

AVALON HOLDINGS CORP  
Form 10-Q  
November 08, 2018

**2018**

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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**FORM 10-Q**

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

**For the quarterly period ended September 30, 2018**

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 1-14105

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**AVALON HOLDINGS CORPORATION**

(Exact name of registrant as specified in its charter)

**Ohio**  
(State or other jurisdiction  
of incorporation or organization)

**34-1863889**  
(I.R.S. Employer  
Identification No.)

**One American Way, Warren, Ohio 44484-5555**  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(330) 856-8800**

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

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

Indicate by a check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See 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 a check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

The registrant had 3,191,100 shares of its Class A Common Stock and 612,231 shares of its Class B Common Stock outstanding as of November 2, 2018.

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**AVALON HOLDINGS CORPORATION AND SUBSIDIARIES**

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**SIGNATURE**

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**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****AVALON HOLDINGS CORPORATION AND SUBSIDIARIES****Condensed Consolidated Statements of Operations (Unaudited)***(in thousands, except per share amounts)*

	<b>Three Months Ended September 30, 2018</b>		<b>Nine Months Ended September 30, 2018</b>	
	<b>2018</b>	<b>2017</b>	<b>2018</b>	<b>2017</b>
Net operating revenues:				
Waste management services	\$12,557	\$10,831	\$32,525	\$27,934
Food, beverage and merchandise sales	2,285	2,326	5,531	5,702
Other golf and related operations	3,306	3,207	8,313	8,007
Total golf and related operations	5,591	5,533	13,844	13,709
Total net operating revenues	18,148	16,364	46,369	41,643
Costs and expenses:				
Waste management services operating costs	9,863	8,792	25,615	22,219
Cost of food, beverage and merchandise	992	970	2,391	2,484
Golf and related operations operating costs	3,337	3,090	8,700	8,646
Depreciation and amortization expense	732	747	2,187	2,256
Selling, general and administrative expenses	2,297	2,240	6,737	6,305
Operating income (loss)	927	525	739	(267 )
Other income (expense):				
Interest expense	(167 )	(176 )	(512 )	(528 )
Other income, net	45	50	218	236
Income (loss) before income taxes	805	399	445	(559 )
Provision for income taxes	52	29	112	81
Net income (loss)	753	370	333	(640 )
Less net loss attributable to non-controlling interest in subsidiary	(96 )	(177 )	(340 )	(382 )
	\$849	\$547	\$673	\$(258 )

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Net income (loss) attributable to Avalon Holdings Corporation common shareholders

Income (loss) per share attributable to Avalon Holdings Corporation common shareholders:

Basic net income (loss) per share	\$0.22	\$0.14	\$0.18	\$(0.07 )
Diluted net income (loss) per share	\$0.21	\$0.14	\$0.17	\$(0.07 )
Weighted average shares outstanding - basic	3,803	3,803	3,803	3,803
Weighted average shares outstanding - diluted	4,049	3,817	3,895	3,803

*See accompanying notes to unaudited condensed consolidated financial statements.*

**AVALON HOLDINGS CORPORATION AND SUBSIDIARIES****Condensed Consolidated Balance Sheets (Unaudited)***(in thousands, except per share amounts)*

	<b>September 30, 2018</b>	<b>December 31, 2017</b>
<b>Assets</b>		
Current Assets:		
Cash and cash equivalents	\$ 1,800	\$ 1,025
Accounts receivable, less allowance for doubtful accounts of \$268 in 2018 and \$237 in 2017	11,334	9,906
Unbilled membership dues receivable	774	580
Inventories	881	850
Prepaid expenses	565	512
Other current assets	35	34
Total current assets	15,389	12,907
Property and equipment, net	45,169	43,215
Leased property under capital leases, net	6,198	6,360
Restricted cash	1,326	2,826
Noncurrent deferred tax asset	8	8
Other assets, net	55	62
Total assets	\$ 68,145	\$ 65,378
<b>Liabilities and Equity</b>		
Current liabilities:		
Current portion of obligations under capital leases	\$ 234	\$ 212
Current portion of long-term debt	570	547
Accounts payable	9,755	7,832
Accrued payroll and other compensation	1,020	739
Accrued income taxes	56	26
Other accrued taxes	340	372
Deferred membership dues revenue	3,351	2,718
Other liabilities and accrued expenses	761	658
Total current liabilities	16,087	13,104
Long-term debt, net of current portion	10,314	10,745
Obligations under capital leases, net of current portion	734	857
Asset retirement obligation	100	100
Equity:		
Avalon Holdings Corporation Shareholders' Equity:		
Class A Common Stock, \$.01 par value	32	32
Class B Common Stock, \$.01 par value	6	6



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Paid-in capital	58,970	58,965
Accumulated deficit	(19,884 )	(20,557 )
Total Avalon Holdings Corporation Shareholders' Equity	39,124	38,446
Non-controlling interest in subsidiary	1,786	2,126
Total equity	40,910	40,572
Total liabilities and equity	\$ 68,145	\$ 65,378

*See accompanying notes to unaudited condensed consolidated financial statements.*

**AVALON HOLDINGS CORPORATION AND SUBSIDIARIES****Condensed Consolidated Statement of Shareholders' Equity (Unaudited)***(in thousands)***For the Nine Months Ended September 30, 2018**

	Shares		Common Stock		Paid-in	Accumulated	Total	Non-	
	Class	Class	Class	Class	Capital	Deficit	Avalon	controlling	
	A	B	A	B			Shareholders'	Interest	
							Equity	in	
								Subsidiary	Total
Balance at January 1, 2018	3,191	612	\$ 32	\$ 6	\$ 58,965	\$ (20,557 )	\$ 38,446	\$ 2,126	\$ 40,572
Stock options - compensation costs	-	-	-	-	5	-	5	-	5
Net income (loss)	-	-	-	-	-	673	673	(340 )	333
Balance at September 30, 2018	3,191	612	\$ 32	\$ 6	\$ 58,970	\$ (19,884 )	\$ 39,124	\$ 1,786	\$ 40,910

*See accompanying notes to unaudited condensed consolidated financial statements.*

**AVALON HOLDINGS CORPORATION AND SUBSIDIARIES****Condensed Consolidated Statements of Cash Flows (Unaudited)***(in thousands)*

	<b>Nine Months Ended September 30, 2018    2017</b>	
Cash flows from operating activities:		
Net income (loss)	\$333	\$(640 )
Reconciliation of net income (loss) to cash provided by operating activities:		
Depreciation and amortization expense	2,187	2,256
Amortization of debt issuance costs	22	16
Compensation costs - stock options	5	10
Deferred rental income	-	(50 )
Provision for losses on accounts receivable	34	17
Gain from disposal of vehicle	(17 )	-
Change in operating assets and liabilities:		
Accounts receivable	(1,462)	771
Unbilled membership dues receivable	(194 )	(278 )
Inventories	(31 )	(152 )
Prepaid expenses	(49 )	(114 )
Other assets	(4 )	(4 )
Accounts payable	1,338	(1,237)
Accrued payroll and other compensation	281	300
Accrued income taxes	30	(41 )
Other accrued taxes	(45 )	(152 )
Deferred membership dues revenue	613	546
Other liabilities and accrued expenses	103	87
Net cash provided by operating activities	3,144	1,335
Cash flows from investing activities:		
Capital expenditures	(2,012)	(1,464)
Acquisition of Boardman Tennis Center facility	(1,269)	-
Proceeds from disposal of vehicle	17	-
Net cash used in investing activities	(3,264)	(1,464)
Cash flows from financing activities:		
Payments of debt issuance costs	(5 )	(42 )
Principal payments on term loan facility	(422 )	(399 )
Principal payments on capital lease obligations	(178 )	(193 )
Net cash used in financing activities	(605 )	(634 )

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Decrease in cash, cash equivalents and restricted cash	(725 )	(763 )
Cash, cash equivalents and restricted cash at beginning of period	3,851	5,204
Cash, cash equivalents and restricted cash at end of period	\$3,126	\$4,441

Supplemental disclosure of cash flow information:

Significant non-cash operating and investing activities:

Capital expenditures included in accounts payable	\$585	\$97
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Significant non-cash investing and financing activities:

Capital lease obligations incurred	\$77	\$630
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Cash paid during the period for interest	\$490	\$512
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Cash paid during the period for income taxes	\$82	\$122
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*See accompanying notes to unaudited condensed consolidated financial statements.*

## **AVALON HOLDINGS CORPORATION AND SUBSIDIARIES**

### **Notes to Unaudited Condensed Consolidated Financial Statements**

**September 30, 2018**

#### **Note 1. Description of Business**

Avalon Holdings Corporation (“Avalon” or the “Company”) was formed on April 30, 1998 as a subsidiary of American Waste Services, Inc. (“AWS”). On June 17, 1998, AWS distributed, as a special dividend, all of the outstanding shares of capital stock of Avalon to the holders of AWS common stock on a pro rata and corresponding basis.

Avalon provides waste management services to industrial, commercial, municipal and governmental customers in selected northeastern and midwestern U.S. markets, captive landfill management services and salt water injection well operations. In addition, Avalon owns Avalon Clubs and Resorts, Inc. (“ACRI”), which includes the operation and management of three golf courses and associated clubhouses, recreation and fitness centers, tennis courts, spa services, dining and banquet facilities and a travel agency. ACRI also owns and operates a hotel and related amenities including dining, banquet and conference facilities, fitness center, indoor junior Olympic size swimming pool and tennis courts.

#### **Note 2. Basis of Presentation**

The unaudited condensed consolidated financial statements of Avalon and related notes included herein have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted consistent with such rules and regulations. The accompanying unaudited condensed consolidated financial statements and related notes should be read in conjunction with the consolidated financial statements and related notes included in Avalon’s 2017 Annual Report to Shareholders.

The unaudited condensed consolidated financial statements include the accounts of Avalon, its wholly owned subsidiaries and those companies in which Avalon has managerial control. All significant intercompany accounts and transactions have been eliminated in consolidation.

In the opinion of management, these unaudited condensed consolidated financial statements include all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the financial position of Avalon as of September 30, 2018, and the results of its operations and cash flows for the interim periods presented.

The operating results for the interim periods are not necessarily indicative of the results to be expected for the full year.

### **Note 3. Recent Accounting Pronouncements**

#### *Adopted Accounting Standards*

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, *Revenue from Contracts with Customers* (“ASU 2014-09”). ASU 2014-09 clarifies the principles used to recognize revenue for all entities. ASU 2014-09 provides a unified five-step model to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration for which the entity expects to be entitled in exchange for those goods or services. The new standard replaces most of the existing revenue recognition standards in U.S. GAAP. In addition, in March 2016, the FASB issued ASU 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, which clarifies how to apply revenue recognition guidance related to whether an entity is a principal or an agent. On January 1, 2018, the Company adopted ASU 2014-09 and ASU 2016-08, and all related amendments using the modified retrospective method. The adoption did not result in an impact to the way the Company records revenue and as such did not result in period reclassifications to or from revenue or its associated costs. As a result of the adoption, the Company separately disclosed contract assets, in our Condensed Consolidated Balance Sheets at September 30, 2018 and December 31, 2017 and associated cash flows in our Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and 2017. The Company does not expect the adoption to have a material impact on an ongoing basis (See Note 5).

In August 2016, the FASB issued ASU 2016-15, *Classification of Certain Cash Receipts and Cash Payments* (“ASU 2016-15”), which is intended to reduce diversity in practice in how certain cash receipts and payments are presented and classified in the statement of cash flows. The standard provides guidance in a number of situations including, among others, settlement of zero-coupon bonds, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, and distributions received from equity method investees. ASU 2016-15 also provides guidance for classifying cash receipts and payments that have aspects of more than one class of cash flows. On January 1, 2018, the Company adopted ASU 2016-15. The adoption of this standard did not have an impact on Avalon’s financial position, results of operations or financial statement disclosures.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows: Restricted Cash* (“ASU 2016-18”), which requires entities to include restricted cash and restricted cash equivalent balances with cash and cash equivalent balances in the statement of cash flows. On January 1, 2018, the Company adopted ASU 2016-18. The adoption of ASU 2016-18 impacted the presentation of our Condensed Consolidated Statements of Cash Flows and resulted in additional disclosure in our Notes to Unaudited Condensed Consolidated Financial Statements for the restricted cash related to the loan proceeds deposited into our project fund account that have not yet been utilized to fund the additional renovation and expansion of The Avalon Inn (See Note 4).

In January 2017, the FASB issued ASU 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business* (“ASU 2017-01”). The purpose of ASU 2017-01 is to change the definition of a business to assist entities with evaluating when a set of transferred assets and activities is a business. The Company adopted ASU 2017-01 on January 1, 2018. The acquisition of the Boardman Tennis Center facility, acquired in March 2018, was accounted for in accordance with ASU 2017-01 (See Note 16).

In March 2018, the FASB issued ASU 2018-05, *Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118* (“ASU 2018-05”). ASU 2018-05 adds the SEC guidance released on December 22, 2017 regarding the Tax Cuts and Jobs Act (the “Tax Act”) to the FASB Accounting Standards Codification. ASU 2018-05 provides additional guidance allowing companies to use a one year measurement period to account for the impacts of the Tax Act in their financial statements. The Company adopted ASU 2018-05 in March 2018. The Company has accounted for the impacts of the Tax Act, including the use of reasonable estimates where necessary. The Company may continue to refine its estimates throughout the measurement period.

#### *Accounting Standards Not Yet Adopted*

In February 2016, the FASB issued ASU 2016-02, *Leases*. The new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required

for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. Avalon is currently reviewing its agreements and in the process of calculating the ROU asset and related lease liability for its golf carts, machinery and equipment for the landfill operations, furniture and fixtures for The Avalon Inn and office copiers under operating leases. The Company is also evaluating the impact the adoption of this guidance will have on its financial position, results of operations, cash flows and related disclosures. Upon adoption, the Company expects that the ROU asset and the lease liability will be recognized in the balance sheets in amounts that will be material.

In June 2016, the FASB issued ASU 2016-13, *Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”), which significantly changes the way entities recognize impairment of many financial assets by requiring immediate recognition of estimated credit losses expected to occur over their remaining life. ASU 2016-13 is effective January 1, 2020, with early adoption permitted January 1, 2019. The adoption of this standard is not expected to have a material impact on Avalon’s financial position, results of operations or financial statement disclosures.



