Cypress Energy Partners, L.P.
Form 10-Q
August 14, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(MARK ONE)

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

For the quarterly period ended June 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 001-36260

CYPRESS ENERGY PARTNERS, L.P.

(Exact name of Registrant as specified in its charter)

Delaware	**61-1721523**
(State of or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

5727 South Lewis Avenue, Suite 300	
Tulsa, Oklahoma	**74105**
(Address of principal executive offices)	(zip code)

Registrant’s telephone number, including area code: **(918) 748-3900**

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

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

Large accelerated filer	Accelerated filer	Non-accelerated filer	Smaller reporting company	Emerging growth company
			(Do not check if a smaller reporting 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 August 7, 2018, the registrant had 11,933,522 common units outstanding.

DOCUMENTS INCORPORATED BY REFERENCE: None.

CYPRESS ENERGY PARTNERS, L.P.

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NAMES OF ENTITIES

Unless the context otherwise requires, references in this Quarterly Report on Form 10-Q to "Cypress Energy Partners, L.P.," "our partnership," "we," "our," "us," or like terms, refer to Cypress Energy Partners, L.P. and its subsidiaries.

References to:

"*Brown*" refers to Brown Integrity, LLC, a 51% owned subsidiary of CEP LLC;

"*CEP LLC*" refers to Cypress Energy Partners, LLC, a wholly-owned subsidiary of the Partnership;

"*CF Inspection*" refers to CF Inspection Management, LLC, owned 49% by TIR-PUC and consolidated under generally accepted accounting principles by TIR-PUC. CF Inspection is 51% owned, managed and controlled by Cynthia A. Field, an affiliate of Holdings;

"*General Partner*" refers to Cypress Energy Partners GP, LLC, a subsidiary of Cypress Energy GP Holdings, LLC;

"*Holdings*" refers to Cypress Energy Holdings, LLC, the owner of Holdings II;

"*Holdings II*" refers to Cypress Energy Holdings II, LLC, the owner of 5,610,549 common units, representing 47.0% of our outstanding common units;

"*Integrity Services*" refers to our Integrity Services business segment;

"*Partnership*" refers to the registrant, Cypress Energy Partners, L.P.;

"*Pipeline Inspection*" refers to our Pipeline Inspection business segment;

"*TIR Entities*" refer collectively to TIR LLC, TIR-Canada, TIR-NDE, TIR-PUC and CF Inspection;

"*TIR LLC*" refers to Tulsa Inspection Resources, LLC, a wholly-owned subsidiary of CEP LLC;

"*TIR-Canada*" refers to Tulsa Inspection Resources – Canada ULC, a wholly-owned subsidiary of CEP LLC;

"*TIR-NDE*" refers to Tulsa Inspection Resources – Nondestructive Examination, LLC, a wholly-owned subsidiary of CEP LLC;

"*TIR-PUC*" refers to Tulsa Inspection Resources – PUC, LLC, a subsidiary of TIR LLC that has elected to be treated as a corporation for federal income tax purposes; and

"*Water Services*" refers to our Water and Environmental Services business segment.

CAUTIONARY REMARKS REGARDING FORWARD-LOOKING STATEMENTS

The information discussed in this Quarterly Report on Form 10-Q includes "forward-looking statements." These forward-looking statements are identified by their use of terms and phrases such as "may," "expect," "estimate," "project," "plan," "believe," "intend," "achievable," "anticipate," "continue," "potential," "should," "could," and similar terms and phrase Although we believe that the expectations reflected in these forward-looking statements are reasonable, they do involve certain assumptions, risks and uncertainties and we can give no assurance that such expectations or assumptions will be achieved. Important factors that could cause actual results to differ materially from those in the forward-looking statements are described under "*Item 1A – Risk Factors*" and "*Item 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations*" in our Annual Report on Form 10-K for the year ended December 31, 2017 and in this report. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements in this paragraph and elsewhere in this Quarterly Report on Form 10-Q and speak only as of the date of this Quarterly Report on Form 10-Q. Other than as required under the securities laws, we do not assume a duty to update these forward-looking statements, whether as a result of new information, subsequent events or circumstances, changes in expectations or otherwise.

PART I. FINANCIAL INFORMATION

ITEM 1. Unaudited Condensed Consolidated Financial Statements

CYPRESS ENERGY PARTNERS, L.P.

Unaudited Condensed Consolidated Balance Sheets

As of June 30, 2018 and December 31, 2017

(in thousands, except unit data)

	June 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$10,499	$24,508
Trade accounts receivable, net	47,692	41,693
Prepaid expenses and other	1,040	2,294
Assets held for sale	—	2,172
Total current assets	59,231	70,667
Property and equipment:		
Property and equipment, at cost	23,057	22,700
Less: Accumulated depreciation	9,991	9,312
Total property and equipment, net	13,066	13,388
Intangible assets, net	24,114	25,477
Goodwill	50,344	53,435
Debt issuance costs, net	1,498	—
Other assets	266	236
Total assets	$148,519	$163,203
LIABILITIES AND OWNERS' EQUITY		
Current liabilities:		
Accounts payable	$3,404	$3,757
Accounts payable - affiliates	3,966	3,173
Accrued payroll and other	11,163	9,109
Liabilities held for sale	—	97
Income taxes payable	346	646
Current portion of long-term debt	—	136,293
Total current liabilities	18,879	153,075
Long-term debt	76,129	—

Asset retirement obligations	142	143
Total liabilities	95,150	153,218
Commitments and contingencies - Note 8		
Owners' equity:		
Partners' capital:		
Common units (11,933,522 and 11,889,958 units outstanding at June 30, 2018 and December 31, 2017, respectively)	33,852	34,614
Preferred units (5,769,231 units outstanding at June 30, 2018)	43,636	—
General partner	(25,876)	(25,876)
Accumulated other comprehensive loss	(2,545)	(2,677)
Total partners' capital	49,067	6,061
Noncontrolling interests	4,302	3,924
Total owners' equity	53,369	9,985
Total liabilities and owners' equity	$ 148,519	$ 163,203

See accompanying notes.

