

QUALITY DISTRIBUTION INC

Form 10-Q

May 14, 2002

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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 MARCH 31, 2002

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: 0-24180

Quality Distribution, Inc.

(Exact name of registrant as specified in its charter)

Florida

59-3239073

(State or other jurisdiction of incorporation  
or organization)

(I.R.S. Employer  
Identification No.)

3802 Corporex Park Drive, Tampa, FL

33619

(Address of Principal Executive Offices)

(Zip Code)

(Former name, former address and former fiscal year, if changed since last report)

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY  
PROCEEDINGS DURING THE PRECEDING FIVE YEARS

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Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.  Yes  No

### APPLICABLE ONLY TO CORPORATE USERS:

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

Class	Outstanding at MARCH 31, 2002
(Common Stock, \$.01 par value)	1,991,726

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Signatures

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 QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (In thousands)

	<b>March 31, 2002 (Unaudited)</b>	<b>December 31, 2001 *</b>
<b>ASSETS</b>		
Current Assets:		
Cash	\$ 1,887	\$ 2,212
Accounts receivable	100,356	98,173
Allowance for doubtful accounts	(9,486)	(9,272)
Inventories	1,075	1,143
Prepaid expenses	6,425	5,767
Prepaid tires	8,806	8,968
Income tax receivable	6	306
Other	2,393	2,666
Total current assets	111,462	109,963
Property, plant and equipment	348,359	348,687
Less accumulated depreciation and amortization	(177,295)	(171,328)
	171,064	177,359
Goodwill, net	150,510	150,510
Intangibles	2,089	2,265
Other Assets	8,335	8,881
	\$ 443,460	\$ 448,978

\* Condensed from audited financial statements

The accompanying notes are an integral part of these condensed consolidated financial statements.

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ITEM 1 FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(In thousands)  
(continued)

	March 31, 2002 (Unaudited)	December 31, 2001 *
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current Liabilities:		
Current maturities of indebtedness	\$ 2,679	\$ 2,677
Accounts payable and accrued expenses	61,945	62,848
Affiliates and owner operators payable	7,125	4,930
Income taxes payable	1,077	1,092
<b>Total current liabilities</b>	<b>72,826</b>	<b>71,547</b>
Long term bank debt, less current maturities	299,011	301,179
Subordinated debt	140,000	140,000
Environmental liabilities	34,874	36,163
Other long term obligations	12,930	13,744
Deferred tax	1,198	1,270
<b>Total liabilities</b>	<b>560,839</b>	<b>563,903</b>
Minority interest in subsidiary	1,833	1,833
Manditorily redeemable preferred stock	17,065	16,499
Manditorily redeemable common stock (30 shares)	1,210	1,210
Stockholders (deficit):		
Common stock, \$.01 par value; 15,000 shares authorized	20	20
Additional paid-in-capital	105,544	105,544
Treasury stock	(628)	(402)
Accumulated (deficit)	(41,082)	(37,435)
Stock recapitalization	(189,589)	(189,589)
Accumulated other comprehensive (loss)	(9,976)	(10,829)
Notes receivable	(1,776)	(1,776)
<b>Total stockholders (deficit)</b>	<b>(137,487)</b>	<b>(134,467)</b>
	<b>\$ 443,460</b>	<b>\$ 448,978</b>

\* Condensed from audited financial statements.

The accompanying notes are an integral part of these condensed consolidated financial statements.

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## FORM 10-Q

ITEM 1 FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)  
(In thousands, except per share data)

	Three months ended March 31,	
	2002	2001
<b>Operating Revenues:</b>		
Transportation	\$ 104,734	\$ 115,076
Other	20,192	15,727
	124,926	130,803
<b>Operating Expenses:</b>		
Purchased transportation	71,116	74,217
Depreciation and amortization	8,113	8,648
Other operating expenses	38,610	39,180
	7,087	8,758
Operating income	7,087	8,758
Interest expense, net	9,907	9,441
Other income (expense)	(36)	13
	(2,856)	(670)
Loss before taxes	(2,856)	(670)
Benefit (provision) for income taxes	(189)	(360)
	(3,045)	(1,030)
Net loss	(3,045)	(1,030)
Preferred stock dividends and accretions	(602)	(397)
	\$ (3,647)	\$ (1,427)
Net loss attributable to common stockholders	\$ (3,647)	\$ (1,427)
<b>Per Share Data:</b>		
Basic and diluted loss per common share	\$ (1.83)	\$ (.71)
	1,996	2,021
Weighted average number of common shares outstanding-basic and diluted	1,996	2,021

The accompanying notes are an integral part of these condensed consolidated financial statements.