**Note 4. Cash, Cash Equivalents and Restricted Cash**

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents for purposes of the Condensed Consolidated Balance Sheets. Avalon maintains its cash balances in various financial institutions. These balances may, at times, exceed federal insured limits. Avalon has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk relating to its cash and cash equivalents.

Cash and cash equivalents that are restricted as to withdrawal or use under the terms of certain contractual agreements are recorded in restricted cash on the Condensed Consolidated Balance Sheets. Restricted cash consists of loan proceeds deposited into a project fund account to fund costs associated with the renovation and expansion of The Avalon Inn in accordance with the provisions of the loan and security agreement (See Note 9).

In the first quarter of 2018, in accordance with our Term Loan Agreement, the Company withdrew \$1.5 million from the restricted cash account for reimbursement for capital expenditures incurred in 2017 related to The Avalon Inn funded with operating cash. The Company utilized approximately \$1.3 million of those proceeds to fund the acquisition of The Boardman Tennis Center facility (See Note 16).

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported within the Condensed Consolidated Balance Sheets that sum to the total of the same such amounts shown in the Condensed Consolidated Statements of Cash Flows. Cash, cash equivalents and restricted cash consist of the following at September 30, 2018 and December 31, 2017 (in thousands):

	<b>September 30, 2018</b>	<b>December 31, 2017</b>
Cash and cash equivalents	\$ 1,800	\$ 1,025
Restricted cash	1,326	2,826
Cash, cash equivalents and restricted cash	\$ 3,126	\$ 3,851

**Note 5. Revenues****Adoption of ASC Topic 606, “Revenue from Contracts with Customers”**

On January 1, 2018, Avalon adopted the new accounting standard FASB Accounting Standards Codification (“ASC”) 606, *Revenue from Contracts with Customers* (“ASC 606”), and all the related amendments using the modified retrospective method for all contracts. The comparative information has not been adjusted and continues to be reported under Topic 605. The Company's accounting policy has been updated to align with Topic 606, and no significant changes to revenue recognition have occurred as a result of the change. The adoption of ASC 606 did not result in an impact to the way the Company records revenue and as such did not result in period reclassifications to or from revenue or its associated costs. As a result of the adoption, the Company separately disclosed contract assets, further described below, in our Condensed Consolidated Balance Sheets at September 30, 2018 and December 31, 2017 and associated cash flows in our Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and 2017.

### **Revenue Recognition**

The Company identifies a contract when it has approval and commitment from both parties, the rights of the parties are identified, payment terms are identified, the contract has commercial substance and collectability of consideration is probable. Revenue is recognized when obligations under the terms of the contract with our customer are satisfied; generally this occurs with the transfer of control of the good or service to the customer. Revenue is measured as the amount of consideration we expect to receive in exchange for transferring goods or providing services. Sales and other taxes we collect concurrent with revenue-producing activities are excluded from revenue. The Company does not incur incremental costs to obtain contracts or costs to fulfill contracts that meet the criteria for capitalization. In addition, the Company does not have material significant payment terms as payment is received at or shortly after the point of sale.

### *Waste Management Services*

Avalon's waste management services provide hazardous and nonhazardous waste brokerage and management services, captive landfill management services and salt water injection well operations. Waste management services are provided to industrial, commercial, municipal and governmental customers primarily in selected northeastern and midwestern United States markets.

Avalon's waste brokerage and management business assists customers with managing and disposing of wastes at approved treatment and disposal sites based upon a customer's needs. Avalon provides a service to its customers whereby Avalon, arrange for, and accept responsibility for the removal, transportation and disposal of waste on behalf of the customer.

Avalon's landfill management business provides technical and operational services to customers owning captive disposal facilities. A captive disposal facility only disposes of waste generated by the owner of such facility. The Company provides turnkey services, including daily operations, facilities management and management reporting for its customers. Currently, Avalon manages one captive disposal facility located in Ohio. The net operating revenues of the captive landfill operations are almost entirely dependent upon the volume of waste generated by the owner of the landfill for whom Avalon manages the facility.

Avalon is a minority owner with managerial control over two salt water injection wells and its associated facility. Operations of the salt water injection wells have been temporarily suspended in accordance with the Chief of the Division of Oil and Gas Resources Management order (See Note 15). Due to the temporary suspension of the salt water injection wells, there were no operating revenues for the three and nine months ended September 30, 2018 and 2017.

For the three months ended September 30, 2018 and 2017, the net operating revenues related to waste management services represented approximately 69% and 66%, respectively, of Avalon's total consolidated net operating revenues. For the nine months ended September 30, 2018 and 2017, the net operating revenues related to waste management services represented approximately 70% and 67%, respectively, of Avalon's total consolidated net operating revenues.

For our waste management services contracts, the customer contracts with us to provide a series of distinct waste management services over time which integrates a set of tasks (i.e. removal, transportation and disposal of waste) into a single project. Avalon provides substantially the same service over time and the same method is used to measure the Company's progress toward complete satisfaction of the performance obligation to transfer each distinct service in the series to the customer. The series of distinct waste management services, which are the same over time, meets the series provision criteria, and as such, the Company treats that series as a single performance obligation. The Company

allocates the transaction price to the single performance obligation and recognizes revenue by applying a single measure of progress to that performance obligation. Avalon transfers control of the service over time and, therefore, satisfies the performance obligation and recognizes the revenue over time as the customer simultaneously receives and consumes the benefits provided by Avalon's performance as we perform.

In addition, as the promise to provide services qualifies as a series accounted for as a single performance obligation, the Company applied the practical expedient guidance that allows an entity that is recognizing revenue over time by using an output method to recognize revenue equal to the amount that the entity has the right to invoice if the invoiced amount corresponds directly to the value transferred to the customer. The Company applied the standard's practical expedient that permits the omission of disclosures relating to unsatisfied performance obligations as most of the Company's waste management service contracts (i) have an original expected length of one year or less and (ii) the Company recognizes revenue at the amount to which the Company has the right to invoice for services performed. For contracts with terms that extend beyond a year, variability will be resolved over the remaining term. The nature of the variability is based on a fixed rate for invoices processed and/or tonnages of waste transported and disposed.

Avalon evaluated whether we are the principal (i.e. report revenues on a gross basis) or agent (i.e. report revenues on a net basis). Avalon reports waste management services on a gross basis, that is, amounts billed to our customers are recorded as revenues, and amounts paid to vendors for providing those services are recorded as operating costs. As principal, Avalon is primarily responsible for fulfilling the promise to provide the waste management service for the customer. Avalon accepts credit risk in the event of nonpayment by the customer and is obligated to pay vendors who provide the service regardless of whether the customer pays the Company. Avalon does have a level of discretion in establishing the pricing for its service.

Our payment terms vary by the type and location of our customer and the service offered. Avalon does not have any financing arrangements with its customers. The term between invoicing and when payment is due is not significant.

The Company assesses each contract amendment individually. Typically, amendments made to our contracts do not materially change the terms of the agreement or performance obligation of the Company. The Company accounts for such contract amendments as if it were part of the existing contract as the material terms contained in the contract do not change. In cases where Avalon views there is a material change in the terms of the agreement, the Company will reevaluate and determine if the contract should be viewed as an entirely new contract, replacement contract or a continuation of the existing contract.

Consideration promised in our waste management contracts do not typically include material variable amounts such as discounts, rebates, refunds, credits, price concessions, incentives, penalties or other such items, and, as such, no estimate is made by the Company for such items.

### ***Golf and Related Operations***

Avalon's golf and related operations include the operation and management of three golf courses and associated clubhouses, recreation and fitness centers, tennis courts, spa services, dining and banquet facilities and a travel agency. The golf and related operations also include the operation of a hotel and its related amenities including dining, banquet and conference facilities, fitness center, indoor junior Olympic size swimming pool and tennis courts. Revenues for the golf and related operations consists primarily of food beverage and merchandise sales, membership dues, greens fees and associated cart rentals, room rentals, fitness activities and spa services. Due to adverse weather conditions, net operating revenues relating to the golf courses, which are located in northeast Ohio and Pennsylvania, were minimal during the first three months of 2018 and 2017.

For the three months ended September 30, 2018 and 2017, the net operating revenues related to the golf and related operations represented approximately 31% and 34%, respectively, of Avalon's total consolidated net operating revenues. For the nine months ended September 30, 2018 and 2017, the net operating revenues related to the golf and related operations represented approximately 30% and 33%, respectively, of Avalon's total consolidated net operating revenues.

For Avalon's golf and related operations, the Avalon Golf and Country Club offers membership packages for use of the country club facilities and its related amenities. Membership agreements are a one year noncancellable commitment and pricing varies based on the membership type selected by the customer. Based on the terms and conditions of the membership contract, resignations received within the membership period do not relieve the member of their annual commitment. Memberships automatically renew on the member's anniversary date unless the member resigns for the upcoming membership period prior to the renewal date.

Membership for the Avalon Golf and Country Club does not contain up-front initiation fees or require monthly minimum spending at the facilities. Annual membership dues do not cover the cost of food, beverage or any other ancillary paid services which are made available to the member nor do they typically provide for discounts on these goods or services. Members have no obligation to purchase or utilize any of these additional goods or services. Avalon is not required to provide such goods or services unless requested and paid for at the point of sale by the member.

Under the terms of the contract, Avalon will provide unlimited use and access to the country club facilities. Avalon's performance obligation in the contract is the "stand ready obligation" to provide access to these facilities for the member for the entire membership term. Avalon providing the "stand ready obligation" for use of the facilities to the member over the entire term of the membership agreement represents a single performance obligation of which Avalon expects the member to receive and consume the benefits of its obligation throughout the membership term, and as such, the Company recognizes membership dues on a straight line basis over the term of the contract. The Company applied the standard's practical expedient that permits the omission of disclosures relating to unsatisfied performance obligations for contracts with an original expected length of one year or less as Avalon Golf and Country Club membership agreements are one year in length.

For our hotel operations, Avalon's performance obligation is to provide lodging facilities. The separate components of providing these services (hotel room, toiletry items, housekeeping, and amenities) are not distinct within the context of the contract as they are all highly dependent and interrelated as part of the obligation to provide the lodging facility. Room sales are driven by a fixed fee charged to a hotel guest to stay at The Avalon Inn for an agreed upon period. The Company agrees to provide a room to the hotel guest for a specified time period for that agreed-upon rate. Our hotel room reservations are performance obligations satisfied over time as the hotel guest simultaneously receives and consumes the benefits provided by the hotel. For performance obligations satisfied over time, our hotel operations measure the progress toward complete satisfaction of the performance obligation and recognize revenue proportionately over the course of the customer's stay.

For food, beverage, and merchandise sales, greens fees and associated cart rental, fitness activities, spa services and other ancillary services, the transaction price is the set price charged by the Company for those goods or services. Upon purchase of the good or service, the Company transfers control of the good or service to the customer and the customer immediately consumes the benefits of the Company's performance and, as such, we recognize revenue at the point of sale.

The following table presents our net operating revenues disaggregated by revenue source (in thousands, unaudited). The comparative information for the three and nine months ended September 30, 2017 has not been adjusted and continues to be reported under the previous revenue standard. Sales and other taxes are excluded from revenues.

	<b>Three Months Ended September 30, 2018</b>		<b>Nine Months Ended September 30, 2018</b>	
	<b>2018</b>	<b>2017</b>	<b>2018</b>	<b>2017</b>
Waste management and brokerage services	\$12,009	\$10,261	\$30,779	\$26,271
Captive landfill management operations	548	570	1,746	1,663
Total waste management services revenues	12,557	10,831	32,525	27,934
Food, beverage and merchandise sales	2,285	2,326	5,531	5,702
Membership dues revenue	1,278	1,285	3,871	3,881
Room rental revenue	739	698	1,781	1,578
Greens fees and cart rental revenue	865	849	1,460	1,425
Other revenue	424	375	1,201	1,123
Total golf and related operations revenue	5,591	5,533	13,844	13,709
Total net operating revenues	\$18,148	\$16,364	\$46,369	\$41,643

Avalon does not have operations located outside the United States and, accordingly, geographical revenue information is not presented.

### **Receivables, Net**

Receivables, net, include amounts billed and currently due from customers. The amounts due are stated at their net realizable value. The Company maintains an allowance for doubtful accounts to provide for the estimated amount of receivables that will not be collected. Customer accounts that are outstanding longer than the contractual payment terms are considered past due. Avalon determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, Avalon's previous accounts receivable loss history, the customer's current ability to pay its obligation to Avalon and the condition of the general economy and the industry as a whole. Avalon writes off accounts receivable when they become uncollectible. Payments subsequently received on such receivables are credited to the allowance for doubtful accounts, or to income, as appropriate under the circumstances. The allowance for doubtful accounts was approximately \$0.3 million at September 30, 2018 and \$0.2 million at

December 31, 2017. At September 30, 2018 one customer accounted for 11% of the waste management services segment's receivables and 10% of the consolidated receivables. At December 31, 2017, no one customer accounted for more than 10% of our accounts receivable.

### **Contract Assets**

Contract assets include unbilled membership dues receivables related to the Avalon Golf and Country Club for the customers membership commitment which are billed on a monthly basis over the course of the annual agreement. Such amounts are stated at their net realizable value. Contract assets related to unbilled membership dues are classified as current as revenue related to such agreements is recognized within the annual membership period. Unbilled membership receivables in our Condensed Consolidated Balance Sheets at September 30, 2018 and December 31, 2017 were \$0.8 million and \$0.6 million, respectively.



The following table presents changes in our contract assets during the three and nine months ended September 30, 2018 (in thousands):

	<b>Balance at Beginning of Period</b>	<b>Unbilled Membership Dues</b>	<b>Billings</b>	<b>Balance at End of Period</b>
<b>Three months ended September 30, 2018</b>				
Contract Assets:				
Unbilled membership dues receivable	\$ 1,009	\$ 184	\$(419 )	\$ 774
<b>Nine months ended September 30, 2018</b>				
Contract Assets:				
Unbilled membership dues receivable	\$ 580	\$ 1,475	\$(1,281 )	\$ 774

#### **Contract Liabilities**

Contract liabilities include unrecognized or deferred revenues relating to membership dues. We record deferred revenue when cash payments are received in advance of satisfying our performance obligation. We classify deferred revenue as current based on the timing of when we expect to recognize revenue for the membership commitment based on the Company satisfying the stand ready performance obligation throughout the annual membership period. The unrecognized or deferred revenues related to membership dues in our Condensed Consolidated Balance Sheets at September 30, 2018 and December 31, 2017 were \$3.4 million and \$2.7 million, respectively.