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CYPRESS ENERGY PARTNERS, L.P.

Unaudited Condensed Consolidated Statements of Operations

For the Three and Six Months Ended June 30, 2018 and 2017

(in thousands, except unit and per unit data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Revenue	$76,468	$74,567	$141,294	$139,289
Costs of services	65,525	65,958	122,222	124,351
Gross margin	10,943	8,609	19,072	14,938
Operating costs and expense:				
General and administrative	5,822	5,329	11,277	10,439
Depreciation, amortization and accretion	1,110	1,206	2,244	2,377
Impairments	—	—	—	3,598
Gain on asset disposals, net	(1,606)	(113)	(3,315)	(113)
Operating income (loss)	5,617	2,187	8,866	(1,363)
Other (expense) income:				
Interest expense, net	(1,668)	(1,795)	(3,624)	(3,504)
Debt issuance cost write-off	(114)	—	(114)	—
Foreign currency gains (losses)	(117)	267	(451)	267
Other, net	125	60	207	105
Net income (loss) before income tax expense	3,843	719	4,884	(4,495)
Income tax expense (benefit)	287	222	368	(71)
Net income (loss)	3,556	497	4,516	(4,424)
Net income (loss) attributable to noncontrolling interests	149	(133)	384	(1,298)
Net income (loss) attributable to partners / controlling interests	3,407	630	4,132	(3,126)
Net loss attributable to general partner	—	(829)	—	(1,750)
Net income (loss) attributable to limited partners	3,407	1,459	4,132	(1,376)
Net income attributable to preferred unitholder	367	—	367	—
Net income (loss) attributable to common unitholders	$3,040	$1,459	$3,765	$(1,376)
Net income (loss) per common limited partner unit:				
Basic	$0.25	$0.12	$0.32	$(0.13)
Diluted	$0.24	$0.12	$0.31	$(0.13)
Weighted average common units outstanding:				
Basic	11,933,390	11,880,452	11,916,127	10,404,026

Diluted	14,298,409	12,002,538	13,323,692	10,404,026
Weighted average subordinated units outstanding - basic and diluted	—	—	—	1,470,083

See accompanying notes.

CYPRESS ENERGY PARTNERS, L.P.

Unaudited Condensed Consolidated Statements of Comprehensive Income (Loss)

For the Three and Six Months Ended June 30, 2018 and 2017

(in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net income (loss)	$3,556	$497	$4,516	$(4,424)
Other comprehensive income (loss) - foreign currency translation	30	(42)	132	20
Comprehensive income (loss)	$3,586	$455	$4,648	$(4,404)
Comprehensive income attributable to preferred unitholders	367	—	367	—
Comprehensive income (loss) attributable to noncontrolling interests	149	(133)	384	(1,298)
Comprehensive loss attributable to general partner	—	(829)	—	(1,750)
Comprehensive income (loss) attributable to common unitholders	$3,070	$1,417	$3,897	$(1,356)

See accompanying notes.

CYPRESS ENERGY PARTNERS, L.P.

Unaudited Condensed Consolidated Statements of Cash Flows

For the Six Months Ended June 30, 2018 and 2017

(in thousands)

	Six Months Ended June 30,	
	2018	2017
Operating activities:		
Net income (loss)	$4,516	$(4,424)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation, amortization and accretion	2,793	2,913
Impairments	—	3,598
Gain on asset disposals, net	(3,315)	(308)
Interest expense from debt issuance cost amortization	247	294
Debt issuance cost write-off	114	—
Equity-based compensation expense	547	766
Equity in earnings of investee	(100)	(57)
Distributions from investee	63	—
Deferred tax benefit, net	—	(358)
Non-cash allocated expenses	—	1,750
Foreign currency (gains) losses, net	451	(267)
Changes in assets and liabilities:		
Trade accounts receivable	(6,059)	(4,727)
Prepaid expenses and other	1,358	(586)
Accounts payable and accrued payroll and other	1,744	3,920
Income taxes payable	(300)	(802)
Net cash provided by operating activities	2,059	1,712
Investing activities:		
Proceeds from fixed asset disposals	12,002	1,578
Purchases of property and equipment	(3,936)	(380)
Net cash provided by investing activities	8,066	1,198
Financing activities:		
Issuance of preferred units, net of issuance costs	43,269	—
Repayments of long-term debt	(60,771)	—
Debt issuance cost payments	(1,250)	—
Taxes paid related to net share settlement of equity-based compensation	(70)	(77)
Distributions to limited partners	(5,004)	(7,318)
Distributions to noncontrolling interests	(6)	(12)
Net cash used in financing activities	(23,832)	(7,407)

Effect of exchange rates on cash	(202)	271
Net decrease in cash and cash equivalents and restricted cash equivalents	(13,909)	(4,226)
Cash and cash equivalents (including restricted cash equivalents of $490 at December 31, 2017 and December 31, 2016), beginning of period	24,998	27,183
Cash and cash equivalents (including restricted cash equivalents of $590 at June 30, 2018 and $490 at June 30, 2017), end of period	$11,089	$22,957
Non-cash items:		
Accounts payable excluded from capital expenditures	$1,288	$473

See accompanying notes.

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CYPRESS ENERGY PARTNERS, L.P.

Unaudited Condensed Consolidated Statement of Owners' Equity

For the Six Months Ended June 30, 2018

(in thousands)

	Common Units	Preferred Units	General Partner	Accumulated Other Comprehensive Loss	Noncontrolling Interests	Total Owners' Equity
Owners' equity at December 31, 2017	$34,614	$—	$(25,876)	$(2,677)	$3,924	$9,985
Net income for the period January 1, 2018 through June 30, 2018	3,765	367	—	—	384	4,516
Issuance of preferred units, net	—	43,269	—	—	—	43,269
Foreign currency translation adjustment	—	—	—	132	—	132
Distributions to partners	(5,004)	—	—	—	—	(5,004)
Distributions to noncontrolling interests	—	—	—	—	(6)	(6)
Equity-based compensation	547	—	—	—	—	547
Taxes paid related to net share settlement of equity-based compensation	(70)	—	—	—	—	(70)
Owners' equity at June 30, 2018	$33,852	$43,636	$(25,876)	$(2,545)	$4,302	$53,369

See accompanying notes.

