

TENNANT CO  
Form 10-Q  
November 02, 2018

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

OR  
 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 1-16191

---

TENNANT COMPANY

(Exact name of registrant as specified in its charter)

Minnesota

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

41-0572550

701 North Lilac Drive

P.O. Box 1452

Minneapolis, Minnesota 55440

(Address of principal executive offices)

(Zip Code)

(763) 540-1200

(Registrant's telephone number, including area code)

---

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes  No

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of October 19, 2018, there were 18,125,000 shares of Common Stock outstanding.

TABLE OF CONTENTS  
PART I - FINANCIAL  
INFORMATION

	Page
Item 1. <u>Financial</u>	
<u>Statements</u>	4
<u>(Unaudited)</u>	
<u>Condensed</u>	
<u>Consolidated</u>	4
<u>Statements of</u>	
<u>Operations</u>	
<u>Condensed</u>	
<u>Consolidated</u>	5
<u>Statements of</u>	
<u>Comprehensive</u>	
<u>Income</u>	
<u>Condensed</u>	
<u>Consolidated</u>	6
<u>Balance Sheets</u>	
<u>Condensed</u>	
<u>Consolidated</u>	7
<u>Statements of Cash</u>	
<u>Flows</u>	
<u>Notes to the</u>	
<u>Condensed</u>	
<u>Consolidated</u>	9
<u>Financial</u>	
<u>Statements</u>	
<u>1. Summary of</u>	
<u>Significant</u>	9
<u>Accounting Policies</u>	
<u>2. Newly Adopted</u>	
<u>Accounting</u>	9
<u>Pronouncements</u>	
<u>3. Revenue from</u>	
<u>Contracts with</u>	11
<u>Customers</u>	
<u>4. Management</u>	
<u>Actions</u>	13
<u>5. Acquisitions and</u>	
<u>Divestitures</u>	14
<u>6. Inventories</u>	16
<u>7. Goodwill and</u>	
<u>Intangible Assets</u>	16
<u>8. Debt</u>	17
<u>9. Warranty</u>	18
<u>10. Derivatives</u>	18
<u>11. Fair Value</u>	
<u>Measurements</u>	21
<u>12. Retirement</u>	
<u>Benefit Plans</u>	22

	<u>13. Commitments and Contingencies</u>	<u>22</u>
	<u>14. Accumulated Other Comprehensive Loss</u>	<u>23</u>
	<u>15. Income Taxes</u>	<u>23</u>
	<u>16. Share-Based Compensation</u>	<u>24</u>
	<u>17. Earnings (Loss) Attributable to Tennant Company Per Share</u>	<u>24</u>
	<u>18. Segment Reporting</u>	<u>25</u>
	<u>19. Separate Financial Information of Guarantor Subsidiaries Management's Discussion and Analysis of Financial Condition and Results of Operations Quantitative and Qualitative Disclosures About Market Risk Controls and Procedures</u>	<u>25</u>
Item 2.	<u>Condition and Results of Operations Quantitative and Qualitative Disclosures About Market Risk Controls and Procedures</u>	<u>36</u>
Item 3.	<u>Disclosures About Market Risk Controls and Procedures</u>	<u>42</u>
Item 4.	<u>Procedures</u>	<u>42</u>
PART II - OTHER INFORMATION		
Item 1.	<u>Legal Proceedings</u>	<u>43</u>
Item 1A.	<u>Risk Factors</u>	<u>43</u>
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>43</u>
Item 6.	<u>Exhibits</u>	<u>44</u>
	<u>Signatures</u>	<u>45</u>

## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements

## TENNANT COMPANY

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands, except shares and per share data)	Three Months Ended		Nine Months Ended	
	September 30		September 30	
	2018	2017	2018	2017
Net Sales	\$273,255	\$261,921	\$838,299	\$723,771
Cost of Sales	165,170	157,317	500,778	434,877
Gross Profit	108,085	104,604	337,521	288,894
Operating Expense:				
Research and Development Expense	7,506	7,907	23,408	24,239
Selling and Administrative Expense	85,140	85,711	269,273	246,993
Total Operating Expense	92,646	93,618	292,681	271,232
Profit from Operations	15,439	10,986	44,840	17,662
Other Income (Expense):				
Interest Income	839	698	2,540	1,575
Interest Expense	(5,986)	(6,093)	(17,736)	(18,720)
Net Foreign Currency Transaction Losses	(295)	(842)	(1,381)	(2,375)
Other Expense, Net	(130)	(422)	(890)	(774)
Total Other Expense, Net	(5,572)	(6,659)	(17,467)	(20,294)
Profit (Loss) Before Income Taxes	9,867	4,327	27,373	(2,632)
Income Tax Expense	158	731	1,598	385
Net Earnings (Loss) Including Noncontrolling Interest	9,709	3,596	25,775	(3,017)
Net Earnings (Loss) Attributable to Noncontrolling Interest	33	37	81	(28)
Net Earnings (Loss) Attributable to Tennant Company	\$9,676	\$3,559	\$25,694	\$(2,989)
Net Earnings (Loss) Attributable to Tennant Company per Share:				
Basic	\$0.54	\$0.20	\$1.43	\$(0.17)
Diluted	\$0.52	\$0.20	\$1.40	\$(0.17)
Weighted Average Shares Outstanding:				
Basic	17,998,917	17,729,857	17,911,880	17,673,656
Diluted	18,439,621	18,171,444	18,344,813	17,673,656
Cash Dividend Declared per Common Share	\$0.21	\$0.21	\$0.63	\$0.63

See accompanying Notes to the Condensed Consolidated Financial Statements.

TENNANT COMPANY  
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(Unaudited)

(In thousands)	Three Months Ended		Nine Months Ended	
	September 30 2018	September 30 2017	September 30 2018	September 30 2017
Net Earnings (Loss) Including Noncontrolling Interest	\$9,709	\$3,596	\$25,775	\$(3,017)
Other Comprehensive (Loss) Income:				
Foreign currency translation adjustments	(3,110)	9,033	(14,202)	25,073
Pension and retiree medical benefits	12	379	105	541
Cash flow hedge	(28)	(1,732)	(1,367)	(6,311)
Income Taxes:				
Foreign currency translation adjustments	280	—	524	—
Pension and retiree medical benefits	(2)	(138)	(156)	(160)
Cash flow hedge	6	646	(814)	2,354
Total Other Comprehensive (Loss) Income, net of tax	(2,842)	8,188	(15,910)	21,497
Total Comprehensive Income Including Noncontrolling Interest	6,867	11,784	9,865	18,480
Comprehensive Income (Loss) Attributable to Noncontrolling Interest	33	37	81	(28)
Comprehensive Income Attributable to Tennant Company	\$6,834	\$11,747	\$9,784	\$18,508

See accompanying Notes to the Condensed Consolidated Financial Statements.

TENNANT COMPANY  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(Unaudited)

	September 30, 2018	December 31, 2017
(In thousands, except shares and per share data)		
<b>ASSETS</b>		
Current Assets:		
Cash and Cash Equivalents	\$53,473	\$58,398
Restricted Cash	534	653
Accounts Receivable, less Allowances of \$2,203 and \$3,241, respectively	208,119	209,516
Inventories	139,793	127,694
Prepaid Expenses	28,356	19,351
Other Current Assets	8,865	7,503
Total Current Assets	439,140	423,115
Property, Plant and Equipment	381,443	382,768
Accumulated Depreciation	(217,625 )	(202,750 )
Property, Plant and Equipment, Net	163,818	180,018
Deferred Income Taxes	15,062	11,134
Goodwill	184,619	186,044
Intangible Assets, Net	152,974	172,347
Other Assets	14,953	21,319
Total Assets	\$970,566	\$993,977
<b>LIABILITIES AND TOTAL EQUITY</b>		
Current Liabilities:		
Current Portion of Long-Term Debt	\$30,999	\$30,883
Accounts Payable	90,778	96,082
Employee Compensation and Benefits	42,157	37,257
Income Taxes Payable	2,972	2,838
Other Current Liabilities	71,842	69,447
Total Current Liabilities	238,748	236,507
Long-Term Liabilities:		
Long-Term Debt	316,937	345,956
Employee-Related Benefits	21,828	23,867
Deferred Income Taxes	48,491	53,225
Other Liabilities	35,479	35,948
Total Long-Term Liabilities	422,735	458,996
Total Liabilities	661,483	695,503
Commitments and Contingencies (Note 13)		
Equity:		
Common Stock, \$0.375 par value; 60,000,000 shares authorized; 18,122,576 and 17,881,177 shares issued and outstanding, respectively	6,796	6,705
Additional Paid-In Capital	26,087	15,089
Retained Earnings	312,539	297,032
Accumulated Other Comprehensive Loss	(38,233 )	(22,323 )
Total Tennant Company Shareholders' Equity	307,189	296,503
Noncontrolling Interest	1,894	1,971
Total Equity	309,083	298,474
Total Liabilities and Total Equity	\$970,566	\$993,977

See accompanying Notes to the Condensed Consolidated Financial Statements.

6

---



TENNANT COMPANY  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

(In thousands)	Nine Months Ended September 30	
	2018	2017
<b>OPERATING ACTIVITIES</b>		
Net Earnings (Loss) Including Noncontrolling Interest	\$25,775	\$(3,017 )
Adjustments to Reconcile Net Earnings (Loss) to Net Cash Provided by Operating Activities:		
Depreciation	24,090	18,515
Amortization of Intangible Assets	17,378	11,430
Amortization of Debt Issuance Costs	1,883	896
Debt Issuance Cost Charges Related to Short-Term Financing	—	6,200
Fair Value Step-Up Adjustment to Acquired Inventory	—	8,445
Deferred Income Taxes	(9,908 )	(4,848 )
Share-Based Compensation Expense	6,008	4,915
Allowance for Doubtful Accounts and Returns	835	983
Other, Net	(459 )	175
Changes in Operating Assets and Liabilities, Net of Assets Acquired:		
Receivables, Net	(342 )	(524 )
Inventories	(19,550 )	(9,866 )
Accounts Payable	(1,756 )	5,747
Employee Compensation and Benefits	5,186	(9,462 )
Other Current Liabilities	(138 )	10,019
Income Taxes	(1,105 )	4,149
Other Assets and Liabilities	(4,428 )	(11,634 )
Net Cash Provided by Operating Activities	43,469	32,123
<b>INVESTING ACTIVITIES</b>		
Purchases of Property, Plant and Equipment	(12,768 )	(16,239 )
Proceeds from Disposals of Property, Plant and Equipment	108	2,456
Proceeds from Principal Payments Received on Long-Term Note Receivable	828	500
Issuance of Long-Term Note Receivable	—	(1,500 )
Proceeds from Sale of Business	4,000	—
Acquisition of Businesses, Net of Cash, Cash Equivalents and Restricted Cash Acquired	—	(353,535)
Purchase of Intangible Assets	(2,607 )	(2,500 )
Net Cash Used in Investing Activities	(10,439 )	(370,818)
<b>FINANCING ACTIVITIES</b>		
Proceeds from Short-Term Debt	—	300,000
Repayments of Short-Term Debt	—	(300,000)
Proceeds from Issuance of Long-Term Debt	—	440,000
Payments of Long-Term Debt	(30,216 )	(81,262 )
Payments of Debt Issuance Costs	—	(16,465 )
Change in Capital Lease Obligations	7	—
Proceeds from Issuance of Common Stock	5,735	4,728
Dividends Paid	(11,356 )	(11,204 )
Net Cash (Used in) Provided by Financing Activities	(35,830 )	335,797
Effect of Exchange Rate Changes on Cash, Cash Equivalents and Restricted Cash	(2,244 )	1,587
Net Decrease in Cash, Cash Equivalents and Restricted Cash	(5,044 )	(1,311 )

Edgar Filing: TENNANT CO - Form 10-Q

Cash, Cash Equivalents and Restricted Cash at Beginning of Period	59,051	58,550
Cash, Cash Equivalents and Restricted Cash at End of Period	\$54,007	\$57,239

7

---

Supplemental Disclosure of Cash Flow Information:

Cash Paid for Income Taxes	\$7,314	\$8,127
----------------------------	---------	---------

Cash Paid for Interest	\$11,297	\$3,741
------------------------	----------	---------

Supplemental Non-cash Investing and Financing Activities:

Capital Expenditures in Accounts Payable	\$635	\$1,265
--	-------	---------

See accompanying Notes to the Condensed Consolidated Financial Statements.

8

---

TENNANT COMPANY

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(In thousands, except shares and per share data)

1. Summary of Significant Accounting Policies

Basis of Presentation – The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with the Securities and Exchange Commission (“SEC”) requirements for interim reporting, which allows certain footnotes and other financial information normally required by accounting principles generally accepted in the United States of America to be condensed or omitted. In our opinion, the Condensed Consolidated Financial Statements contain all adjustments (consisting of only normal recurring adjustments) necessary for the fair presentation of our financial position and results of operations.

These statements should be read in conjunction with the Consolidated Financial Statements and Notes included in our annual report on Form 10-K for the year ended December 31, 2017. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year.

Revenue Recognition – Revenue is recognized upon transfer of control of promised products or services to customers in an amount that reflects the consideration we expect to receive in exchange for those products and services.

Generally, these criteria are met at the time the product is shipped.

We also enter into contracts that can include combinations of products and services, which are generally capable of being distinct and are accounted for as separate performance obligations. Revenue is recognized net of allowances for returns and any taxes collected from customers, which are subsequently remitted to governmental authorities.

Further details regarding revenue recognition are discussed in Notes 2 and 3.

New Accounting Pronouncements – Further details regarding the adoption of new accounting standards are discussed in Note 2.

We documented the summary of significant accounting policies in the Notes to the Consolidated Financial Statements of our annual report on Form 10-K for the fiscal year ended December 31, 2017. Other than the accounting policies noted above, there have been no material changes to our accounting policies since the filing of that report.

2. Newly Adopted Accounting Pronouncements

Revenue from Contracts with Customers

On January 1, 2018, we adopted Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (Topic 606) and all the related amendments (“new revenue standard”) to all contracts not completed at the date of initial application using the modified retrospective method. The cumulative effect of initially applying the new revenue standard as an adjustment to the opening balance of retained earnings was not material to the company. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods, and there are no material differences between the reported results under the new revenue standard and those that would have been reported under legacy U.S. GAAP.