The following table presents changes in our contract liabilities during the three and nine months ended September 30, 2018 (in thousands):

	<b>Balance at Beginning of Period</b>	<b>Revenue Recognized</b>	<b>Billings</b>	<b>Balance at End of Period</b>
<b>Three months ended September 30, 2018</b>				
Contract Liabilities:				
Deferred membership dues revenue	\$ 4,034	\$ 595	\$(1,278 )	\$ 3,351
<b>Nine months ended September 30, 2018</b>				
Contract Liabilities:				

Deferred membership dues revenue                    \$ 2,718      \$4,504    \$ (3,871    ) \$ 3,351

**Note 6. Property and Equipment**

Property and equipment is stated at cost and depreciated using the straight-line method over the estimated useful life of the asset which varies from 10 to 30 years for land improvements; 5 to 50 years in the case of buildings and improvements; and from 3 to 10 years for machinery and equipment, vehicles and office furniture and equipment.

Major additions and improvements are charged to the property and equipment accounts while replacements, maintenance and repairs, which do not improve or extend the life of the respective asset, are expensed as incurred. The cost of assets retired or otherwise disposed of and the related accumulated depreciation is eliminated from the accounts in the year of disposal. Gains or losses resulting from disposals of property and equipment are credited or charged to operations. Interest costs are capitalized on significant construction projects.

Property and equipment at September 30, 2018 and December 31, 2017 consists of the following (in thousands):

	<b>September 30, 2018</b>	<b>December 31, 2017</b>
Land and land improvements	\$ 14,524	\$ 14,318
Buildings and improvements	36,379	34,721
Machinery and equipment	9,577	9,151
Office furniture and fixtures	6,455	6,301
Vehicles	472	467
Construction in progress	1,597	294
	69,004	65,252
Less accumulated depreciation and amortization	(23,835 )	(22,037 )
Property and equipment, net	\$ 45,169	\$ 43,215

At September 30, 2018, the Company did not have any significant fixed contractual commitments for construction projects.

#### **Note 7. Capital Leased Assets**

In November 2003, Avalon entered into a long-term agreement with Squaw Creek Country Club to lease and operate its golf course and related facilities. The lease has an initial term of ten (10) years with four (4) consecutive ten (10) year renewal term options unilaterally exercisable by Avalon. Under the lease, Avalon is obligated to pay \$15,000 in annual rent and make leasehold improvements of \$150,000 per year. Amounts expended by Avalon for leasehold improvements during a given year in excess of \$150,000 will be carried forward and applied to future leasehold improvement obligations. Based upon the amount of leasehold improvements already made, Avalon expects to exercise all its remaining renewal options.

In 2018 and 2017, the golf and related operations entered into leases for a vehicle and golf course maintenance equipment that were determined to be capital leases. The amounts capitalized in the Condensed Consolidated Balance Sheets under the caption “Leased property under capital leases, net” relating to these assets were approximately \$0.8 million at September 30, 2018 and December 31, 2017.

In addition, during 2017, the captive landfill operations entered into a lease for a piece of equipment that was determined to be a capital lease. The amount capitalized in the Condensed Consolidated Balance Sheets under the caption “Leased property under capital leases, net” relating to this asset was approximately \$0.1 million at September 30, 2018 and December 31, 2017.

Leased property under capital leases at September 30, 2018 and December 31, 2017 consists of the following (in thousands):

	<b>September 30, 2018</b>	<b>December 31, 2017</b>
Leased property under capital leases	\$ 11,553	\$ 11,361
Less accumulated amortization	(5,355 )	(5,001 )
Leased property under capital leases, net	\$ 6,198	\$ 6,360

**Note 8. Basic and Diluted Net Income (Loss) per Share**

Basic net income (loss) per share attributable to Avalon Holdings Corporation common shareholders is computed by dividing the net income (loss) by the weighted average number of common shares outstanding, which were 3,803,331 for each period.

Diluted net income (loss) per share attributable to Avalon Holdings Corporation common shareholders is computed by dividing net income (loss) by the weighted average number of common shares outstanding plus any weighted common equivalent shares determined to be outstanding during the period using the treasury method. The weighted common equivalent shares included in the calculation are related to stock options granted by Avalon where the weighted average market price of Avalon's common stock for the period presented is greater than the option exercise price of the stock option.

For the three months ended September 30, 2018 and 2017, the diluted weighted average number of shares outstanding was 4,048,683 and 3,816,726, respectively.

For the nine months ended September 30, 2018, the diluted weighted average number of shares outstanding was 3,895,129. For the nine months ended September 30, 2017, the diluted per share amount reported is equal to the basic per share amount because Avalon was in a net loss position and as a result, such dilution would be considered anti-dilutive. Assuming dilution, the weighted average number of common shares outstanding for the nine months ended September 30, 2017 was 3,844,639.

#### **Note 9. Term Loan and Line of Credit Agreements**

On December 20, 2016, Avalon and certain direct and indirect wholly owned subsidiaries entered into a loan and security agreement (the "Term Loan Agreement") with Laurel Capital Corporation which provides for a \$12.0 million term loan. At closing, \$9.1 million of the proceeds were used to pay off amounts outstanding under the then existing line of credit agreement and associated accrued interest with Home Savings Bank, dated May 21, 2015, as amended, and pay related transaction costs associated with the Term Loan Agreement. The line of credit agreement with Home Savings Bank was terminated in conjunction with the repayment. Remaining proceeds of \$2.9 million under the Term Loan Agreement were deposited in a project fund account to fund costs of renovating and expanding The Avalon Inn. At September 30, 2018 and December 31, 2017, the remaining proceeds of \$1.3 million and \$2.8 million, respectively, are presented in the Condensed Consolidated Balance Sheets as "Restricted cash." On December 4, 2017 the Term Loan Agreement was amended to restate the definition of "Total Fixed Charges" utilized in the calculation of the "Fixed Charge Coverage Ratio."

The \$12.0 million term loan amount is payable in 119 equal monthly installments of principal and interest, based on a fifteen (15) year maturity schedule which commenced on January 20, 2017. The Term Loan Agreement matures on December 20, 2026 at which time the final balloon payment equal to the remaining outstanding principal, interest and fees are due. Borrowings under the Term Loan Agreement bear interest at a fixed rate of 5.35% until the fifth anniversary date of the closing at which time the interest rate will be reset to a fixed rate equal to the greater of (a) 5.35% per annum or (b) the sum of the Index Rate on the date two (2) business days prior to the reset date and 3.95%, provided that the applicable rate shall in no event exceed 7.50% per annum.

Avalon has the right to prepay the amount outstanding under the Term Loan Agreement, in whole or in part, at any time upon payment of the principal amount of the loan to be prepaid plus accrued unpaid interest thereon to the prepayment date, plus an applicable prepayment penalty. The prepayment penalty, expressed as a percentage of the principal of the loan being prepaid, is five percent (5%) on any prepayment in the first five years; four percent (4%) on any prepayment in the sixth and seventh year; three percent (3%) on any prepayment in the eighth and ninth year; and two percent (2%) on any prepayment in the tenth year.

Borrowings are secured by certain real property and related business assets as defined in the Term Loan Agreement. The Term Loan Agreement also contains certain financial and other covenants, customary representations, warranties and events of default. Avalon was in compliance with the Term Loan Agreement covenants at September 30, 2018 and December 31, 2017.

The Company incurred approximately \$191,000 of debt issuance costs in connection with the Term Loan Agreement. These debt issuance costs were capitalized and will be amortized over the life of the Term Loan Agreement. In accordance with ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs*, these costs are presented in the Condensed Consolidated Balance Sheets as a direct reduction from the carrying amount of the term loan liability.

On May 31, 2018, Avalon entered into a new business loan agreement with Home Savings Bank, (the “Line of Credit Agreement”) which provides for a line of credit of up to \$5.0 million maturing on May 31, 2020. Under the Line of Credit Agreement, borrowings in excess of \$1.0 million are subject to a borrowing base which is calculated based off a specific level of eligible accounts receivable of the waste management business as defined in the agreement. The existing line of credit agreement with Home Savings Bank, dated December 20, 2016, as amended, which was entered into concurrently with the Term Loan Agreement, was terminated in conjunction with the new Line of Credit Agreement. No amounts were outstanding under the existing line of credit agreement at termination.

No amounts were drawn under the Line of Credit Agreement at September 30, 2018. Outstanding borrowings under the Line of Credit Agreement bear interest at Prime Rate plus .25%. At September 30, 2018, the interest rate on the Line of Credit Agreement was 5.25%. Effective October 1, 2018, the interest rate on the Line of Credit Agreement increased to 5.50%.

Borrowings under the Line of Credit Agreement are secured by certain business assets of the Company including accounts receivable, inventory and equipment. The Line of Credit Agreement also contains certain financial and other covenants, customary representations, warranties and events of default. Avalon was in compliance with the line of credit agreements covenants at September 30, 2018 and December 31, 2017.

During both the three and nine month periods ended September 30, 2018 and 2017, the weighted average interest rate on outstanding borrowings was 5.35%.

Obligations under the Company’s debt agreements at September 30, 2018 and December 31, 2017 consist of the following (in thousands):

	<b>September 30, 2018</b>		
	<b>Gross Amount</b>	<b>Debt Issuance Costs</b>	<b>Net Amount</b>
Term loan agreement	\$11,042	\$ (158 )	\$ 10,884
Less current portion	589	(19 )	570
Long-term debt	\$10,453	\$ (139 )	\$ 10,314

	<b>December 31, 2017</b>		
	<b>Gross Amount</b>	<b>Debt Issuance Costs</b>	<b>Net Amount</b>
Term loan agreement	\$11,464	\$ (172 )	\$ 11,292

Less current portion	566	(19	)	547
Long-term debt	\$10,898	\$ (153	)	\$ 10,745

Future maturities of long-term debt are as follows (in thousands):

**For the**  
**Twelve**  
**Month**  
**Period**  
**Ending**  
**September**  
**30,**

2019	\$589
2020	621
2021	655
2022	691
2023	728
Thereafter	7,758
Total	\$11,042



## **Note 10. Income Taxes**

During the three month periods ended September 30, 2018 and 2017, net income attributable to Avalon Holdings Corporation shareholders was \$0.8 million and \$0.5 million, respectively. The Company recorded net income attributable to Avalon Holdings Corporation common shareholders of \$0.7 million in the first nine months of 2018 compared with a net loss attributable to Avalon Holdings Corporation common shareholders of \$0.3 million in the first nine months of 2017. Avalon recorded a state income tax provision in both the three and nine month periods ended September 30, 2018 and 2017, which was related entirely to the waste management and brokerage operations. Due to the recording of a full valuation allowance against the Company's federal net deferred tax assets, the overall effective tax rate in both periods reflects taxes owed in certain U.S state jurisdictions. Avalon's income tax on the income (loss) before taxes was offset by a change in the valuation allowance. A valuation allowance is provided when it is more likely than not that deferred tax assets relating to certain federal and state loss carryforwards will not be realized. Avalon continues to maintain a valuation allowance against the majority of its deferred tax amounts until it is evident that the deferred tax asset will be utilized in the future.

On December 22, 2017, legislation commonly known as the Tax Act was signed into law. The Tax Act changes existing U.S. tax law and includes numerous provisions that will affect Avalon, including our income tax accounting, disclosure and tax compliance. The most impactful changes within the Tax Act are those that will reduce the U.S. corporate tax rates, business-related exclusions and deductions and credits. ASC 740, "Income Taxes," requires the effects of changes in tax rates and laws on deferred tax balances to be recognized in the period in which the legislation is enacted. To the extent that a company's accounting for certain income tax effects of the Tax Act is incomplete but for which they are able to determine a reasonable estimate, the company must record a provisional amount in the financial statements. Consequently, as of the date of enactment, and during the nine months ended September 30, 2018, Avalon valued all deferred tax assets and liabilities at the newly enacted Corporate U.S income tax rate. Avalon has a full valuation allowance on its federal deferred tax assets. Avalon is still in the process of estimating the full tax impact and expects to finalize its adoption of this guidance at year end.

## **Note 11. Long-Term Incentive Plan**

The purpose of the Avalon Holdings Corporation 2009 Long-term Incentive Plan (the "Plan") is (a) to improve individual employee performance by providing long-term incentives and rewards to employees of Avalon, (b) to assist Avalon in attracting, retaining and motivating employees and non-employee directors with experience and ability, and (c) to associate the interests of such employees and directors with those of the Avalon shareholders. Under the Plan, 1,300,000 shares have been reserved for the issuance of stock options of which 760,000 options were outstanding at September 30, 2018. The stock options, vest ratably over a five year period and have a contractual term of ten years from the date of grant. At the end of each contractual vesting period, the share price of the Avalon common stock, traded on a public stock exchange (NYSE Amex), must reach a predetermined price within three years following such

contractual vesting period before the stock options are exercisable (See table below). If the Avalon common stock price does not reach the predetermined price, the stock options will either be cancelled or the period will be extended at the discretion of the Board of Directors. In 2018 and 2017, the Board of Directors extended the period of time for certain vested options that were not exercisable due to those options not meeting the predetermined stock price within the three years following the contractual vesting period.

The grant-date fair values of these stock option awards were estimated using the Monte Carlo Simulation. The Monte Carlo Simulation was selected to determine the fair value because it incorporates six minimum considerations; 1) the exercise price of the option, 2) the expected term of the option, taking into account both the contractual term of the option, the effects of employees' expected exercise and post-vesting employment termination behavior, as well as the possibility of change in control events during the contractual term of the option agreements, 3) the current fair value of the underlying equity, 4) the expected volatility of the value of the underlying share for the expected term of the option, 5) the expected dividends on the underlying share for the expected term of the option and 6) the risk-free interest rate(s) for the expected term of the option.

The grant date fair value of the underlying equity was determined to be equal to Avalon's publicly traded stock price as of the grant dates times the sum of the Class A and Class B common shares outstanding.

The expected term, or time until the option is exercised, is typically based on historical exercising behavior of previous option holders of a company's stock. Due to the fact that the Company has had no historical exercising activity, the simplified method is applied. Because of the nature of the vesting described above, the options are separated into five blocks, with each block having its own vesting period and expected term.

