Advanced Emissions Solutions, Inc.
Form 10-Q
November 06, 2018

United States
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018
or
¨TRANSITION REPORT PURSUANT TO 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number: 001-37822

Advanced Emissions Solutions, Inc.
(Exact name of registrant as specified in its charter)

Delaware	27-5472457
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

640 Plaza Drive, Suite 270, Highlands Ranch, CO	80129
(Address of principal executive offices)	(Zip Code)

(720) 598-3500
(Registrant’s telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	o	Accelerated filer	x
Non-accelerated filer	o	Smaller reporting company	x
		Emerging growth company	¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date.

Class	Outstanding at November 1, 2018
Common stock, par value $0.001 per share	19,915,631

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Part I. – FINANCIAL INFORMATION
Item 1. Consolidated Financial Statements
Advanced Emissions Solutions, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(Unaudited)

(in thousands, except share data)	As of September 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$31,914	$ 30,693
Receivables, net	817	1,113
Receivables, related parties, net	4,104	3,247
Prepaid expenses and other assets	2,631	1,835
Total current assets	39,466	36,888
Property and equipment, net of accumulated depreciation of $1,126 and $1,486, respectively	229	410
Equity method investments	5,383	4,351
Deferred tax assets	36,008	38,661
Other long-term assets	2,070	2,308
Total Assets	$83,156	$ 82,618
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$660	$ 1,000
Accrued payroll and related liabilities	1,970	1,384
Billings in excess of costs on uncompleted contracts	—	1,830
Other current liabilities	627	2,664
Total current liabilities	3,257	6,878
Other long-term liabilities	295	2,285
Total Liabilities	3,552	9,163
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock: par value of $.001 per share, 50,000,000 shares authorized, none outstanding	—	—
Common stock: par value of $.001 per share, 100,000,000 shares authorized, 22,646,524 and 22,465,821 shares issued, and 19,921,128 and 20,752,055 shares outstanding at September 30, 2018 and December 31, 2017, respectively	23	22
Treasury stock, at cost: 2,725,396 and 1,713,766 shares as of September 30, 2018 and December 31, 2017, respectively	(27,566)	(16,397)
Additional paid-in capital	96,251	105,308
Retained earnings (deficit)	10,896	(15,478)
Total stockholders' equity	79,604	73,455
Total Liabilities and Stockholders' Equity	$83,156	$ 82,618

See Notes to the Condensed Consolidated Financial Statements.

Advanced Emissions Solutions, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(Unaudited)

(in thousands, except per share data)	Three Months Ended September 30, 2018	2017	Nine Months Ended September 30, 2018	2017
Revenues:				
Chemicals	$1,043	$717	$2,390	$3,844
License royalties, related party	4,104	2,804	10,857	6,425
Equipment sales	—	1,577	72	31,304
Total revenues	5,147	5,098	13,319	41,573
Operating expenses:				
Chemicals cost of revenue, exclusive of depreciation and amortization	954	574	2,567	2,977
Equipment sales cost of revenue, exclusive of depreciation and amortization	—	1,467	(346)	28,260
Payroll and benefits	2,555	1,679	7,528	5,894
Rent and occupancy	250	255	766	555
Legal and professional fees	698	1,062	3,459	3,316
General and administrative	584	1,114	2,332	2,964
Depreciation and amortization	74	87	262	687
Total operating expenses	5,115	6,238	16,568	44,653
Operating income (loss)	32	(1,140)	(3,249)	(3,080)
Other income (expense):				
Earnings from equity method investments	9,715	12,120	37,857	36,089
Interest expense	(399)	(678)	(1,147)	(1,999)
Other	86	(924)	146	2,492
Total other income	9,402	10,518	36,856	36,582
Income before income tax expense	9,434	9,378	33,607	33,502
Income tax expense	3,931	3,586	5,151	12,614
Net income	$5,503	$5,792	$28,456	$20,888
Earnings per common share (Note 1):				
Basic	$0.28	$0.28	$1.41	$0.96
Diluted	$0.28	$0.28	$1.40	$0.96
Weighted-average number of common shares outstanding:				
Basic	19,726	20,808	20,090	21,569
Diluted	19,876	20,854	20,228	21,598
Cash dividends declared per common share outstanding:	$0.25	$0.25	$0.75	$0.50

See Notes to the Condensed Consolidated Financial Statements.

Advanced Emissions Solutions, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Nine Months Ended September 30,	
(in thousands)	2018	2017
Cash flows from operating activities		
Net income	$28,456	$20,888
Adjustments to reconcile net income to net cash used in operating activities:		
Deferred tax expense from change in valuation allowance	2,731	—
Depreciation and amortization	262	687
Debt prepayment penalty and amortization of debt issuance costs	—	109
Impairment of cost method investment	—	464
Provision for bad debt expense	153	—
Stock-based compensation expense	1,929	1,648
Earnings from equity method investments	(37,857)	(36,089)
Other non-cash items, net	37	436
Changes in operating assets and liabilities:		
Receivables	482	7,027
Related party receivables	(857)	(869)
Prepaid expenses and other assets	(797)	(513)
Costs incurred on uncompleted contracts	15,945	27,081
Deferred tax assets, net	(966)	11,086
Other long-term assets	—	(766)
Accounts payable	(340)	(603)
Accrued payroll and related liabilities	587	(825)
Other current liabilities	(1,974)	(917)
Billings on uncompleted contracts	(15,945)	(30,140)
Other long-term liabilities	(157)	147
Legal settlements and accruals	—	(11,606)
Distributions from equity method investees, return on investment	4,000	3,675
Net cash used in operating activities	(4,311)	(9,080)

	Nine Months Ended September 30,	
(in thousands)	2018	2017
Cash flows from investing activities		
Distributions from equity method investees in excess of cumulative earnings	33,575	33,363
Acquisition of property, equipment and intangibles, net	(191)	(343)
Purchases of and contributions to equity method investees	(750)	(61)
Net cash provided by investing activities	32,634	32,959
Cash flows from financing activities		
Dividends paid	(15,226)	(10,458)
Repurchase of common shares	(11,169)	(13,024)
Repurchase of common shares to satisfy tax withholdings	(707)	(518)
Borrowings on Line of Credit	—	808
Repayments on Line of Credit	—	(808)
Net cash used in financing activities	(27,102)	(24,000)
Increase (decrease) in Cash and Cash Equivalents and Restricted Cash	1,221	(121)
Cash and Cash Equivalents and Restricted Cash, beginning of period	30,693	26,944
Cash and Cash Equivalents and Restricted Cash, end of period	$31,914	$26,823
Supplemental disclosure of cash flow information:		
Cash paid for interest	$1,020	$2,391
Cash paid for income taxes	$4,756	$1,160
Supplemental disclosure of non-cash investing and financing activities:		
Dividends declared, not paid	$85	$93

See Notes to the Condensed Consolidated Financial Statements.

Advanced Emissions Solutions, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1 - Basis of Presentation

Nature of Operations

Advanced Emissions Solutions, Inc. ("ADES" or the "Company") is a Delaware corporation with its principal office located in Highlands Ranch, Colorado. The Company is principally engaged in emissions control ("EC") technologies and associated consumables, equipment and services. The Company's proprietary environmental technologies enable customers to reduce emissions of mercury and other pollutants, maximize utilization levels and improve operating efficiencies to meet the challenges of existing and pending EC regulations. The Company generates substantial earnings and tax credits under Section 45 ("Section 45 tax credits") of the Internal Revenue Code ("IRC") from its equity investments in certain entities and royalty payments related to technologies that are licensed to Tinuum Group, LLC, a Colorado limited liability company ("Tinuum Group"). Such technologies allow Tinuum Group to provide its customers with various solutions to enhance combustion and reduce emissions of nitrogen oxide ("NO_x") and mercury from coal burned to generate electrical power. The Company’s sales occur principally throughout the United States. See Note 10 for additional information regarding the Company's operating segments.

Basis of Presentation

The accompanying Condensed Consolidated Financial Statements of ADES are unaudited and have been prepared in conformity with accounting principles generally accepted in the United States ("U.S. GAAP") and with Article 10 of Regulation S-X of the Securities and Exchange Commission. In compliance with those instructions, certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with U.S. GAAP have been condensed or omitted.

The unaudited Condensed Consolidated Financial Statements of ADES in this quarterly report ("Quarterly Report") are presented on a consolidated basis and include ADES and its wholly-owned subsidiaries (collectively, the "Company"). Also included within the unaudited Condensed Consolidated Financial Statements are the Company's unconsolidated equity investments, Tinuum Group, Tinuum Services, LLC ("Tinuum Services"), and GWN Manager, LLC ("GWN Manager"), which are accounted for under the equity method of accounting, and Highview Enterprises Limited (the "Highview Investment"), which is accounted for in accordance with U.S. GAAP applicable to equity investments that do not qualify for the equity method of accounting.