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CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

1. Organization and Operations

Cypress Energy Partners, L.P. (the "Partnership") is a Delaware limited partnership formed in 2013 to provide independent pipeline inspection and integrity services to producers, public utility companies, and pipeline companies and to provide saltwater disposal and other water and environmental services to U.S. onshore oil and natural gas producers and trucking companies. Trading of our common units began January 15, 2014 on the New York Stock Exchange under the symbol "CELP".

Our business is organized into the Pipeline Inspection Services ("Pipeline Inspection"), Integrity Services ("Integrity Services"), and Water and Environmental Services ("Water Services") segments. The Pipeline Inspection segment provides pipeline inspection and other services to energy exploration and production ("E&P") companies, public utility companies, and midstream companies and their vendors throughout the United States and Canada. The inspectors of Pipeline Inspection perform a variety of inspection services on midstream pipelines, gathering systems, and distribution systems, including data gathering and supervision of third-party construction, inspection, and maintenance and repair projects. The Integrity Services segment provides independent integrity services to major natural gas and petroleum pipeline companies and to pipeline construction companies located in the United States. Field personnel in this segment primarily perform hydrostatic testing on newly-constructed and existing natural gas and petroleum pipelines. The Water Services segment is comprised of eight commercial saltwater disposal facilities in the Bakken Shale region of the Williston Basin in North Dakota. These facilities provide services to oil and natural gas producers and trucking companies. All of the saltwater disposal facilities utilize specialized equipment and remote monitoring to minimize the facilities' downtime and increase the facilities' efficiency for peak utilization. These facilities also utilize oil skimming processes that remove oil from water delivered to the sites. We sell the oil produced from these skimming processes, which contributes to our revenues. In addition to these saltwater disposal facilities, we provide management and staffing services to a saltwater disposal facility in which we we own a 25% ownership interest (see Note 7).

2. Basis of Presentation and Summary of Significant Accounting Policies

Basis of Presentation

The Unaudited Condensed Consolidated Financial Statements as of and for the three months ended June 30, 2018 and 2017 and for the six months ended June 30, 2018 and 2017 include our accounts and those of our controlled subsidiaries. Investments over which we exercise significant influence, but do not control, are accounted for using the equity method of accounting. All significant intercompany transactions and account balances have been eliminated in consolidation. The Unaudited Condensed Consolidated Balance Sheet at December 31, 2017 is derived from our audited financial statements.

The accompanying Unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim consolidated financial information and in accordance with the rules and regulations of the Securities and Exchange Commission (the "SEC"). The Unaudited Condensed Consolidated Financial Statements include all adjustments considered necessary for a fair presentation of the consolidated financial position and consolidated results of operations for the interim periods presented. Such adjustments consist only of normal recurring items, unless otherwise disclosed herein. Accordingly, the Unaudited Condensed Consolidated Financial Statements do not include all of the information and notes required by GAAP for complete consolidated financial statements. However, we believe that the disclosures made are adequate to make the information not misleading. These interim Unaudited Condensed Consolidated Financial Statements should be read in conjunction with our audited financial statements as of and for the year ended December 31, 2017 included in our Form 10-K. The results of operations for interim periods are not necessarily indicative of the results to be expected for a full year.

Use of Estimates in the Preparation of Financial Statements

The preparation of our Unaudited Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Actual results could differ from those estimates.

Significant Accounting Policies

Our significant accounting policies are consistent with those disclosed in Note 2 to our audited financial statements as of and for the year ended December 31, 2017 included in our Form 10-K, except for the adoption of Accounting Standards Update ("ASU") 2014-09 - *Revenue from Contracts with Customers* and ASU 2016-18 - *Statement of Cash Flows - Restricted Cash* on January 1, 2018. Under ASU 2014-09, an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Based on this new accounting guidance, our revenue is earned and recognized through the service offerings of our three reportable business segments. Our sales contracts have terms of less than one year. As such, we have used the practical expedient contained within the accounting guidance which exempts us from the requirement to disclose the transaction price allocated to remaining performance obligations if the performance obligation is part of a contract with an original expected duration of one year or less. See Note 10 for disaggregated revenue reported by segment. The adoption and application of this ASU had no effect on our Unaudited Condensed Consolidated Financial Statements, other than additional disclosures included in this Form 10-Q. Under ASU 2016-18, an entity is required to show changes in the total of cash, cash equivalents,

restricted cash, and restricted cash equivalents in the statement of cash flows. The adoption and application of this ASU has modified the presentation of cash, cash equivalents, restricted cash, and restricted cash equivalents on our Unaudited Condensed Consolidated Statements of Cash Flows applied on a retrospective basis.

CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

Accounts Receivable and Allowance for Bad Debts

We grant unsecured credit to customers under normal industry standards and terms, and have established policies and procedures that allow for an evaluation of each of our customer's creditworthiness. The Partnership determines allowances for bad debts based on management's assessment of the creditworthiness of our customers. Trade receivables are written off against the allowance when deemed uncollectible. Recoveries of trade receivables previously written off are recorded when cash is received. In the first quarter of 2017, we received $0.3 million on accounts receivable previously reserved, which we recorded as a reduction to *general and administrative expense* in our Unaudited Consolidated Statements of Operations.

Income Taxes

As a limited partnership, we generally are not subject to federal, state, or local income taxes. The tax on our net income is generally borne by the individual partners. Net income (loss) for financial statement purposes may differ significantly from taxable income (loss) of the partners as a result of differences between the tax basis and financial reporting basis of assets and liabilities and the taxable income allocation requirements under our partnership agreement. The aggregated difference in the basis of our net assets for financial and tax reporting purposes cannot be readily determined because information regarding each partner's tax attributes is not available to us.