The new revenue standard also required us to record a refund liability and a corresponding asset for our right to recover products from customers upon settling the refund liability to account for the transfer of products with a right of return. The impact of this provision of the new revenue standard is immaterial to our financial statements. The new revenue standard also provided additional clarity that resulted in a reclassification from Accounts Receivable to Other Current Liabilities to reflect a change in the presentation of our sales return reserves on the balance sheet, which were previously recorded net of Accounts Receivable. Provisions for estimated sales returns will continue to be recorded at the time the related revenue is recognized.

The reclassification from Accounts Receivable to Other Current Liabilities in accordance with the detail described above impacted the Condensed Consolidated Balance Sheet as of September 30, 2018, as follows (in thousands):

	As Reported	Balances Without Adoption of ASC 606	Effect of Change Higher/(Lower)
<b>ASSETS</b>			
Accounts Receivable	\$208,119	\$206,960	\$ 1,159
Total Current Assets	439,140	437,981	1,159
Total Assets	\$970,566	\$969,407	\$ 1,159
<b>LIABILITIES</b>			
Other Current Liabilities	\$71,842	\$70,683	\$ 1,159
Total Current Liabilities	238,748	237,589	1,159
Total Liabilities	\$661,483	\$660,324	\$ 1,159

For additional disclosures regarding the new revenue standard, see Note 3.

#### Intra-Entity Transfers of Assets Other than Inventory

On January 1, 2018, we adopted ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other than Inventory. The ASU requires the tax effects of all intra-entity sales of assets other than inventory to be recognized in the period in which the transaction occurs. The adoption of this ASU resulted in a \$94 cumulative effect adjustment recorded in Retained Earnings as of the beginning of 2018 that reflects a \$1,281 reduction in a long-term deferred charge, mostly offset by the establishment of a deferred tax asset of \$1,187. The reduction in the long-term asset and establishment of the deferred tax asset impacted Other Assets and Deferred Income Taxes, respectively, on our Condensed Consolidated Balance Sheets.

#### Statement of Cash Flows – Restricted Cash

On January 1, 2018, we adopted ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash. The ASU requires companies to explain the changes in the combined total of restricted and unrestricted balances in the Condensed Consolidated Statements of cash flows. Therefore, amounts generally described as restricted cash or restricted cash equivalents should be combined with unrestricted cash and cash equivalents when reconciling the beginning and end of period balances on the Condensed Consolidated Statements of Cash Flows. In accordance with the ASU, we adopted the standard on a retrospective basis to all periods presented.

#### Compensation – Retirement Benefits

On January 1, 2018, we adopted ASU No. 2017-07, Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The ASU requires employers to report the service cost component of net pension and postretirement benefit costs in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net pension and postretirement benefit costs are required to be presented in the Condensed Consolidated Statements of Operations separately from the service cost component in nonoperating expenses. In accordance with the ASU, we adopted the standard on a retrospective basis to all periods presented. As a result, we reclassified \$60 of net benefit credits and \$74 of net benefit costs from Selling and Administrative Expense to Other Expense, Net on the Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2017, respectively. The reclassification represents the other components of net pension and postretirement benefit costs that are now presented in the Condensed Consolidated Statements of Operations separately from the service cost in Total Other Expense, Net. As a basis for the retrospective application of the ASU, we used the practical expedient that permits us to use the amounts disclosed for the various components of net benefit cost in Note 12.

#### Income Statement—Reporting Comprehensive Income

On January 1, 2018, we elected to adopt early ASU No. 2018-02, Income Statement—Reporting Comprehensive Income (Topic 220). The ASU gives companies the option to reclassify stranded tax effects caused by the newly enacted

legislation referred to as the Tax Cuts and Jobs Act (the "Tax Act") from Accumulated Other Comprehensive Loss to Retained Earnings. The adoption resulted in a \$1,263 cumulative effect adjustment which increased Retained Earnings as of the beginning of 2018 and reduced the deferred income tax benefits in Accumulated Other Comprehensive Loss relating to cash flow hedges and pension and retiree medical benefits.

## Income Taxes

In March 2018, we adopted ASU No. 2018-05, Income Taxes (Topic 740): Amendments to SEC paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118. The ASU updates the income tax accounting in U.S. GAAP to reflect the SEC interpretive guidance released on December 22, 2017, when the Tax Act was signed into law. Additional information regarding the adoption of this standard is contained in Note 15.

## 3. Revenue from Contracts with Customers

Under the new revenue standard, revenue is recognized when control transfers under the terms of the contract with our customers. 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. We do not account for shipping and handling as a distinct performance obligation as we generally perform shipping and handling activities after we transfer control of goods to the customer. We have elected to account for shipping and handling costs associated with outbound freight after control of goods has transferred to a customer as a fulfillment cost. Incidental items that are immaterial in the context of the contract are not recognized as a separate performance obligation. We do not have any significantly extended payment terms as payment is generally received within one year of the point of sale.

In general, we transfer control and recognize a sale at the point in time when products are shipped from our manufacturing facilities both direct to consumers and to distributors. Service revenue is recognized in the period the service is performed or ratably over the period of the related service contract. Consideration related to service contracts is deferred if the proceeds are received in advance of the satisfaction of the performance obligations and recognized over the contract period as the performance obligation is met. We use an output method to measure progress toward completion for certain prepaid service contracts, as this method appropriately depicts performance towards satisfaction of the performance obligations.

For contracts with multiple performance obligations (i.e., a product and service component), we allocate the transaction price to the performance obligations in proportion to their stand-alone selling prices. We use an observable price to determine the stand-alone selling price for separate performance obligations. When allocating on a relative stand-alone selling price basis, any discounts contained within the contract are allocated proportionately to all of the performance obligations in the contract.

## Disaggregation of Revenue

The following tables illustrate the disaggregation of revenue by geographic area, groups of similar products and services and sales channels for the three and nine months ended September 30, 2018 and 2017 (in thousands):

## Net Sales by geographic area

	Three Months Ended		Nine Months Ended	
	September 30 2018	September 30 2017	September 30 2018	September 30 2017
Americas	\$175,341	\$161,037	\$516,731	\$472,953
Europe, Middle East and Africa	74,254	78,851	250,480	189,483
Asia Pacific	23,660	22,033	71,088	61,335
Total	\$273,255	\$261,921	\$838,299	\$723,771

Net Sales are attributed to each geographic area based on the end user country and are net of intercompany sales.

## Net Sales by groups of similar products and services

	Three Months Ended		Nine Months Ended	
	September 30 2018	September 30 2017	September 30 2018	September 30 2017
Equipment	\$178,165	\$165,203	\$542,317	\$455,311
Parts and Consumables	53,639	53,535	168,491	149,260
Specialty Surface Coatings	7,139	8,007	21,434	22,491
Service and Other	34,312	35,176	106,057	96,709

Total \$273,255 \$261,921 \$838,299 \$723,771

11

---



## Net Sales by sales channel

	Three Months		Nine Months Ended	
	Ended		September 30	
	September 30	September 30	September 30	September 30
	2018	2017	2018	2017
Sales Direct to Consumer	\$180,901	\$172,484	\$547,079	\$490,533
Sales to Distributors	92,354	89,437	291,220	233,238
Total	\$273,255	\$261,921	\$838,299	\$723,771

## Contract Liabilities

## Sales Returns

The right of return may exist explicitly or implicitly with our customers. When the right of return exists, we adjust the transaction price for the estimated effect of returns. We estimate the expected returns using the expected value method by assessing historical sales levels and the timing and magnitude of historical sales return levels as a percent of sales and projecting this experience into the future.

## Sales Incentives

Our sales contracts may contain various customer incentives, such as volume-based rebates or other promotions. We reduce the transaction price for certain customer programs and incentive offerings that represent variable consideration. Sales incentives given to our customers are recorded using the most likely amount approach for estimating the amount of consideration to which the company will be entitled. We forecast the most likely amount of the incentive to be paid at the time of sale, update this forecast quarterly, and adjust the transaction price accordingly to reflect the new amount of incentives expected to be earned by the customer. A majority of our customer incentives are settled within one year. We record our accruals for volume-based rebates and other promotions in Other Current Liabilities on our Condensed Consolidated Balance Sheets.

The change in our sales incentive accrual balance for the nine months ended September 30, 2018 was as follows:

	Nine Months
	Ended
	September 30
	2018
Beginning balance	\$ 13,466
Additions to sales incentive accrual	22,078
Contract payments	(21,677 )
Foreign currency fluctuations	(239 )
Ending balance	\$ 13,628

## Deferred Revenue

We sell separately priced prepaid contracts to our customers where we receive payment at the inception of the contract and defer recognition of the consideration received because we have to satisfy future performance obligations. Our deferred revenue balance is primarily attributed to prepaid maintenance contracts on our machines ranging from 12 months to 60 months. In circumstances where prepaid contracts are bundled with machines, we use an observable price to determine stand-alone selling price for separate performance obligations.

The change in the deferred revenue balance for the nine months ended September 30, 2018 was as follows:

	Nine Months
	Ended
	September 30
	2018
Beginning balance	\$ 7,787
Increase in deferred revenue representing our obligation to satisfy future performance obligations	11,032
Decrease in deferred revenue for amounts recognized in Net Sales for satisfied performance obligations	(10,475 )
Foreign currency fluctuations	(140 )

Ending balance

\$ 8,204

12

---

At September 30, 2018, \$5,064 and \$3,140 of deferred revenue was reported in Other Current Liabilities and Other Liabilities, respectively, on our Condensed Consolidated Balance Sheets. Of this, we expect to recognize the following approximate amounts in Net Sales in the following periods:

Remaining 2018	\$2,502
2019	2,958
2020	1,595
2021	692
2022	381
Thereafter	76
Total	\$8,204

At December 31, 2017, \$5,304 and \$2,483 of deferred revenue was reported in Other Current Liabilities and Other Liabilities, respectively, on our Condensed Consolidated Balance Sheets.

#### Practical Expedients and Exemptions

We generally expense the incremental costs of obtaining a contract when incurred because the amortization period would be less than one year. These costs relate primarily to sales commissions and are recorded in Selling and Administrative Expense in the Condensed Consolidated Statements of Operations.

We do not disclose the value of unsatisfied performance obligations for contracts with an original expected length of one year or less. In addition, we do not adjust the promised amount of consideration for the effects of a significant financing component if we expect, at contract inception, that the period between when we transfer a promised good or service to a customer and when the customer pays for that good or service will be one year or less.

#### 4. Management Actions

During the first quarter of 2017, we implemented a restructuring action to better align our global resources and expense structure with a lower growth global economic environment. The pre-tax charge of \$8,018, including other associated costs of \$961, consisted primarily of severance and was included within Selling and Administrative Expense in the Condensed Consolidated Statements of Operations. The charge impacted our Americas, Europe, Middle East and Africa (EMEA) and Asia Pacific (APAC) operating segments. The savings offset the pre-tax charge approximately one year from the date of the action. Additional costs will not be incurred related to this restructuring action.

During the fourth quarter of 2017, we implemented a restructuring action primarily driven by integration actions related to our acquisition of the IPC Group. The restructuring action consisted primarily of severance and included reductions in overall staffing to streamline and right-size the organization to support anticipated business requirements. The pre-tax charge of \$2,501 was included within Selling and Administrative Expense in the Condensed Consolidated Statements of Operations. The charge impacted our Americas, EMEA and APAC operating segments. We believe the anticipated savings will offset the pre-tax charge in approximately one year from the date of the action. Additional costs will not be incurred related to this restructuring action.

A reconciliation of the beginning and ending liability balances is as follows:

	Severance and Related Costs
2017 restructuring actions	\$ 9,558
Cash payments	(6,312 )
Foreign currency adjustments	190
December 31, 2017 balance	\$ 3,436
2018 utilization:	
Cash payments	(1,694 )
Foreign currency adjustments	(64 )
September 30, 2018 balance	\$ 1,678



## 5. Acquisitions and Divestitures

On September 4, 2018, we signed a definitive agreement to acquire Hefei Gaomei Cleaning Machines Co., Ltd. and Anhui Rongen Environmental Protection Technology Co., Ltd (collectively "Gaomei"), privately held designers and manufacturers of commercial cleaning solutions based in China. We expect the acquisition to be completed in the first quarter of 2019. The purchase price and net assets to be acquired are not significant to our consolidated financial statements.

During the third quarter of 2018, we sold our Waterstar business for \$4,000 in cash. The resulting gain was approximately \$1,000 and is reflected within Selling and Administrative Expense in operating profit in our Condensed Consolidated Statements of Operations.

On April 6, 2017, we acquired the outstanding capital stock of IP Cleaning S.p.A. and its subsidiaries ("IPC Group") for a purchase price of \$353,769, net of cash acquired of \$8,804. The primary seller was Ambienta SGR S.p.A., a European private equity fund. IPC Group, based in Italy, is a designer and manufacturer of innovative professional cleaning equipment, cleaning tools and supplies. The acquisition strengthens our presence and market share in Europe and allows us to better leverage our EMEA cost structure. We funded the acquisition of IPC Group, along with related fees, including refinancing of existing debt, with funds raised through borrowings under a senior secured credit facility in an aggregate principal amount of \$420,000. Further details regarding our acquisition financing arrangements are discussed in Note 8.

The following table summarizes the final fair value measurement of the assets acquired and liabilities assumed as of the date of acquisition:

ASSETS	
Receivables	\$39,984
Inventories	46,442
Other Current Assets	7,456
Assets Held for Sale	2,247
Property, Plant and Equipment	63,890
Intangible Assets Subject to Amortization:	
Trade Name	26,753
Customer Lists	123,061
Technology	9,631
Other Assets	2,000
Total Identifiable Assets Acquired	321,464
LIABILITIES	
Accounts Payable	32,227
Accrued Expenses	18,130
Deferred Income Taxes	56,950
Other Liabilities	10,964
Total Identifiable Liabilities Assumed	118,271
Net Identifiable Assets Acquired	203,193
Noncontrolling Interest	(1,896 )
Goodwill	152,472
Total Purchase Price, net of Cash Acquired	\$353,769

Based on the final fair value measurement of the assets acquired and liabilities assumed, we allocated \$152,472 to goodwill for the expected synergies from combining IPC Group with our existing business. None of the goodwill is expected to be deductible for income tax purposes. In connection with the finalization of the fair value measurements in the first quarter of 2018, we recorded a measurement period adjustment, which increased goodwill by \$4,627 with offsetting adjustments to various income tax assets and liabilities.