Results of operations and cash flows for the interim periods are not necessarily indicative of the results that may be expected for the entire year. All significant intercompany transactions and accounts were eliminated for all periods presented in this Quarterly Report.

In the opinion of management, these Condensed Consolidated Financial Statements include all normal and recurring adjustments considered necessary for a fair presentation of the results of operations, financial position and cash flows for the interim periods presented. These Condensed Consolidated Financial Statements of ADES should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2017 (the "2017 Form 10-K"). Except for accounting for revenue from contracts with customers, which is discussed in Note 2, significant accounting policies disclosed therein have not changed.

Earnings Per Share

Basic earnings per share is computed using the two-class method, which is an earnings allocation formula that determines earnings per share for common stock and any participating securities according to dividend and participating rights in undistributed earnings. The Company's restricted stock awards ("RSA's") granted prior to December 31, 2016 contain non-forfeitable rights to dividends or dividend equivalents and are deemed to be participating securities. RSA's granted subsequent to December 31, 2016 do not contain non-forfeitable rights to dividends and are not deemed to be participating securities.

Under the two-class method, net income for the period is allocated between common stockholders and the holders of the participating securities based on the weighted-average number of common shares outstanding during the period, excluding participating, unvested RSA's ("common shares"), and the weighted-average number of participating unvested RSA's outstanding during the period, respectively. The allocated, undistributed income for the period is then divided by the weighted-average number of common shares and participating, unvested RSA's outstanding during the period to arrive at basic earnings per common share and participating security for the period, respectively. Pursuant to U.S. GAAP, the Company has elected not to separately present basic or diluted earnings per share attributable to participating securities in the Condensed Consolidated Statements of Operations.

Diluted earnings per share is computed in a manner consistent with that of basic earnings per share, while considering other potentially dilutive securities. Potentially dilutive securities consist of both unvested, participating and non-participating RSA's, as well as outstanding options to purchase common stock ("Stock Options") and contingent performance stock units ("PSU's") (collectively, "Potential dilutive shares"). The dilutive effect, if any, for non-participating RSA's, Stock Options and PSU's is determined using the greater of dilution as calculated under the treasury stock method or the two-class method. Potential dilutive shares are excluded from diluted earnings per share when their effect is anti-dilutive. When there is a net loss for a period, all Potential dilutive shares are anti-dilutive and are excluded from the calculation of diluted loss per share for that period.

Each PSU represents a contingent right to receive shares of the Company’s common stock, and the number of shares may range from zero to two times the number of PSU's granted on the award date depending upon the price performance of the Company's common stock as measured against a general index and a specific peer group index over requisite performance periods. The number of Potential dilutive shares related to PSU's is based on the number of shares of the Company's common stock, if any, that would be issuable at the end of the respective reporting period, assuming that the end of the reporting period is the end of the contingency period applicable to such PSU's. See Note 7 for additional information related to PSU's.

The following table sets forth the calculations of basic and diluted earnings per share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands, except per share amounts)	2018	2017	2018	2017
Net income	$5,503	$5,792	$28,456	$20,888
Less: Dividends and undistributed income allocated to participating securities	18	32	94	141
Income attributable to common stockholders	$5,485	$5,760	$28,362	$20,747
Basic weighted-average common shares outstanding	19,726	20,808	20,090	21,569
Add: dilutive effect of equity instruments	150	46	138	29
Diluted weighted-average shares outstanding	19,876	20,854	20,228	21,598
Earnings per share - basic	$0.28	$0.28	$1.41	$0.96
Earnings per share - diluted	$0.28	$0.28	$1.40	$0.96

For the three and nine months ended September 30, 2018 and 2017, RSA's and Stock Options convertible to 0.3 million and 0.2 million shares, respectively, and 0.3 million and 0.2 million shares, respectively, of common stock for each of the periods presented were outstanding but were not included in the computation of diluted net income per share because the effect would have been anti-dilutive. For the nine months ended September 30, 2018, Stock Options to purchase 0.1 million shares were outstanding, which vest based on the Company achieving specified performance targets, but were not included in the computation of diluted net income per share for a portion of the period because they were determined not to be contingently issuable. For the three and nine months ended September 30, 2017, Stock Options to purchase 0.4 million and 0.4 million shares, respectively, of common stock, which vest based on the Company achieving specified performance targets, were outstanding, but were not included in the computation of diluted net income per share because they were determined not to be contingently issuable.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to makes estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. There have been no changes in the Company’s critical accounting estimates from those that were disclosed in the 2017 Form 10-K, except for the adoption of ASC 606 - Revenue from Contracts with Customers ("ASC 606"), effective January 1, 2018, which affected revenue recognition and warranty estimates accruals related to the Company's extended equipment contracts, and an estimated liability related to a royalty settlement agreement, both of which are no longer considered significant estimates. Actual results could differ from these estimates.

Risks and Uncertainties

The Company’s earnings are significantly affected by equity earnings it receives from Tinuum Group. As of September 30, 2018, Tinuum Group has 18 invested RC facilities of which 11 are leased to a single customer. A majority of these leases are periodically renewed and the loss of this customer by Tinuum Group would have a significant adverse impact on its financial position, results of operations and cash flows, which in turn would have material adverse impact on the Company’s financial position, results of operations and cash flows.

Reclassifications
Certain balances have been reclassified from the prior year to conform to the current year presentation. No reclassifications have any impact to income before income taxes or net income.
New Accounting Guidance
In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) ("ASU 2016-02"), which requires lessees to recognize a right of use asset and related lease liability for those leases classified as operating leases at the commencement date and have lease terms of more than 12 months. This topic retains the distinction between finance leases and operating leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, and interim periods within those years, and must be applied under a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. In July 2018, the FASB issued ASU 2018-11, Leases (Topic 842): Targeted Improvements ("ASU 2018-11"). The amendments in ASU 2018-11 provide entities with an additional (and optional) transition method to adopt the new lease requirements by allowing entities to initially apply the requirements by recognizing a cumulative effect adjustment to the opening balance of retained earnings in the period of adoption. Consequently, an entity’s reporting for the comparative periods presented in the financial statements in which the entity adopts the new lease requirements would continue to be in accordance with current GAAP (Topic 840). An entity electing this additional (and optional) transition method must provide the required Topic 840 disclosures for all periods that continue to be in accordance with Topic 840. The amendments do not change the existing disclosure requirements in Topic 840. The Company intends to adopt ASC 2016-02 effective January 1, 2019 using the additional (and optional) transition method provided under ASU 2018-11.
As of the date of this filing, the Company has materially completed its assessment of ASU 2016-02 and related amendments for the impact to the financial statements as of the adoption date, completed a detailed review of existing lease agreements, continued its review of controls and procedures that may need to be revised or added from the adoption of ASU 2016-02 and completed the documentation of the standard's financial statement impact at adoption and financial statement disclosure changes. Based on the Company's current assessment of ASU 2016-02, it has determined that at adoption it will record approximately $0.2 million of "right of use" assets and incremental lease liabilities, respectively, with no impact to the opening balance of retained earnings.
In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326) Measurement of Credit Losses on Financial Instruments ("ASU 2016-13"). The main objective of ASU 2016-13 is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the amendments in ASU 2016-13 replace the incurred loss impairment methodology in current U.S. GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, including interim periods within those years, and must be adopted under a modified retrospective method approach. Entities may adopt ASU 2016-13 earlier as of the fiscal years beginning after December 15, 2018, including interim periods within those years. The Company is currently evaluating the provisions of this guidance and assessing its impact on the Company's financial statements and disclosures. The Company does not believe this standard will have a material impact on the Company's financial statements and disclosures.
In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement (Topic 820) Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement ("ASU 2018-13"). The amendments in ASU 2018-13 improve the effectiveness of fair value measurement disclosures and modify the disclosure requirements on fair value measurements in Topic 820, Fair Value Measurement ("Topic 820"), based on the concepts in FASB Concepts Statement, Conceptual Framework for Financial Reporting - Chapter 8: Notes to Financial Statements, including the consideration of costs and benefits. ASU 2018-13 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The amendments on changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements, and the narrative description of measurement uncertainty should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied

retrospectively to all periods presented upon their effective date. Early adoption is permitted upon issuance of this Update. An entity is permitted to early adopt any removed or modified disclosures upon issuance of this Update and delay adoption of the additional disclosures until their effective date. The Company is currently evaluating the provisions of this Update and assessing its impact on the Company's financial statement disclosures. The Company does not believe this standard will have a material impact on the Company's financial statement disclosures.