The income of Tulsa Inspection Resources – Canada, ULC, our Canadian subsidiary, is taxable in Canada. Tulsa Inspection Resources – PUC, LLC, a subsidiary of our Pipeline Inspection segment that performs pipeline inspection services for utility customers, and Brown Integrity – PUC, LLC, a subsidiary in which we own a 51% membership interest, have elected to be taxed as corporations for U.S. federal income tax purposes, and therefore, these subsidiaries are subject to U.S. federal and state income tax. The amounts recognized as income tax expense (benefit), income taxes payable, and deferred tax assets / liabilities in our Unaudited Condensed Consolidated Financial Statements include the Canadian income taxes and U.S. federal and state income taxes referred to above in this paragraph, as well as partnership-level taxes levied by various states, which include, most notably, franchise taxes assessed by the state of Texas.

As a publicly-traded partnership, we are subject to a statutory requirement that 90% of our total gross income classify as "qualifying income" (as defined by the Internal Revenue Code, related Treasury Regulations, and Internal Revenue

Service pronouncements), determined on a calendar-year basis. If our qualifying income does not meet this statutory requirement, we could be taxed as a corporation for federal and state income tax purposes. Our income has met the statutory qualifying income requirement for each year since our initial public offering ("IPO").

Noncontrolling Interest

We own a 51% interest in Brown Integrity, LLC (“Brown”) and a 49% interest in CF Inspection Management, LLC (“CF Inspection”). The accounts of these subsidiaries are included in our Unaudited Condensed Consolidated Financial Statements. The portion of the net income (loss) of these entities that is attributable to outside owners is reported as *net income (loss) attributable to noncontrolling interests* in our Unaudited Condensed Consolidated Statements of Operations, and the portion of the net assets of these entities that is attributable to outside owners is reported as *noncontrolling interests* in our Unaudited Condensed Consolidated Balance Sheets.

Property and Equipment

Property and equipment consists of land, land and leasehold improvements, buildings, facilities, wells and related equipment, computer and office equipment, and vehicles. We record property and equipment at cost. Costs of renewals and improvements that substantially extend the useful lives of the assets are capitalized. Maintenance and repairs are expensed as incurred. We depreciate property and equipment on a straight-line basis over the estimated useful lives of the assets. Upon retirement or disposition of an asset, we remove the cost and related accumulated depreciation from the balance sheet and report the resulting gain or loss, if any, in the Unaudited Condensed Consolidated Statements of Operations.

CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

Identifiable Intangible Assets

Our intangible assets consist primarily of customer relationships, trade names, and our database of inspectors. We recorded these intangible assets as part of our accounting for the acquisitions of businesses, and we amortize these assets on a straight-line basis over their estimated useful lives, which typically range from 5 – 20 years.

We review our intangible assets for impairment whenever events or circumstances indicate that the asset group to which they relate may be impaired. To perform an impairment assessment, we first determine whether the cash flows expected to be generated from the asset group exceed the carrying value of the asset group. If such estimated cash flows do not exceed the carrying value of the asset group, we reduce the carrying values of the assets to their fair values and record a corresponding impairment loss.

Goodwill

Goodwill is not amortized, but is subject to an annual review for impairment on November 1 (or at other dates if events or changes in circumstances indicate that the carrying value of goodwill may be impaired) at a reporting unit level. The reporting units used to evaluate and measure goodwill for impairment are determined primarily from the manner in which the business that relates to the applicable goodwill is managed or operated. We have determined that our Pipeline Inspection, Integrity Services, and Water Services segments are the appropriate reporting units for testing goodwill impairment.

To perform a goodwill impairment assessment, we perform an analysis to assess whether it is more likely than not that the fair value of the reporting unit exceeds its carrying value. If we determine that it is more likely than not that the carrying value of the reporting unit exceeds its fair value, we reduce the carrying value of goodwill and record a corresponding impairment expense.

Impairments of Property and Equipment

We assess property and equipment for possible impairment whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. Such indicators include, among others, the nature of the asset, the projected future economic benefit of the asset, changes in regulatory and political environments, and historical and future cash flow and profitability measurements. If the carrying value of an asset exceeds the future undiscounted cash flows expected from the asset, we recognize an impairment charge for the excess of the carrying value of the asset over its estimated fair value. Determinations as to whether and how much an asset is impaired involve management estimates on highly uncertain matters such as future commodity prices, the effects of inflation on operating expenses, and the outlook for national or regional market supply and demand for the services we provide.

Accrued Payroll and Other

Accrued payroll and other on our Unaudited Condensed Consolidated Balance Sheets includes the following:

	June 30, 2018	December 31, 2017
	(in thousands)	
Accrued payroll	$9,276	$ 6,893
Customer deposits	1,451	1,510
Other	436	706
	$11,163	$ 9,109

Foreign Currency Translation

Our Unaudited Condensed Consolidated Financial Statements are reported in U.S. dollars. We translate our Canadian-dollar-denominated assets and liabilities into U.S. dollars at the exchange rate in effect at the balance sheet date. We translate our Canadian-dollar-denominated revenues and expenses into U.S. dollars at the average exchange rate in effect during the period in which the applicable revenues and expenses were recorded.

CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

Our Unaudited Condensed Consolidated Balance Sheet at June 30, 2018 includes $2.5 million of *accumulated other comprehensive loss* associated with accumulated currency translation adjustments, all of which relate to our Canadian operations. If at some point in the future we were to sell or substantially liquidate our Canadian operations, we would reclassify the balance in *accumulated other comprehensive loss* to other accounts within *partners' capital*, which would be reported in the Unaudited Condensed Consolidated Statement of Operations as a reduction to net income.

Our Canadian subsidiary has certain intercompany payables to our U.S.-based subsidiaries. These intercompany payables and receivables among our consolidated subsidiaries are eliminated in our Unaudited Condensed Consolidated Balance Sheets. Beginning April 1, 2017, we report currency translation adjustments on these intercompany payables and receivables within *foreign currency gains (losses)* in our Unaudited Condensed Consolidated Statements of Operations, with offsetting amounts reported within *other comprehensive income (loss)* in our Unaudited Condensed Consolidated Statements of Comprehensive Income (Loss).