The final fair value of the acquired intangible assets is \$159,445. The expected lives of the acquired amortizable intangible assets are approximately 15 years for customer lists, 10 years for trade names and 10 years for technology. Trade names are being amortized on a straight-line basis while the customer lists and technology are being amortized on an accelerated basis. We recorded amortization expense of \$5,401 and \$16,424 in Selling and Administrative Expense on our Condensed Consolidated Statements of Operations for these acquired intangible assets for the three and nine months ended September 30, 2018, respectively.

The following unaudited pro forma financial information presents the combined results of operations of Tennant Company as if the 2017 acquisition of the IPC Group had occurred as of January 1, 2016. The unaudited pro forma financial information is presented for informational purposes only. It is not necessarily indicative of what our consolidated results of operations actually would have been had the acquisition occurred at the beginning of fiscal 2016. No pro forma results are presented for the three or nine months ended September 30, 2018, as the results of the acquired company are included in the actual results.

Pro Forma Financial Information (Unaudited)

	Three Months Ended September 30 2017	Nine Months Ended September 30 2017
(In thousands, except per share data)		
Net Sales		
Pro forma	\$ 261,921	\$ 777,832
As reported	261,921	723,771
Net Earnings (Loss) Attributable to Tennant Company		
Pro forma	\$ 5,800	\$ 14,875
As reported	3,559	(2,989 )
Net Earnings (Loss) Attributable to Tennant Company per Share		
Pro forma	\$ 0.32	\$ 0.84
As reported	0.20	(0.17 )

The unaudited pro forma financial information above gives effect to the following:

- incremental depreciation and amortization expense related to the fair value of the property, plant and equipment and identified intangible assets;
- exclusion of the purchase accounting impact of the inventory step-up related to the sale of acquired inventory;
- incremental interest expense related to additional debt used to finance the acquisition;
- exclusion of non-recurring acquisition-related transaction and financing costs; and
- pro forma adjustments tax affected based on the jurisdiction where the costs were incurred.

## 6. Inventories

Inventories are valued at the lower of cost or market. Inventories at September 30, 2018 and December 31, 2017 consisted of the following:

	September 30, 2018	December 31, 2017
Inventories carried at LIFO:		
Finished goods	\$ 48,471	\$ 43,439
Raw materials, production parts and work-in-process	28,994	23,694
LIFO reserve	(30,668 )	(28,429 )
Total LIFO inventories	46,797	38,704
Inventories carried at FIFO:		
Finished goods	53,138	54,161
Raw materials, production parts and work-in-process	39,858	34,829
Total FIFO inventories	92,996	88,990
Total inventories	\$ 139,793	\$ 127,694

The LIFO reserve approximates the difference between LIFO carrying cost and FIFO.

## 7. Goodwill and Intangible Assets

The changes in the carrying value of Goodwill for the nine months ended September 30, 2018 were as follows:

	Goodwill	Accumulated Impairment Losses	Total
Balance as of December 31, 2017	\$227,224	\$ (41,180 )	\$ 186,044
Purchase accounting adjustments	4,627	—	4,627
Foreign currency fluctuations	(7,542 )	1,490	(6,052 )
Balance as of September 30, 2018	\$224,309	\$ (39,690 )	\$ 184,619

The balances of acquired Intangible Assets, excluding Goodwill, as of September 30, 2018 and December 31, 2017, were as follows:

	Customer Lists	Trade Names	Technology	Total
Balance as of September 30, 2018				
Original cost	\$144,760	\$30,945	\$ 17,134	\$192,839
Accumulated amortization	(29,908 )	(4,631 )	(5,326 )	(39,865 )
Carrying value	\$114,852	\$26,314	\$ 11,808	\$152,974
Weighted average original life (in years)	15	10	11	
Balance as of December 31, 2017				
Original cost	\$149,355	\$31,968	\$ 14,589	\$195,912
Accumulated amortization	(17,870 )	(2,436 )	(3,259 )	(23,565 )
Carrying value	\$131,485	\$29,532	\$ 11,330	\$172,347
Weighted average original life (in years)	15	10	11	

The purchase accounting adjustments recorded during the first quarter of 2018 were based on the fair value adjustments related to our acquisition of the IPC Group, as described further in Note 5.

During the first nine months of 2018, we purchased a technology license for \$2,500. The license was recorded in Intangible Assets, Net as technology on the Condensed Consolidated Balance Sheets as of September 30, 2018. Amortization expense on Intangible Assets for the three and nine months ended September 30, 2018 was \$5,720 and \$17,378, respectively. Amortization expense on Intangible Assets for the three and nine months ended September 30, 2017 was \$7,650 and \$11,430, respectively.

Estimated aggregate amortization expense based on the current carrying value of amortizable Intangible Assets for each of the five succeeding years and thereafter is as follows:

Remaining 2018	\$5,456
2019	21,268
2020	19,827
2021	18,244
2022	15,965
Thereafter	72,214
Total	\$ 152,974

#### 8. Debt

##### Financial Covenants

In 2017, the Company and certain of our foreign subsidiaries entered into a Credit Agreement (the "2017 Credit Agreement") with JPMorgan, as administrative agent, Goldman Sachs Bank USA, as syndication agent, Wells Fargo, National Association, U.S. Bank National Association, and HSBC Bank USA, National Association, as co-documentation agents, and the lenders (including JPMorgan) from time to time party thereto.

The 2017 Credit Agreement contains customary representations, warranties and covenants, including, but not limited to, covenants restricting the company's ability to incur indebtedness and liens and merge or consolidate with another entity. The 2017 Credit Agreement also contains financial covenants, requiring us to maintain a ratio of consolidated total indebtedness to consolidated earnings before income, taxes, depreciation and amortization, subject to certain adjustments ("Adjusted EBITDA") of not greater than 4.00 to 1, as well as requiring us to maintain a ratio of consolidated Adjusted EBITDA to consolidated interest expense of no less than 3.50 to 1 for the quarter ended September 30, 2018. The 2017 Credit Agreement also contains a financial covenant requiring us to maintain a senior secured net indebtedness to Adjusted EBITDA ratio of not greater than 3.50 to 1. These financial covenants may restrict our ability to pay dividends and purchase outstanding shares of our common stock. We were in compliance with our financial covenants at September 30, 2018.

We will be required to repay the senior credit agreement with 25% to 50% of our excess cash flow from the preceding fiscal year, as defined in the agreement, unless our net leverage ratio for such preceding fiscal year is less than or equal to 3.00 to 1, which will be first measured using our fiscal year ended December 31, 2018.

Our Senior Notes also contain certain restrictions, which are generally less restrictive than those contained in the 2017 Credit Agreement.

##### Registration Rights Agreement

In connection with the issuance and sale of the Senior Notes, the company entered into a Registration Rights Agreement, dated April 18, 2017, among the company, the Guarantors and Goldman, Sachs & Co. and J.P. Morgan Securities LLC (the "Registration Rights Agreement"). Pursuant to the Registration Rights Agreement, the company agreed (1) to use its commercially reasonable efforts to consummate an exchange offer to exchange the Senior Notes for new registered notes (the "Exchange Notes"), with terms substantially identical in all material respects with the Senior Notes (except that the Exchange Notes will not contain terms with respect to additional interest, registration rights or transfer restrictions) and (2) if required, to have a shelf registration statement declared effective with respect to resales of the Senior Notes.

On January 22, 2018, we commenced the exchange offer required by the Registration Rights Agreement. The exchange offer closed on February 23, 2018. We did not incur any additional indebtedness as a result of the exchange offer. As a result, we are not required to pay additional interest on the Senior Notes.



## Debt Outstanding

Debt outstanding at September 30, 2018 and December 31, 2017 consisted of the following:

	September 30, 2018	December 31, 2017
Long-Term Debt:		
Senior unsecured notes	\$ 300,000	\$ 300,000
Credit facility borrowings	50,000	80,000
Capital lease obligations	2,955	3,279
Total Long-Term Debt	352,955	383,279
Less: unamortized debt issuance costs	(5,020 )	(6,440 )
Less: current maturities of credit facility borrowings, net of debt issuance costs <sup>(1)</sup>	(29,704 )	(29,413 )
Less: current maturities of capital lease obligations <sup>(1)</sup>	(1,294 )	(1,470 )
Long-term portion	\$ 316,937	\$ 345,956

<sup>(1)</sup> Current maturities of long-term debt include \$30,000 of current maturities, less \$296 of unamortized debt issuance costs, under our 2017 Credit Agreement and \$1,294 of current maturities of capital lease obligations.

As of September 30, 2018, we had outstanding borrowings under our Senior Unsecured Notes of \$300,000. We had outstanding borrowings under our 2017 Credit Agreement, totaling \$30,000 under our term loan facility and \$20,000 under our revolving facility, leaving \$180,000 of unused borrowing capacity on our revolving facility. Although we are only required to make a minimum principal payment of \$6,250 during the next year, we have both the intent and the ability to pay an additional \$23,750 during the next year on our term loan facility. As such, we have classified \$30,000 as current maturities of long-term debt. In addition, we had letters of credit and bank guarantees outstanding in the amount of \$5,724, leaving approximately \$174,276 of unused borrowing capacity on our revolving facility. Commitment fees on unused lines of credit for the nine months ended September 30, 2018 were \$455. The overall weighted average cost of debt is approximately 5.4% and net of a related cross-currency swap instrument is approximately 4.5%. Further details regarding the cross-currency swap instrument are discussed in Note 10.

## 9. Warranty

We record a liability for warranty claims at the time of sale. The amount of the liability is based on the trend in the historical ratio of claims to sales, the historical length of time between the sale and resulting warranty claim, new product introductions and other factors. Warranty terms on machines generally range from one to four years. However, the majority of our claims are paid out within the first six to nine months following a sale. The majority of the liability for estimated warranty claims represents amounts to be paid out in the near term for qualified warranty issues, with immaterial amounts reserved to be paid for older equipment warranty issues.

The changes in warranty reserves for the nine months ended September 30, 2018 and 2017 were as follows:

	Nine Months Ended September 30	
	2018	2017
Beginning balance	\$ 12,676	\$ 10,960
Additions charged to expense	10,883	8,879
Acquired warranty obligations	—	384
Foreign currency fluctuations	(193 )	225
Claims paid	(9,805 )	(8,912 )
Ending balance	\$ 13,561	\$ 11,536

## 10. Derivatives

## Hedge Accounting and Hedging Programs

We recognize all derivative instruments as either assets or liabilities in our Condensed Consolidated Balance Sheets and measure them at fair value. Gains and losses resulting from changes in fair value are accounted for depending on the use of the derivative and whether it is designated and qualifies for hedge accounting.



## Balance Sheet Hedging

### Hedges of Foreign Currency Assets and Liabilities

We hedge portions of our net recognized foreign currency denominated assets and liabilities with foreign exchange forward contracts to reduce the risk that the value of these assets and liabilities will be adversely affected by changes in exchange rates. At September 30, 2018 and December 31, 2017, the notional amounts of foreign currency forward exchange contracts outstanding not designated as hedging instruments were \$47,614 and \$60,858, respectively.

### Cash Flow Hedging

#### Hedges of Forecasted Foreign Currency Transactions

In countries outside the U.S., we transact business in U.S. dollars and in various other currencies. We may use foreign exchange option contracts or forward contracts to hedge certain cash flow exposures resulting from changes in these foreign currency exchange rates. These foreign exchange contracts, carried at fair value, have maturities of up to one year. We enter into these foreign exchange contracts to hedge a portion of our forecasted foreign currency denominated revenue in the normal course of business, and accordingly, they are not speculative in nature. The notional amounts of outstanding foreign currency forward contracts designated as cash flow hedges were \$2,952 and \$2,928 as of September 30, 2018 and December 31, 2017, respectively. The notional amounts of outstanding foreign currency option contracts designated as cash flow hedges were \$8,737 and \$8,619 as of September 30, 2018 and December 31, 2017, respectively.

### Foreign Currency Derivatives

We use foreign currency exchange rate derivatives to hedge our exposure to fluctuations in exchange rates for anticipated intercompany cash transactions between Tennant Company and its subsidiaries. We entered into Euro to U.S. dollar foreign exchange cross currency swaps for all of the anticipated cash flows associated with an intercompany loan from a wholly owned European subsidiary. We enter into these foreign exchange cross currency swaps to hedge the foreign currency denominated cash flows associated with this intercompany loan, and accordingly, they are not speculative in nature. These cross currency swaps are designated as cash flow hedges. The hedged cash flows as of September 30, 2018 and December 31, 2017 included €175,800 and €181,200 of total notional values, respectively. As of September 30, 2018, the aggregate scheduled interest payments over the course of the loan and related swaps amounted to €25,800. The scheduled maturity and principal payment of the loan and related swaps of €150,000 are due in April 2022.

The fair value of derivative instruments on our Condensed Consolidated Balance Sheets as of September 30, 2018 and December 31, 2017 was as follows:

	September 30, 2018		December 31, 2017	
	Fair Value Asset Derivatives	Fair Value Liability Derivatives	Fair Value Asset Derivatives	Fair Value Liability Derivatives
Derivatives designated as hedging instruments:				
Foreign currency option contracts <sup>(1)</sup>	\$ 113	\$ —	\$ 86	\$ —
Foreign currency forward contracts <sup>(1)</sup>	7,038	29,868	7,218	34,961
Derivatives not designated as hedging instruments:				
Foreign currency forward contracts <sup>(1)</sup>	\$ 653	\$ 358	\$ 442	\$ 425

(1) Contracts that mature within the next 12 months are included in Other Current Assets and Other Current Liabilities for asset derivatives and liability derivatives, respectively, on our Condensed Consolidated Balance Sheets. Contracts with maturities greater than 12 months are included in Other Assets and Other Liabilities for asset derivatives and liability derivatives, respectively, in our Condensed Consolidated Balance Sheets. Amounts included in our Condensed Consolidated Balance Sheets are recorded net where a right of offset exists with the same derivative counterparty.

As of September 30, 2018, we anticipate reclassifying approximately \$2,129 of gains from Accumulated Other Comprehensive Loss to net earnings during the next 12 months.