Note 2 - Revenues

Adoption of ASC 606

On January 1, 2018, the Company adopted ASC 606 using the modified retrospective method applied to those contracts that were not completed as of January 1, 2018. The Company recognized the cumulative effect of initially applying ASC 606 to the opening balance of the Accumulated deficit. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

The financial statement impact from the adoption of ASC 606 as of January 1, 2018 was primarily due to the following:

- The recognition of revenues and related cost of revenue from Equipment Sales for three uncompleted dry sorbent injection ("DSI") equipment systems (the "DSI Systems") as of December 31, 2017, which were accounted for under the guidance in ASC 605-35, Revenue Recognition - Construction-Type and Production-Type Contracts ("ASC 605-35"). Under ASC 605-35, the Company accounted for revenues and associated cost of revenue for equipment systems from inception of the contract under the completed contract method and recognized revenue and cost of revenue when the equipment systems were deemed substantially complete. As of December 31, 2017, none of the DSI Systems had met the revenue recognition criteria under the completed contract method. As of January 1, 2018, the Company has determined that the performance obligation associated with each DSI System has been satisfied under ASC 606 guidance.
- The recognition of revenues and related cost of revenue for a licensing arrangement (the "Licensing Arrangement") in which the Company satisfied its performance obligation under ASC 606 as of January 1, 2018.

As a result, the Company's deferred revenue and related deferred project costs on the three DSI Systems and the Licensing Arrangement, and the resultant income tax effects, were recognized through a cumulative effect adjustment to the Accumulated deficit as of January 1, 2018. In addition, the Company recorded a contract asset in the amount of $0.3 million related to one DSI System contract for which the Company has completed its performance obligations but is not contractually able to bill the customer until the end of the warranty period.

The cumulative effect of the change from the adoption of ASC 606 to the Consolidated Balance Sheet as of January 1, 2018 is shown in the table that follows:

(in thousands)	Balance as of December 31, 2017	Impact of Adoption	Balance as of January 1, 2018
Balance Sheet			
Receivables, net	$ 1,113	$ 339	$ 1,452
Deferred tax assets	$ 38,661	$ (889)	$ 37,772
Other long-term assets	$ 2,308	$ (322)	$ 1,986
Billings in excess of costs on uncompleted contracts	$ 1,830	$ (1,830)	$—
Other current liabilities	$ 2,664	$ 9	$ 2,673
Other long-term liabilities	$ 2,285	$ (2,000)	$ 285
Accumulated deficit	$ (15,478)	$ 2,950	$ (12,528)

The following tables show the impact of the adoption of ASC 606 on the Condensed Consolidated Balance Sheet and Condensed Consolidated Statement of Operations as of and for the three and nine months ended September 30, 2018, respectively:

(in thousands)	Balance as Reported September 30, 2018	Impact of Adoption	Balance as Adjusted September 30, 2018
Balance Sheet			
Receivables, net	$ 817	$—	$ 817
Deferred tax assets	$ 36,008	$ 425	$ 36,433

Other long-term assets	$ 2,070	$ 322	$ 2,392
Billings in excess of costs on uncompleted contracts	$ —	$ —	$ —
Other current liabilities	$ 627	$ —	$ 627
Other long-term liabilities	$ 295	$ 2,000	$ 2,295
Retained earnings (deficit)	$ 10,896	$ (1,253)	$ 9,643

	For the three months ended		
(in thousands)	As Reported September 30, 2018	Impact of Adoption	As Adjusted September 30, 2018
Statement of Operations			
Revenues:			
Equipment sales	$—	$10,042	$ 10,042
License royalties, related party	$4,104	$(4,104)	$ —
Total revenues	$5,147	$5,938	$ 11,085
Operating expenses:			
Equipment sales cost of revenue	$—	$7,874	$ 7,874
Total operating expenses	$5,115	$7,874	$ 12,989
Operating loss	$32	$(1,936)	$ (1,904)
Other income (expense)			
Royalties, related party	$—	$4,104	$ 4,104
Total other income (expense)	$9,402	$4,104	$ 13,506
Income before income tax expense	$9,434	$2,168	$ 11,602
Income tax expense	$3,931	$464	$ 4,395
Net income	$5,503	$1,704	$ 7,207

	For the nine months ended		
(in thousands)	As Reported September 30, 2018	Impact of Adoption	As Adjusted September 30, 2018
Statement of Operations			
Revenues:			
Equipment sales	$72	$17,574	$ 17,646
License royalties, related party	$10,857	$(10,857)	$ —
Total revenues	$13,319	$6,717	$ 20,036
Operating expenses:			
Equipment sales cost of revenue	$(346)	$15,399	$ 15,053
Total operating expenses	$16,568	$15,399	$ 31,967
Operating loss	$(3,249)	$(8,682)	$ (11,931)
Other income (expense)			
Royalties, related party	$—	$10,857	$ 10,857
Total other income (expense)	$36,856	$10,857	$ 47,713
Income before income tax expense	$33,607	$2,175	$ 35,782
Income tax expense	$5,151	$464	$ 5,615
Net income	$28,456	$1,711	$ 30,167

As of and for the three and nine months ended September 30, 2018, the significant difference between the financial statement balances reported compared to the financial statement balances without the adoption of ASC 606 were as follows:

- Equipment sales -As of adoption, the Company derecognized contract assets of $16.5 million and contract liabilities of $18.3 million and recorded a contract asset of $0.3 million related to the three DSI Systems contracts that met the revenue recognition requirements under ASC 606. After tax, the net adjustment for the three DSI Systems was $1.7 million. Under revenue recognition guidance in effect prior to the adoption of ASC 606, one DSI Systems contract would have met revenue recognition criteria as of June 30, 2018, and a second DSI System contract would have met revenue recognition criteria as of September 30, 2018. For the first DSI System contract, the Company would have recorded $7.5 million of Equipment sales and $7.5 million Equipment sales cost of revenue, respectively, for the three months ended June 30, 2018. For the second DSI System contract, the Company would have recognized Equipment sales of $10.0 million and Equipment sales cost of revenue of $7.9 million, respectively, for the three months ended September 30, 2018. For the nine months ended September 30, 2018, the Company would have recognized $17.6 million of Equipment sales and $15.4 million of Equipment sales cost of revenue, respectively, for the two DSI System contracts.

- Licensing Arrangement - As of adoption, the Company derecognized a contract liability of $2.0 million and a contract asset of $0.3 million related to the Licensing Arrangement, which met the revenue recognition requirements under ASC 606. After tax, the net adjustment for this contract was $1.3 million. Under revenue recognition guidance in effect prior to the adoption of ASC 606, this contract would not have met revenue recognition criteria as of September 30, 2018.
- Royalties, related party - As of adoption, and based on guidance provided in ASC 606 related to licensing arrangements where royalties are earned on a usage-based royalty arrangement, for the three and nine months ended September 30, 2018, as well as the corresponding periods from the prior year, the Company has reported license royalties earned from Tinuum Group as revenues rather than as non-operating income under financial statement presentation guidance in effect prior to the adoption of ASC 606. This reclassification had no impact to the Company’s income before income tax expense or net income for all periods presented.

Revenue Recognition

The Company recognizes revenue from a contract with a customer when a performance obligation under the terms of a contract with a customer is satisfied, which is when the customer controls the promised goods or services that are transferred in satisfaction of the performance obligation. Revenue is measured as the amount of consideration that is expected to be received in exchange for transferring goods or providing services, and the transaction price is generally fixed and generally does not contain variable or noncash consideration. In addition, the Company’s contracts with customers generally do not contain customer refund or return provisions or other similar obligations. Transfer of control and satisfaction of performance obligations are further discussed in each of the revenue components listed below.

The Company uses estimates and judgments in determining the nature and timing of satisfaction of performance obligations, the standalone selling price (“SSP”) of performance obligations and the allocation of the transaction price to multiple performance obligations.

The Company’s principal revenue components are Chemical sales and License royalties.

Chemicals

The Company recognizes revenue for direct sales of proprietary chemicals and other ancillary items when the customer obtains control, which is generally at the point in time that delivery to and acceptance by the customer has occurred. Customer contracts for sales of chemicals are short duration and performance obligations generally do not extend beyond one year.