New Accounting Standards

On January 1, 2018, we adopted the following new accounting standards issued by the Financial Accounting Standards Board ("FASB");

The FASB issued Accounting Standards Update ("ASU") 2014-09 – *Revenue from Contracts with Customers* in May 2014. ASU 2014-09 is intended to clarify the principles for recognizing revenue and to develop a common standard for recognizing revenue for GAAP and International Financial Reporting Standards that is applicable to all organizations. This guidance requires an entity to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration the entity expects to receive in exchange for those goods and services. It also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. We adopted this new standard utilizing the modified retrospective transition approach. The adoption of this ASU had no effect on our Unaudited Condensed Consolidated Financial Statements other than additional disclosures included in the Form 10-Q.

The FASB issued ASU 2016-18 - *Statement of Cash Flows - Restricted Cash* in November 2016. This ASU requires entities to show the changes in the total of cash, cash equivalents, restricted cash, and restricted cash equivalents in the

statement of cash flows on a retrospective basis. The requirements of this ASU have been reflected in our Unaudited Condensed Consolidated Statements of Cash Flows for all periods presented.

Other accounting guidance proposed by the FASB that may impact our Unaudited Condensed Consolidated Financial Statements, which we have not yet adopted includes:

The FASB issued ASU 2016-02 – *Leases* in February 2016 and has issued subsequent standard setting guidance related to the implementation of this ASU. This guidance attempts to increase transparency and comparability among organizations by recognizing certain lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The main difference between previous GAAP methodology and the method proposed by this new guidance is the recognition on the balance sheet of certain lease assets and lease liabilities by lessees for those leases that were classified as operating leases under previous GAAP. Entities are required to adopt this ASU using a modified retrospective approach, subject to certain optional practical expedients, and apply its provisions to leasing arrangement existing at or entered into after the earliest comparative period presented in the financial statements. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. We are currently evaluating the impact this ASU will have on our Unaudited Condensed Consolidated Balance Sheets.

CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

3. Impairments

During the three months ended March 31, 2017, the largest customer of TIR-Canada, the Canadian subsidiary of our Pipeline Inspection segment, completed a bid process and selected different service providers for its inspection projects. During the six months ended June 30, 2017, pipeline inspection services to this customer accounted for approximately $18.8 million of revenue and $1.3 million of gross margin, which represented approximately 89% of the revenues and 94% of the gross margin of our Canadian operations (and approximately 14% of our consolidated revenues and 9% of our consolidated gross margin for the six months ended June 30, 2017). In consideration of the loss of this contract, we recorded impairments to the carrying values of certain intangible assets of $1.3 million during the three months ended March 31, 2017. Of this amount, $1.1 million related to customer relationships and $0.2 million related to trade names. We continue to perform inspection and integrity work for customers in Canada.

During the three months ended March 31, 2017, we recorded an impairment to the remaining $1.6 million carrying value of the goodwill of our Integrity Services segment. Revenues of this segment were lower than we had expected for the first quarter of 2017. In addition, for this segment, the level of bidding activity for work is typically high in March and April once customers have finalized their budgets for the upcoming year. While we won bids on a number of projects, and our backlog began to improve, the improvement in the backlog was slower than we had originally anticipated and we revised downward our expectations of the near-term operating results of the segment. We estimated the fair value of the Integrity Services segment utilizing the income approach (discounted cash flows valuation method), which is a Level 3 input as defined in ASC 820 – *Fair Value Measurement*. Significant inputs in the valuation included projections of future revenue, anticipated operating costs and appropriate discount rates. Significant assumptions included a 2% annual growth rate of cash flows and a discount rate of 18%. We determined through this analysis that the fair value of goodwill of the Integrity Services segment was fully impaired. These calculations represent Level 3 non-recurring fair value measurement.

During the three months ended March 31, 2017, we recorded an impairment of $0.7 million to the property and equipment at one of our saltwater disposal facilities. We have experienced low volumes at his facility due to competition in the area and to low levels of exploration and production activity near the facility. The impairment reduced the carrying value of the facility to $0.1 million, all of which is attributable to land.

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Notes to the Unaudited Condensed Consolidated Financial Statements

4. Credit Agreement

On May 29, 2018, we entered into an amended and restated credit agreement (as amended and restated, the "Credit Agreement") that provides up to $90.0 million in borrowing capacity, subject to certain limitations, and contains an accordion feature that allows us to increase the borrowing capacity to $110.0 million if the lenders agree to increase their commitments in the future or if other lenders join the facility. The Credit Agreement matures May 29, 2021. The obligations under the Credit Agreement are secured by a first priority lien on substantially all of our assets. The credit agreement as it existed prior to the May 29, 2018 amendment will hereinafter be referred to as the "Previous Credit Agreement" or, together with the Credit Agreement, as the "Credit Agreements".

Outstanding borrowings at June 30, 2018 were $76.1 million and are reflected as *long-term debt* on the Unaudited Condensed Consolidated Balance Sheets beginning May 29, 2018. Debt issuance costs are reported as *debt issuance costs, net* on the Unaudited Condensed Consolidated Balance Sheets and total $1.5 million at June 30, 2018. Outstanding borrowings at December 31, 2017 were $136.9 million and are reflected net of debt issuance costs of $0.6 million as *current portion of long-term debt* on the Unaudited Condensed Consolidated Balance Sheet. The carrying value of the partnership's long-term debt approximates fair value as the borrowings under the Credit Agreement are considered to be priced at market for debt instruments having similar terms and conditions (Level 2 of the fair value hierarchy).

We incurred certain debt issuance costs associated with the Previous Credit Agreement, which we were amortizing on a straight-line basis over the life of the Previous Credit Agreement. Upon amending the Credit Agreement in May 2018, we wrote off $0.1 million of these debt issuance costs and reported this expense within *debt issuance cost write-off* in our Unaudited Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2018, which represented the portion of the unamortized debt issuance costs attributable to lenders who are no longer participating in the credit facility subsequent to the amendment. The remaining debt issuance costs associated with the Previous Credit Agreement, along with $1.3 million of debt issuance costs associated with the amended and restated Credit Agreement, are being amortized on a straight-line basis over the three-year term of the Credit Agreement.