The effect of foreign currency derivative instruments designated as cash flow hedges and of foreign currency derivative instruments not designated as hedges in our Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2018 was as follows:

	Three Months Ended September 30, 2018		Nine Months Ended September 30, 2018	
	Foreign Currency Option Contracts	Foreign Currency Forward Contracts	Foreign Currency Option Contracts	Foreign Currency Forward Contracts
Derivatives in cash flow hedging relationships:				
Net (loss) gain recognized in Other Comprehensive (Loss) Income, net of tax <sup>(1)</sup>	\$ (89)	\$ 1,253	\$ (40)	\$ 4,929
Net loss reclassified from Accumulated Other Comprehensive Loss into earnings, net of tax, effective portion to Net Sales	(7 )	(33 )	(91 )	(34 )
Net gain reclassified from Accumulated Other Comprehensive Loss into earnings, net of tax, effective portion to Interest Income	—	487	—	1,345
Net gain reclassified from Accumulated Other Comprehensive Loss into earnings, net of tax, effective portion to Net Foreign Currency Transaction Losses	—	739	—	4,724
Net (loss) gain recognized in earnings <sup>(2)</sup>	(5 )	2	3	8
Derivatives not designated as hedging instruments:				
Net (loss) gain recognized in earnings <sup>(3)</sup>	\$—	\$ (658 )	\$—	\$ 1,174

The effect of foreign currency derivative instruments designated as cash flow hedges and of foreign currency derivative instruments not designated as hedges in our Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2017 was as follows:

	Three Months Ended September 30, 2017		Nine Months Ended September 30, 2017	
	Foreign Currency Option Contracts	Foreign Currency Forward Contracts	Foreign Currency Option Contracts	Foreign Currency Forward Contracts
Derivatives in cash flow hedging relationships:				
Net loss recognized in Other Comprehensive (Loss) Income, net of tax <sup>(1)</sup>	\$ (40)	\$ (4,492 )	\$ (177 )	\$ (14,026)
Net (loss) gain reclassified from Accumulated Other Comprehensive Loss into earnings, net of tax, effective portion to Net Sales	(141 )	26	(140 )	(76 )
Net gain reclassified from Accumulated Other Comprehensive Loss into earnings, net of tax, effective portion to Interest Income	—	374	—	823
Net loss reclassified from Accumulated Other Comprehensive Loss into earnings, net of tax, effective portion to Net Foreign Currency Transaction Losses	—	(3,705 )	—	(10,853 )
Net (loss) gain recognized in earnings <sup>(2)</sup>	(7 )	3	(12 )	8
Derivatives not designated as hedging instruments:				
Net loss recognized in earnings <sup>(3)</sup>	\$—	\$ (2,062 )	\$ (1,132)	\$ (7,369 )

<sup>(1)</sup> Net change in the fair value of the effective portion classified in Other Comprehensive (Loss) Income.

<sup>(2)</sup> Ineffective portion and amount excluded from effectiveness testing classified in Net Foreign Currency Transaction Losses.

<sup>(3)</sup> Classified in Net Foreign Currency Transaction Losses.



## 11. Fair Value Measurements

Estimates of fair value for financial assets and financial liabilities are based on the framework established in the accounting guidance for fair value measurements. The framework defines fair value, provides guidance for measuring fair value and requires certain disclosures. The framework discusses valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow) and the cost approach (cost to replace the service capacity of an asset or replacement cost). The framework utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

Level 1: Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.

Level 3: Unobservable inputs that reflect the reporting entity's own assumptions.

Our population of assets and liabilities subject to fair value measurements at September 30, 2018 is as follows:

	Fair Value	Level 1	Level 2	Level 3
Assets:				
Foreign currency forward exchange contracts	\$7,691	\$ —	—\$7,691	\$ —
Foreign currency option contracts	113	—	113	—
Total Assets	\$7,804	\$ —	—\$7,804	\$ —
Liabilities:				
Foreign currency forward exchange contracts	\$30,226	\$ —	—\$30,226	\$ —
Total Liabilities	\$30,226	\$ —	—\$30,226	\$ —

Our population of assets and liabilities subject to fair value measurements at December 31, 2017 is as follows:

	Fair Value	Level 1	Level 2	Level 3
Assets:				
Foreign currency forward exchange contracts	\$7,660	\$ —	—\$7,660	\$ —
Foreign currency option contracts	86	—	86	—
Total Assets	\$7,746	\$ —	—\$7,746	\$ —
Liabilities:				
Foreign currency forward exchange contracts	\$35,386	\$ —	—\$35,386	\$ —
Total Liabilities	\$35,386	\$ —	—\$35,386	\$ —

Our foreign currency forward exchange and option contracts are valued using observable Level 2 market expectations at the measurement date and standard valuation techniques to convert future amounts to a single present value amount. Further details regarding our foreign currency forward exchange and option contracts are discussed in Note 10.

The carrying amounts reported in the Condensed Consolidated Balance Sheets for Cash and Cash Equivalents, Restricted Cash, Accounts Receivable, Other Current Assets, Accounts Payable and Other Current Liabilities approximate fair value due to their short-term nature.

The fair market value of our Long-Term Debt approximates cost based on the borrowing rates currently available to us for bank loans with similar terms and remaining maturities.

From time to time, we measure certain assets at fair value on a non-recurring basis, including evaluation of long-lived assets, goodwill and other intangible assets, as part of a business acquisition. These assets are measured and recognized at amounts equal to the fair value determined as of the date of acquisition. Fair value valuations are based on the information available as of the acquisition date and the expectations and assumptions that have been deemed reasonable by us. There are inherent uncertainties and management judgment required in these determinations. The fair value measurements of assets and liabilities assumed as part of a business acquisition are based on valuations involving significant unobservable inputs, or Level 3, in the fair value hierarchy.





These assets are also subject to periodic impairment testing by comparing the respective carrying value of each asset to the estimated fair value of the reporting unit or asset group in which they reside. In the event we determine these assets to be impaired, we would recognize an impairment loss equal to the amount by which the carrying value of the reporting unit, impairment asset or asset group exceeds its estimated fair value. These periodic impairment tests utilize company-specific assumptions involving unobservable inputs, or Level 3, in the fair value hierarchy.

## 12. Retirement Benefit Plans

Our defined benefit pension plans and postretirement medical plan are described in Note 13 of our annual report on Form 10-K for the year ended December 31, 2017. We have contributed \$36 and \$139 during the third quarter of 2018 and \$187 and \$695 during the first nine months of 2018 to our pension plans and postretirement medical plan, respectively.

The components of the net benefit cost for the three and nine months ended September 30, 2018 and 2017 were as follows:

	Three Months Ended					
	September 30					
	Pension Benefits				Postretirement	
	U.S. Plans		Non-U.S. Plans		Medical Benefits	
	2018	2017	2018	2017	2018	2017
Service cost	\$—	\$—	\$33	\$124	\$ 6	\$ 6
Interest cost	10	373	82	96	70	91
Expected return on plan assets	—	(581 )	(77 )	(101 )	—	—
Amortization of net actuarial loss	13	12	—	—	—	—
Amortization of prior service cost	—	—	54	50	—	—
Foreign currency	—	—	(118 )	135	—	—
Net periodic benefit cost (credit)	23	(196 )	(26 )	304	76	97
Net benefit cost (credit)	\$23	\$(196)	\$(26)	\$304	\$ 76	\$ 97
	Nine Months Ended					
	September 30					
	Pension Benefits				Postretirement	
	U.S. Plans		Non-U.S. Plans		Medical Benefits	
	2018	2017	2018	2017	2018	2017
Service cost	\$—	\$—	\$105	\$172	\$ 34	\$ 46
Interest cost	32	1,153	240	315	220	272
Expected return on plan assets	—	(1,752)	(268 )	(298 )	—	—
Amortization of net actuarial loss	37	33	—	—	—	—
Amortization of prior service cost	—	—	160	146	—	—
Foreign currency	—	—	(212 )	364	—	—
Net periodic benefit cost (credit)	69	(566 )	25	699	254	318
Settlement charge	50	205	—	—	—	—
Net benefit cost (credit)	\$119	\$(361)	\$25	\$699	\$ 254	\$ 318

## 13. Commitments and Contingencies

Certain operating leases for vehicles contain residual value guarantee provisions, which would become due at the expiration of the operating lease agreement if the fair value of the leased vehicles is less than the guaranteed residual value. As of September 30, 2018, of those leases that contain residual value guarantees, the aggregate residual value at lease expiration was \$13,990, of which we have guaranteed \$8,371. As of September 30, 2018, we have recorded a liability for the estimated end of term loss related to this residual value guarantee of \$317 for certain vehicles within our fleet. Our fleet also contains vehicles we estimate will settle at a gain. Gains on these vehicles will be recognized at the end of the lease term.



## 14. Accumulated Other Comprehensive Loss

Components of Accumulated Other Comprehensive Loss, net of tax, within the Condensed Consolidated Balance Sheets, are as follows:

	September 30, 2018	December 31, 2017
Foreign currency translation adjustments	\$(29,456)	\$(15,778)
Pension and retiree medical benefits	(1,661 )	(1,610 )
Cash flow hedge	(7,116 )	(4,935 )
Total Accumulated Other Comprehensive Loss	\$(38,233)	\$(22,323)

The changes in components of Accumulated Other Comprehensive Loss, net of tax, are as follows:

	Foreign Currency Translation Adjustments	Pension and Post Retirement Benefits	Cash Flow Hedge	Total
December 31, 2017	\$(15,778 )	\$(1,610 )	\$(4,935 )	\$(22,323)
Other comprehensive (loss) income before reclassifications	(13,678 )	19	4,889	(8,770 )
Amounts reclassified from Accumulated Other Comprehensive Loss	—	67	(5,944 )	(5,877 )
Adjustments to Accumulated Other Comprehensive Loss for disproportionate income tax effects recognized from the adoption of ASU 2018-02	—	(137 )	(1,126 )	(1,263 )
Net current period other comprehensive loss	(13,678 )	(51 )	(2,181 )	(15,910 )
September 30, 2018	\$(29,456 )	\$(1,661 )	\$(7,116 )	\$(38,233)

## 15. Income Taxes

We and our subsidiaries are subject to U.S. federal income tax as well as income tax of numerous state and foreign jurisdictions. We are generally no longer subject to U.S. federal tax examinations for taxable years before 2016 and, with limited exceptions, state and foreign income tax examinations for taxable years before 2013.

We recognize potential accrued interest and penalties related to unrecognized tax benefits in Income Tax Expense. In addition to the liability of \$6,067 for unrecognized tax benefits as of September 30, 2018, there was approximately \$489 for accrued interest and penalties. The total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate as of September 30, 2018 was \$5,842. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be revised and reflected as an adjustment of the Income Tax Expense.

The Internal Revenue Service completed its examination of the U.S. income tax return for the 2015 tax year during the third quarter of 2018. The IRS's adjustments to certain tax positions were not material and were fully reserved. We are currently undergoing income tax examinations in various state and foreign jurisdictions covering 2014 to 2016.

Although the final outcome of these examinations cannot be currently determined, we believe that we have adequate reserves with respect to these examinations.

On December 22, 2017, the Tax Act was signed into law. The Tax Act made broad and complex changes to the U.S. tax code which includes a lowering of the U.S. federal corporate income tax rate from 35% to 21% effective January 1, 2018, accelerated expensing of qualified capital investments for a specific period, limitations of the deductibility of interest expense and executive compensation, and a transition from a worldwide to a territorial tax system, which requires companies to pay a one-time transition tax on certain unrepatriated earnings from foreign subsidiaries.

ASC 740, Income Taxes, requires a company to record the effects of a tax law change in the period of enactment. ASU 2018-05 allows a company to record a provisional amount when it does not have the necessary information available, prepared or analyzed in reasonable detail to complete its accounting for the change in the tax law. The measurement period ends when the company has obtained, prepared and analyzed the information necessary to finalize its accounting, but cannot extend beyond one year. In the fourth quarter of 2017, we included a provisional amount for the one-time transition tax on certain unrepatriated earnings. The accounting for the income tax effect of the one-time transition tax on certain unrepatriated earnings was finalized in the third quarter of 2018, impacting the year-to-date overall effective tax rate by (1.3)%. In the fourth quarter of 2017, we remeasured our deferred taxes at the reduced corporate tax rate of 21% and recognized the change as a discrete income tax expense. The accounting for the remeasurement of the deferred taxes was finalized in the third quarter of 2018, and the impact to the year-to-date overall effective tax rate was immaterial.

We recorded income tax expense of \$158 during the third quarter of 2018, or 1.6% of earnings before income taxes. During the first nine months of 2018, we recorded income tax expense of \$1,598, or 5.8% of earnings before income taxes. This amount primarily reflects two items: (1) the Tax Act resulted in a lower tax rate beginning in the first quarter of 2018. This includes the estimated impacts of requiring a current inclusion in U.S. federal income of certain earnings of controlled foreign corporations, allowing a domestic corporation an immediate deduction in the U.S. taxable income for a portion of its foreign-derived intangible income, the base erosion anti-abuse tax, and limitations on the deductibility of executive compensation. These estimates had an immaterial impact on our effective income tax rate for 2018; and (2) during 2018, we recorded discrete income tax items to adjust our finalized transition tax liability by \$(362), and we realized two discrete tax benefits, totaling \$3,568, resulting from the exercise of soon-to-expire stock options and a favorable tax ruling from Italian tax authorities related to the deductibility of interest expense in Italy. We will continue to monitor and evaluate guidance and clarifications from the Internal Revenue Service as it relates to the Tax Act and will record adjustments as necessary.

#### 16. Share-Based Compensation

Our share-based compensation plans are described in Note 17 of our annual report on Form 10-K for the year ended December 31, 2017. During the three months ended September 30, 2018 and 2017, we recognized total Share-Based Compensation Expense of \$1,893 and \$1,293, respectively. During the nine months ended September 30, 2018 and 2017, we recognized total Share-Based Compensation Expense of \$6,008 and \$4,915, respectively. The total excess tax benefit recognized for share-based compensation arrangements during the nine months ended September 30, 2018 and 2017 was \$2,073 and \$1,149, respectively.