Certain chemical customer contracts are comprised of evaluation tests of the Company’s chemicals’ effectiveness and efficiency in reducing emissions. These contracts entail the delivery of chemicals to the customer and the Company's evaluation of results of emissions reduction over the term of the contract. Under these types of arrangements, which are generally for durations that are short term, the Company has determined that the customer is simultaneously receiving benefits of emissions reduction from the consumption of the chemicals over the testing period and this represents a single performance obligation that is satisfied over time. This determination may require significant judgment. The Company recognizes revenue over time using an input model that is generally based on the cost of chemicals consumed by the customer during the testing period. The use of an input model and the use of total costs as the measure of progress in the satisfaction of the performance obligations may require significant judgment. In addition, under these types of contracts, the Company has determined that the services performed and related costs incurred by the Company during the testing period represent costs to fulfill a contract.

License Royalties

The Company generates revenues from royalties (“M-45 Royalties”) earned under a licensing arrangement (“M-45 License”) of its M-45™ and M-45-PC™ emissions control technologies (“M-45 Technology”) between the Company and Tinuum Group. The Company recognizes M-45 Royalties at a point in time based on the use of the M-45

Technology at certain RC facilities or through Tinuum Group’s use of licensed technology for rates in excess of amounts allowed for RC application. The amount of M-45 Royalties recognized is generally based on a percentage of pre-tax margins (as defined in the M-45 License) of the RC facilities using the M-45 Technology.

Arrangements with Multiple Performance Obligations

Contracts with customers may include multiple performance obligations, which are comprised of the sale of chemicals, equipment and services performed as part of an emissions reduction arrangement. For such arrangements, the Company allocates revenue to each performance obligation based on its relative SSP. When a directly observable SSP for a performance obligation is not available, the Company primarily estimates SSPs based on the expected cost plus a margin method. These estimates as well as the timing of the satisfaction of performance obligations associated with the services component represent significant judgments made by the Company. These arrangements are generally short duration and performance obligations generally do not extend beyond one year.

Contract Assets and Liabilities

Contract assets are comprised of unbilled receivables and are included in Receivables, net in the Condensed Consolidated Balance Sheet. Unbilled receivables represent a conditional right to consideration in exchange for goods or services transferred to a customer.

Trade receivables represent an unconditional right to consideration in exchange for goods or services transferred to a customer. The Company invoices its customers in accordance with the terms of the contract. Credit terms are generally net 30 from the date of invoice. The timing between the satisfaction of performance obligations and when payment is due from the customer is generally not significant. The Company records allowances for doubtful trade receivables when it is probable that the balances will not be collected.

Contract liabilities are comprised of deferred revenue, which represents an obligation to transfer goods or services to a customer for which the Company has received consideration from the customer and, if deliverable within one year or less, is included in Other current liabilities in the Condensed Consolidated Balance Sheet and, if deliverable outside of one year, is included in Other long-term liabilities in the Condensed Consolidated Balance Sheet.

Disaggregation of Revenue

During the three and nine months ended September 30, 2018, all performance obligations related to revenues recognized were satisfied at a point in time. The Company disaggregates its revenues by its major components as well as between its two operating segments, which are further discussed in Note 10 to the condensed consolidated financial statements. The following tables disaggregate revenues by major source for the three and nine months ended September 30, 2018 (in thousands):

	Three Months Ended September 30, 2018		
	Segment		
	EC	RC	Total
Revenue component			
Chemical sales	$1,043	$—	$1,043
License royalties, related party	—	4,104	4,104
Equipment sales	—	—	—
Revenues from customers	1,043	4,104	5,147
Earnings from equity method investments	—	9,715	9,715
Segment revenues	$1,043	$13,819	$14,862

	Nine Months Ended September 30, 2018		
	Segment		
	EC	RC	Total
Revenue component			
Chemical sales	$2,390	$—	$2,390
License royalties, related party	—	10,857	10,857
Equipment sales	72	—	72
Revenues from customers	2,462	10,857	13,319
Earnings from equity method investments	—	37,857	37,857

Segment revenues	$2,462	$48,714	$51,176

Practical Expedients and Exemptions

The Company does not disclose the value of unsatisfied performance obligations for contracts with an original expected length of one year or less.

Sales and other taxes that are collected concurrently with revenue-producing activities are excluded from revenue.

The Company has also elected to account for freight costs as activities to fulfill the promise to transfer the goods, and therefore these activities are also not assessed as a separate service to customers.

The Company accounts for all shipping and handling activities that occur after control of the related good transfers as fulfillment activities. These activities are included in Cost of Revenue line items of the Condensed Consolidated Statement of Operations.

The Company generally expenses sales commissions when incurred because the amortization period of the asset that the Company would have recognized is one year or less. These costs are recorded within sales and marketing expenses within the General and administrative line item of the Condensed Consolidated Statement of Operations.

Note 3 - Equity Method Investments

Tinuum Group, LLC

The Company's ownership interest in Tinuum Group was 42.5% as of September 30, 2018 and December 31, 2017. Tinuum Group supplies technology equipment and technical services at select coal-fired generators, but its primary purpose is to put into operation facilities that produce and sell RC that lower emissions and therefore qualify for Section 45 tax credits. Tinuum Group has been determined to be a variable interest entity ("VIE"); however, the Company does not have the power to direct the activities that most significantly impact Tinuum Group's economic performance and has therefore accounted for the investment under the equity method of accounting. The Company determined that the voting partners of Tinuum Group have identical voting rights, equity control interests and board control interests, and therefore, concluded that the power to direct the activities that most significantly impact Tinuum Group's economic performance was shared.

The following table summarizes the results of operations of Tinuum Group:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
Gross profit	$26,530	$23,812	$81,626	$70,895
Operating, selling, general and administrative expenses	5,908	5,174	17,406	14,975
Income from operations	20,622	18,638	64,220	55,920
Other expenses	(577)	(3,331)	(2,801)	(4,278)
Class B preferred return	—	(384)	(12)	(1,526)
Loss attributable to noncontrolling interest	17,126	11,953	38,145	29,240
Net income available to members	$37,171	$26,876	$99,552	$79,356
ADES equity earnings from Tinuum Group	$8,075	$11,050	$33,575	$33,363

As of September 30, 2018 and December 31, 2017, the amount of Tinuum Group's temporary Class B preferred equity was zero and $0.8 million, respectively.

The difference between the Company's proportionate share of Tinuum Group's net income available to members (at its equity interest of 42.5%) as presented in the table below and the Company's earnings from its Tinuum Group equity method investment as reported in the Condensed Consolidated Statements of Operations relates to the Company receiving distributions in excess of the carrying value of the equity investment, and therefore recognizing such excess distributions as equity method earnings in the period the distributions occur, as discussed below.

As shown in the tables below, the Company’s carrying value in Tinuum Group was reduced to zero for the three and nine months ended September 30, 2018, as cumulative cash distributions received from Tinuum Group exceeded the Company's pro-rata share of cumulative earnings in Tinuum Group. The carrying value of the Company's investment in Tinuum Group shall remain zero as long as the cumulative amount of distributions received from Tinuum Group continues to exceed the Company's cumulative pro-rata share of Tinuum Group's net income available to its members. For periods during which the ending balance of the Company's investment in Tinuum Group is zero, the Company only recognizes equity earnings from Tinuum Group to the extent that cash distributions are received from Tinuum Group during the period. For periods during which the ending

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balance of the Company's investment is greater than zero (e.g., when the cumulative earnings in Tinuum Group exceeds cumulative cash distributions received), the Company recognizes its pro-rata share of Tinuum Group's net income available to its members for the period, less any amount necessary to recover the cumulative earnings short-fall balance as of the end of the immediately preceding period. During the three and nine months ended September 30, 2018, the Company's cumulative amount of distributions received from Tinuum Group exceeded the Company's cumulative pro-rata share of Tinuum Group's net income available to its members. As such, the Company recognized equity earnings from Tinuum Group for the three and nine months ended September 30, 2018 of $8.1 million and $33.6 million, respectively. During the three and nine months ended September 30, 2017, the Company recognized equity earnings from Tinuum Group in the amount of $11.1 million and $33.4 million, respectively. As of September 30, 2018 and 2017, the Company's carrying value in Tinuum Group was zero and zero, respectively. Thus, the amount of equity earnings or loss reported on the Company's Condensed Consolidated Statement of Operations may differ from a mathematical calculation of net income or loss attributable to the equity interest based upon the factor of the equity interest and the net income or loss attributable to members as shown on Tinuum Group’s statement of operations. Additionally, for periods during which the carrying value of the Company's investment in Tinuum Group is greater than zero, distributions from Tinuum Group are reported on the Condensed Consolidated Statements of Cash Flows as "Distributions from equity method investees, return on investment" within Operating cash flows. For periods during which the carrying value of the Company's investment in Tinuum Group is zero, such cash distributions are reported on the Condensed Consolidated Statements of Cash Flows as "Distributions from equity method investees in excess of investment basis" within Investing cash flows.

