shares in the sixth year. The cash distributions are based upon the appraised value of Recology stock and other assets, if any, as of the most recent valuation of the participant's account.

The Parent makes contributions to the ESOP to make benefit payments to eligible participants under the Plan.

7. SUBSEQUENT EVENTS

On March 11, 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic and recommended containment and mitigation measures worldwide. The COVID-19 outbreak in the United States has caused business disruption through mandated and voluntary closings of businesses and shelter in place orders. While the disruption is currently expected to be temporary, there is considerable uncertainty around the duration of the closings and shelter in place orders. It is at least reasonably possible that this matter will negatively impact the Company. However, the financial impact and duration cannot be reasonably estimated at this time.

The Company has evaluated subsequent events through March 31, 2020, the date the financial statements were available to be issued and is not aware of any material modifications that should be made to these financial statements for them to be in conformity with generally accepted accounting principles.

SUPPLEMENTARY INFORMATION

RECOLOGY WESTERN OREGON - NORTH COAST COLLECTIONS INC.

(A Wholly - Owned Subsidiary of Recology Inc.)

Schedule of Expenses

For the Year Ended December 31, 2019

Operational expenses	
Contract labor	\$ 2,698
Depreciation	264
Fuel	463,989
Insurance	137,227
Supplies	65,947
Freight	3,557
Operational lease expense	844,521
Recycling processing costs	490,410
Repair and maintenance	1,297,408
Taxes and licenses	189,564
Other operational expenses	24,385
Total operational expenses	<u>\$ 3,519,970</u>

General and administrative expenses	
General administration allocation	\$ 1,072,852
Regional management and accounting fees	372,257
Advertising and promotion	11,110
Bad debt	30,595
Contributions	34,825
Billing services	44,504
Dues and subscriptions	10,887
Education and training	4,751
Bank service charges	36,477
Meals	9,374
Office supplies	20,226
Postage	21,252
Professional services	20,512
Telephone	69,480
Travel	15,564
Other administration	8,178
Total general and administrative expenses	<u>\$ 1,782,844</u>