The expected volatility was based on the observed historical volatility of Avalon common stock for a period prior to the grant date. There were no expected dividends and the risk-free interest rate was based on yield data for U. S. Treasury securities over a period consistent with the expected term.

The following table is a summary of the stock option activity:

	<b>Number of Options Granted</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Fair Value at Grant Date</b>
Outstanding at January 1, 2018	760,000	2.51	1.00
Options granted	-	-	-
Options exercised	-	-	-
Options cancelled or forfeited	-	-	-
Outstanding at September 30, 2018	760,000	\$ 2.51	\$ 1.00
Options Vested	706,000		
Exercisable at September 30, 2018	706,000		

The stock options vest and become exercisable based upon achieving two critical metrics as follows:

- 1) Contract Vesting Term: The stock options vest ratably over a five year period.
- 2) The Avalon common stock price traded on a public stock exchange (NYSE Amex) must reach the predetermined vesting price within three years after the options become vested under the contractual vesting term.

The table below represents the period and predetermined stock price needed for vesting.

<b>Begins Vesting</b>	<b>Ends Vesting</b>	<b>Predetermined Vesting Price</b>
Block 1 12 months after Grant Dates	48 months after Grant Dates	\$ 3.43
Block 2 24 months after Grant Dates	60 months after Grant Dates	\$ 4.69
Block 3 36 months after Grant Dates	72 months after Grant Dates	\$ 6.43
Block 4 48 months after Grant Dates	84 months after Grant Dates	\$ 8.81
Block 5 60 months after Grant Dates	96 months after Grant Dates	\$ 12.07

In the third quarter of 2018, the predetermined stock price was reached for exercising all vested options that have previously met the time vesting requirement.

Compensation costs were approximately \$1,000 and \$3,000 for the three months ended September 30, 2018 and 2017, respectively, and \$5,000 and \$10,000 for the nine months ended September 30, 2018 and 2017, respectively, based upon the estimated grant date fair value calculations. As of September 30, 2018, there was approximately \$24,000 of total unrecognized compensation costs related to non-vested share-based compensation arrangements granted under the Plan. That cost is expected to be recognized over a weighted-average period of 5.67 years.

#### **Note 12. Legal Matters**

In the ordinary course of conducting its business, Avalon becomes involved in lawsuits, administrative proceedings and governmental investigations, including those related to environmental matters. Some of these proceedings may result in fines, penalties or judgments being assessed against Avalon which, from time to time, may have an impact on its business and financial condition. Although the outcome of such lawsuits or other proceedings cannot be predicted with certainty, Avalon does not believe that any uninsured ultimate liabilities, fines or penalties resulting from such pending proceedings, individually or in the aggregate, will have a material adverse effect on its liquidity, financial position or results of operations (See Note 15).

In August 2018, Avalon filed a complaint in the United States District Court for the Southern District of New York against Guy Gentile and MintBroker International, Ltd (collectively “MintBroker”). The complaint seeks to recover from MintBroker all short-swing trading profits realized through its purchases and subsequent sales of the Avalon Class A Common Stock during the six month period ending on or about August 1, 2018, in accordance with Section 16(b) of the Securities Exchange Act of 1934, as amended, based on MintBroker’s Schedule 13(d), Form 3 and Form 4 filings made with the Securities and Exchange Commission. A court date is tentatively scheduled in December 2018.

### **Note 13. Business Segment Information**

In determining the segment information, Avalon considered its operating and management structure and the types of information subject to regular review by its “chief operating decision maker.” Using the criteria of FASB ASC 280 *Segment Reporting*, Avalon’s reportable segments include waste management services and golf and related operations. Avalon accounts for intersegment net operating revenues as if the transactions were to third parties. The segment disclosures are presented on this basis for all periods presented.

Avalon’s primary business segment, the waste management services segment, provides hazardous and nonhazardous brokerage and management services to industrial, commercial, municipal and governmental customers, captive landfill management for an industrial customer and salt water injection well operations.

Avalon’s golf and related operations segment consists of three golf courses and associated clubhouses which provide dining and banquet facilities, a hotel which provides lodging, dining, banquet and conference facilities, a recreation center and a travel agency. Revenue for the golf and related operations segment consists primarily of membership dues, greens fees, cart rentals, room rentals, merchandise sales, tennis and fitness activities, spa services and food and beverage sales.

Avalon does not have significant operations located outside the United States and, accordingly, geographical segment information is not presented.

For the nine months ended September 30, 2018, no one customer accounted for 10% of Avalon’s consolidated or reportable segment net operating revenues. For the nine months ended September 30, 2017, one customer accounted for 10% of the waste management services segment’s net operating revenues to external customers and 7% of the consolidated net operating revenues.

The accounting policies of the segments are consistent with those described for the consolidated financial statements in the summary of significant accounting policies included in Avalon's 2017 Annual Report to Shareholders. Avalon measures segment profit for internal reporting purposes as income (loss) before taxes.

Business segment information including the reconciliation of segment income before taxes to income (loss) before taxes is as follows (in thousands):

	<b>Three Months Ended September 30, 2018</b>		<b>Nine Months Ended September 30, 2017</b>	
<b>Net operating revenues from:</b>				
Waste management services:				
External customer revenues	\$12,557	\$10,831	\$32,525	\$27,934
Intersegment revenues	-	-	-	-
Total waste management services	12,557	10,831	32,525	27,934
Golf and related operations:				
External customer revenues	5,591	5,533	13,844	13,709
Intersegment revenues	15	12	57	49
Total golf and related operations	5,606	5,545	13,901	13,758
Segment operating revenues	18,163	16,376	46,426	41,692
Intersegment eliminations	(15 )	(12 )	(57 )	(49 )
Total net operating revenues	\$18,148	\$16,364	\$46,369	\$41,643

	<b>Three Months Ended September 30, 2018</b>		<b>Nine Months Ended September 30, 2017</b>	
<b>Income (loss) before income taxes:</b>				
Waste management services	\$1,244	\$624	\$2,768	\$1,852
Golf and related operations	455	674	455	298
Segment income before income taxes	1,699	1,298	3,223	2,150
Corporate interest expense	(154 )	(162 )	(474 )	(490 )
Corporate other income, net	1	2	14	6
General corporate expenses	(741 )	(739 )	(2,318)	(2,225)
Income (loss) before income taxes	\$805	\$399	\$445	\$(559 )

	<b>September 30, 2018</b>	<b>December 31, 2017</b>
<b>Identifiable assets:</b>		
Waste management services	\$ 29,290	\$ 26,449
Golf and related operations	47,819	45,188
Corporate	47,268	49,549
Subtotal	124,377	121,186
Elimination of intersegment receivables	(56,232 )	(55,808 )
Total	\$ 68,145	\$ 65,378

In comparing the total assets at September 30, 2018 with those at December 31, 2017, the increase in total assets of the waste management services segment of \$2.8 million is a result of an increase in intersegment transactions, which are eliminated in consolidation, and an increase in accounts receivable partially offset by a lower net book value of property and equipment as a result of current year depreciation on the salt water injection wells. The increase in total assets of the golf and related operations segment of \$2.6 million is primarily due to the acquisition of the Boardman Tennis Center facility and capital expenditures related to the expansion of The Avalon Inn, and to a lesser extent, an increase in accounts receivable, partially offset by current year depreciation on property and equipment. The decrease in corporate total assets of \$2.3 million is primarily due to a decrease in restricted cash that was released from restriction and subsequently utilized to fund the acquisition of the Boardman Tennis Center facility and a decrease in intersegment transactions, which are eliminated in consolidation, partially offset by an increase in operating cash and cash equivalents.

#### **Note 14. Certain Relationships and Related Transactions**

In August 2013, Avalon created a new Ohio limited liability company, AWMS Holdings, LLC, to act as a holding company to form and own a series of wholly owned subsidiaries that will own and operate Class II salt water injection wells and facilities (together the “facilities”). AWMS Holdings, LLC, offers investment opportunities to accredited

investors by selling membership units of AWMS Holdings, LLC through private placement offerings. The monies received from these offerings, along with internally contributed capital, are used to construct the facilities necessary for the operation of salt water injection wells. AWMS Water Solutions, LLC, a wholly owned subsidiary of Avalon, manages all the salt water injection well operations, including the marketing and sales function and all decisions regarding the well operations for a percentage of the gross revenues.

In 2014 and 2013, Avalon, through a wholly owned subsidiary made capital contributions totaling approximately \$3.4 million, which included cash and certain well assets, including the permits, in exchange for membership units of AWMS Holdings, LLC. Through a private placement offering for the purchase of membership units, AWMS Holdings, LLC raised approximately \$3.8 million from accredited investors in 2014 and 2013. Management and outside directors of Avalon, who qualified as accredited investors, invested approximately \$1.0 million in AWMS Holdings, LLC.



As a result of a private placement offering, Avalon is not the majority owner of AWMS Holdings, LLC. At September 30, 2018 and December 31, 2017, respectively, Avalon owns approximately 47% of AWMS Holdings, LLC. In accordance with ASC 810-10 and related amendment, due to the managerial control of American Water Solutions, LLC, AWMS Holdings, LLC is a variable interest entity, and the financial statements of AWMS Holdings, LLC and subsidiaries are included in Avalon's consolidated financial statements. ASC 810-10 requires noncontrolling interests to be reported as a separate component of equity. The amount of net loss attributable to the noncontrolling interest is recorded in "net loss attributable to noncontrolling interest" in our Condensed Consolidated Statements of Operations.

### **Note 15. Injection Wells Suspension**

As a result of a seismic event with a magnitude of 2.1 occurring on August 31, 2014, the Chief of the Division of Oil and Gas Resources Management ("Chief" or "Division") issued Orders on September 3, 2014, to immediately suspend all operations of both of Avalon's saltwater injection wells. The Orders were based on the findings that the two saltwater injection wells were located in close proximity to an area of known seismic activity and also that the saltwater injection wells pose a risk of increasing or creating seismic activity. The two saltwater injection wells are located approximately 112 feet apart. Based on these findings, the Chief ordered the immediate suspension of all operations of the two saltwater injection wells, until the Division could further evaluate the wells.

On September 5, 2014, Avalon submitted the information required by the Chief's Order in regards to its AWMS #1 injection well, and the Chief lifted the suspension for that well on September 18, 2014. On September 19, 2014, Avalon submitted information and a written plan required by the Chief's Order proposing the establishment of certain operations and management controls on injections at the AWMS #2 injection well. To date, the Division has not responded to that plan despite Avalon's requests for feedback.

On October 2, 2014, Avalon filed an appeal with the Ohio Oil and Gas Commission (the "Commission") disputing the basis for suspending operations of AWMS #2 and also the authority of the Chief to immediately suspend such operations. On March 11, 2015, an appeal hearing was held. The Chief stated during the hearing that the suspension is only temporary, and that he expects that AWMS #2 will be allowed to inject once the state's final policymaking is complete.

On August 12, 2015, the Commission upheld the temporary suspension of injection operations of AWMS #2 stating that the temporary suspension will allow the Chief to more fully evaluate the facts in anticipation of the Division's implementation of a comprehensive regulatory plan that will specifically address injection-induced seismicity. Avalon appealed that decision in September 2015 to the Franklin County Court of Common Pleas, but that appeal was dismissed on a filing technicality. Avalon appealed the dismissal to the Ohio 10th District Court of Appeals, which found the Commission erred in its filing of their decision. Following the Commission's proper notice, Avalon appealed again to the Franklin County Court of Common Pleas (the "Court").

On November 1, 2016 an appeal hearing was held in that Court. On December 23, 2016, the Court issued its Decision and Order in Avalon's favor, and vacated the Commission's decision. The Court found that the Division's suspension and refusal to work with the Company for over 26 months was arbitrary and not in accordance with reason. Subsequent to the ruling, and in accordance with the Court's Decision and Order, both Avalon and the Division submitted their proposed restart plans to the Court. Avalon's plan sets forth both the initial volumes and pressures and increases in volume and pressure while continuously monitoring seismicity and addressing the concerns of public health and safety.

On February 21, 2017, the Court issued its Final Decision and Order. The Court's Final Decision and Order sets conditions for the restarting of AWMS #2 in accordance with the proposed restart plans filed by Avalon with minor revisions. While the Company was making preparations for restarting the well and opening the facility, the Division appealed the Final Decision and Order and filed a Motion to Stay the Court Order on February 22, 2017. The Motion to Stay was granted by the Ohio 10th District Court of Appeals on March 21, 2017. On September 14, 2017, an appeal hearing was held.

On July 31, 2018 the Ohio 10<sup>th</sup> District Court of Appeals issued its decision on the appeal. In the decision, the Ohio 10<sup>th</sup> District Court of Appeals overruled the majority of the Division's assignments of error, but also found that the Franklin County Court of Common Pleas abused its discretion in issuing the restart order for the Company's injection well. The Ohio 10<sup>th</sup> District Court of Appeals therefore reinstated the previous Ohio Oil and Gas Commission decision in this matter.

On September 12, 2018, the Company appealed the Ohio 10<sup>th</sup> District Court of Appeals decision to the Ohio Supreme Court. Avalon will continue in its effort to receive a favorable ruling lifting the temporary suspension. The operations of Company's #2 injection well will remain suspended until that time.

In addition, on August 26, 2016, Avalon filed a complaint in the 11<sup>th</sup> Appellate District Court in Trumbull County, Ohio for a Peremptory Writ of Mandamus to compel the Director of the Ohio Department of Natural Resources (“ODNR”) to initiate appropriations procedures to determine damages from the illegal regulatory taking of the Company’s property, or issue an alternative remedy at law. There is currently no implemented state-wide policy on induced seismicity and The ODNR has refused to communicate with the Company regarding the status and requirements of any policymaking. The Company believes that the actions, and lack of responsible actions, by ODNR, which were triggered by a seismic event that presented no hazard or risk to any individual or to the environment, is a clear violation of the Company’s property rights and a violation of the Fifth and Fourteenth Amendments to the U.S. Constitution; Article I, Section 19 of the Ohio Constitution; and Ohio Revised Code Chapter 163.

The hearing was scheduled to commence on June 25, 2018. On June 8, 2018, the 11<sup>th</sup> Appellate District Court in Trumbull County, Ohio issued a motion to stay all further proceedings in the writ of mandamus action until a ruling is made on the suspension order by the Ohio 10<sup>th</sup> District Court of Appeals. On September 17, 2018, the Company filed a motion to lift the stay in the proceeding based on the Ohio 10<sup>th</sup> District Court of Appeals ruling. To date, the hearing date has not been rescheduled. The ODNR has stated that they will not oppose the lifting of the stay. The Company intends to vigorously pursue the complaint and obtain due process and fair compensation.