The following tables present the Company's investment balance, equity earnings and cash distributions in excess of the investment balance for the three and nine months ended September 30, 2018 and 2017 (in thousands):

Description	Date(s)	Investment balance	ADES equity earnings (loss)	Cash distributions	Memorandum Account: Cash distributions and equity earnings in (excess) of investment balance
Beginning balance	12/31/2017	$ —	$ —	$ —	$ (12,218)
ADES proportionate share of income from Tinuum Group (1)	First Quarter	12,458	12,458	—	—
Recovery of prior cash distributions in excess of investment balance (prior to cash distributions)	First Quarter	(12,218)	(12,218)	—	12,218
Cash distributions from Tinuum Group	First Quarter	(11,050)	—	11,050	—
Adjustment for current year cash distributions in excess of investment balance	First Quarter	10,810	10,810	—	(10,810)
Total investment balance, equity earnings (loss) and cash distributions	3/31/2018	$ —	$ 11,050	$ 11,050	$ (10,810)
ADES proportionate share of income from Tinuum Group (1)	Second Quarter	$ 14,059	$ 14,059	$ —	$ —
Recovery of prior cash distributions in excess of investment balance (prior to cash distributions)	Second Quarter	(10,810)	(10,810)	—	10,810
Cash distributions from Tinuum Group	Second Quarter	(14,450)	—	14,450	—
Adjustment for current year cash distributions in excess of investment balance	Second Quarter	11,201	11,201		(11,201)
Total investment balance, equity earnings (loss) and cash distributions	6/30/2018	$ —	$ 14,450	$ 14,450	$ (11,201)
ADES proportionate share of income from Tinuum Group (1)	Third Quarter	$ 15,798	$ 15,798	$ —	$ —
Recovery of prior cash distributions in excess of investment balance (prior to cash distributions)	Third Quarter	(11,201)	(11,201)	—	11,201
Cash distributions from Tinuum Group	Third Quarter	(8,075)	—	8,075	—
Adjustment for current year cash distributions in excess of investment balance	Third Quarter	3,478	3,478	—	(3,478)
Total investment balance, equity earnings (loss) and cash distributions	9/30/2018	$ —	$ 8,075	$ 8,075	$ (3,478)

Description	Date(s)	Investment balance	ADES equity earnings (loss)	Cash distributions	Memorandum Account: Cash distributions and equity earnings in (excess) of investment balance
Beginning balance	12/31/2016	$ —	$—	$ —	$ (9,894)
ADES proportionate share of income from Tinuum Group (1)	First Quarter	10,457	10,457	—	—
Recovery of prior cash distributions in excess of investment balance (prior to cash distributions)	First Quarter	(9,894)	(9,894)	—	9,894
Cash distributions from Tinuum Group	First Quarter	(13,175)	—	13,175	—
Adjustment for current year cash distributions in excess of investment balance	First Quarter	12,612	12,612	—	(12,612)
Total investment balance, equity earnings (loss) and cash distributions	3/31/2017	$ —	$13,175	$ 13,175	$ (12,612)
ADES proportionate share of income from Tinuum Group (1)	Second Quarter	$ 11,761	$11,761	$ —	$ —
Recovery of prior cash distributions in excess of investment balance (prior to cash distributions)	Second Quarter	(11,761)	(11,761)	—	11,761
Cash distributions from Tinuum Group	Second Quarter	(9,138)	—	9,138	—
Adjustment for current year cash distributions in excess of investment balance	Second Quarter	9,138	9,138	—	(9,138)
Total investment balance, equity earnings (loss) and cash distributions	6/30/2017	$ —	$9,138	$ 9,138	$ (9,989)
ADES proportionate share of income from Tinuum Group (1)	Third Quarter	$ 11,393	$11,393	$ —	$ —
Recovery of prior cash distributions in excess of investment balance (prior to cash distributions)	Third Quarter	(9,989)	(9,989)	—	9,989
Cash distributions from Tinuum Group	Third Quarter	(11,050)	—	11,050	—
Adjustment for current year cash distributions in excess of investment balance	Third Quarter	9,646	9,646	—	(9,646)
Total investment balance, equity earnings (loss) and cash distributions	9/30/2017	$ —	$11,050	$ 11,050	$ (9,646)

(1) For the three and nine months ended September 30, 2018 and 2017, the amounts of the Company's 42.5% proportionate share of net income available to members as shown in the table above may differ from mathematical calculations of the Company’s 42.5% equity interest in Tinuum Group multiplied by the amounts of net income available to members as shown in the table above of Tinuum Group results of operations due to adjustments related to the Class B preferred return.

Tinuum Services, LLC

The Company has a 50% voting and economic interest in Tinuum Services, which is equivalent to the voting and economic interest of NexGen Refined Coal, LLC ("NexGen"). The Company has determined that Tinuum Services is not a VIE and has evaluated its consolidation analysis under the voting interest model. Because the Company does not own greater than 50% of the outstanding voting shares, either directly or indirectly, it has accounted for its investment in Tinuum Services under the equity method of accounting. The Company's investment in Tinuum Services as of September 30, 2018 and December 31, 2017 was $5.3 million and $4.3 million, respectively. During the nine months ended September 30, 2018, the Company funded a capital call of $0.8 million, which increased its investment balance in Tinuum Services.

The following table summarizes the results of operations of Tinuum Services:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
Gross loss	$(21,362)	$(17,344)	$(64,069)	$(47,472)
Operating, selling, general and administrative expenses	43,947	34,872	127,783	106,825
Loss from operations	(65,309)	(52,216)	(191,852)	(154,297)
Other income	78	34	443	103
Loss attributable to noncontrolling interest	68,509	54,305	199,971	159,627
Net income	$3,278	$2,123	$8,562	$5,433
ADES equity earnings from Tinuum Services	$1,639	$1,061	$4,281	$2,717

Included within the Consolidated Statements of Operations of Tinuum Services for the three and nine months ended September 30, 2018 and 2017, respectively, were losses related to VIE's of Tinuum Services. These losses do not impact the Company's equity earnings from Tinuum Services as 100% of those losses are attributable to a noncontrolling interest and eliminated in the calculations of Tinuum Services' net income attributable to the Company's interest.

The following table details the components of the Company's respective equity method investments included within the Earnings from equity method investments line item on the Condensed Consolidated Statements of Operations:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
Earnings from Tinuum Group	$8,075	$11,050	$33,575	$33,363
Earnings from Tinuum Services	1,639	1,061	4,281	2,717
Earnings from other	1	9	1	9
Earnings from equity method investments	$9,715	$12,120	$37,857	$36,089

The following table details the components of the cash distributions from the Company's respective equity method investments included in the Condensed Consolidated Statements of Cash Flows. Distributions from equity method investees are reported on the Condensed Consolidated Statements of Cash Flows as "Distributions from equity method investees, return on investment" within Operating cash flows until such time as the carrying value in an equity method investee company is reduced to zero; thereafter, such distributions are reported as "Distributions from equity method investees in excess of cumulative earnings" within Investing cash flows.

	Nine Months Ended September 30,	
(in thousands)	2018	2017
Distributions from equity method investees, return on investment		
Tinuum Services	$4,000	$3,675
	$4,000	$3,675
Distributions from equity method investees in excess of investment basis		
Tinuum Group	$33,575	$33,363
	$33,575	$33,363

Note 4 - Borrowings

Line of Credit

On September 30, 2018, ADA-ES., Inc., a wholly-owned subsidiary of the Company ("ADA"), as borrower, the Company, as guarantor, and a bank (the "Lender") entered into an amendment (the "Twelfth Amendment") to the 2013 Loan and Security Agreement (the "Line of Credit"). The Twelfth Amendment decreased the Line of Credit to $5.0 million due to decreased collateral requirements, extended the maturity date of the Line of Credit to September 30, 2020 and permitted the Line of Credit to be used as collateral (in place of restricted cash) for letters of credit

("LC's") up to $5.0 million related to equipment projects and certain other agreements. Under the Line of Credit, there is no minimum balance requirement based on the Company meeting certain conditions and maintaining minimum trailing twelve-month EBITDA (earnings before interest, taxes, depreciation and amortization), as previously defined in the "Eleventh Amendment" to the Line of Credit, of $24.0 million.

As of September 30, 2018, there were no outstanding borrowings under the Line of Credit.