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FORM 10-Q  
ITEM 1 FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited) - (In thousands)

	Three months ended March 31,	
	2002	2001
Cash flows provided by (used in)		
Operating activities:		
Net loss	\$(3,045)	\$(1,030)
Adjustments for non cash charges	8,985	9,420
Changes in assets and liabilities	(2,028)	946
	3,912	9,336
Investing activities:		
Capital expenditures	(2,939)	(6,619)
Proceeds from asset dispositions	1,008	1,122
	(1,931)	(5,497)
Financing activities:		
Payment of debt obligation	(2,169)	(1,251)
Preferred stock redemption		(2,600)
Other	(263)	275
	(2,432)	(3,576)
Net increase (decrease) in cash	(451)	263
Effect of exchange rate changes on cash	126	(583)
Cash, beginning of period	2,212	2,636
	\$ 1,887	\$ 2,316
Supplemental disclosures of cash flow information:		
Cash payments for:		
Interest	\$ 6,550	\$ 6,315
Income taxes	\$ 73	\$ 208
Supplemental disclosures of Non-cash activities:		
Preferred Stock Accretion	\$ 566	\$ 361
Unrealized gain or (loss) on derivative instruments	\$ (142)	(903)

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FORM 10-Q  
Item 1. FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of Presentation

The accompanying unaudited condensed, consolidated financial statements of Quality Distribution, Inc. (the Company) have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments and accruals) considered necessary for a fair presentation have been included. Certain reclassifications have been made in the fiscal 2001 statements to conform to the 2002 presentation.

For further information, refer to the consolidated financial statements and notes thereto for the year ended December 31, 2001 included in the Company's annual report on Form 10-K which was filed March 29, 2002.

Operating results for the first quarter ended March 31, 2002 are not necessarily indicative of the results that may be expected for the entire fiscal year.

2. LIQUIDITY:

Our credit agreements include financial covenants which were modified December 14, 2001 as part of an amendment (the Fourth Amendment) thereto. The new financial covenants are less restrictive than the original covenants and remain in effect for four consecutive calendar quarters ending December 31, 2002. Our credit agreement includes financial covenants which require minimum or maximum ratios to be maintained. The financial covenants in the Fourth Amendment are less restrictive than the previously existing covenants and cover the calendar quarters through December 31, 2002. The Company currently believes that it will be in compliance with the covenants through December 31, 2002. In addition, the Fourth Amendment restricts the future availability of the revolving credit facility to an incremental \$15 million above the balance at the date of the agreement, plus places restrictions on the amount of capital expenditures allowed.

On April 5, 2002, we entered into a fifth amendment (the Fifth Amendment) to our credit agreement. The Fifth Amendment will further amend the financial covenants through the date of the final maturity of our credit agreement. Such revised covenants will be less restrictive than the previously existing covenants for the period beginning March 31, 2003 through final maturity of our credit agreement. The revised covenants in the Fifth Amendment will only become effective if we are able to satisfy certain conditions. If the Debt/Equity Exchange is consummated as a result of the Exchange Offer, then the conditions to effectiveness will be satisfied. There can be no assurance that the amendments to the financial covenants in the Fifth Amendment will become effective, or that if they do, that we will be able to comply with such revised financial covenants. (See note 7 Subsequent Events for a discussion of the Exchange Offer).

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## 3. COMPREHENSIVE INCOME:

Comprehensive Income is as follows: (dollars in thousands)

	Three Months Ended March 31,	
	2002	2001
Net loss	\$ (3,045)	\$ (1,030)
Other comprehensive income (loss):		
Foreign currency translation adjustments	(79)	(421)
Unrealized gain or (loss) on derivative instruments	933	(903)
Comprehensive loss	\$ (2,191)	\$ (2,354)

## 4. DERIVATIVES:

The Company utilizes derivative financial instruments to reduce its exposure to market risks from changes in interest rates and foreign exchange rates. The instruments primarily used to mitigate these risks are interest rate swaps and foreign exchange contracts. The Company is exposed to credit related losses in the event of nonperformance by counterparties to these financial instruments; however, counterparties to these agreements are major financial institutions; and the risk of loss due to nonperformance is considered by management to be minimal. The Company does not hold nor issue interest rate swaps or foreign exchange contracts for trading purposes.