At December 31, 2017, in accordance with FASB ASC 360-10-35, *Property, Plant and Equipment – Overall – Subsequent Measurement*, Avalon assessed the recoverability of the carrying values of the salt water injection wells based on the Chief’s decision to temporarily suspend operations of the wells. Avalon believes the suspension order is temporary and will reopen and, as such, the Company estimated future cash flows directly associated with and which are expected to arise as a direct result of the wells once the suspension is lifted. The assumptions used by management in developing the estimates of future cash flows were based on current market conditions and comparable prior periods while in operation. Based on the estimated undiscounted sum of the future cash flows, the net book value of the property, plant and equipment relating to the wells of approximately \$3.7 million at December 31, 2017 was recoverable in less than the estimated remaining useful life of those assets. There were no changes to this assessment at September 30, 2018.

Management continues to consider whether indicators of impairment are present and tests for recoverability, as necessary. Although the Company believes that the suspension order is temporary, there can be no guarantee that the salt water injection wells will resume operations. If management concludes that the suspension is other than temporary and the carrying amount of the salt water injection wells are not recoverable, Avalon may record an impairment charge up to \$3.3 million, the carrying value of the salt water injection wells at September 30, 2018.

## **Note 16. Asset Acquisition**

On March 7, 2018, Avalon, through a newly created subsidiary, Avalon Mahoning Sports Center, Inc., completed the acquisition of the Boardman Tennis Center facility in Boardman, Ohio for approximately \$1.3 million in cash. In accordance with our Term Loan Agreement, the Company withdrew funds from the restricted cash account for reimbursement for capital expenditures incurred in 2017 related to The Avalon Inn that were paid with operating cash to fund the acquisition of the Boardman Tennis Center facility. Subsequent to the acquisition, the Boardman Tennis Center facility was renamed The Avalon Athletic Club at Boardman. The primary assets of The Avalon Athletic Club at Boardman include the acquired real property consisting of the building and associated land.

The Avalon Athletic Club at Boardman is currently in operation providing indoor tennis court rental and lessons. The operating results are included in the Company's Condensed Consolidated Statements of Operations and within Avalon's golf and related operations segment from the date of acquisition. The net operating revenues and results of operations related to the Avalon Athletic Club at Boardman from the period of acquisition are not significant and, accordingly, are not provided.

In the third quarter of 2018, the Company started renovating the facility. The renovations include converting the facility into a multipurpose recreation center which will include indoor tennis courts, indoor basketball, volleyball and pickleball courts and a fitness area.

The acquisition of the facility and its associated renovation is consistent with the Company's athletics and fitness business strategy. Members of the Avalon Golf and Country Club will have access to the renovated facility and all the athletic and fitness related activities that will be offered by The Avalon Athletic Club at Boardman. In addition, hotel guests at The Avalon Inn will also be able to utilize the facility during their stay. The Avalon Athletic Club at Boardman will earn revenue through membership fees, athletic and fitness related activities.

The Company accounted for the acquisition of The Avalon Athletic Club at Boardman in accordance with ASU 2017-01. In accordance with ASU 2017-01, the Company evaluated whether to account for the transaction as either a business or asset acquisition. The Company determined that all of the fair value of the gross assets acquired was concentrated in the Boardman Tennis Center building and associated land. In accordance with the guidance, assets that are attached to each other, such as land and a building residing on the land which cannot be physically removed and used separately from each other without incurring significant cost are considered to be a single identifiable asset. In accordance with ASU 2017-01, the Company accounted for the transaction as an asset acquisition as all of the value of the gross assets acquired resides in that single asset.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the transaction date (in thousands):

**Assets acquired:**

Building and land	\$1,302
Total assets acquired:	1,302

**Liabilities assumed:**

Accrued liabilities	33
Total liabilities assumed	33
Total consideration	\$1,269

## **Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

*The following discussion provides information which management believes is relevant to an assessment and understanding of the operations and financial condition of Avalon Holdings Corporation and its subsidiaries. As used in this report, the term “Avalon” or the “Company” means Avalon Holdings Corporation, its wholly owned subsidiaries and variable interest entities when it has been determined that Avalon is the primary beneficiary of those company’s operations, taken as a whole, unless the context indicates otherwise.*

*Statements included in Management’s Discussion and Analysis of Financial Condition and Results of Operations which are not historical in nature are intended to be, and are hereby identified as, “forward looking statements”. Avalon cautions readers that forward looking statements, including, without limitation, those relating to Avalon’s future business prospects, revenues, working capital, liquidity, capital needs, interest costs, and income, are subject to certain risks and uncertainties that could cause actual results to differ materially from those indicated in the forward looking statements, due to risks and factors identified herein and from time to time in Avalon’s reports filed with the Securities and Exchange Commission.*

### **Liquidity and Capital Resources**

For the nine months ended September 30, 2018, Avalon utilized existing cash and cash provided by operations to meet operating needs, make required monthly payments on the term loan facility and to fund capital expenditures which included the renovation of the Avalon Athletic Club at Boardman and the continued renovation and expansion of The Avalon Inn as described below.

In addition, during the first quarter of 2018, in accordance with our Term Loan Agreement, the Company withdrew \$1.5 million from the restricted cash account for reimbursement for capital expenditures incurred in 2017 related to The Avalon Inn funded with operating cash. The Company utilized approximately \$1.3 million of those proceeds to fund the acquisition of The Boardman Tennis Center facility as described below.

On March 7, 2018, Avalon, through a newly created subsidiary, Avalon Mahoning Sports Center, Inc., completed the acquisition of the Boardman Tennis Center facility in Boardman, Ohio for approximately \$1.3 million in cash. In accordance with our Term Loan Agreement, the Company withdrew funds from the restricted cash account for reimbursement for capital expenditures incurred in 2017 related to The Avalon Inn that were paid with operating cash to fund the acquisition of the Boardman Tennis Center facility. Subsequent to the acquisition, the Boardman Tennis Center facility was renamed The Avalon Athletic Club at Boardman. The primary assets of The Avalon Athletic Club

at Boardman include the acquired real property consisting of the building and associated land.

The Avalon Athletic Club at Boardman is currently in operation providing indoor tennis court rental and lessons. The operating results are included in the Company's Condensed Consolidated Statements of Operations and within Avalon's golf and related operations segment from the date of acquisition.

In the third quarter of 2018, the Company started renovating the facility. The renovations include converting the facility into a multipurpose recreation center which will include indoor tennis courts, indoor basketball, volleyball and pickleball courts and a fitness area.

The acquisition of the facility and its associated renovation is consistent with the Company's athletics and fitness business strategy. Members of the Avalon Golf and Country Club will have access to the renovated facility and all the athletic and fitness related activities that will be offered by The Avalon Athletic Club at Boardman. In addition, hotel guests at The Avalon Inn will also be able to utilize the facility during their stay. The Avalon Athletic Club at Boardman will earn revenue through membership fees, athletic and fitness related activities.

During the nine months ended September 30, 2018, Avalon incurred capital expenditures of \$2.6 million of which \$2.0 million of such expenditures was paid to vendors and primarily related to the continued renovation and expansion of The Avalon Inn and approximately \$0.1 million of such expenditures related to a vehicle acquired under a new capital lease agreement. During the nine months ended September 30, 2017, Avalon incurred capital expenditures of \$2.2 million of which \$1.5 million of such expenditures was paid to vendors and primarily related to the continued renovation and expansion of The Avalon Inn and \$0.6 million of such expenditures related to golf course maintenance equipment acquired under new capital lease agreements. In 2018 and 2017, The Avalon Inn was in operation but still in the process of being renovated and expanded. The renovations and expansion include the renovation of existing hotel rooms and recreation center and the addition of a new restaurant, bars, outdoor resort pool and Roman Bath. Avalon's aggregate capital expenditures in 2018 are expected to be in the range of \$3 million to \$4 million, funded with cash in our project fund account and cash generated from operations. Capital expenditures will principally relate to the continued renovation and expansion of The Avalon Inn, renovation of The Avalon Athletic Club at Boardman facility, building improvements and equipment purchases.

On December 20, 2016, Avalon and certain direct and indirect wholly owned subsidiaries entered into a loan and security agreement (the “Term Loan Agreement”) with Laurel Capital Corporation which provides for a \$12.0 million term loan. At closing, \$9.1 million of the proceeds were used to pay off amounts outstanding under the then existing line of credit agreement and associated accrued interest with Home Savings Bank, dated May 21, 2015, as amended, and pay related transaction costs associated with the Term Loan Agreement. The line of credit agreement with Home Savings Bank was terminated in conjunction with the repayment. Remaining proceeds of \$2.9 million under the Term Loan Agreement were deposited in a project fund account to fund costs of renovating and expanding The Avalon Inn. At September 30, 2018 and December 31, 2017, the remaining proceeds of \$1.3 million and \$2.8 million, respectively, are presented in the Condensed Consolidated Balance Sheets as “Restricted cash.” On December 4, 2017 the Term Loan Agreement was amended to restate the definition of “Total Fixed Charges” utilized in the calculation of the “Fixed Charge Coverage Ratio.”

The \$12.0 million term loan amount is payable in 119 equal monthly installments of principal and interest, based on a fifteen (15) year maturity schedule which commenced on January 20, 2017. The Term Loan Agreement matures on December 20, 2026 at which time the final balloon payment equal to the remaining outstanding principal, interest and fees are due. Borrowings under the Term Loan Agreement bear interest at a fixed rate of 5.35% until the fifth anniversary date of the closing at which time the interest rate will be reset to a fixed rate equal to the greater of (a) 5.35% per annum or (b) the sum of the Index Rate on the date two (2) business days prior to the reset date and 3.95%, provided that the applicable rate shall in no event exceed 7.50% per annum.

Avalon has the right to prepay the amount outstanding under the Term Loan Agreement, in whole or in part, at any time upon payment of the principal amount of the loan to be prepaid plus accrued unpaid interest thereon to the prepayment date, plus an applicable prepayment penalty. The prepayment penalty, expressed as a percentage of the principal of the loan being prepaid, is five percent (5%) on any prepayment in the first five years; four percent (4%) on any prepayment in the sixth and seventh year; three percent (3%) on any prepayment in the eighth and ninth year; and two percent (2%) on any prepayment in the tenth year.

Borrowings are secured by certain real property and related business assets as defined in the Term Loan Agreement. The Term Loan Agreement also contains certain financial and other covenants, customary representations, warranties and events of default. Avalon was in compliance with the Term Loan Agreement covenants at September 30, 2018 and December 31, 2017.

On May 31, 2018, Avalon entered into a new business loan agreement with Home Savings Bank, (the “Line of Credit Agreement”) which provides for a line of credit of up to \$5.0 million maturing on May 31, 2020. Under the Line of Credit Agreement, borrowings in excess of \$1.0 million are subject to a borrowing base which is calculated based off a specific level of eligible accounts receivable of the waste management business as defined in the agreement. The existing line of credit agreement with Home Savings Bank, dated December 20, 2016, as amended, which was entered into concurrently with the Term Loan Agreement, was terminated in conjunction with the new Line of Credit Agreement. No amounts were outstanding under the existing line of credit agreement at termination.



No amounts were drawn under the Line of Credit Agreement at September 30, 2018. Outstanding borrowings under the Line of Credit Agreement bear interest at Prime Rate plus .25%. At September 30, 2018, the interest rate on the Line of Credit Agreement was 5.25%. Effective October 1, 2018, the interest rate on the Line of Credit Agreement increased to 5.50%.

Borrowings under the Line of Credit Agreement are secured by certain business assets of the Company including accounts receivable, inventory and equipment. The Line of Credit Agreement also contains certain financial and other covenants, customary representations, warranties and events of default. Avalon was in compliance with the line of credit agreements covenants at September 30, 2018 and December 31, 2017.

During both the three and nine month periods ended September 30, 2018 and 2017, the weighted average interest rate on outstanding borrowings was 5.35%.

In November 2003, Avalon entered into a long-term agreement with Squaw Creek Country Club to lease and operate its golf course and related facilities. The lease has an initial term of ten (10) years with four (4) consecutive ten (10) year renewal term options unilaterally exercisable by Avalon. Under the lease, Avalon is obligated to pay \$15,000 in annual rent and make leasehold improvements of \$150,000 per year. Amounts expended by Avalon for leasehold improvements during a given year in excess of \$150,000 will be carried forward and applied to future leasehold improvement obligations. Based upon the amount of leasehold improvements already made, Avalon expects to exercise all of its remaining renewal options.

At September 30, 2018 and December 31, 2017, there was a working capital deficit of \$0.7 million and \$0.2 million, respectively. Working capital was negatively impacted primarily by an increase in accounts payable and deferred membership dues revenue partially offset by an increase in cash and cash equivalents and accounts receivable.

Accounts receivable increased to \$11.3 million at September 30, 2018 compared with \$9.9 million at December 31, 2017. The increase was primarily the result of increased sales related to the waste management services segment in the third quarter of 2018 compared with the fourth quarter of 2017 and the timing of receipt on those associated receivables. Net operating revenues related to the waste management segment were \$12.6 million in the third quarter of 2018 compared with \$10.5 million in the fourth quarter of 2017.

Unbilled membership dues receivable increased to \$0.8 million at September 30, 2018 compared to \$0.6 million at December 31, 2017 due to the associated timing of membership renewals which are billed on a monthly basis over the course of the annual agreement.

Accounts payable increased to \$9.8 million at September 30, 2018 compared with \$7.8 million at December 31, 2017. The increase in accounts payable is primarily due to an increase in the amounts due to disposal facilities and transportation carriers of the waste brokerage and management services business associated with the increase in net operating revenues in the third quarter of 2018 compared with the fourth quarter of 2017 and the associated timing of those vendor payments in the ordinary course of business. To a lesser extent, accounts payable also increased due to the timing of payment related to a construction billing associated with the expansion of The Avalon Inn.

Accrued payroll and other compensation increased to \$1.0 million at September 30, 2018 compared to \$0.7 million at December 31, 2017. The increase was primarily the result of timing of payment of certain accrued bonuses.