All borrowings under the Credit Agreement bear interest, at our option, on a leveraged based grid pricing at (i) a base rate plus a margin of 1.5% to 3.0% per annum ("Base Rate Borrowing") or (ii) an adjusted LIBOR rate plus a margin of 2.5% to 4.0% per annum ("LIBOR Borrowings"). The applicable margin is determined based on the leverage ratio of the Partnership, as defined in the Credit Agreement. Generally, the interest rate on our borrowings ranged between 4.74%

and 5.95% for the six months ended June 30, 2018 and 3.90% and 4.97% for the six months ended June 30, 2017. Interest on Base Rate Borrowings is payable monthly. Interest on LIBOR Borrowings is paid upon maturity of the underlying LIBOR contract, but no less often than quarterly. Commitment fees are charged at a rate of 0.50% on any unused credit and are payable quarterly. Interest paid during the three months ended June 30, 2018 and 2017 was $1.7 million, including commitment fees. Interest paid during the six months ended June 30, 2018 and 2017 was $3.5 million and $3.3 million, respectively, including commitment fees.

The Credit Agreement contains various customary covenants and restrictive provisions. The Credit Agreement also requires maintenance of certain financial covenants, including a leverage ratio (as defined in the Credit Agreement) of not more than 4.0 to 1.0 and an interest coverage ratio (as defined in the Credit Agreement) of not less than 3.0 to 1.0. At June 30, 2018, our leverage ratio was 3.58 to 1.0 and our interest coverage ratio was 4.99 to 1.0, pursuant to the Credit Agreement. Upon the occurrence and during the continuation of an event of default, subject to the terms and conditions of the Credit Agreement, the lenders may declare any outstanding principal, together with any accrued and unpaid interest, to be immediately due and payable and may exercise the other remedies set forth or referred to in the Credit Agreement. We were in compliance with all debt covenants as of June 30, 2018.

In addition, the Credit Agreement restricts our ability to make distributions on, or redeem or repurchase, our equity interests, with certain exceptions detailed in the Credit Agreement. However, we may make distributions of available cash so long as, both at the time of the distribution and after giving effect to the distribution, no default exists under the Credit Agreement, we are in compliance with the financial covenants in the Credit Agreement, and we have at least $5.0 million of unused capacity on the Credit Agreement at the time of the distribution.

CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

5. Income Taxes

The *income tax expense (benefit)* reported in our Unaudited Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2018 and 2017 differs from the statutory tax rate of 21% in 2018 and 35% in 2017 due to the fact that, as a partnership, we are generally not subject to U.S. federal or state income taxes. Our income tax provision relates primarily to our corporate subsidiaries that service public utility customers, which are subject to U.S. federal and state income taxes, our Canadian subsidiary, which is subject to Canadian federal and provincial income taxes, and to certain other state income taxes, including the Texas franchise tax.

6. Equity

Series A Preferred Units

On May 29, 2018 (the "Closing Date"), we entered into a Series A Preferred Unit Purchase Agreement (the "Preferred Unit Purchase Agreement") with Stephenson Equity, Co. No. 3 (the "Purchaser"), an affiliate of our General Partner, where we issued and sold in a private placement 5,769,231 Series A Preferred Units representing limited partner interests in the Partnership (the "Preferred Units") to the Purchaser for a cash purchase price of $7.54 per Preferred Unit, resulting in proceeds to the Partnership of $43.5 million. We used proceeds from the transaction to reduce outstanding borrowings on our revolving credit facility. Concurrent with the closing of this transaction, we entered into an Amended and Restated Credit Agreement dated as of May 29, 2018, to amend and restate the terms of our credit facility, as more fully described in Note 4.

The Preferred Unit Purchase Agreement also provides us with the right to exercise an option at any time during the six months after the Closing Date, to issue and sell to the Purchaser up to $6.5 million of additional Preferred Units. The Preferred Unit Purchase Agreement sets forth the method of determining the purchase price of these additional units, which price will in turn determine the number of units to be issued and sold.

The Preferred Unit Purchase Agreement contains customary representations, warranties, and covenants of the Partnership and the Purchaser. The Partnership and the Purchaser agreed to indemnify each other and their respective

officers, directors, managers, employees, agents, counsel, accountants, investment bankers, and other representatives against certain losses resulting from breaches of their respective representations, warranties, and covenants, subject to certain negotiated limitations and survival periods set forth in the Preferred Unit Purchase Agreement.

Pursuant to the Preferred Unit Purchase Agreement, and in connection with the closing of this transaction, our General Partner executed the First Amendment to First Amended and Restated Agreement of Limited Partnership of the Partnership, which authorizes and establishes the rights and preferences of the Preferred Units. The Preferred Units shall have voting rights that are identical to the voting rights of the common units into which such Preferred Units would be converted at the then-applicable conversion rate.

The Purchaser is entitled to receive quarterly distributions that represent an annual return of 9.5% on the Preferred Units. Of this 9.5% annual return, we will be required to pay at least 2.5% in cash and will have the option to pay the remaining 7.0% in kind (in the form of issuing additional preferred units) for the first twelve quarters after the Closing Date.

After the third anniversary of the Closing Date, the Purchaser will have the option to convert the Preferred Units into common units on a one-for-one basis. If certain conditions are met after the third anniversary of the Closing Date, we will have the option to cause the Preferred Units to convert to common units. After the third anniversary of the Closing Date, we will also have the option to redeem the Preferred Units. The Partnership may redeem the Preferred Units (a) before November 29, 2018 at a redemption price equal to 100% of the issue price (plus $0.2 million), (b) at any time after the third anniversary of the closing date and on or prior to the fourth anniversary of the closing date at a redemption price equal to 105% of the issue price, and (c) at any time after the fourth anniversary of the closing date at a redemption price equal to 101% of the issue price.