During the first nine months of 2018, we issued 16,377 restricted shares. The weighted average grant date fair value of each share awarded was \$67.70. Restricted share awards generally have a three year vesting period from the effective date of the grant. The total fair value of shares vested during the nine months ended September 30, 2018 and 2017 was \$863 and \$1,295, respectively.

#### 17. Earnings (Loss) Attributable to Tennant Company Per Share

The computations of Basic and Diluted Earnings (Loss) per Share were as follows:

	Three Months		Nine Months Ended	
	Ended		September 30	
	September 30	September 30	September 30	September 30
	2018	2017	2018	2017
Numerator:				
Net Earnings (Loss) Attributable to Tennant Company	\$9,676	\$ 3,559	\$25,694	\$ (2,989 )
Denominator:				
Basic - Weighted Average Shares Outstanding	17,998,917	17,729,857	17,911,880	17,673,656
Effect of dilutive securities:				
Share-based compensation plans	440,704	441,587	432,933	—
Diluted - Weighted Average Shares Outstanding	18,439,621	18,171,444	18,344,813	17,673,656
Basic Earnings (Loss) per Share	\$0.54	\$ 0.20	\$ 1.43	\$ (0.17 )
Diluted Earnings (Loss) per Share	\$0.52	\$ 0.20	\$ 1.40	\$ (0.17 )



Excluded from the dilutive securities shown above were options to purchase and shares to be paid out under share-based compensation plans of 139,106 and 340,239 shares of common stock during the three months ended September 30, 2018 and 2017, respectively. Excluded from the dilutive securities shown above were options to purchase and shares to be paid out under share-based compensation plans of 214,605 and 714,687 shares of common stock during the nine months ended September 30, 2018 and 2017, respectively. These exclusions were made if the exercise prices of the options are greater than the average market price of our common stock for the period, if the number of shares we can repurchase under the treasury stock method exceeds the weighted average shares outstanding in the options or if we have a net loss, as these effects are anti-dilutive.

#### 18. Segment Reporting

We are organized into four operating segments: North America, Latin America, EMEA and APAC. We combine our North America and Latin America operating segments into the "Americas" for reporting Net Sales by geographic area. In accordance with the objective and basic principles of the applicable accounting guidance, we aggregate our operating segments into one reportable segment that consists of the design, manufacture and sale of products used primarily in the maintenance of nonresidential surfaces.

Further disclosures regarding our net sales by geographic area are discussed in Note 3.

#### 19. Separate Financial Information of Guarantor Subsidiaries

The following condensed consolidated guarantor financial information is presented to comply with the requirements of Rule 3-10 of Regulation S-X.

In 2017, we issued and sold \$300,000 in aggregate principal amount of our 5.625% Senior Notes due 2025 (the "Notes"), pursuant to an Indenture, dated as of April 18, 2017, among the company, the Guarantors (as defined below), and Wells Fargo Bank, National Association, a national banking association, as trustee. The Notes are unconditionally and jointly and severally guaranteed by Tennant Coatings, Inc. and Tennant Sales and Service Company (collectively, the "Guarantors"), which are wholly owned subsidiaries of the company.

The Notes and the guarantees constitute senior unsecured obligations of the company and the Guarantors, respectively. The Notes and the guarantees, respectively, are: (a) equal in right of payment with all of the company's and the Guarantors' senior debt, without giving effect to collateral arrangements; (b) senior in right of payment to all of the company's and the Guarantors' future subordinated debt, if any; (c) effectively subordinated in right of payment to all of the company's and the Guarantors' debt and obligations that are secured, including borrowings under the company's senior secured credit facilities for so long as the senior secured credit facilities are secured, to the extent of the value of the assets securing such liens; and (d) structurally subordinated in right of payment to all liabilities (including trade payables) of the company's and the Guarantors' subsidiaries that do not guarantee the Notes.

The following condensed consolidated financial information presents the Condensed Consolidated Statements of Operations and the Condensed Consolidated Statements of Comprehensive Income for each of the three and nine months ended September 30, 2018 and September 30, 2017, the related Condensed Consolidated Balance Sheets as of September 30, 2018 and December 31, 2017, and the related Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and September 30, 2017, of Tennant Company ("Parent"), the Guarantor Subsidiaries on a combined basis, the Non-Guarantor Subsidiaries on a combined basis and elimination entries necessary to consolidate the Parent with the Guarantor and Non-Guarantor Subsidiaries. The following condensed consolidated financial statements should be read in conjunction with the consolidated financial statements of the company and notes thereto of which this note is an integral part.

Condensed Consolidated Statement of Operations  
For the three months ended September 30, 2018

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net Sales	\$126,110	\$160,226	\$131,418	\$(144,499)	\$273,255
Cost of Sales	86,781	135,058	87,707	(144,376)	165,170
Gross Profit	39,329	25,168	43,711	(123)	108,085
Operating Expense:					
Research and Development Expense	6,096	279	1,131	—	7,506
Selling and Administrative Expense	26,765	18,091	39,473	811	85,140
Total Operating Expense	32,861	18,370	40,604	811	92,646
Profit from Operations	6,468	6,798	3,107	(934)	15,439
Other Income (Expense):					
Equity in Earnings of Affiliates	5,256	262	205	(5,723)	—
Interest (Expense) Income, Net	(5,230)	—	92	(9)	(5,147)
Intercompany Interest Income (Expense)	3,621	(1,450)	(2,171)	—	—
Net Foreign Currency Transaction (Losses) Gains	(69)	4	(230)	—	(295)
Other Expense, Net	(179)	(473)	(263)	785	(130)
Total Other Income (Expense), Net	3,399	(1,657)	(2,367)	(4,947)	(5,572)
Profit Before Income Taxes	9,867	5,141	740	(5,881)	9,867
Income Tax Expense (Benefit)	158	1,230	(865)	(365)	158
Net Earnings Including Noncontrolling Interest	9,709	3,911	1,605	(5,516)	9,709
Net Earnings Attributable to Noncontrolling Interest <sup>33</sup>	—	—	33	(33)	33
Net Earnings Attributable to Tennant Company	\$9,676	\$3,911	\$1,572	\$(5,483)	\$9,676

Condensed Consolidated Statement of Operations  
For the nine months ended September 30, 2018

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net Sales	\$ 366,093	\$ 472,524	\$ 422,887	\$ (423,205 )	\$ 838,299
Cost of Sales	249,065	395,327	278,207	(421,821 )	500,778
Gross Profit	117,028	77,197	144,680	(1,384 )	337,521
Operating Expense:					
Research and Development Expense	18,625	825	3,958	—	23,408
Selling and Administrative Expense	84,478	57,151	126,833	811	269,273
Total Operating Expense	103,103	57,976	130,791	811	292,681
Profit from Operations	13,925	19,221	13,889	(2,195 )	44,840
Other Income (Expense):					
Equity in Earnings of Affiliates	19,657	1,356	4,234	(25,247 )	—
Interest (Expense) Income, Net	(15,726 )	—	558	(28 )	(15,196 )
Intercompany Interest Income (Expense)	10,989	(4,308 )	(6,681 )	—	—
Net Foreign Currency Transaction Losses	(354 )	(2 )	(1,025 )	—	(1,381 )
Other (Expense) Income, Net	(1,118 )	(1,610 )	1,113	725	(890 )
Total Other Income (Expense), Net	13,448	(4,564 )	(1,801 )	(24,550 )	(17,467 )
Profit Before Income Taxes	27,373	14,657	12,088	(26,745 )	27,373
Income Tax Expense	1,598	3,520	705	(4,225 )	1,598
Net Earnings Including Noncontrolling Interest	25,775	11,137	11,383	(22,520 )	25,775
Net Earnings Attributable to Noncontrolling Interest	81	—	81	(81 )	81
Net Earnings Attributable to Tennant Company	\$ 25,694	\$ 11,137	\$ 11,302	\$ (22,439 )	\$ 25,694



Condensed Consolidated Statement of Operations  
For the three months ended September 30, 2017

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net Sales	\$111,835	\$ 146,495	\$ 131,457	\$(127,866 )	\$261,921
Cost of Sales	76,974	120,523	88,411	(128,591 )	157,317
Gross Profit	34,861	25,972	43,046	725	104,604
<b>Operating Expense:</b>					
Research and Development Expense	6,312	86	1,509	—	7,907
Selling and Administrative Expense	23,498	19,074	43,139	—	85,711
Total Operating Expense	29,810	19,160	44,648	—	93,618
Profit (Loss) from Operations	5,051	6,812	(1,602 )	725	10,986
<b>Other Income (Expense):</b>					
Equity in Earnings of Affiliates	2,039	376	—	(2,415 )	—
Interest Expense, Net	(5,275 )	—	(111 )	(9 )	(5,395 )
Intercompany Interest Income (Expense)	3,774	(1,455 )	(2,319 )	—	—
Net Foreign Currency Transaction Gains (Losses)	357	2	(1,201 )	—	(842 )
Other (Expense) Income, Net	(1,619 )	(204 )	1,424	(23 )	(422 )
Total Other Expense, Net	(724 )	(1,281 )	(2,207 )	(2,447 )	(6,659 )
Profit (Loss) Before Income Taxes	4,327	5,531	(3,809 )	(1,722 )	4,327
Income Tax Expense	731	2,034	2,819	(4,853 )	731
Net Earnings (Loss) Including Noncontrolling Interest	3,596	3,497	(6,628 )	3,131	3,596
Net Earnings Attributable to Noncontrolling Interest	37	—	37	(37 )	37
Net Earnings (Loss) Attributable to Tennant Company	\$3,559	\$ 3,497	\$ (6,665 )	\$ 3,168	\$3,559

Condensed Consolidated Statement of Operations  
For the nine months ended September 30, 2017

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net Sales	\$ 337,034	\$ 442,090	\$ 331,491	\$ (386,844 )	\$ 723,771
Cost of Sales	230,753	363,034	228,838	(387,748 )	434,877
Gross Profit	106,281	79,056	102,653	904	288,894
Operating Expense:					
Research and Development Expense	20,838	245	3,156	—	24,239
Selling and Administrative Expense	85,697	58,881	102,415	—	246,993
Total Operating Expense	106,535	59,126	105,571	—	271,232
(Loss) Profit from Operations	(254 )	19,930	(2,918 )	904	17,662
Other Income (Expense):					
Equity in Earnings of Affiliates	7,493	1,500	—	(8,993 )	—
Interest Expense, Net	(16,866 )	—	(257 )	(22 )	(17,145 )
Intercompany Interest Income (Expense)	8,742	(4,323 )	(4,419 )	—	—
Net Foreign Currency Transaction Gains (Losses)	553	—	(2,928 )	—	(2,375 )
Other (Expense) Income, Net	(2,300 )	(430 )	2,014	(58 )	(774 )
Total Other Expense, Net	(2,378 )	(3,253 )	(5,590 )	(9,073 )	(20,294 )
(Loss) Profit Before Income Taxes	(2,632 )	16,677	(8,508 )	(8,169 )	(2,632 )
Income Tax Expense	385	5,993	5,481	(11,474 )	385
Net (Loss) Earnings Including Noncontrolling Interest	(3,017 )	10,684	(13,989 )	3,305	(3,017 )
Net Loss Attributable to Noncontrolling Interest	(28 )	—	(28 )	28	(28 )
Net (Loss) Earnings Attributable to Tennant Company	\$(2,989 )	\$ 10,684	\$(13,961 )	\$ 3,277	\$(2,989 )

Condensed Consolidated Statement of Comprehensive Income  
For the three months ended September 30, 2018

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net Earnings Including Noncontrolling Interest	\$9,709	\$ 3,911	\$ 1,605	\$ (5,516 )	\$ 9,709
Other Comprehensive Loss:					
Foreign currency translation adjustments	(3,110 )	228	(3,664 )	3,436	(3,110 )
Pension and retiree medical benefits	12	—	—	—	12
Cash flow hedge	(28 )	—	—	—	(28 )
Income Taxes:					
Foreign currency translation adjustments	280	—	280	(280 )	280
Pension and retiree medical benefits	(2 )	—	—	—	(2 )
Cash flow hedge	6	—	—	—	6
Total Other Comprehensive Loss, net of tax	(2,842 )	228	(3,384 )	3,156	(2,842 )
Total Comprehensive Income (Loss) Including Noncontrolling Interest	6,867	4,139	(1,779 )	(2,360 )	6,867
Comprehensive Income Attributable to Noncontrolling Interest	33	—	33	(33 )	33
Comprehensive Income (Loss) Attributable to Tennant Company	\$6,834	\$ 4,139	\$ (1,812 )	\$ (2,327 )	\$ 6,834

Condensed Consolidated Statement of Comprehensive Income  
For the nine months ended September 30, 2018

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net Earnings Including Noncontrolling Interest	\$25,775	\$ 11,137	\$ 11,383	\$ (22,520 )	\$ 25,775
Other Comprehensive Loss:					
Foreign currency translation adjustments	(14,202 )	(262 )	(20,103 )	20,365	(14,202 )
Pension and retiree medical benefits	105	—	19	(19 )	105
Cash flow hedge	(1,367 )	—	—	—	(1,367 )
Income Taxes:					
Foreign currency translation adjustments	524	—	524	(524 )	524
Pension and retiree medical benefits	(156 )	—	—	—	(156 )
Cash flow hedge	(814 )	—	—	—	(814 )
Total Other Comprehensive Loss, net of tax	(15,910 )	(262 )	(19,560 )	19,822	(15,910 )
Total Comprehensive Income (Loss) Including Noncontrolling Interest	9,865	10,875	(8,177 )	(2,698 )	9,865
Comprehensive Income Attributable to Noncontrolling Interest	81	—	81	(81 )	81
Comprehensive Income (Loss) Attributable to Tennant Company	\$9,784	\$ 10,875	\$ (8,258 )	\$ (2,617 )	\$ 9,784

Condensed Consolidated Statement of Comprehensive Income  
For the three months ended September 30, 2017