Deferred revenue relating to membership dues was approximately \$3.4 million at September 30, 2018 compared to \$2.7 million at December 31, 2017. The increase in deferred revenues was primarily due to the associated timing of annual membership renewals and, to a lesser extent, an increase in memberships during the first nine months of 2018. The number of members at September 30, 2018 was 4,424 compared to 4,338 at December 31, 2017.

Management believes that anticipated cash provided from future operations, will be, for the foreseeable future, sufficient to meet operating requirements and make required monthly payments under our term loan facility. If business conditions warrant additional monies needed to fund capital expenditure programs, Avalon will take actions such as refinancing or restructuring our current debt agreements, incurring additional indebtedness, issuance of common stock or issuance of a security with characteristics of both debt and equity.

## **Growth Strategy**

### ***Waste Management Segment***

Our growth strategy for the waste management services segment focuses on increasing revenue, gaining market share and enhancing shareholder value through internal growth. Although we are a waste management services company, we do not own any landfills or provide waste collection services. However, because of our many relationships with various disposal facilities and transporters, we are able to be more flexible and provide alternative solutions to a customer's waste disposal or recycling needs. We intend to capitalize on our management and sales staff which has extensive experience in all aspects of the waste business. As such, we intend to manage our internal growth as follows:

- ***Sales and Marketing Activities.*** We will focus on retaining existing customers and obtaining new business through our well-managed sales and marketing activities. We seek to manage our sales and marketing activities to enable us to capitalize on our position in many of the markets in which we operate. We provide a tailored program to all of our customers in response to their particular needs. We accomplish this by centralizing services to effectively manage their needs, such as minimizing their procurement costs.

We currently have a number of professional sales and marketing employees in the field who are compensated using a commission structure that is focused on generating high levels of quality revenue. For the most part, these employees directly solicit business from existing and prospective customers. We emphasize our rate and cost structures when we train new and existing sales personnel. We intend to hire additional qualified professional sales personnel to expand into different geographical areas.

- ***Development Activities.*** We will seek to identify opportunities to further position us as an integrated service provider in markets where we provide services. In addition, we will continue to utilize the extensive experience of our management and sales staff to bid on significant one-time projects and those that require special expertise. Where appropriate, we may seek to obtain permits that would provide vertically integrated waste services or expand the service offerings or leverage our existing volumes with current vendors to provide for long term, cost competitive strategic positioning within our existing markets.

### ***Golf and Related Operations Segment***

In August 2014, the Company acquired The Avalon Inn which was integrated into the golf and related operations segment. The acquisition is consistent with the Company's business strategy in that The Avalon Inn provides guests with a self-contained vacation experience, offering hotel guests golf packages to all of the golf courses of the Avalon Golf and Country Club and allows its guests to utilize the facilities at each of the clubhouses. Members of the Avalon Golf and Country Club also have access to all of the amenities offered by The Avalon Inn. The Avalon Inn is open year-round and provides a consistent, comfortable environment where our guests can enjoy our various amenities and activities. Avalon believes that the combination of its three golf facilities and The Avalon Inn will result in additional memberships in the Avalon Golf and Country Club.

On March 7, 2018, Avalon acquired The Avalon Athletic Club at Boardman which was integrated into the golf and related operations segment. The acquisition is consistent with the Company's athletics and fitness business strategy. Members of the Avalon Golf and Country Clubs will have access to all the athletic and fitness related activities that will be offered by The Avalon Athletic Club at Boardman. In addition, hotel guests of The Avalon Inn will also be able to utilize the facility during their stay.

In addition, several private country clubs in the northeast Ohio area are experiencing economic difficulties. Avalon believes some of these clubs may represent an attractive investment opportunity. While Avalon has not entered into any pending agreements for acquisitions, it may do so at any time and will continue to consider acquisitions that make economic sense.

### **Results of Operations**

Avalon's primary business segment, the waste management services segment, provides hazardous and nonhazardous waste brokerage and management services, captive landfill management services and salt water injection well operations. The golf and related operations segment includes the operation and management of three golf courses and related country clubs and facilities, a hotel and its associated amenities, a recreation center and a travel agency.

### **Performance in the third quarter of 2018 compared with the third quarter of 2017**

#### ***Overall Performance***

Net operating revenues increased to \$18.1 million in the third quarter of 2018 compared with \$16.3 million in the third quarter of 2017. This increase was primarily due to an increase in net operating revenues of the waste management services segment. Net operating revenues of the waste management services segment were \$12.5 million in the third quarter of 2018 compared with \$10.8 million in the third quarter of 2017. Net operating revenues of the golf and related operations segment were approximately \$5.6 million in the third quarter of 2018 compared to \$5.5 million in the third quarter of 2017.

Costs of operations related to the waste management segment increased to \$9.9 million in the third quarter of 2018 compared with \$8.8 million in the third quarter of 2017. The increase in the cost of operations between years for the waste management segment is primarily due to the increased net operating revenues between periods as these costs vary directly with the associated net operating revenues. Cost of operations for the golf and related operations segment was \$4.3 million in the third quarter of 2018 compared to \$4.1 million in the third quarter of 2017.

Depreciation and amortization expense was approximately \$0.7 million in both the third quarter of 2018 and 2017.

Consolidated selling, general and administrative expenses were \$2.3 million in the third quarter of 2018 compared with \$2.2 million in the third quarter of 2017. The increase in selling, general and administrative costs was primarily due to increased employee related costs.

Interest expense was \$0.2 million in both the third quarter of 2018 and 2017. During both the three month periods ended September 30, 2018 and 2017, the weighted average interest rate on outstanding borrowings was 5.35%.

Net income attributable to Avalon Holdings Corporation common shareholders was \$0.8 million, or \$0.22 per share, in the third quarter of 2018 compared with net income attributable to Avalon Holdings Corporation common shareholders of \$0.5 million, or \$0.14 per share, in the third quarter of 2017.

### ***Segment Performance***

Segment performance should be read in conjunction with Note 13 to the Condensed Consolidated Financial Statements.

### ***Waste Management Services Segment***

The net operating revenues of the waste management services segment increased to \$12.5 million in the third quarter of 2018 compared with \$10.8 million in the third quarter of 2017. The waste management services segment includes waste disposal brokerage and management services, captive landfill management operations and salt water injection well operations.

The net operating revenues of the waste brokerage and management services business increased to \$12.0 million in the third quarter of 2018 from \$10.2 million in the third quarter of 2017. This increase was due to an increase in net operating revenues relating to continuous work of the waste disposal brokerage business. Continuous work of the waste disposal brokerage business increased \$1.6 million between periods related to increased work from multiple customers. Net operating revenues related to continuous work were approximately \$6.6 million in the third quarter of 2018 compared with \$5.0 million in the third quarter of 2017. In addition, net operating revenue increased between periods due to event work relating to multiple projects. Event work is defined as bid projects under contract that occurs on a one-time basis over a short period of time. Such work can fluctuate significantly from year to year. Net operating revenues related to event work were approximately \$5.3 million in the third quarter of 2018 compared with \$4.6 million in the third quarter of 2017. The increase in net operating revenues noted above were partially offset by a decrease in net operating revenues related to managerial, consulting and clerical services. Net operating revenue

relating to managerial, consulting and clerical services, which is performed for one customer, is entirely dependent on that customer's needs. Net operating revenues related to managerial, consulting and clerical services decreased to \$0.1 million in the third quarter of 2018 compared with \$0.6 million in the third quarter of 2017.

The net operating revenues of the captive landfill management operations were approximately \$0.5 million in the third quarter of 2018 compared to \$0.6 million in the third quarter of 2017. The net operating revenues of the captive landfill operations are almost entirely dependent upon the volume of waste generated by the owner of the landfill for whom Avalon manages the facility.

Due to the temporary suspension of the salt water injections wells described below, there were no operating revenues during the third quarter of 2018 and 2017. As a result of a seismic event with a magnitude of 2.1 occurring on August 31, 2014, the Chief of the Division of Oil and Gas Resources Management ("Chief" or "Division") issued Orders on September 3, 2014, to immediately suspend all operations of both of Avalon's saltwater injection wells. The Orders were based on the findings that the two saltwater injection wells were located in close proximity to an area of known seismic activity and also that the saltwater injection wells pose a risk of increasing or creating seismic activity. The two saltwater injection wells are located approximately 112 feet apart. Based on these findings, the Chief ordered the immediate suspension of all operations of the two saltwater injection wells, until the Division could further evaluate the wells.

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On July 31, 2018 the Ohio 10<sup>th</sup> District Court of Appeals issued its decision on the appeal. In the decision, the Ohio 10<sup>th</sup> District Court of Appeals overruled the majority of the Division’s assignments of error, but also found that the Franklin County Court of Common Pleas abused its discretion in issuing the restart order for the Company’s injection well. The Ohio 10<sup>th</sup> District Court of Appeals therefore reinstated the previous Ohio Oil and Gas Commission decision in this matter.

On September 12, 2018, the Company appealed the Ohio 10<sup>th</sup> District Court of Appeals decision to the Ohio Supreme Court. Avalon will continue in its effort to receive a favorable ruling lifting the temporary suspension. The operations of Company’s #2 injection well will remain suspended until that time.



In addition, on August 26, 2016, Avalon filed a complaint in the 11<sup>th</sup> Appellate District Court in Trumbull County, Ohio for a Peremptory Writ of Mandamus to compel the Director of the Ohio Department of Natural Resources (“ODNR”) to initiate appropriations procedures to determine damages from the illegal regulatory taking of the Company’s property, or issue an alternative remedy at law. There is currently no implemented state-wide policy on induced seismicity and The ODNR has refused to communicate with the Company regarding the status and requirements of any policymaking. The Company believes that the actions, and lack of responsible actions, by ODNR, which were triggered by a seismic event that presented no hazard or risk to any individual or to the environment, is a clear violation of the Company’s property rights and a violation of the Fifth and Fourteenth Amendments to the U.S. Constitution; Article I, Section 19 of the Ohio Constitution; and Ohio Revised Code Chapter 163.

The hearing was scheduled to commence on June 25, 2018. On June 8, 2018, the 11<sup>th</sup> Appellate District Court in Trumbull County, Ohio issued a motion to stay all further proceedings in the writ of mandamus action until a ruling is made on the suspension order by the Ohio 10<sup>th</sup> District Court of Appeals. On September 17, 2018, the Company filed a motion to lift the stay in the proceeding based on the Ohio 10<sup>th</sup> District Court of Appeals ruling. To date, the hearing date has not been rescheduled. The ODNR has stated that they will not oppose the lifting of the stay. The Company intends to vigorously pursue the complaint and obtain due process and fair compensation.

Costs of operations related to the waste management segment increased to \$9.9 million in the third quarter of 2018 compared with \$8.8 million in the third quarter of 2017. The increase in the cost of operations between years for the waste management segment is primarily due to the increased net operating revenues between periods as these costs vary directly with the associated net operating revenues. The overall gross margin percentage of the waste brokerage and management services business was approximately 21% in the third quarter of 2018 compared with 18% in the third quarter of 2017. The increase in the overall gross margin percentage was attributable to the higher gross profit generated from both the continuous and event work projects during the quarter.

Income before income taxes for the waste management services segment was approximately \$1.2 million in the third quarter of 2018 compared to \$0.6 million in the third quarter of 2017. Income before income taxes of the waste brokerage and management services business was approximately \$1.3 million in the third quarter of 2018 compared to \$0.8 million in the third quarter of 2017. The increased income before taxes was primarily attributable to the increased net operating revenues and associated gross margin from both the continuous and event work projects during the quarter. Income before income taxes of the captive landfill operations was approximately \$0.1 million in both the third quarter of 2018 and 2017. During the third quarter of 2018 and 2017, the salt water injection wells incurred a loss before income taxes of approximately \$0.2 million and \$0.3 million respectively. The loss was primarily due to depreciation expense recorded on the facility and legal and professional costs incurred relating to Avalon's appeal and mandamus processes described above.

### ***Golf and Related Operations Segment***

Net operating revenues of the golf and related operations segment were approximately \$5.6 million in the third quarter of 2018 compared to \$5.5 million in the third quarter of 2017. Avalon's golf and related operations segment consists of the operation and management of three golf courses and related country clubs which provide dining and banquet facilities, a hotel which provides lodging, dining, banquet and conference facilities, a recreation center and a travel agency.

Food, beverage and merchandise sales were \$2.3 million in both the third quarter of 2018 and 2017. Other net operating revenues related to the golf and related operations were \$3.3 million in the third quarter of 2018 compared to \$3.2 million in the third quarter of 2017. Net operating revenues related to room rental was approximately \$0.7 million in both the third quarter of 2018 and 2017. Membership dues revenue was approximately \$1.3 million in the third quarter of 2018 and 2017. The average number of members during the third quarter of 2018 was 4,446 compared to 4,412 in the prior period. Greens fees and associated cart rentals were approximately \$0.9 million in the third quarter of 2018 compared to \$0.8 million in the third quarter of 2017. Other revenues consisting of athletic, fitness, travel agency and spa related activities were approximately \$0.4 million in both the third quarter of 2018 and 2017.

Cost of food, beverage and merchandise was approximately \$1.0 million in both the third quarter of 2018 and 2017. Golf and related operations operating costs increased to approximately \$3.3 million in the third quarter of 2018 compared with \$3.1 million in the third quarter of 2017. The increase was primarily attributable to higher employee related costs.

Income before income taxes for the golf and related operations was approximately \$0.5 million in the third quarter of 2018 compared with \$0.7 million in the third quarter of 2017. The change between periods was primarily due to higher employee related costs.

***General Corporate Expenses***

General corporate expenses were \$0.7 million in both the third quarter of 2018 and 2017.

***Interest Expense***

Interest expense was \$0.2 million in both the third quarter of 2018 and 2017. During both the three month periods ended September 30, 2018 and 2017, the weighted average interest rate on outstanding borrowings was 5.35%.

***Net Income***

Net income attributable to Avalon Holdings Corporation common shareholders was \$0.8 million in the third quarter of 2018 compared to \$0.5 million in the third quarter of 2017. Avalon recorded a state income tax provision in both the third quarter of 2018 and 2017, which was related entirely to the waste management and brokerage operations. Due to the recording of a full valuation allowance against the Company's federal net deferred tax assets, the overall effective tax rate in both periods reflects taxes owed in certain U.S state jurisdictions. Avalon's income tax on the income before taxes was offset by a change in the valuation allowance. A valuation allowance is provided when it is more likely than not that deferred tax assets relating to certain federal and state loss carryforwards will not be realized. Avalon continues to maintain a valuation allowance against the majority of its deferred tax amounts until it is evident that the deferred tax asset will be utilized in the future.