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Notes to the Unaudited Condensed Consolidated Financial Statements

Earnings Per Unit

Our *net income (loss)* is attributable and allocable to four ownership groups: (1) our preferred unitholder, (2) the noncontrolling interests in certain subsidiaries, (3) our General Partner, and (4) our common unitholders. Income attributable to our preferred unitholder represents the 9.5% annual return to which the owner of the Preferred Units is entitled. Income (loss) attributable to noncontrolling interests represent 49% of the income (loss) generated by Brown and 51% of the income (loss) generated by CF Inspection. Losses attributable to the General Partner include expenses incurred by Holdings and not charged to us. Income (loss) attributable to common units represents our remaining net income (loss), after consideration of amounts attributable to our preferred unitholder, the noncontrolling interests, and our General Partner. In February 2017, all of the then-outstanding subordinated units converted into common units. Since the subordinated units did not share in the distribution of cash generated subsequent to December 31, 2016, we did not allocate any income or loss after that date to the subordinated units.

Basic net income (loss) per common limited partner unit is calculated as *net income (loss) attributable to common unitholders* divided by the basic weighted average common units outstanding. *Diluted net income (loss) per common limited partner unit* includes the *net income attributable to preferred unitholder* and the dilutive effect of the potential conversion of the preferred units and the dilutive effect of the unvested equity compensation. The following summarizes the calculation of the *basic net income (loss) per common limited partner unit* for the three and six months ended June 30, 2018 and 2017:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
	(in thousands, except per unit data)			
Net income (loss) attributable to common unitholders	$3,040	$1,459	$3,765	$(1,376)
Weighted average common units outstanding	11,933	11,880	11,916	10,404
Basic net income (loss) per common limited partner unit	$0.25	$0.12	$0.32	$(0.13)

The following summarizes the calculation of the *diluted net income (loss) per common limited partner unit* for the three and six months ended June 30, 2018 and 2017:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
	(in thousands, except per unit data)			
Net income (loss) attributable to common unitholders	$3,040	$1,459	$3,765	$(1,376)
Net income attributable to preferred unitholder	367	—	367	—
Net income (loss) attributable to limited partners	$3,407	$1,459	$4,132	$(1,376)
Weighted average common units outstanding	11,933	11,880	11,916	10,404
Effect of dilutive securities				
Weighted average preferred units outstanding	2,029	—	1,020	—
Long-term incentive plan unvested units	336	122	388	—
Diluted weighted average common units outstanding	14,298	12,002	13,324	10,404
Diluted net income (loss) per common limited partner unit	$0.24	$0.12	$0.31	$(0.13)

For the six months ended June 30, 2017, we experienced a *net loss attributable to common unitholders*. The unvested equity compensation awards would have been antidilutive and, therefore, were not included in the computation of *diluted net loss per common limited partner unit*.

CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

Cash Distributions

The following table summarizes the cash distributions declared and paid to our limited partners since our IPO.

Payment Date	Per Unit Cash Distributions	Total Cash Distributions	Total Cash Distributions to Affiliates (a)
		(in thousands)	
Total 2014 Distributions	1.104646	13,064	8,296
Total 2015 Distributions	1.625652	19,232	12,284
Total 2016 Distributions	1.625652	19,258	12,414
February 13, 2017	0.406413	4,823	3,107
May 13, 2017	0.210000	2,495	1,606
August 12, 2017	0.210000	2,495	1,607
November 14, 2017	0.210000	2,497	1,608
Total 2017 Distributions	1.036413	12,310	7,928
February 14, 2018	0.210000	2,498	1,599
May 15, 2018	0.210000	2,506	1,604
August 14, 2018 (b)	0.210000	2,506	1,604
Total 2018 Distributions (through August 14, 2018)	0.630000	7,510	4,807
Total Distributions (through August 14, 2018 since IPO)	$ 6.022363	$71,374	$ 45,729

(a) Approximately 64.0% of the Partnership’s outstanding common units at June 30, 2018 were held by affiliates.

(b) Second quarter 2018 distribution was declared and will be paid in the third quarter of 2018.

CYPRESS ENERGY PARTNERS, L.P.
Notes to the Unaudited Condensed Consolidated Financial Statements

Equity Compensation

Our General Partner has adopted a long-term incentive plan (“LTIP”) that authorizes the issuance of up to 1,182,600 common units. Certain directors and employees of the Partnership have been awarded Phantom Restricted Units under the terms of the LTIP. The fair value of the awards is determined based on the quoted market value of the publicly-traded common units at each grant date, adjusted for a discount to reflect the fact that distributions are not paid on the restricted units during the vesting period. Compensation expense is recorded on a straight-line basis over the vesting period of each grant. We recorded expense of $0.5 million and $0.8 million during the six months ended June 30, 2018 and 2017, respectively, related to the unit awards.

The following table summarizes the LTIP unit activity for the six months ended June 30, 2018 and 2017:

	Six Months Ended June 30,			
	2018		**2017**	
	Number of Units	Weighted Average Grant Date Fair Value / Unit	Number of Units	Weighted Average Grant Date Fair Value / Unit
Unvested units at January 1	664,509	$ 8.46	573,902	$ 9.86
Unvested units granted	396,484	$ 3.24	246,200	$ 7.15
Units vested	(54,763)	$ 13.18	(30,657)	$ 15.99
Unvested units forfeited	(43,383)	$ 5.82	(21,802)	$ 8.21
Unvested units at June 30	962,847	$ 6.16	767,643	$ 8.79

The majority of the awards vest in three tranches, with one-third of the units vesting three years from the grant date, one-third vesting four years from the grant date, and one-third vesting five years from the grant date. However, certain of the awards have different, and typically shorter, vesting periods. Two of the grants, which total 77,495 units, vest three years from the grant date, contingent upon the recipient meeting certain performance targets. Total unearned compensation associated with the LTIP was $3.6 million at June 30, 2018, and the awards had an average remaining life of 2.41 years.

CYPRESS ENERGY PARTNERS, L.P.