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net Earnings (Loss) Including Noncontrolling Interest	\$3,596	\$ 3,497	\$ (6,628 )	\$ 3,131	\$3,596
Other Comprehensive Income (Loss):					
Foreign currency translation adjustments	9,033	289	9,221	(9,510 )	9,033
Pension and retiree medical benefits	379	—	10	(10 )	379
Cash flow hedge	(1,732 )	—	—	—	(1,732 )
Income Taxes:					
Foreign currency translation adjustments	—	—	—	—	—
Pension and retiree medical benefits	(138 )	—	—	—	(138 )
Cash flow hedge	646	—	—	—	646
Total Other Comprehensive Income, net of tax	8,188	289	9,231	(9,520 )	8,188
Total Comprehensive Income Including Noncontrolling Interest	11,784	3,786	2,603	(6,389 )	11,784
Comprehensive Income Attributable to Noncontrolling Interest	37	—	37	(37 )	37
Comprehensive Income Attributable to Tennant Company	\$11,747	\$ 3,786	\$ 2,566	\$ (6,352 )	\$11,747

Condensed Consolidated Statement of Comprehensive Income  
For the nine months ended September 30, 2017

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
Net (Loss) Earnings Including Noncontrolling Interest	\$(3,017 )	\$ 10,684	\$ (13,989 )	\$ 3,305	\$(3,017 )
Other Comprehensive Income (Loss):					
Foreign currency translation adjustments	25,073	693	1,330	(2,023 )	25,073
Pension and retiree medical benefits	541	—	151	(151 )	541
Cash flow hedge	(6,311 )	—	—	—	(6,311 )
Income Taxes:					
Foreign currency translation adjustments	—	—	—	—	—
Pension and retiree medical benefits	(160 )	—	(15 )	15	(160 )
Cash flow hedge	2,354	—	—	—	2,354
Total Other Comprehensive Income, net of tax	21,497	693	1,466	(2,159 )	21,497
Total Comprehensive Income (Loss) Including Noncontrolling Interest	18,480	11,377	(12,523 )	1,146	18,480
Comprehensive (Loss) Income Attributable to Noncontrolling Interest	(28 )	—	(28 )	28	(28 )
Comprehensive Income (Loss) Attributable to Tennant Company	\$18,508	\$ 11,377	\$ (12,495 )	\$ 1,118	\$18,508

Condensed Consolidated Balance Sheet  
As of September 30, 2018

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
<b>ASSETS</b>					
Current Assets:					
Cash and Cash Equivalents	\$18,082	\$ 668	\$ 34,723	\$ —	\$53,473
Restricted Cash	—	—	534	—	534
Net Receivables	494	93,464	114,161	—	208,119
Intercompany Receivables	31,488	142,708	—	(174,196 )	—
Inventories	35,858	15,118	99,220	(10,403 )	139,793
Prepaid Expenses	17,673	705	9,978	—	28,356
Other Current Assets	4,691	340	3,834	—	8,865
Total Current Assets	108,286	253,003	262,450	(184,599 )	439,140
Property, Plant and Equipment	228,237	12,533	140,673	—	381,443
Accumulated Depreciation	(156,476 )	(6,459 )	(54,690 )	—	(217,625 )
Property, Plant and Equipment, Net	71,761	6,074	85,983	—	163,818
Deferred Income Taxes	3,127	3,078	8,857	—	15,062
Investment in Affiliates	403,903	12,133	18,487	(434,523 )	—
Intercompany Loans	303,670	—	3,997	(307,667 )	—
Goodwill	12,870	1,726	170,023	—	184,619
Intangible Assets, Net	4,210	2,738	146,026	—	152,974
Other Assets	6,057	—	8,896	—	14,953
Total Assets	\$913,884	\$ 278,752	\$ 704,719	\$ (926,789 )	\$970,566
<b>LIABILITIES AND TOTAL EQUITY</b>					
Current Liabilities:					
Current Portion of Long-Term Debt	\$29,705	\$ —	\$ 1,294	\$ —	\$30,999
Accounts Payable	34,447	6,727	49,604	—	90,778
Intercompany Payables	143,095	—	31,101	(174,196 )	—
Employee Compensation and Benefits	10,588	12,873	18,696	—	42,157
Income Taxes Payable	469	—	2,801	(298 )	2,972
Other Current Liabilities	28,216	14,348	28,980	298	71,842
Total Current Liabilities	246,520	33,948	132,476	(174,196 )	238,748
Long-Term Liabilities:					
Long-Term Debt	315,277	—	1,660	—	316,937
Intercompany Loans	3,997	128,000	175,670	(307,667 )	—
Employee-Related Benefits	11,519	1,916	8,393	—	21,828
Deferred Income Taxes	—	—	48,491	—	48,491
Other Liabilities	27,488	3,336	4,655	—	35,479
Total Long-Term Liabilities	358,281	133,252	238,869	(307,667 )	422,735
Total Liabilities	604,801	167,200	371,345	(481,863 )	661,483
Equity:					
Common Stock	6,796	—	11,131	(11,131 )	6,796
Additional Paid-In Capital	26,087	77,551	388,216	(465,767 )	26,087
Retained Earnings	312,539	34,932	(9,916 )	(25,016 )	312,539
Accumulated Other Comprehensive Loss	(38,233 )	(931 )	(57,951 )	58,882	(38,233 )
Total Tennant Company Shareholders' Equity	307,189	111,552	331,480	(443,032 )	307,189
Noncontrolling Interest	1,894	—	1,894	(1,894 )	1,894

Edgar Filing: TENNANT CO - Form 10-Q

Total Equity	309,083	111,552	333,374	(444,926 )	309,083
Total Liabilities and Total Equity	\$913,884	\$ 278,752	\$ 704,719	\$(926,789 )	\$970,566

32

---

Condensed Consolidated Balance Sheet  
As of December 31, 2017

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
<b>ASSETS</b>					
Current Assets:					
Cash and Cash Equivalents	\$ 18,469	\$ 507	\$ 39,422	\$ —	\$ 58,398
Restricted Cash	—	—	653	—	653
Net Receivables	683	88,629	120,204	—	209,516
Intercompany Receivables	53,444	133,778	—	(187,222 )	—
Inventories	29,450	12,695	94,542	(8,993 )	127,694
Prepaid Expenses	8,774	1,172	9,405	—	19,351
Other Current Assets	4,030	—	3,473	—	7,503
Total Current Assets	114,850	236,781	267,699	(196,215 )	423,115
Property, Plant and Equipment	225,064	12,155	145,549	—	382,768
Accumulated Depreciation	(146,320 )	(6,333 )	(50,097 )	—	(202,750 )
Property, Plant and Equipment, Net	78,744	5,822	95,452	—	180,018
Deferred Income Taxes	1,308	2,669	7,157	—	11,134
Investment in Affiliates	392,486	11,273	20,811	(424,570 )	—
Intercompany Loans	304,822	—	4,983	(309,805 )	—
Goodwill	12,869	1,739	171,436	—	186,044
Intangible Assets, Net	2,105	2,898	167,344	—	172,347
Other Assets	10,363	—	10,956	—	21,319
Total Assets	\$ 917,547	\$ 261,182	\$ 745,838	\$ (930,590 )	\$ 993,977
<b>LIABILITIES AND TOTAL EQUITY</b>					
Current Liabilities:					
Current Portion of Long-Term Debt	\$ 29,413	\$ —	\$ 1,470	\$ —	\$ 30,883
Accounts Payable	39,927	3,018	53,137	—	96,082
Intercompany Payables	133,778	1,963	51,481	(187,222 )	—
Employee Compensation and Benefits	8,311	10,355	18,591	—	37,257
Income Taxes Payable	366	—	2,472	—	2,838
Other Current Liabilities	20,183	15,760	33,504	—	69,447
Total Current Liabilities	231,978	31,096	160,655	(187,222 )	236,507
Long-Term Liabilities:					
Long-Term Debt	344,147	—	1,809	—	345,956
Intercompany Loans	—	128,000	181,805	(309,805 )	—
Employee-Related Benefits	11,160	3,992	8,715	—	23,867
Deferred Income Taxes	—	—	53,225	—	53,225
Other Liabilities	31,788	2,483	1,677	—	35,948
Total Long-Term Liabilities	387,095	134,475	247,231	(309,805 )	458,996
Total Liabilities	619,073	165,571	407,886	(497,027 )	695,503
Equity:					
Common Stock	6,705	—	11,131	(11,131 )	6,705
Additional Paid-In Capital	15,089	72,483	384,460	(456,943 )	15,089
Retained Earnings	297,032	23,797	(21,219 )	(2,578 )	297,032
Accumulated Other Comprehensive Loss	(22,323 )	(669 )	(38,391 )	39,060	(22,323 )
Total Tennant Company Shareholders' Equity	296,503	95,611	335,981	(431,592 )	296,503
Noncontrolling Interest	1,971	—	1,971	(1,971 )	1,971

Edgar Filing: TENNANT CO - Form 10-Q

Total Equity	298,474	95,611	337,952	(433,563 )	298,474
Total Liabilities and Total Equity	\$917,547	\$ 261,182	\$ 745,838	\$(930,590 )	\$993,977

33

---



Condensed Consolidated Statement of Cash Flows  
For the nine months ended September 30, 2018

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Total Tennant Company
<b>OPERATING ACTIVITIES</b>					
Net Cash Provided by (Used in) Operating Activities	\$43,661	\$ 219	\$ (411 )	\$ —	\$43,469
<b>INVESTING ACTIVITIES</b>					
Purchases of Property, Plant and Equipment	(4,505 )	(58 )	(8,205 )	—	(12,768 )
Proceeds from Disposals of Property, Plant and Equipment	20	—	88	—	108
Proceeds from Principal Payments Received on Long-Term Note Receivable	—	—	828	—	828
Proceeds from Sale of Business	—	—	4,000	—	4,000
Purchase of Intangible Assets	(2,500 )	—	(107 )	—	(2,607 )
Change in Investments in Subsidiaries	(1,817 )	—	—	1,817	—
Loan Payments from Subsidiaries	1,218	—	—	(1,218)	—
Loan Payments from Parent	—	—	986	(986 )	—
Net Cash Used in Investing Activities	(7,584 )	(58 )	(2,410 )	(387 )	(10,439 )
<b>FINANCING ACTIVITIES</b>					
Payments of Long-Term Debt	(30,000 )	—	(216 )	—	(30,216 )
Change in Capital Lease Obligations	—	—	7	—	7
Change in Subsidiary Equity	—	—	1,817	(1,817)	—
Loan Payments to Parent	—	—	(1,218 )	1,218	—
Loan Payments to Subsidiaries	(986 )	—	—	986	—
Proceeds from Issuances of Common Stock	5,735	—	—	—	5,735
Dividends Paid	(11,356 )	—	—	—	(11,356 )
Net Cash (Used in) Provided by Financing Activities	(36,607 )	—	390	387	(35,830 )
Effect of Exchange Rate Changes on Cash, Cash Equivalents and Restricted Cash	143	—	(2,387 )	—	(2,244 )
Net (Decrease) Increase in Cash, Cash Equivalents and Restricted Cash	(387 )	161	(4,818 )	—	(5,044 )
Cash, Cash Equivalents and Restricted Cash at Beginning of Period	18,469	507	40,075	—	59,051
Cash, Cash Equivalents and Restricted Cash at End of Period	\$18,082	\$ 668	\$ 35,257	\$ —	\$54,007

Condensed Consolidated Statement of Cash Flows  
For the nine months ended September 30, 2017

(in thousands)	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Elimination	Total Tennant Company
<b>OPERATING ACTIVITIES</b>					
Net Cash (Used in) Provided by Operating Activities	\$(555 )	\$ 798	\$ 31,880	\$ —	\$ 32,123
<b>INVESTING ACTIVITIES</b>					
Purchases of Property, Plant and Equipment	(7,400 )	—	(8,839 )	—	(16,239 )
Proceeds from Disposals of Property, Plant and Equipment	17	—	2,439	—	2,456
Proceeds from Principal Payments Received on Long-Term Note Receivable	—	—	500	—	500
Issuance of Long-Term Note Receivable	—	—	(1,500 )	—	(1,500 )
Acquisition of Businesses, Net of Cash Acquired	(304 )	—	(353,231 )	—	(353,535 )
Purchase of Intangible Asset	(2,500 )	—	—	—	(2,500 )
Change in Investments in Subsidiaries	(193,639)	—	—	193,639	—
Loan (Payments) Borrowings from Subsidiaries	(159,780)	—	—	159,780	—
Net Cash Used in Investing Activities	(363,606)	—	(360,631 )	353,419	(370,818)
<b>FINANCING ACTIVITIES</b>					
Proceeds from Short-Term Debt	300,000	—	—	—	300,000
Repayments of Short-Term Debt	(300,000)	—	—	—	(300,000)
Loan Borrowings (Payments) from Parent	—	—	159,780	(159,780)	—
Change in Subsidiary Equity	—	—	193,639	(193,639)	—
Proceeds from Issuance of Long-Term Debt	440,000	—	—	—	440,000
Payments of Long-Term Debt	(81,143 )	—	(119 )	—	(81,262 )
Payments of Debt Issuance Costs	(16,465 )	—	—	—	(16,465 )
Proceeds from Issuance of Common Stock	4,728	—	—	—	4,728
Dividends Paid	(11,204 )	—	—	—	(11,204 )
Net Cash Provided by Financing Activities	335,916	—	353,300	(353,419)	335,797
Effect of Exchange Rate Changes on Cash, Cash Equivalents and Restricted Cash	(68 )	—	1,655	—	1,587
Net (Decrease) Increase in Cash, Cash Equivalents and Restricted Cash	(28,313 )	798	26,204	—	(1,311 )
Cash, Cash Equivalents and Restricted Cash at Beginning of Period	38,484	226	19,840	—	58,550
Cash, Cash Equivalents and Restricted Cash at End of Period	\$ 10,171	\$ 1,024	\$ 46,044	\$ —	\$ 57,239

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

## Overview

Tennant Company is a world leader in designing, manufacturing and marketing solutions that empower customers to achieve quality cleaning performance, reduce environmental impact and help create a cleaner, safer, healthier world. Tennant is committed to creating and commercializing breakthrough, sustainable cleaning innovations to enhance its broad suite of products, including floor maintenance and outdoor cleaning equipment, detergent-free and other sustainable cleaning technologies, aftermarket parts and consumables, equipment maintenance and repair service, specialty surface coatings and asset management solutions. Tennant products are used in many types of environments, including retail establishments, distribution centers, factories and warehouses, public venues such as arenas and stadiums, office buildings, schools and universities, hospitals and clinics, parking lots and streets, and more. Customers include contract cleaners to whom organizations outsource facilities maintenance, as well as businesses that perform facilities maintenance themselves. The company reaches these customers through the industry's largest direct sales and service organization and through a strong and well-supported network of authorized distributors worldwide.