Other

In March 2017, a customer drew on an LC related to an equipment system in the amount of $0.8 million, which was funded by borrowing availability under the Line of Credit. The Company subsequently repaid this amount to the Lender as of March 31, 2017. The Company is contesting the LC draw on this LC and is pursuing legal actions to recover the entire amount from the customer. The Company recorded an asset for the LC Draw net of an estimated allowance of $0.4 million. This amount is included in Other long-term assets on the Condensed Consolidated Balance Sheets.

The following table presents the LC's outstanding and collateral, by asset type, reported on the Condensed Consolidated Balance Sheets. There were no LC's outstanding or collateral as of September 30, 2018.

	As of December 31, 2017	
(in thousands)	LC Outstanding	Utilization of LOC Availability
Royalty Award	$3,500	$ 3,500
Total LC outstanding	$3,500	$ 3,500

Note 5 - Commitments and Contingencies

Legal Proceedings

The Company is from time to time subject to, and is presently involved in, various pending or threatened legal actions and proceedings, including those that arise in the ordinary course of its business. Such matters are subject to many uncertainties and to outcomes, the financial impacts of which are not predictable with assurance and that may not be known for extended periods of time. The Company records a liability in its consolidated financial statements for costs related to claims, settlements, and judgments where management has assessed that a loss is probable and an amount can be reasonably estimated.

Settlement and royalty indemnity

In 2011, the Company and Norit International B.V. ("Norit") entered into a settlement agreement (the "Norit Settlement Agreement") whereby the Company paid amounts related to a non-solicitation breach of contract claim ("Norit Litigation"), and was also required to pay additional damages (the "Royalty Award") related to certain future revenues generated from an activated carbon manufacturing plant (the "Red River Plant") that the Company owned through a joint venture with ADA Carbon Solutions, LLC ("Carbon Solutions"). Payments due under the Royalty Award were due quarterly in arrears through June 2018. Additionally, in 2011, the Company entered into the Settlement Agreement Regarding ADA-ES’ Indemnity Obligations (the "Indemnity Settlement Agreement") whereby the Company agreed to settle certain indemnity obligations asserted against the Company related to the Norit Litigation and relinquished all of its equity interest in Carbon Solutions.

Under the Norit Settlement Agreement, the Company was required to pledge LC's as collateral for a portion of Royalty Award future payments due. In March 2017, the Company was required to increase its LC's under the Royalty Award based on a provision that required additional amounts be pledged because the Company had achieved annual earnings in excess of $20.0 million for the fiscal year ended December 31, 2016. Under this provision, the Company was required to provide an additional LC of $5.0 million, which was secured under the Line of Credit in March 2017. Under a separate provision of the Norit Settlement Agreement effective during 2017, the Company was required to increase the LC's, subject to the aggregate amount of estimated future payments due related to the Royalty Award, for any dividends issued by the Company prior to January 1, 2018 in amount equal to 50% of the aggregate fair market value of such dividends (the "Dividends Provision"). Based on the estimated remaining future payments due under the Royalty Award, the Dividends Provision did not impact the amount of LC's pledged during 2017.

During the nine months ended September 30, 2017, the Company revised its estimate for future Royalty Award payments based in part on an updated forecast provided to the Company from Carbon Solutions. This forecast included a material reduction in estimated future revenues generated at the Red River Plant. Based primarily on the updated forecast, the Company recorded a $3.4 million reduction to the Royalty Award accrual.

In December 2017, the Company, Carbon Solutions and the parent company of Carbon Solutions agreed to terminate certain provisions of the Indemnity Settlement Agreement (the "Indemnity Termination Agreement"). Pursuant to an agreement executed concurrently with the Indemnity Termination Agreement, the Company, Norit and an affiliate of Norit (collectively referred to as "Norit") agreed to a final payment in the amount of $3.3 million (the "Settlement Payment") to settle all outstanding royalty obligations owed under the terms of the Norit Settlement Agreement. This amount was paid by the Company on December 29, 2017.

Under the Indemnity Termination Agreement, and upon payment of the Settlement Payment, the Company was relieved of certain financial and indemnity obligations required by the terms of the Norit Settlement Agreement, including the obligation to maintain LC's securing future royalty payment obligations. As of December 31, 2017, $3.5 million in LC's related to the Royalty Award were outstanding, but were canceled by all parties in January 2018, pursuant to the Indemnity Termination Agreement.

Advanced Emission Solutions, Inc. Profit Sharing Retirement Plan

The Advanced Emissions Solutions, Inc. Profit Sharing Retirement Plan (the “401(k) Plan”) is subject to the jurisdiction of the Internal Revenue Service ("IRS") and the Department of Labor ("DOL").

In 2016, the DOL opened an investigation into the 401(k) Plan, and the Company (in its role as Plan Sponsor) cooperated with that investigation. In February 2018, as part of ongoing discussions, the Company and the DOL came to an agreement whereby the Company would make a restorative payment to the 401(k) Plan in the amount of $1.0 million as an estimate of lost earnings for 401(k) Plan participants as of January 1, 2015. Thereafter, the DOL would close the investigation with no further action against the 401(k) Plan or its fiduciaries, including any further investigation. The Company determined this contingency to be both probable and reasonably estimable and accrued $1.0 million as of December 31, 2017. The liability was recorded in the Other current liabilities line item on the Consolidated Balance Sheet. The expense recognized related to this accrual was included in the Other line item in the Consolidated Statements of Operations for the year ended December 31, 2017. The Company made a payment of $1.0 million to the 401(k) Plan on June 1, 2018 and no liability existed as of September 30, 2018. On September 7, 2018, the Company received notification that the DOL had closed its investigation and no further action is required by the Company.

Other Commitments and Contingencies

Tinuum Group

The Company also has certain limited obligations contingent upon future events in connection with the activities of Tinuum Group. The Company, NexGen and two entities affiliated with NexGen have provided an affiliate of the Goldman Sachs Group, Inc. with limited guaranties (the "Tinuum Group Party Guaranties") related to certain losses it may suffer as a result of inaccuracies or breach of representations and covenants. The Company also is a party to a contribution agreement with NexGen under which any party called upon to pay on a Tinuum Group Party Guaranty is entitled to receive contributions from the other party equal to 50% of the amount paid. No liability or expense provision has been recorded by the Company related to this contingent obligation as the Company believes that it is not probable that a loss will occur with respect to Tinuum Group Party Guaranties.

Note 6 - Stockholders' Equity

Stock Repurchase Program

Under a stock repurchase program authorized by the Board in December 2017 (the "Stock Repurchase Program"), during the three and nine months ended September 30, 2018, the Company purchased zero and 825,418 shares, respectively, of its common stock for cash of zero and $9.1 million, respectively, inclusive of commissions and fees. Of these amounts, $2.2 million was purchased in a single block through a privately negotiated transaction. Under the terms of the Stock Repurchase Program, the Company was authorized to purchase up to $20.0 million of its outstanding common stock, and it remained in effect until July 31, 2018.

On September 12, 2018, the Company repurchased 186,212 shares of its common stock for $2.1 million in a single block through a privately negotiated transaction.

On May 5, 2017, the Board authorized the commencement of a modified Dutch Auction tender offer ("Tender Offer") to purchase for cash up to 925,000 shares of the Company's common stock at a price per share of not less than $9.40 nor greater than $10.80, for a maximum aggregate purchase price of $10.0 million, with an option to purchase an additional 2% of the outstanding shares of common stock if the Tender Offer was oversubscribed. The Tender Offer expired on June 6, 2017 and a total of 2,858,425 shares were validly tendered and not properly withdrawn at or below the final purchase price of $9.40 per share.

Because the Tender Offer was oversubscribed, the Company purchased a prorated portion of the shares properly tendered by each tendering stockholder (other than "odd lot" holders whose shares were purchased on a priority basis) at the final per share purchase price. Accordingly, the Company acquired 1,370,891 shares of its common stock

("Tendered Shares") at a price of $9.40 per share, for a total cost of approximately $12.9 million, excluding fees and other expenses related to the Tender Offer. The Tendered Shares represented approximately 6.2% of the Company's outstanding shares prior to the Tender Offer. The Tendered Shares include the 925,000 shares the Company initially offered to purchase and 445,891 additional shares that the

Company elected to purchase pursuant to its right to purchase up to an additional 2% of its outstanding shares of common stock. The Company recorded the Tendered Shares at cost, which included fees and expenses related to the Tender Offer, and reported the Tendered Shares as Treasury Stock in the Condensed Consolidated Balance Sheet.

The Company’s Board and executive officers did not participate in the Tender Offer, except for one director of the Board, who is a manager of a financial institution and holds dispositive powers over the shares of the Company's common stock held by the financial institution, which tendered 70,178 of its shares of the Company's common stock.