Notes to the Unaudited Condensed Consolidated Financial Statements

7. Related-Party Transactions

Omnibus Agreement and Other Support from Holdings

We are party to an omnibus agreement with Holdings and other related parties. The omnibus agreement governs the following matters, among other things:

- our payment of a quarterly administrative fee in the amount of $1.0 million to Holdings for providing certain partnership overhead services, including certain executive management services by certain officers and employees of our General Partner. This fee also includes the incremental general and administrative expenses we incur as a result of being a publicly-traded partnership. For the three and six months ended June 30, 2017, Holdings provided sponsor support to us by waiving payment of the quarterly administrative fee;

- our right of first offer on Holdings' and its subsidiaries' assets used in, and entities primarily engaged in, providing saltwater disposal and other water and environmental services; and

- indemnification of us by Holdings for certain environmental and other liabilities, including events and conditions associated with the operation of assets that occurred prior to the closing of the IPO and our obligation to indemnify Holdings for events and conditions associated with the operation of our assets that occur after the closing of the IPO and for environmental liabilities related to our assets to the extent Holdings is not required to indemnify us.

So long as affiliates of Holdings control our General Partner, the omnibus agreement will remain in effect, unless we and Holdings agree to terminate it sooner. If affiliates of Holdings cease to control our General Partner, either party may terminate the omnibus agreement, provided that the indemnification obligations will remain in full force and effect in accordance with their terms. We and Holdings may agree to amend the omnibus agreement; however, amendments will also require the approval of the Conflicts Committee of our Board of Directors. As part of our new Credit Agreement, Holdings agreed to waive the omnibus fee to support us in the event our leverage ratio were to exceed 3.75 times our trailing twelve-month Adjusted EBITDA at any quarter-end during the term of the credit facility.

Holdings incurred expenses of $0.8 million and $1.8 million on our behalf during the three and six months ended June 30, 2017, respectively. These expenses are reported within *general and administrative* and within *net loss attributable to general partner* in the accompanying Unaudited Condensed Consolidated Statements of Operations.

Alati Arnegard, LLC

We provide management services to Alati Arnegard, LLC ("Arnegard"), an entity in which we hold a 25% membership interest. Management fee revenue earned from Arnegard totaled $0.2 million and $0.1 million for the three months ended June 30, 2018 and 2017, respectively, and $0.3 million for the six months ended June 30, 2018 and 2017. Accounts receivable from Arnegard were $0.1 million at June 30, 2018 and December 31, 2017, and are included in *trade accounts receivable, net* in the Unaudited Condensed Consolidated Balance Sheets.

CF Inspection Management, LLC

We have also entered into a joint venture with CF Inspection, a nationally-qualified woman-owned inspection firm affiliated with one of Holdings' owners. We own 49% of CF Inspection and Cynthia A. Field, the daughter of Charles C. Stephenson, Jr., owns the remaining 51% of CF Inspection. For the six months ended June 30, 2018, CF Inspection represented approximately 3.2% of our consolidated revenue.

Sale of Preferred Equity

As described in Note 6, we issued and sold $43.5 million of preferred equity to an affiliate in May 2018.

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Notes to the Unaudited Condensed Consolidated Financial Statements

8. Commitments and Contingencies

Security Deposits

We have various performance obligations which are secured with short-term security deposits (reflected as restricted cash equivalents on our Unaudited Condensed Consolidated Statements of Cash Flows) of $0.6 million and $0.5 million at June 30, 2018 and December 31, 2017, respectively, included in *prepaid expenses and other* on the Unaudited Condensed Consolidated Balance Sheets.

Employment Contract Commitments

We have an employment agreement with a certain member of management. This agreement provides for minimum annual compensation for specified terms, after which employment will continue on an “at will” basis. The agreement provides for severance payments in the event of specified termination of employment. At June 30, 2018, the aggregate commitment for future compensation and severance was approximately $0.5 million.

Compliance Audit Contingencies

Certain customer master service agreements (“MSA’s”) offer our customers the opportunity to perform periodic compliance audits, which include the examination of the accuracy of our invoices. Should our invoices be determined to be inconsistent with the MSA, the MSA’s may provide the customer the right to receive a credit or refund for any overcharges identified. As of June 30, 2018 and December 31, 2017, there have been no reserves established for compliance audit contingencies.

Legal Proceedings

From time to time, we are subject to legal proceedings and claims that arise in the ordinary course of business. Currently, we are not a party to any material pending or overly threatened legal or governmental proceedings, other than proceedings and claims that arise in the ordinary course and are incidental to our business.

9. Sale of Saltwater Disposal Facilities

In May 2018, we sold our subsidiary Cypress Energy Partners – Orla SWD, LLC ("Orla"), which owns a saltwater disposal facility in Monahans, Texas, to an unrelated party for $8.0 million of cash proceeds. We recorded a gain on this transaction of $1.6 million, which represents the excess of the cash proceeds over the net book value of assets sold. The net book value of the assets sold included $3.0 million of allocated goodwill, calculated based on the estimated fair value of the Orla facility relative to the estimated fair value of the Water Services reporting unit as a whole. This calculation is considered Level 3 and the fair values included in this calculation were determined utilizing discounted cash flows of the Orla facility and the Water Services reporting unit as a whole as of the date of sale.

In January 2018, we sold our subsidiary Cypress Energy Partners – Pecos SWD, LLC ("Pecos"), which owns a saltwater disposal facility in Pecos, Texas, to an unrelated party for $4.0 million of cash proceeds and a royalty interest in the future revenues of the facility. We concluded this represented the sale of a business and we will record the royalties in the periods in which they are received. We recorded a gain on this transaction of $1.8 million, which represents the excess of the cash proceeds over the net book value of assets sold. The net book value of the assets sold included $2.0 million of allocated goodwill, calculated based on the estimated fair value of the Pecos facility relative to the estimated fair value of the Water Services reporting unit as a whole. This calculation is considered Level 3 and the fair values included in this calculation were determined utilizing discounted cash flows of the Pecos facility and the Water Services reporting unit as a whole as of the date of sale. *Assets held for sale* and *liabilities held for sale* on the Unaudited Condensed Consolidated Balance Sheet at December 31, 2017 represent the carrying values of the Pecos saltwater facility prior to its sale.

These gains, net of $0.1 million of charges related to the abandonment of a capital expansion project, are reported within *gain on asset disposals, net* on the Unaudited Condensed Consolidated Statements of Operations. We used the cash proceeds from these sales to repay $12.0 million of outstanding borrowings under our revolving credit facility.