## Historical Results

The following table compares the historical results of operations for the three and nine months ended September 30, 2018 and 2017, respectively, and as a percentage of Net Sales (in thousands, except per share data and percentages):

	Three Months Ended				Nine Months Ended			
	September 30		September 30		September 30		September 30	
	2018	%	2017	%	2018	%	2017	%
Net Sales	\$273,255	100.0	\$261,921	100.0	\$838,299	100.0	\$723,771	100.0
Cost of Sales	165,170	60.4	157,317	60.1	500,778	59.7	434,877	60.1
Gross Profit	108,085	39.6	104,604	39.9	337,521	40.3	288,894	39.9
Operating Expense:								
Research and Development Expense	7,506	2.7	7,907	3.0	23,408	2.8	24,239	3.3
Selling and Administrative Expense	85,140	31.2	85,711	32.7	269,273	32.1	246,993	34.1
Total Operating Expense	92,646	33.9	93,618	35.7	292,681	34.9	271,232	37.5
Profit from Operations	15,439	5.7	10,986	4.2	44,840	5.3	17,662	2.4
Other Income (Expense):								
Interest Income	839	0.3	698	0.3	2,540	0.3	1,575	0.2
Interest Expense	(5,986)	(2.2)	(6,093)	(2.3)	(17,736)	(2.1)	(18,720)	(2.6)
Net Foreign Currency Transaction Losses	(295)	(0.1)	(842)	(0.3)	(1,381)	(0.2)	(2,375)	(0.3)
Other Expense, Net	(130)	—	(422)	(0.2)	(890)	(0.1)	(774)	(0.1)
Total Other Expense, Net	(5,572)	(2.0)	(6,659)	(2.5)	(17,467)	(2.1)	(20,294)	(2.8)
Profit (Loss) Before Income Taxes	9,867	3.6	4,327	1.7	27,373	3.3	(2,632)	(0.4)
Income Tax Expense	158	0.1	731	0.3	1,598	0.2	385	0.1
Net Earnings (Loss) Including Noncontrolling Interest	9,709	3.6	3,596	1.4	25,775	3.1	(3,017)	(0.4)
Net Earnings (Loss) Attributable to Noncontrolling Interest	33	—	37	—	81	—	(28)	—
Net Earnings (Loss) Attributable to Tennant Company	\$9,676	3.5	\$3,559	1.4	\$25,694	3.1	\$(2,989)	(0.4)
Net Earnings (Loss) Attributable to Tennant Company per Share - Diluted	\$0.52		\$0.20		\$1.40		\$(0.17)	

## Net Sales

Consolidated Net Sales for the third quarter of 2018 totaled \$273.3 million, a 4.3% increase as compared to consolidated Net Sales of \$261.9 million in the third quarter of 2017. Consolidated Net Sales for the first nine months of 2018 totaled \$838.3 million, a 15.8% increase as compared to consolidated Net Sales of \$723.8 million for the first nine months of 2017.

The components of the consolidated Net Sales change for the three and nine months ended September 30, 2018 as compared to the same periods in 2017 were as follows:

	2018 v. 2017	
	Three Months Ended	Nine Months Ended
	September 30	September 30
Organic Growth:		
Volume	4.6%	4.3%
Price	1.5%	1.6%
Organic Growth	6.1%	5.9%
Foreign Currency	(1.7%)	1.2%
Acquisitions and Divestitures	(0.1%)	8.7%
Total	4.3%	15.8%

The 4.3% increase in consolidated Net Sales in the third quarter of 2018 as compared to the same period in 2017 was driven by:

An organic sales increase of approximately 6.1%, which excludes the effects of foreign currency exchange and acquisitions and divestitures, resulting from an approximate 4.6% volume increase and a 1.5% price increase. The volume increase was primarily due to volume increases in our Americas strategic account and distribution channels, along with continued growth in our service and parts and consumables businesses, in addition to higher sales volumes in the APAC region led by industrial product growth in China. These sales increases were partially offset by lower sales in the EMEA region, due to a higher comparable sales growth in the third quarter of 2017. The price increase was the result of selling price increases, which averaged 3% in most geographies, with an effective date of February 1, 2018. We expect the increase in selling prices to increase Net Sales in the range of 1% to 2% for the 2018 full year. The impact to gross margin is estimated to be minimal as these selling price increases were taken to offset inflation. An unfavorable impact from foreign currency exchange of approximately (1.7%).

The 15.8% increase in consolidated Net Sales in the first nine months of 2018 as compared to the same period in 2017 was driven by:

8.7% from the second quarter 2017 acquisition of the IPC Group.

An organic sales increase of approximately 5.9%, which excludes the effects of foreign currency exchange and acquisitions and divestitures, resulting from an approximate 4.3% volume increase and a 1.6% price increase. The volume increase was primarily due to increased sales of commercial equipment in the Americas and industrial equipment in APAC, mostly attributed to strong sales through strategic accounts in these regions. The price increase was the result of selling price increases, which averaged 3% in most geographies, with an effective date of February 1, 2018. We expect the increase in selling prices to increase Net Sales in the range of 1% to 2% for the 2018 full year. The impact to gross margin is estimated to be minimal as these selling price increases were taken to offset inflation. A favorable impact from foreign currency exchange of approximately 1.2%.

The following table sets forth the Net Sales by geographic area for the three and nine months ended September 30, 2018 and 2017 and the percentage change from the prior year (in thousands, except percentages):

	Three Months Ended			Nine Months Ended		
	September 30			September 30		
	2018	2017	%	2018	2017	%
Americas	\$175,341	\$161,037	8.9	\$516,731	\$472,953	9.3
Europe, Middle East and Africa	74,254	78,851	(5.8)	250,480	189,483	32.2
Asia Pacific	23,660	22,033	7.4	71,088	61,335	15.9

Edgar Filing: TENNANT CO - Form 10-Q

Total \$273,255 \$261,921 4.3 \$838,299 \$723,771 15.8

37

---

#### Americas

Net Sales in the Americas were \$175.3 million for the third quarter of 2018, an increase of 8.9% from the third quarter of 2017. An unfavorable direct impact of foreign currency translation exchange effects within the Americas impacted Net Sales by approximately 1.6% in the third quarter of 2018. As a result, organic sales growth in the Americas favorably impacted Net Sales by approximately 10.6% due to strong equipment sales in North America resulting from increased sales to the strategic account and distribution channels and increased parts and service sales, primarily a result of improved productivity in our service organization and continued broad-based strength in Brazil.

Net Sales in the Americas were \$516.7 million for the first nine months of 2018, an increase of 9.3% from the first nine months of 2017. The direct impact of the second quarter 2017 acquisition of the IPC Group favorably impacted Net Sales by approximately 1.6%. In addition, an unfavorable impact of foreign currency translation exchange effects within the Americas impacted Net Sales by approximately 0.5% in the first nine months of 2018. As a result, organic sales growth in the Americas favorably impacted Net Sales by approximately 8.2% due to strong equipment sales in North America resulting from increased sales to all sales channels and broad based sales growth in Brazil. The Americas also experienced increased parts and service sales in the first nine months of 2018, primarily a result of improved productivity in our service organization.

#### Europe, Middle East and Africa

EMEA Net Sales were \$74.3 million for the third quarter of 2018, a decrease of 5.8% from the third quarter of 2017. An unfavorable impact of foreign currency translation exchange effects within EMEA impacted Net Sales by approximately 1.3% in the third quarter of 2018. Organic sales declines in EMEA unfavorably impacted Net Sales by approximately 4.5% due to sales declines in the France and Italian markets due to a challenging comparable sales performance from the third quarter of 2017. Net Sales declines for the third quarter of 2018 were partially offset by sales growth in the UK.

EMEA Net Sales were \$250.5 million for the first nine months of 2018, an increase of 32.2% from the first nine months of 2017. The direct impact of the second quarter 2017 acquisition of the IPC Group favorably impacted Net Sales by approximately 26.3%. In addition, a favorable impact of foreign currency translation exchange effects within EMEA impacted Net Sales by approximately 5.9% in the first nine months of 2018. As a result, organic sales growth in EMEA was essentially flat.

#### Asia Pacific

APAC Net Sales were \$23.7 million for the third quarter of 2018, an increase of 7.4% from the third quarter of 2017. An unfavorable direct impact of foreign currency translation exchange effects within APAC impacted Net Sales by approximately 3.2% in the third quarter of 2018. As a result, organic sales growth in APAC favorably impacted Net Sales by approximately 10.6% primarily due to sales growth in China across all products and channels partially offset by declines in other parts of the region.

APAC Net Sales were \$71.1 million for the first nine months of 2018, an increase of 15.9% from the first nine months of 2017. The direct impact of the second quarter 2017 acquisition of the IPC Group favorably impacted Net Sales by approximately 9.1%. In addition, a favorable direct impact of foreign currency translation exchange effects within APAC impacted Net Sales by approximately 0.8% in the first nine months of 2018. As a result, organic sales growth in APAC favorably impacted Net Sales by approximately 6.0% due to sales growth in Australia and China from strong industrial product sales through the direct and strategic account channels.

#### Gross Profit

Gross Profit margin of 39.6% was 30 basis points lower in the third quarter of 2018 compared to the third quarter of 2017. Gross Profit margin was unfavorably impacted by robust strategic account sales impacting our mix and manufacturing productivity issues associated with raw material and labor shortages as well as higher freight and logistics costs and newly enacted tariffs. The unfavorable Gross Profit Margin impacts were partially offset by improved operational performance in both manufacturing and service resulting from our operational effectiveness strategies as well as favorable pricing in North America and EMEA. In addition, Gross Profit margin was favorably impacted by a \$2.2 million, or approximately 85 basis points, fair value inventory step-up flow through related to our acquisition of the IPC Group in the third quarter of 2017 that did not repeat in the third quarter of 2018.

Gross Profit margin of 40.3% was 40 basis points higher in the first nine months of 2018 compared to the first nine months of 2017. Gross Profit margin was unfavorably impacted by robust strategic account sales impacting our mix, manufacturing productivity issues associated with raw material and labor shortages and an inventory write down related to our Coatings business. The unfavorable Gross Profit margin impacts were partially offset by improved operational performance in both manufacturing and service. In addition, Gross Profit margin was favorably impacted by an \$8.4 million, or approximately 120 basis points, fair value inventory step-up flow through related to our acquisition of the IPC Group in first nine months of 2017 that did not repeat in the first nine months of 2018.

We expect the full year Gross Profit margin to be approximately 40.5% of net sales.

#### Operating Expense

##### Research & Development Expense

We continue to invest in developing innovative products and technologies and the advancement of detergent-free products, fleet management and other sustainable technologies. New products and product variants launched in the first nine months of 2018 included the T600 series of scrubbers. In the fourth quarter of 2018, we plan to introduce our first autonomous floor care machine.

Research and Development ("R&D") Expense was \$7.5 million, or 2.7% as a percentage of Net Sales, for the third quarter of 2018, a decrease of 30 basis points compared to the third quarter of 2017. R&D Expense was \$23.4 million, or 2.8% as a percentage of Net Sales, for the first nine months of 2018, a decrease of 50 basis points compared to the first nine months of 2017.

The decrease in R&D as a percentage of sales reflects the impact of 2018 higher revenue and the timing of anticipated project spend in 2018, including investment in our strategic relationship with Brain Corp., to accelerate development of our autonomous floor cleaning technology. We continue to invest in R&D at levels necessary to propel our clear technology leadership position. We expect the full year spending for R&D to be approximately 3.0% of net sales.

##### Selling & Administrative Expense

Selling and Administrative Expense ("S&A Expense") was \$85.1 million, a decrease of \$0.6 million, or 0.7%, compared to the third quarter of 2017. As a percentage of Net Sales, S&A Expense for the third quarter of 2018 decreased 150 basis points to 31.2% from 32.7% in the third quarter of 2017.

For the third quarter of 2018, S&A Expense was impacted by \$1.9 million, or 70 basis points, lower amortization expense related to the acquisition of the IPC Group compared to the third quarter of 2017 and a gain of approximately \$1 million, or 35 basis points, related to the sale of our Waterstar business recorded in the third quarter of 2018.

Partially offsetting this favorability was \$0.6 million, or 25 basis points, higher acquisition and integration costs, as well as \$0.2 million, or 10 basis points, for non-operational professional service fees recorded in the third quarter of 2018.

Excluding these items, S&A Expense as a percentage of Net Sales for the third quarter of 2018 was 80 basis points lower compared to the same period in the prior year, primarily due to our continued balance of disciplined spending control with investments in key growth initiatives.

S&A Expense for the first nine months of 2018 increased by \$22.3 million, or 9.0%, compared to the first nine months of 2017. As a percentage of Net Sales, S&A Expense for the first nine months of 2018 decreased 200 basis points to 32.1% from 34.1% in the first nine months of 2017.

For the first nine months of 2018, S&A Expense was impacted by an \$8.0 million restructuring charge, or approximately 100 basis points, recorded in the third quarter of 2017 that did not repeat in the first nine months of 2018, a decrease of \$3.1 million, or 40 basis points, in acquisition and integration costs, as well as a gain of approximately \$1 million, or 10 basis points, related to the sale of our Waterstar business recorded in the third quarter of 2018. Partially offsetting this favorability was \$6.0 million, or 70 basis points, higher amortization expense related to the acquisition of the IPC Group compared to the first nine months of 2017, and \$1.8 million, or 20 basis points, for non-operational professional service fees recorded in the third quarter of 2018.

Excluding these costs, S&A Expense as a percentage of Net Sales was 140 basis points lower in the first nine months of 2018 compared to the first nine months of 2017 due primarily to our continued balance of disciplined spending control with investments in key growth initiatives.

##### Total Other Expense, Net

##### Interest Income

Interest Income was \$0.8 million in the third quarter of 2018, relatively flat compared to Interest Income of \$0.7 million in the third quarter of 2017. For the first nine months of 2018, Interest Income was \$2.5 million compared to Interest Income of \$1.6 million in the first nine months of 2017. The increase in Interest Income was primarily due to interest income related to foreign currency swap activities.