Quarterly Cash Dividend

Dividends declared by the Board, and paid quarterly per share on all outstanding shares of comment stock during the three and nine months ended September 30, 2018 and 2017 were as follows:

	2018 Per share	Date paid	2017 Per share	Date paid
Dividends declared during quarter ended:				
March 31	$ 0.25	March 8, 2018	$ —	—
June 30	0.25	June 8, 2018	0.25	July 17, 2017
September 30	0.25	September 6, 2018	0.25	September 7, 2017
	$ 0.75		$ 0.50	

A portion of the dividends declared remain accrued subsequent to the payment dates and represent dividends accumulated on nonvested shares of common stock held by employees and directors of the Company that contain forfeitable dividend rights that are not payable until the underlying shares of common stock vest. These amounts are included in both Other current liabilities and Other long-term liabilities on the Condensed Consolidated Balance Sheet as of September 30, 2018.

Tax Asset Protection Plan

United States federal income tax rules, and Section 382 of the Internal Revenue Code in particular, could substantially limit the use of net operating losses and other tax assets if ADES experiences an "ownership change" (as defined in the Internal Revenue Code). In general, an ownership change occurs if there is a cumulative change in the ownership of ADES by "5 percent stockholders" that exceeds 50 percentage points over a rolling three-year period.

On May 5, 2017, the Board approved the declaration of a dividend of rights to purchase Series B Junior Participating Preferred Stock for each outstanding share of common stock as part of a tax asset protection plan (the "Tax Asset Protection Plan") designed to protect the Company’s ability to utilize its net operating losses and tax credits. The Tax Asset Protection Plan is intended to act as a deterrent to any person acquiring beneficial ownership of 4.99% or more of the Company’s outstanding common stock.

On April 6, 2018, the Board approved the First Amendment to the Tax Asset Protection Plan (the "Amendment") that amends the Tax Asset Protection Plan dated May 5, 2017 (the "TAPP"). The Amendment amends the definition of "Final Expiration Date" under the TAPP to extend the duration of the TAPP and makes associated changes in connection therewith. At the Company's 2018 annual meeting, the Company's stockholders approved the Amendment, thus the Final Expiration Date will be the close of business on December 31, 2019.

Note 7 - Stock-Based Compensation

The Company grants equity-based awards to employees and non-employee directors that may include RSA's, stock options, PSU's and stock appreciation rights ("SAR's"). Stock-based compensation expense related to employees is included within the Payroll and benefits line item in the Condensed Consolidated Statements of Operations. Stock-based compensation expense related to non-employee directors is included within the General and administrative line item in the Condensed Consolidated Statements of Operations.

Total stock-based compensation expense for the three and nine months ended September 30, 2018 and 2017 was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
RSA expense	$919	$298	$1,871	$1,103
Stock option expense	—	143	58	443
PSU expense	—	34	—	102
Total stock-based compensation expense	$919	$475	$1,929	$1,648

The amount of unrecognized compensation cost as of September 30, 2018, and the expected weighted-average period over which the cost will be recognized is as follows:

	As of September 30, 2018	
(in thousands)	Unrecognized Compensation Cost	Expected Weighted-Average Period of Recognition (in years)
RSA expense	$ 2,118	2.19
Total unrecognized stock-based compensation expense	$ 2,118	2.19

Restricted Stock Awards

Restricted stock is typically granted with vesting terms of three years. The fair value of RSA's is determined based on the closing price of the Company’s common stock on the authorization date of the grant multiplied by the number of shares subject to the stock award. Compensation expense for RSA's is generally recognized on a straight-line basis over the entire vesting period. A summary of RSA activity under the Company's various stock compensation plans for the nine months ended September 30, 2018 is presented below:

	Shares	Weighted-Average Grant Date Fair Value
Non-vested at January 1, 2018	276,607	$ 9.03
Granted	205,998	$ 11.00
Vested	(180,740)	$ 9.85
Forfeited	(1,135)	$ 10.44
Non-vested at September 30, 2018	300,730	$ 9.88

Stock Options

Stock options generally vest over three years or upon satisfaction of performance-based conditions and have a contractual limit of five years from the date of grant to exercise. The fair value of stock options granted is determined on the date of grant using the Black-Scholes option pricing model and the related expense is recognized on a straight-line basis over the entire vesting period.

A summary of stock option activity for the nine months ended September 30, 2018 is presented below:

	Number of Options Outstanding and Exercisable	Weighted-Average Exercise Price	Aggregate Intrinsic Value (in thousands)	Weighted-Average Remaining Contractual Term (in years)
Options outstanding, January 1, 2018	622,446	$ 11.64		

Options granted	—	—		
Options exercised	(92,666)	8.25		
Options expired / forfeited	—	—		
Options outstanding, September 30, 2018	529,780	$ 12.23	$ 592	1.71
Options exercisable, September 30, 2018	529,780	$ 12.23	$ 592	1.71

The Company did not receive cash from the exercise of stock options during the three months ended September 30, 2018 as 67,715 shares were withheld as payment of the exercise price. The total intrinsic value of options exercised during the three months ended September 30, 2018 was $0.3 million.

Performance Share Units

Compensation expense is recognized for PSU awards on a straight-line basis over the applicable service period, which is generally three years, based on the estimated fair value at the date of grant using a Monte Carlo simulation model. There were no PSU's granted during the nine months ended September 30, 2018.

A summary of PSU activity for the nine months ended September 30, 2018 is presented below:

	Units	Weighted-Average Grant Date Fair Value
Non-vested at January 1, 2018	19,406	$ 19.95
Granted	—	—
Vested / Settled [(1)]	(19,406)	$ 19.95
Forfeited / Canceled	—	—
Non-vested at September 30, 2018	—	$ —

[(1)] The number of units shown in the table above were based on target performance. The final number of shares of common stock issued was based on the achievement of market conditions established within the awards.

The following table shows the PSU's that were settled by issuing shares of the Company's common stock relative to a broad stock index and a peer group performance index.

	Year of Grant	Net Number of Issued Shares upon Vesting	Shares Withheld to Settle Tax Withholding Obligations	TSR Multiple Range		Russell 3000 Multiple	
				Low	High	Low	High
Nine Months Ended September 30, 2018							
	2015	12,311	4,061	112.50	112.50	—	—
Nine Months Ended September 30, 2017							
	2014	6,476	3,573	0.75	1.00	—	—
	2015	3,869	2,310	0.60	0.60	—	—

Note 8 - Supplemental Financial Information

Supplemental Balance Sheet Information

The following table summarizes the components of Prepaid expenses and other assets and Other long-term assets as presented in the Condensed Consolidated Balance Sheets:

(in thousands)	As of September 30, 2018	December 31, 2017
Prepaid expenses and other assets:		
Prepaid expenses	$435	$ 776
Inventory	13	74
Prepaid income taxes	2,153	902
Other	30	83
	$2,631	$ 1,835
Other long-term assets:		
Deposits	$222	$ 223
Intangibles, net	889	805
Highview Investment	552	552
Other	407	728
	$2,070	$ 2,308

Included within Other long-term assets is the Company's investment ("Highview Investment") in Highview Enterprises Limited's equity securities ("Highview"), a London, England based developmental stage company specializing in power storage. In 2014, the Company acquired an 8% ownership interest in the common stock of Highview for $2.8 million in cash. As of September 30, 2018, the Company's ownership interest is approximately 4%. The Highview Investment is evaluated for impairment upon an indicator of impairment such as an event or change in circumstances that may have a significant adverse effect on the fair value of the investment. During the year ended December 31, 2017, the Company recorded an impairment charge of $0.5 million which is included in the Other line item in the Condensed Consolidated Statement of Operations based on an estimated fair value of £1.00 per share compared to the carrying value prior to the impairment charge of £2.00 per share. The estimated fair value as of December 31, 2017 was based on an equity financing that Highview commenced during the third quarter of 2017 at a price of £1.00 per share.

The following table details the components of Other current liabilities and Other long-term liabilities as presented in the Condensed Consolidated Balance Sheets:

(in thousands)	As of September 30, 2018	December 31, 2017
Other current liabilities:		
Income taxes payable	$25	$ 207
Estimated restorative payment to the 401(k) Plan (1)	—	1,000
Dividends payable	57	45
Warranty liabilities	26	316
Other	519	1,096
	$627	$ 2,664
Other long-term liabilities:		
Deferred rent	$128	$ 192
Dividends payable	167	93
Deferred revenue, related party	—	2,000
	$295	$ 2,285

(1) See Note 5 for further discussion on the 401(k) Plan.