## **Performance in the first nine months of 2018 compared with the first nine months of 2017**

### ***Overall Performance***

Net operating revenues increased to \$46.4 million in the first nine months of 2018 compared with \$41.6 million in the first nine months of 2017. This increase was primarily due to an increase in net operating revenues of the waste management services segment. Net operating revenues of the waste management services segment were \$32.5 million in the first nine months of 2018 compared with \$27.9 million in the first nine months of 2017. Net operating revenues of the golf and related operations segment were approximately \$13.9 million in the first nine months of 2018 compared to \$13.7 million in the first nine months of 2017.

Costs of operations related to the waste management segment increased to \$25.6 million in the first nine months of 2018 compared with \$22.2 million in the first nine months of 2017. The increase in the cost of operations between years for the waste management segment is primarily due to the increased net operating revenues between periods as these costs vary directly with the associated net operating revenues. Cost of operations for the golf and related operations segment were \$11.1 million in both the first nine months of 2018 and 2017.

Depreciation and amortization expense was approximately \$2.2 million in the first nine months of 2018 compared to \$2.3 million in the first nine months of 2017.

Consolidated selling, general and administrative expenses were \$6.7 million in the first nine months of 2018 compared with \$6.3 million in the first nine months of 2017. The increase in selling, general and administrative costs was primarily attributable to higher employee related costs and, to a lesser extent, an increase in advertising and sales promotions during the golf season and higher professional costs.

Interest expense was approximately \$0.5 million in both the first nine months of 2018 and 2017. During both the nine month periods ended September 30, 2018 and 2017, the weighted average interest rate on outstanding borrowings was 5.35%.

Net income attributable to Avalon Holdings Corporation common shareholders was \$0.7 million, or \$0.18 per share, in the first nine months of 2018 compared with a net loss attributable to Avalon Holdings Corporation common shareholders of \$0.3 million, or \$0.07 per share, in the first nine months of 2017.

***Segment Performance***

Segment performance should be read in conjunction with Note 13 to the Condensed Consolidated Financial Statements.

***Waste Management Services Segment***

The net operating revenues of the waste management services segment increased to \$32.5 million in the first nine months of 2018 compared with \$27.9 million in the first nine months of 2017.

The net operating revenues of the waste brokerage and management services business increased to \$30.8 million in the first nine months of 2018 from \$26.3 million in the first nine months of 2017. This increase was due to an increase in net operating revenues relating to continuous work of the waste disposal brokerage business. Continuous work of the waste disposal brokerage business increased \$3.1 million between periods as a result of increased work from multiple customers. Net operating revenues related to continuous work were approximately \$18.4 million in the first nine months of 2018 compared with \$15.3 million in the first nine months of 2017. In addition, net operating revenue increased \$1.6 million between periods due to event work relating to multiple projects. Event work is defined as bid projects under contract that occurs on a one-time basis over a short period of time. Such work can fluctuate significantly from year to year. Net operating revenues related to event work were approximately \$11.5 million in the first nine months of 2018 compared with \$9.9 million in the first nine months of 2017. The increase in net operating revenues noted above were partially offset by a decrease in net operating revenues related to managerial, consulting and clerical services. Net operating revenue relating to managerial, consulting and clerical services, which is performed for one customer, is entirely dependent on that customer's needs. Net operating revenues related to managerial, consulting and clerical services decreased to \$0.9 million in the first nine months of 2018 compared with \$1.1 million in the first nine months of 2017.

The net operating revenues of the captive landfill management operations were approximately \$1.7 million in the first nine months of 2018 compared to \$1.6 million in the first nine months of 2017. The net operating revenues of the captive landfill operations are almost entirely dependent upon the volume of waste generated by the owner of the landfill for whom Avalon manages the facility.

Due to the temporary suspension of the salt water injections wells noted above, there were no operating revenues during the first nine months of 2018 and 2017.

Costs of operations related to the waste management segment increased to \$25.6 million in the first nine months of 2018 compared with \$22.2 million in the first nine months of 2017. The increase in the cost of operations between years for the waste management segment is primarily due to the increased net operating revenues between periods as these costs vary directly with the associated net operating revenues. The overall gross margin percentage of the waste brokerage and management services business was approximately 21% in the first nine months of 2018 compared to 20% in the first nine months of 2017. The increase in the overall gross margin percentage was attributable to the higher gross profit generated from event work projects during the first nine months of 2018.

Income before income taxes for the waste management services segment was approximately \$2.8 million in the first nine months of 2018 compared to \$1.9 million in the first nine months of 2017. Income before income taxes of the waste brokerage and management services business was approximately \$3.1 million in the first nine months of 2018 compared to \$2.3 million in the first nine months of 2017. The increased income before taxes was primarily attributable to the increased gross margin from the higher net operating revenues related to both continuous and event work during the first nine months of 2018. Income before income taxes of the captive landfill operations was approximately \$0.3 million in the first nine months of 2018 and 2017. During the first nine months of 2018 and 2017, the salt water injection wells incurred a loss before income taxes of approximately \$0.6 million and \$0.7 million, respectively. The loss was primarily due to depreciation expense recorded on the facility and legal and professional costs incurred relating to Avalon's appeal and mandamus processes described above.

### ***Golf and Related Operations Segment***

Net operating revenues of the golf and related operations segment were approximately \$13.9 million in the first nine months of 2018 compared to \$13.7 million in the first nine months of 2017.

Food, beverage and merchandise sales were \$5.5 million in the first nine months of 2018 compared to \$5.7 million in the first nine months of 2017. The decrease was primarily due to a decrease in food and beverage revenue related to the clubs between periods.

Other net operating revenues related to the golf and related operations were \$8.4 million in the first nine months of 2018 compared to \$8.0 million in the first nine months of 2017. Net operating revenues related to room rental was approximately \$1.8 million in the first nine months of 2018 compared with \$1.6 million in the first nine months of 2017. The increase in net operating revenues related to room rental was due to higher occupancy and associated average room rates during the first nine months of 2018 compared with the prior period. Membership dues revenue was approximately \$3.9 million in both the first nine months of 2018 and 2017. The increase in membership dues revenue attributable to the increase in membership rates that went into effect on the member's annual renewal date was offset by a decrease in the average number of members between periods. The average number of members during the first nine months of 2018 was 4,443 compared to 4,604 in the prior period. Greens fees and associated cart rentals were \$1.5 million in the first nine months of 2018 compared to \$1.4 million in the first nine months of 2017. Other revenues consisting of athletic, fitness, travel agency and spa related activities were approximately \$1.2 million in the first nine months of 2018 compared to \$1.1 million in the first nine months of 2017. Due to adverse weather conditions, net operating revenues relating to the golf courses, which are located in northeast Ohio and western Pennsylvania, were minimal during the first three months of 2018 and 2017.

Cost of operations for the golf and related operations segment were \$11.1 million in both the first nine months of 2018 and 2017. Cost of food, beverage and merchandise was approximately \$2.4 million in the first nine months of 2018 compared to \$2.5 million in the first nine months of 2017. The decrease is primarily attributable to the decreased food revenue and its associated cost coupled with lower average cost of food. Golf and related operations operating costs increased to approximately \$8.7 million in the first nine months of 2018 compared with \$8.6 million in the first nine months of 2017. The increase was primarily a result of higher employee related costs and increased use of lawn care maintenance products for the golf courses.

Income before taxes for the golf and related operations was \$0.5 million in the first nine months of 2018 compared with \$0.3 million in the first nine months of 2017. The change between periods was primarily due to higher occupancy and associated room rates attributable to The Avalon Inn.

The ability to attract new members and retain members is very important to the success of the golf and related operations segment. Avalon is continually using different marketing strategies to attract and retain members, such as local television advertising and/or various membership promotions. A significant decline in members could adversely impact the financial results of the golf and related operations segment.

### ***General Corporate Expenses***

General corporate expenses were \$2.3 million in the first nine months of 2018 compared to \$2.2 million in the first nine months of 2017. The increase in general corporate expenses related to higher legal and professional costs.

### ***Interest Expense***

Interest expense was \$0.5 million in both the first nine months of 2018 and 2017. During both the three month periods ended September 30, 2018 and 2017, the weighted average interest rate on outstanding borrowings was 5.35%.

### ***Net Income (Loss)***

Net income attributable to Avalon Holdings Corporation common shareholders was \$0.7 million in the first nine months of 2018 compared to a net loss attributable to Avalon Holdings Corporation common shareholders of \$0.3 million in the first nine months of 2017. Avalon recorded a state income tax provision in both the first nine months of 2018 and 2017, which was related entirely to the waste management and brokerage operations. Due to the recording of a full valuation allowance against the Company's federal net deferred tax assets, the overall effective tax rate in both periods reflects taxes owed in certain U.S state jurisdictions. Avalon's income tax on the income (loss) before taxes was offset by a change in the valuation allowance. A valuation allowance is provided when it is more likely than not that deferred tax assets relating to certain federal and state loss carryforwards will not be realized. Avalon continues to maintain a valuation allowance against the majority of its deferred tax amounts until it is evident that the deferred tax asset will be utilized in the future.



## Trends and Uncertainties

In the ordinary course of conducting its business, Avalon becomes involved in lawsuits, administrative proceedings and governmental investigations, including those relating to environmental matters. Some of these proceedings may result in fines, penalties or judgments being assessed against Avalon which, from time to time, may have an impact on its business and financial condition. Although the outcome of such lawsuits or other proceedings cannot be predicted with certainty, management assesses the probability of loss and accrues a liability as appropriate. Avalon does not believe that any uninsured ultimate liabilities, fines or penalties resulting from such pending proceedings, individually or in the aggregate, will have a material adverse effect on its liquidity, financial position or results of operations.

On December 22, 2017, legislation commonly known as the Tax Cuts and Jobs Act (the "Tax Act") was signed into law. The Tax Act changes existing U.S. tax law and includes numerous provisions that will affect Avalon, including our income tax accounting, disclosure and tax compliance. The most impactful changes within the Tax Act are those that will reduce the U.S. corporate tax rates, business-related exclusions and deductions and credits. Accounting Standards Codification Topic 740, "*Income Taxes*," requires the effects of changes in tax rates and laws on deferred tax balances to be recognized in the period in which the legislation is enacted. To the extent that a company's accounting for certain income tax effects of the Tax Act is incomplete but for which they are able to determine a reasonable estimate, the company must record a provisional amount in the financial statements. Consequently, as of the date of enactment, and during the nine months ended September 30, 2018, Avalon valued all deferred tax assets and liabilities at the newly enacted Corporate U.S income tax rate. Avalon has a full valuation allowance on its federal deferred tax assets. Avalon is still in the process of estimating the full tax impact and expects to finalize its adoption of this guidance at year end.

The federal government and numerous state and local governmental bodies are continuing to consider legislation or regulations to either restrict or impede the disposal and/or transportation of waste. A portion of Avalon's waste brokerage and management services revenues is derived from the disposal and/or transportation of out-of-state waste. Any law or regulation restricting or impeding the transportation of waste or the acceptance of out-of-state waste for disposal could have a negative effect on Avalon.

Avalon's waste brokerage and management services business obtains and retains customers by providing services and identifying cost-efficient disposal options unique to a customer's needs. Consolidation within the solid waste industry has resulted in reducing the number of disposal options available to waste generators and may cause disposal pricing to increase. Avalon's waste brokerage and management services business may not be able to pass these price increases onto some of its customers, which, in turn, may adversely impact Avalon's future financial performance.

A significant portion of Avalon's business is generated from waste brokerage and management services provided to customers that are not subject to long-term contracts. In light of current economic, regulatory and competitive conditions, there can be no assurance that Avalon's current customers will continue to transact business with Avalon at historical levels. Failure by Avalon to retain its current customers or to replace lost business could adversely impact the future financial performance of Avalon.

Avalon's captive landfill management business is dependent upon a single customer as its sole source of revenue. If the captive landfill management business is unable to retain this customer, Avalon's future financial performance could be adversely impacted.

Saltwater disposal wells are regulated by the Ohio Department of Natural Resources ("ODNR"), with portions of the disposal facilities regulated by the Ohio EPA. As exploitation of the Marcellus and Utica shale formations by the hydrofracturing process develops, regulatory and public awareness of the environmental risks of saltwater brine and its disposal in saltwater disposal wells is growing and consequently, it is expected that regulation governing the construction and operation of saltwater disposal wells will increase in scope and complexity. Increased regulation may result in increased construction and/or operating costs, which could adversely affect the financial results of Avalon.

There is a continuing risk during the saltwater disposal well's operation of an environmental event causing contamination to the water tables in the surrounding area, or seismic events. The occurrence of a spill or contamination at a disposal well site could result in remedial expenses and/or result in the operations at the well site being suspended and/or terminated by the Ohio EPA or the ODNR. Incurring remedial expenses and/or a suspension or termination of Avalon's right to operate one or more saltwater disposal wells at the well site could have an adverse effect on Avalon's financial results.

As a result of a seismic event with a magnitude of 2.1 occurring on August 31, 2014, the Chief of the Division of Oil and Gas Resources Management ("Chief" or "Division") issued Orders on September 3, 2014, to immediately suspend all operations of both of Avalon's saltwater injection wells. The Orders were based on the findings that the two saltwater injection wells were located in close proximity to an area of known seismic activity and also that the saltwater injection wells pose a risk of increasing or creating seismic activity. The two saltwater injection wells are located approximately 112 feet apart. Based on these findings, the Chief ordered the immediate suspension of all operations of the two saltwater injection wells, until the Division could further evaluate the wells.

On September 5, 2014, Avalon submitted the information required by the Chief's Order in regards to its AWMS #1 injection well, and the Chief lifted the suspension for that well on September 18, 2014. On September 19, 2014, Avalon submitted information and a written plan required by the Chief's Order proposing the establishment of certain operations and management controls on injections at the AWMS #2 injection well. To date, the Division has not responded to that plan despite Avalon's requests for feedback.

On October 2, 2014, Avalon filed an appeal with the Ohio Oil and Gas Commission (the "Commission") disputing the basis for suspending operations of AWMS #2 and also the authority of the Chief to immediately suspend such operations. On March 11, 2015, an appeal hearing was held. The Chief stated during the hearing that the suspension is only temporary, and that he expects that AWMS #2 will be allowed to inject once the state's final policymaking is complete.