#### Interest Expense

Interest Expense was \$6.0 million in the third quarter of 2018 compared to Interest Expense of \$6.1 million in the third quarter of 2017. For the first nine months of 2018, Interest Expense was \$17.7 million compared to Interest Expense of \$18.7 million in the first nine months of 2017. The lower Interest Expense in the third quarter and first nine months of 2018 compared to the same periods in 2017 was primarily due to carrying a lower level of debt on our Condensed Consolidated Balance Sheets throughout the first nine months of 2018 compared to the same period in 2017, partially offset by higher debt issuance charges from paying down debt balances faster than contractually required.

#### Net Foreign Currency Transaction Losses

Net Foreign Currency Transaction Losses in the third quarter of 2018 were \$0.3 million compared to Net Foreign Currency Transaction Losses of \$0.8 million in the third quarter of 2017. For the first nine months of 2018, Net Foreign Currency Transaction Losses were \$1.4 million compared to Net Foreign Currency Transaction Losses of \$2.4 million in the first nine months of 2017. The favorable change in the impact from foreign currency transactions in the first nine months of 2018 was primarily due to a \$1.1 million mark-to-market adjustment of a foreign exchange call option held in connection with our acquisition of IPC Group in April 2017 that did not repeat in 2018.

#### Other Expense, Net

Other Expense, Net was \$0.1 million and \$0.9 million in the third quarter and first nine months of 2018, respectively, relatively flat compared to the same periods in 2017.

#### Income Taxes

The effective tax rate in the third quarter of 2018 was 1.6% compared to the effective tax rate in the third quarter of the prior year of 16.9%.

The tax expense for the third quarter of 2018 included a \$0.3 million tax benefit associated with \$1.5 million of acquisition and integration related costs associated with our acquisition of the IPC Group, a \$0.1 million tax benefit associated with \$0.2 million of costs related to non-operational professional service fees and a \$0.2 million tax expense associated with a \$1.0 million gain on the sale of Waterstar. These special items impacted the third quarter 2018 effective tax rate by (4.0%).

The effective tax rate in the third quarter of 2017 was 16.9%. The tax expense for the third quarter of 2017 included a \$0.6 million tax benefit associated with \$2.2 million of expense related to inventory step-up amortization and a \$0.3 million tax benefit associated with \$0.9 million of acquisition costs related to the IPC Group acquisition. These special items impacted the third quarter 2017 effective tax rate by (4.8%).

Excluding these special items, the rate decreased due primarily to the mix in expected full year taxable earnings by country, discrete tax expense benefit related to exercised stock options, a favorable tax ruling with the Italian tax authorities in connection with the acquisition of IPC Group, the reduction in our estimated transition tax liability and the reduction in the U.S. federal income tax rate in the Tax Act.

The year-to-date overall effective tax rate was 5.8% for 2018 compared to (14.6%) for 2017. The 2018 special items impacted the year-to-date overall effective tax rate by (4.1%). The 2017 special items impacted the year-to-date overall effective tax rate by (41.5%).

Excluding these special items, the rate decreased due primarily to the mix in expected full year taxable earnings by country, discrete tax expense benefit related to the exercise of soon-to-expire stock options, a favorable tax ruling from the Italian tax authorities related to the deductibility of interest expense in Italy, the reduction in our estimated transition tax liability and the reduction in the U.S. federal income tax rate in the Tax Act.

In general, it is our practice and intention to permanently reinvest the earnings of our foreign subsidiaries and repatriate earnings only when the tax impact is zero or immaterial and that position has not changed following incurring the transition tax under the Tax Act. No deferred taxes have been provided for withholding taxes or other taxes that would result upon repatriation of our foreign investments to the United States.

#### Liquidity and Capital Resources

##### Liquidity

Cash and Cash Equivalents totaled \$53.5 million at September 30, 2018, as compared to \$58.4 million as of December 31, 2017. Wherever possible, cash management is centralized and intercompany financing is used to

provide working capital to subsidiaries as needed. Our current ratio was 1.8 as of September 30, 2018 and December 31, 2017, and our working capital was \$200.4 million and \$186.6 million, respectively. Our debt-to-capital ratio was 53.1% as of September 30, 2018, compared to 56.0% as of December 31, 2017.

### Cash Flow From Operating Activities

Operating Activities provided \$43.5 million of cash for the nine months ended September 30, 2018. Cash provided by operating activities was driven primarily by cash inflows from net earnings adding back non-cash items and a \$5.2 million increase in Employee Compensation and Benefits liabilities. These cash inflows were offset by cash outflows resulting from an increase in Inventories of \$19.6 million to support future sales growth.

Operating Activities provided \$32.1 million of cash for the nine months ended September 30, 2017. Cash provided by operating activities was driven primarily by cash inflows from net earnings adding back non-cash items and an increase in Accounts Payable of \$5.7 million resulting from timing of payments. These cash inflows were partially offset by cash outflows due to an increase in Inventories of \$9.9 million to support future sales growth and a decrease in Employee Compensation and Benefits of \$9.5 million due to payment of accrued employee incentives.

Two metrics used by management to evaluate how effectively we utilize our net assets are "Accounts Receivable Days Sales Outstanding" ("DSO") and "Days Inventory on Hand" ("DIOH"), on a first-in, first-out ("FIFO") basis. The metrics are calculated on a rolling three month basis in order to more readily reflect changing trends in the business. These metrics as of September 30, 2018 and December 31, 2017 were as follows (in days):

	September 30, 2018	December 31, 2017
DSO	67	63
DIOH	101	96

As of September 30, 2018, DSO increased four days compared to December 31, 2017, primarily due to mix of business and payment terms offered, partially offset by the trend of continued proactive management of our receivables by enforcing tighter credit limits and continuing to successfully collect past due balances.

As of September 30, 2018, DIOH increased five days compared to December 31, 2017, primarily due increased levels of inventory in support of higher anticipated sales levels and launches of new products offset by progress from inventory reduction initiatives.

### Cash Flow From Investing Activities

Investing activities during the nine months ended September 30, 2018 used \$10.4 million. We used \$12.8 million for net capital expenditures. Net capital expenditures included investments in information technology process improvement projects, tooling related to new product development and manufacturing equipment. We also used \$2.6 million to purchase a technology license and other intangibles. In addition, we received \$4 million in proceeds due to the sale of the Waterstar business.

Investing activities during the nine months ended September 30, 2017 used \$370.8 million. We used \$353.5 million in relation to our acquisition of the IPC Group and the final installment payment for the acquisition of the Florock brand. In addition, we used \$16.2 million and \$2.5 million for net capital expenditures and for the purchase of the distribution rights to sell the i-mop, respectively. Net capital expenditures included investments in information technology process improvement projects, tooling related to new product development and manufacturing equipment. We also used \$1.5 million as a result of a loan to i-team North America B.V., a joint venture that operates as the distributor of the i-mop in North America.

### Cash Flow From Financing Activities

Net cash used in financing activities was \$35.8 million during the first nine months of 2018. Payments of Long-Term Debt used \$30.2 million and dividend payments used \$11.4 million, partially offset by proceeds from the issuance of Common Stock of \$5.7 million.

Net cash provided by financing activities was \$335.8 million during the first nine months of 2017. Proceeds from the incurrence of Long-Term Debt and the issuance of Common Stock provided \$440.0 million and \$4.7 million, respectively. These cash inflows were partially offset by cash outflows resulting from \$81.3 million of Long-Term Debt payments, \$16.5 million related to payments of debt issuance costs and dividend payments of \$11.2 million.

#### Newly Issued Accounting Guidance

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). This ASU changes current U.S. GAAP for lessees to recognize lease assets and lease liabilities on the balance sheet for those leases classified as operating leases under previous U.S. GAAP. Under the new guidance, lessor accounting is largely unchanged. The amendments in this ASU are effective for annual periods beginning after December 15, 2018, including interim periods within that reporting period, which is our fiscal 2019. Early application is permitted. Lessees and lessors must apply 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. The transition approach would not require any transition accounting for leases that expired before the earliest comparative period presented. A full retrospective transition approach is prohibited for both lessees and lessors. We will adopt this ASU beginning in 2019. We are currently evaluating the impact of this amended guidance on our consolidated financial statements and related disclosures.

#### Cautionary Statement Relevant to Forward-Looking Information

This Form 10-Q, including “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 2, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements generally can be identified by the use of forward-looking terminology such as “may,” “will,” “expect,” “intend,” “estimate,” “anticipate,” “believe,” “project,” or “continue” or similar words or the negative thereof. Forward-looking statements do not relate to strictly historical or current facts and provide current expectations of forecasts of future events. Any such expectations or forecasts of future events are subject to a variety of factors. Particular risks and uncertainties presently facing us include: our ability to effectively manage organizational changes; our ability to attract, retain and develop key personnel and create effective succession planning strategies; the competition in our business; fluctuations in the cost, quality, or availability of raw materials and purchased components; our ability to successfully upgrade and evolve our information technology systems; our ability to develop and commercialize new innovative products and services; our ability to integrate acquisitions, including IPC; our ability to generate sufficient cash to satisfy our debt obligations; geopolitical and economic uncertainty throughout the world; our ability to successfully protect our information technology systems from cyber security risks; the occurrence of a significant business interruption; our ability to comply with laws and regulations; the potential disruption of our business from actions of activist investors or others; the relative strength of the U.S. dollar, which affects the cost of our materials and products purchased and sold internationally; unforeseen product liability claims or product quality issues; and our internal control over financial reporting risks resulting from our acquisition of the IPC Group. We caution that forward-looking statements must be considered carefully and that actual results may differ in material ways due to risks and uncertainties both known and unknown. Shareholders, potential investors and other readers are urged to consider these factors in evaluating forward-looking statements and are cautioned not to place undue reliance on such forward-looking statements. Additional information about factors that could materially affect our results can be found in Part I, Item 1A, Risk Factors in our annual report on Form 10-K for the year ended December 31, 2017 and Part II, Item 1A of this Form 10-Q.

We undertake no obligation to update or revise any forward-looking statement, whether as a result of new information, future events or otherwise, except as required by law. Investors are advised to consult any further disclosures by us in our filings with the SEC and in other written statements on related subjects. It is not possible to anticipate or foresee all risk factors, and investors should not consider any list of such factors to be an exhaustive or complete list of all risks or uncertainties.

#### Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in our market risk since December 31, 2017. For additional information, refer to Item 7A of our 2017 annual report on Form 10-K for the year ended December 31, 2017.

#### Item 4. Controls and Procedures

##### Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Principal Financial and Accounting Officer, have evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2018 (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”). Based on that evaluation, our Chief Executive Officer and our Principal Financial and Accounting Officer have concluded that

our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our principal executive and our principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

**Changes in Internal Controls**

There were no changes in our internal controls over financial reporting during the most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II – OTHER INFORMATION

## Item 1. Legal Proceedings

There are no material pending legal proceedings other than ordinary routine litigation incidental to our business.

## Item 1A. Risk Factors

We documented our risk factors in Item 1A of Part I of our annual report on Form 10-K for the fiscal year ended December 31, 2017. There have been no material changes to our risk factors since the filing of that report.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On October 31, 2016, the Board of Directors authorized the repurchase of an additional 1,000,000 shares of our common stock. This is in addition to the 392,892 shares remaining under our prior repurchase program. Share repurchases are made from time to time in the open market or through privately negotiated transactions, primarily to offset the dilutive effect of shares issued through our share-based compensation programs. As of September 30, 2018, our 2017 Credit Agreement restricts the payment of dividends or repurchasing of stock if, after giving effect to such payments and assuming no default exists or would result from such payment, our leverage ratio is greater than 2.50 to 1, in such case limiting such payments to an amount ranging from \$50.0 million to \$75.0 million during any fiscal year based on our leverage ratio after giving effect to such payment. Our Senior Notes due 2025 also contain certain restrictions, which are generally less restrictive than those contained in the 2017 Credit Agreement.

For the Quarter Ended September 30, 2018	Total Number of Shares Purchased <sup>(1)</sup>	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
July 1 - 31, 2018	120	\$ 79.00	—	1,392,892
August 1 - 31, 2018	1,207	80.86	—	1,392,892
September 1 - 30, 2018	—	—	—	1,392,892
Total	1,327	\$ 80.69	—	1,392,892

<sup>(1)</sup> Includes 1,327 shares delivered or attested to in satisfaction of the exercise price and/or tax withholding obligations by employees who exercised stock options or restricted stock under employee share-based compensation plans.

Item 6. Exhibits

Item #	Description	Method of Filing
3i	<u>Restated Articles of Incorporation</u>	Incorporated by reference to Exhibit 3i to the Company's report on Form 10-Q for the quarterly period ended June 30, 2006.
3ii	<u>Amended and Restated By-Laws</u>	Incorporated by reference to Exhibit 3iii to the Company's Form 8-K dated December 14, 2010.
3iii	<u>Articles of Amendment of Restated Articles of Incorporation of Tennant Company</u>	Incorporated by reference to Exhibit 3iii to the Company's report on Form 10-Q for the quarterly period ended March 31, 2018.
4.1	<u>Indenture dated as of April 18, 2017</u>	Incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed April 24, 2017.
10.1	<u>Cash Incentive Plan</u>	Incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed August 20, 2018.
31.1	<u>Rule 13a-14(a)/15d-14(a) Certification of CEO</u>	Filed herewith electronically.
31.2	<u>Rule 13a-14(a)/15d-14(a) Certification of CFO</u>	Filed herewith electronically.
32.1	<u>Section 1350 Certification of CEO</u>	Filed herewith electronically.
32.2	<u>Section 1350 Certification of CFO</u>	Filed herewith electronically.
101	<p>The following financial information from Tennant Company's Quarterly Report on Form 10-Q for the period ended September 30, 2018, formatted in Extensible Business Reporting Language (XBRL): (i) Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2018 and 2017; (ii) Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2018 and 2017; (iii) Condensed Consolidated Balance Sheets as of September 30, 2018 and December 31, 2017; (iv) Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and 2017; and (v) Notes to the Condensed Consolidated Financial Statements.</p>	Filed herewith electronically.





SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TENNANT COMPANY

Date: November 2, 2018 /s/ H. Chris Killingstad  
H. Chris Killingstad  
President and Chief Executive Officer

Date: November 2, 2018 /s/ Thomas Paulson  
Thomas Paulson  
Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)