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The tables below detail additional components of Other current liabilities as presented above:
The changes in the carrying amount of the Company's warranty obligations from December 31, 2017 through September 30, 2018 were as follows:

(in thousands)	As of September 30, 2018
Balance, beginning of period	$ 316
Warranties accrued, net	9
Consumption of warranty obligations accrued	(337)
Change in estimate related to previous warranties accrued	38
Balance, end of period	$ 26

Supplemental Condensed Consolidated Statements of Operations Information
The following table details the components of Interest expense in the Condensed Consolidated Statements of Operations:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
453A interest	$388	$614	$1,128	$1,646
Credit agreement interest	—	64	—	137
Other	11	—	19	216
	$399	$678	$1,147	$1,999

The following table details the components of the Other line item of the Condensed Consolidated Statements of Operations:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
Impairment of Highview investment	$—	$(464)	$—	$(464)
Revision in estimated royalty indemnity liability	—	—	—	3,400
Other	86	(460)	146	(444)
	$86	$(924)	$146	$2,492

Note 9 - Income Taxes
For the three and nine months ended September 30, 2018 and 2017, the Company's income tax expense and effective tax rates based on forecasted pretax income were:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands, except for rate)	2018	2017	2018	2017
Income tax expense	$3,931	$3,586	$5,151	$12,614
Effective tax rate	42 %	38 %	15 %	38 %

The effective tax rates for the three and nine months ended September 30, 2018 and 2017 were different from the federal statutory rates in effect during the respective periods due to state income tax expense, net of federal benefit, and from changes in the valuation allowance against deferred tax assets. During the three and nine months ended September 30, 2018, we recorded an increase and decrease, respectively, of the valuation allowance based on changes in forecasts of future taxable income.

The income tax expense recorded for the three and nine months ended September 30, 2018 was comprised of estimated federal income tax expense of $2.9 million and $3.4 million, respectively, and estimated state income tax expense of $1.0 million and $1.8 million, respectively. The income tax expense recorded for the three and nine months ended September 30, 2017 was comprised of estimated federal income tax expense of $3.2 million and $11.9 million, respectively, and estimated state income tax expense of $0.4 million and $0.7 million, respectively.

On December 22, 2017 (the "Enactment Date"), the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act makes broad and complex changes to the U.S. tax code and the key provision applicable to the Company for the three and nine months ended September 30, 2018 was the reduction of the U.S. federal corporate tax rate from 35 percent to 21 percent.

Concurrent with the enactment of the Tax Act, in December 2017, the SEC staff issued Staff Accounting Bulletin 118 ("SAB 118"), which provides guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Enactment Date for companies to complete the accounting under Accounting Standards Codification 740 - Income Taxes ("ASC 740"). In March 2018, the FASB codified SAB 118 into ASC 740. In accordance with SAB 118, a company must reflect the income tax effects of those aspects of the Tax Act for which the accounting under ASC 740 is complete. To the extent that an entity's accounting for certain income tax effects of the Tax Act is incomplete but it is able to determine a reasonable estimate, it must record a provisional estimate in the financial statements. If a company cannot determine a provisional estimate to be included in the financial statements, it should continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the enactment of the Tax Act. The Company's accounting for the income tax effects of the Tax Act affecting its consolidated financial statements was generally complete as of December 31, 2017 and there were no effects from the Tax Act on the condensed consolidated financial statements as of and for the three and nine months ended September 30, 2018. The Company does not anticipate any other accounting impacts of the Tax Act during the period within one year from the Enactment Date; however, it will continue to assess any potential impact from the Tax Act through this period.

The Company assesses the valuation allowance recorded against deferred tax assets at each reporting date. The determination of whether a valuation allowance for deferred tax assets is appropriate requires the evaluation of positive and negative evidence that can be objectively verified. Consideration must be given to all sources of taxable income available to realize the deferred tax asset, including, as applicable, the future reversal of existing temporary differences, future taxable income forecasts exclusive of the reversal of temporary differences and carryforwards, taxable income in carryback years and tax planning strategies. In estimating income taxes, the Company assesses the relative merits and risks of the appropriate income tax treatment of transactions taking into account statutory, judicial, and regulatory guidance. As of September 30, 2018, the Company increased the valuation allowance as a result of updating its forecasts of future taxable income, which was primarily driven by updated forecasts of capital expenditures on RC facilities that are in the engineering and installation phase.

Note 10 - Business Segment Information

Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by a company's chief operating decision maker ("CODM"), or a decision-making group, in deciding how to allocate resources and in assessing financial performance. As of September 30, 2018, the Company's CODM was the Company's CEO. The Company's operating and reportable segments are organized by products and services provided.

As of September 30, 2018, the Company has two reportable segments: (1) Refined Coal ("RC"); and (2) Emissions Control ("EC").

The business segment measurements provided to and evaluated by the CODM are computed in accordance with the principles listed below:

- The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies in the 2017 Form 10-K, except as described below.
- RC segment revenues includes the Company's equity method earnings and losses from the Company's equity method investments and royalties earned from Tinuum Group.
- Segment operating income (loss) includes segment revenues and allocation of certain "Corporate general and administrative expenses," which include Payroll and benefits, Rent and occupancy, Legal and professional fees, General and administrative and Depreciation and amortization.
- RC segment operating income includes interest expense directly attributable to the RC segment.

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As of September 30, 2018 and December 31, 2017, substantially all of the Company's material assets are located in the U.S. and all significant customers are U.S. companies. The following table presents the Company's operating segment results for the three and nine months ended September 30, 2018 and 2017:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
Revenues:				
Refined Coal:				
Earnings in equity method investments	$9,715	$12,120	$37,857	$36,089
Royalties, related party	4,104	2,804	10,857	6,425
	13,819	14,924	48,714	42,514
Emissions Control:				
Chemicals	1,043	717	2,390	3,844
Equipment Sales	—	1,577	72	31,304
	1,043	2,294	2,462	35,148
Total segment reporting revenues	14,862	17,218	51,176	77,662
Adjustments to reconcile to reported revenues:				
Refined Coal:				
Earnings in equity method investments	(9,715)	(12,120)	(37,857)	(36,089)
Total reported revenues	$5,147	$5,098	$13,319	$41,573
Segment operating income (loss):				
Refined Coal (1)	$12,798	$13,991	$45,775	$40,149
Emissions Control	(1,168)	(895)	(3,493)	1,265
Total segment operating income	$11,630	$13,096	$42,282	$41,414

(1) Included within the RC segment operating income for the three and nine months ended September 30, 2018 and 2017 is 453A interest expense of $0.4 million and $1.1 million and $0.6 million and $1.6 million, respectively.

A reconciliation of reportable segment operating income to the Company's consolidated net income is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2018	2017	2018	2017
Segment operating income	$11,630	$13,096	$42,282	$41,414
Adjustments to reconcile to net income attributable to the Company				
Corporate payroll and benefits	(957)	(1,222)	(3,054)	(4,375)
Corporate rent and occupancy	(135)	(91)	(414)	(208)
Corporate legal and professional fees	(634)	(964)	(3,222)	(3,091)
Corporate general and administrative	(523)	(857)	(2,069)	(2,513)
Corporate depreciation and amortization	(23)	(38)	(97)	(296)
Corporate interest (expense) income, net	(10)	(46)	(18)	(329)
Other income (expense), net	86	(500)	199	2,900
Income tax expense	(3,931)	(3,586)	(5,151)	(12,614)
Net income	$5,503	$5,792	$28,456	$20,888

Corporate general and administrative expenses include certain costs that benefit the business as a whole but are not directly related to one of the Company's segments. Such costs include, but are not limited to, accounting and human resources staff, information systems costs, legal fees, facility costs, audit fees and corporate governance expenses.

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A reconciliation of reportable segment assets to the Company's consolidated assets is as follows:

(in thousands)	As of September 30, 2018	December 31, 2017
Assets:		
Refined Coal[(1)]	$10,033	$ 8,092
Emissions Control	2,593	3,755
Total segment assets	12,626	11,847
All Other and Corporate[(2)]	70,530	70,771
Consolidated	$83,156	$ 82,618

(1) Includes $5.4 million and $4.4 million of investments in equity method investees, respectively.

(2) Included within All Other and Corporate are the Company's deferred tax assets.

Note 11 - Fair Value Measurements

Fair value of financial instruments

The carrying amounts of financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, approximate fair value due to the short maturity of these instruments. Accordingly, these instruments are not presented in the table below. The following table provides the estimated fair values of the remaining financial instruments:

	As of September 30, 2018		As of December 31, 2017	
(in thousands)	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Instruments:				