On August 12, 2015, the Commission upheld the temporary suspension of injection operations of AWMS #2 stating that the temporary suspension will allow the Chief to more fully evaluate the facts in anticipation of the Division's implementation of a comprehensive regulatory plan that will specifically address injection-induced seismicity. Avalon appealed that decision in September 2015 to the Franklin County Court of Common Pleas, but that appeal was dismissed on a filing technicality. Avalon appealed the dismissal to the Ohio 10th District Court of Appeals, which found the Commission erred in its filing of their decision. Following the Commission's proper notice, Avalon appealed again to the Franklin County Court of Common Pleas (the "Court").

On November 1, 2016 an appeal hearing was held in that Court. On December 23, 2016, the Court issued its Decision and Order in Avalon's favor, and vacated the Commission's decision. The Court found that the Division's suspension and refusal to work with the Company for over 26 months was arbitrary and not in accordance with reason. Subsequent to the ruling, and in accordance with the Court's Decision and Order, both Avalon and the Division submitted their proposed restart plans to the Court. Avalon's plan sets forth both the initial volumes and pressures and increases in volume and pressure while continuously monitoring seismicity and addressing the concerns of public health and safety.

On February 21, 2017, the Court issued its Final Decision and Order. The Court's Final Decision and Order sets conditions for the restarting of AWMS #2 in accordance with the proposed restart plans filed by Avalon with minor revisions. While the Company was making preparations for restarting the well and opening the facility, the Division appealed the Final Decision and Order and filed a Motion to Stay the Court Order on February 22, 2017. The Motion to Stay was granted by the Ohio 10th District Court of Appeals on March 21, 2017. On September 14, 2017, an appeal hearing was held.

On July 31, 2018 the Ohio 10<sup>th</sup> District Court of Appeals issued its decision on the appeal. In the decision, the Ohio 10<sup>th</sup> District Court of Appeals overruled the majority of the Division's assignments of error, but also found that the Franklin County Court of Common Pleas abused its discretion in issuing the restart order for the Company's injection well. The Ohio 10<sup>th</sup> District Court of Appeals therefore reinstated the previous Ohio Oil and Gas Commission decision in this matter.

On September 12, 2018, the Company appealed the Ohio 10<sup>th</sup> District Court of Appeals decision to the Ohio Supreme Court. Avalon will continue in its effort to receive a favorable ruling lifting the temporary suspension. The operations of Company's #2 injection well will remain suspended until that time.

In addition, on August 26, 2016, Avalon filed a complaint in the 11<sup>th</sup> Appellate District Court in Trumbull County, Ohio for a Peremptory Writ of Mandamus to compel the Director of the Ohio Department of Natural Resources ("ODNR") to initiate appropriations procedures to determine damages from the illegal regulatory taking of the Company's property, or issue an alternative remedy at law. There is currently no implemented state-wide policy on induced seismicity and The ODNR has refused to communicate with the Company regarding the status and requirements of any policymaking. The Company believes that the actions, and lack of responsible actions, by ODNR, which were triggered by a seismic event that presented no hazard or risk to any individual or to the environment, is a clear violation of the Company's property rights and a violation of the Fifth and Fourteenth Amendments to the U.S. Constitution; Article I, Section 19 of the Ohio Constitution; and Ohio Revised Code Chapter 163.

The hearing was scheduled to commence on June 25, 2018. On June 8, 2018, the 11<sup>th</sup> Appellate District Court in Trumbull County, Ohio issued a motion to stay all further proceedings in the writ of mandamus action until a ruling is made on the suspension order by the Ohio 10th District Court of Appeals. On September 17, 2018, the Company filed

a motion to lift the stay in the proceeding based on the Ohio 10<sup>th</sup> District Court of Appeals ruling. To date, the hearing date has not been rescheduled. The ODNR has stated that they will not oppose the lifting of the stay. The Company intends to vigorously pursue the complaint and obtain due process and fair compensation.

At December 31, 2017, Avalon assessed the recoverability of the carrying values of the salt water injection wells based on the Chief's decision to temporarily suspend operations of the wells. Avalon believes the suspension order is temporary and will reopen and, as such, the Company estimated future cash flows directly associated with and which are expected to arise as a direct result of the wells once the suspension is lifted. The assumptions used by management in developing the estimates of future cash flows were based on current market conditions and comparable prior periods while in operation. Based on the estimated undiscounted sum of the future cash flows, the net book value of the property, plant and equipment relating to the wells of approximately \$3.7 million at December 31, 2017 was recoverable in less than the estimated remaining useful life of those assets. There were no changes to this assessment at September 30, 2018.

Management continues to consider whether indicators of impairment are present and tests for recoverability, as necessary. Although the Company believes that the suspension order is temporary, there can be no guarantee that the salt water injection wells will resume operations. If management concludes that the suspension is other than temporary and the carrying amount of the salt water injection wells are not recoverable, Avalon may record an impairment charge up to \$3.3 million, the carrying value of the salt water injection wells at September 30, 2018.

Economic challenges throughout the industries served by Avalon may result in payment defaults by customers. While Avalon continuously endeavors to limit customer credit risks, customer-specific financial downturns are not controllable by management. Significant customer payment defaults would have a material adverse impact upon Avalon's future financial performance.

The Avalon Golf and Country Club operates golf courses and related clubhouses at each of its three facilities. The Avalon Golf and Country Club facilities also offer swimming pools, fitness centers, tennis courts, dining and banquet facilities and spa services. In addition, The Avalon Inn provides guests with a self-contained vacation experience, offering hotel guests golf packages to all of the golf courses of the Avalon Golf and Country Club and allows its guests to utilize the facilities at each of the clubhouses. Members of the Avalon Golf and Country Club also have access to all of the amenities offered by The Avalon Inn. The Avalon Golf and Country Club competes with many public courses and country clubs in the area. Although the golf courses continue to be available to the general public, the primary source of revenues is derived from the members of the Avalon Golf and Country Club. Avalon believes that the combination of its three facilities and The Avalon Inn will result in additional memberships in the Avalon Golf and Country Club. The ability to retain current members and attract new members has been an ongoing challenge. Although Avalon was able to increase the number of members of the Avalon Golf and Country Club, as of September 30, 2018, Avalon has not attained its membership goals. There can be no assurance as to when such goals will be attained and when the golf and related operations will ultimately become profitable. Avalon is continually using different marketing strategies to attract new members, such as local television advertising and various membership promotions. A significant decline in members could adversely affect the future financial performance of Avalon.

All three of Avalon's golf course operations and The Avalon Inn currently hold liquor licenses for their respective facilities. If, for some reason, any one of these facilities were to lose their liquor license, the financial performance of the golf and related operations would be adversely affected.

Avalon's operations are somewhat seasonal in nature since a significant portion of those operations are primarily conducted in selected northeastern and midwestern states. Additionally, Avalon's golf courses are located in northeast Ohio and western Pennsylvania and are significantly dependent upon weather conditions during the golf season. As a result, Avalon's financial performance is adversely affected by adverse weather conditions.

## **Recent Accounting Pronouncements**

### *Adopted Accounting Standards*

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"). ASU 2014-09 clarifies the principles used to recognize revenue for all entities. ASU 2014-09 provides a unified five-step model to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration for which the entity expects to be entitled in exchange for those goods or services. The new standard replaces most of the existing revenue recognition standards in U.S. GAAP. In addition, in March 2016, the FASB issued ASU 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, which clarifies

how to apply revenue recognition guidance related to whether an entity is a principal or an agent. On January 1, 2018, the Company adopted ASU 2014-09 and ASU 2016-08, and all related amendments using the modified retrospective method. The adoption did not result in an impact to the way the Company records revenue and as such did not result in period reclassifications to or from revenue or its associated costs. As a result of the adoption, the Company separately disclosed contract assets, in our Condensed Consolidated Balance Sheets at September 30, 2018 and December 31, 2017 and associated cash flows in our Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and 2017. The Company does not expect the adoption to have a material impact on an ongoing basis.

In August 2016, the FASB issued ASU 2016-15, *Classification of Certain Cash Receipts and Cash Payments* (“ASU 2016-15”), which is intended to reduce diversity in practice in how certain cash receipts and payments are presented and classified in the statement of cash flows. The standard provides guidance in a number of situations including, among others, settlement of zero-coupon bonds, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, and distributions received from equity method investees. ASU 2016-15 also provides guidance for classifying cash receipts and payments that have aspects of more than one class of cash flows. On January 1, 2018, the Company adopted ASU 2016-15. The adoption of this standard did not have an impact on Avalon’s financial position, results of operations or financial statement disclosures.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows: Restricted Cash* (“ASU 2016-18”), which requires entities to include restricted cash and restricted cash equivalent balances with cash and cash equivalent balances in the statement of cash flows. On January 1, 2018, the Company adopted ASU 2016-18. The adoption of ASU 2016-18 impacted the presentation of our Condensed Consolidated Statements of Cash Flows and resulted in additional disclosure in our Notes to Unaudited Condensed Consolidated Financial Statements for the restricted cash related to the loan proceeds deposited into our project fund account that have not yet been utilized to fund the additional renovation and expansion of The Avalon Inn.

In January 2017, the FASB issued ASU 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business* (“ASU 2017-01”). The purpose of ASU 2017-01 is to change the definition of a business to assist entities with evaluating when a set of transferred assets and activities is a business. The Company adopted ASU 2017-01 on January 1, 2018. The acquisition of the Boardman Tennis Center facility, acquired in March 2018, was accounted for in accordance with ASU 2017-01.

In March 2018, the FASB issued ASU 2018-05, *Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118* (“ASU 2018-05”). ASU 2018-05 adds the SEC guidance released on December 22, 2017 regarding the Tax Cuts and Jobs Act (the “Tax Act”) to the FASB Accounting Standards Codification. ASU 2018-05 provides additional guidance allowing companies to use a one year measurement period to account for the impacts of the Tax Act in their financial statements. The Company adopted ASU 2018-05 in March 2018. The Company has accounted for the impacts of the Tax Act, including the use of reasonable estimates where necessary. The Company may continue to refine its estimates throughout the measurement period.

#### *Accounting Standards Not Yet Adopted*

In February 2016, the FASB issued ASU 2016-02, *Leases*. The new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. Avalon is currently reviewing its agreements and in the process of calculating the ROU asset and related lease liability for its golf carts, machinery and equipment for the landfill operations, furniture and fixtures for The Avalon Inn and office copiers under operating leases. The Company is also evaluating the impact the adoption of this guidance will have on its financial position, results of operations, cash flows and related disclosures. Upon adoption, the Company expects that the ROU asset and the lease liability will be recognized in the balance sheets in amounts that will be material.



In June 2016, the FASB issued ASU 2016-13, *Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”), which significantly changes the way entities recognize impairment of many financial assets by requiring immediate recognition of estimated credit losses expected to occur over their remaining life. ASU 2016-13 is effective January 1, 2020, with early adoption permitted January 1, 2019. The adoption of this standard is not expected to have a material impact on Avalon’s financial position, results of operations or financial statement disclosures.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

Avalon does not have significant exposure to changing interest rates. Borrowings under our Term Loan Agreement bear interest at a fixed rate of 5.35% until the fifth anniversary date of the closing at which time the interest rate will be reset to a fixed rate equal to the greater of (a) 5.35% per annum or (b) the sum of the Index Rate on the date two (2) business days prior to the reset date and 3.95%, provided that the applicable rate shall in no event exceed 7.50% per annum. Outstanding borrowings under our Line of Credit Agreement bear interest at Prime Rate plus .25%. At September 30, 2018, the interest rate on the Line of Credit Agreement was 5.25%. Effective October 1, 2018, the interest rate on the Line of Credit Agreement increased to 5.50%. No amounts were outstanding under the Line of Credit Agreement at September 30, 2018.

Avalon does not undertake any specific actions to cover its exposure to interest rate risk and Avalon is not a party to any interest rate risk management transactions. Avalon does not purchase or hold any derivative financial instruments.

### **Item 4. Controls and Procedures**

As required by Rule 13a-15 under the Securities Exchange Act of 1934 (the "Exchange Act"), Avalon's management conducted an evaluation, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of September 30, 2018. For purposes of the foregoing, the term disclosure controls and procedures means controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's ("SEC") rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Avalon's disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives as outlined above. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that they believe that, as of September 30, 2018, our disclosure controls and procedures were effective at a reasonable assurance level.

#### **Changes in Internal Controls over Financial Reporting.**

There were no changes in our internal controls over financial reporting during the fiscal quarter ended September 30, 2018 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting. We implemented internal controls to ensure we adequately evaluated our contracts and properly assessed the impact of the new accounting standard related to revenue recognition on our financial statements to facilitate their adoption on January 1, 2018. There were no significant changes to our internal control over financial reporting due to the adoption of the new standard.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings**

Reference is made to “Item 3. Legal Proceedings” in Avalon’s Annual Report on Form 10-K for the year ended December 31, 2017 for a description of legal proceedings.

### **Item 2. Changes in Securities and Use of Proceeds**

None

### **Item 3. Defaults upon Senior Securities**

None

### **Item 4. Mine Safety Disclosures**

None

### **Item 5. Other Information**

None

### **Item 6. Exhibits and Reports on Form 8-K**

(a) Exhibits

Exhibit 31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Exhibit 32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Exhibit 101.INS\* XBRL Instance

Exhibit 101.SCH\* XBRL Taxonomy Extension Schema

Exhibit 101.CAL\* XBRL Taxonomy Extension Calculation

Exhibit 101.DEF\* XBRL Taxonomy Extension Definition

Exhibit 101.LAB\* XBRL Taxonomy Extension Labels

Exhibit 101.PRE\* XBRL Taxonomy Extension Presentation

XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

(b) Reports on Form 8-K

On July 30, 2018, Avalon issued a press release regarding the recent trading activity of the Company's common stock.

On August 1, 2018, Avalon reported the Ohio 10<sup>th</sup> District Court of Appeals decision on the appeal of Company's salt water injection well restart order.

SIGNATURE

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.

AVALON  
HOLDINGS  
CORPORATION  
(Registrant)

Date: November 8, 2018 By: /s/ Bryan P. Saksa  
Bryan P. Saksa, Chief  
Financial Officer and  
Treasurer (Principal  
Financial and  
Accounting  
Officer and Duly  
Authorized Officer)