The Financial Accounting Standards Board ( FASB ) issued, then subsequently amended, Statement of Financial Accounting Standards ( SFAS ) No. 133, Accounting for Derivative Instruments and Hedging Activities, which became effective for the Company on January 1, 2001. Under SFAS No. 133, as amended, all derivative instruments (including certain derivative instruments embedded in other contracts) are recognized in the balance sheet at their fair values and changes in fair value are recognized immediately in earnings, unless the derivatives qualify as hedges of future cash flows. For derivatives qualifying as hedges of future cash flows, the effective portion of changes in fair value is recorded temporarily in equity, then recognized in earnings along with the related effects of the hedged items. Any ineffective portion of a hedge is reported in earnings as it occurs.

The Company has approximately \$344 million and \$341.7 million of variable interest debt at December 31, 2001 and March 31, 2002, respectively. The Company has entered into interest rate swap agreements designated as a partial hedge of its variable rate debt. The purpose of these swaps is to fix interest rates on variable rate debt and reduce certain exposures to interest rate fluctuations.

The notional amounts of \$160 million at December 31, 2001 and March 31, 2002 do not represent a measure of exposure of the Company. The Company will pay counterparties interest at a fixed rate ranging from 4.765% to 5.155%, and the counterparties will pay the Company interest at a variable rate equal to LIBOR. The LIBOR rate applicable to these agreements at December 31, 2001 and March 31, 2002 was 1.90% and 2.03%, respectively. These agreements mature and renew every three months and expire at dates ranging from July 2, 2002 to September 22, 2002. A 10% fluctuation in interest rates would have a \$1.3 million impact, net of interest rate swap agreements, on future earnings on an annual basis.

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The nature of the Company's business activities necessarily involves the management of various financial and market risks, including those related to changes in interest rates and currency exchange rates. The Company uses derivative financial instruments to mitigate or eliminate certain of those risks. The January 1, 2001 accounting changes described above affected only the pattern and the timing of the non-cash accounting recognition.

A reconciliation of current period changes in the component of accumulated other comprehensive loss as it relates to derivatives is as follows:

	<b>Three Months Ended</b>	
	<b>March 31, 2002</b>	<b>March 31, 2001</b>
<b>(In thousands)</b>		
Balance beginning of period	\$(3,346)	\$ 337
Current period declines in fair value	(142)	(1,444)
Reclassifications to earnings	1,075	204
Balance at end of period	<u>\$(2,413)</u>	<u>\$ (903)</u>

Additional disclosures required by SFAS No. 133, as amended, are provided in the following paragraphs.

**Hedges of Future Cash Flows**

Per SFAS 133, the ineffective portion of changes in fair values of hedge positions should be reported in earnings. All hedges were effective at March 31, 2002, and as such, there are no earnings reclassifications at March 31, 2002 or 2001, due to ineffective hedges. There were no amounts excluded from the measure of effectiveness related to the hedge of future cash flows.

For the three months ended March 31, 2002 and 2001, \$1.1 million and \$.2 million, respectively, was reclassified to earnings as interest expense. The \$(2.4) million recorded in accumulated other comprehensive loss at March 31, 2002 is expected to be reclassified to future earnings, contemporaneously with and primarily offsetting changes in interest expenses on floating-rate instruments. The actual amounts that will be reclassified to earnings will vary from this amount as a result of changes in market conditions.

**5. ENVIRONMENTAL MATTERS:**

Our activities involve the handling, transportation, storage and disposal of bulk liquid chemicals, many of which are classified as hazardous materials, hazardous substances, or hazardous waste. Our tank wash and terminal operations engage in the storage or discharge of wastewater and storm-water that may have contained hazardous substances, and from time to time we store diesel fuel and other petroleum products at our terminals. As such, we are subject to environmental, health and safety laws and regulation by U.S. federal, state, local and Canadian government authorities. Environmental laws and regulations are complex, change frequently and have tended to become more stringent over time. There can be no assurance that violations of such laws or regulations will not be identified or occur in the future, or that such laws and regulations will not change in a manner that could impose material costs to us.

Facility managers are responsible for environmental compliance. Self-audits along with audits conducted by our internal audit staff are required to assess operations, safety training and procedures, equipment and grounds maintenance, emergency response capabilities and waste management. We may also contract

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with an independent environmental consulting firm that conducts periodic, unscheduled, compliance assessments which focus on conditions with the potential to result in releases of hazardous substances or petroleum, and which also include screening for evidence of past spills or releases. Our relationship to our affiliates could, under certain circumstances, result in our incurring liability for environmental contamination attributable to an affiliate's operations, although we have not incurred any material derivative liability in the past. Our environmental management program has been extended to our affiliates.

We are staffed with environmental experts who manage our environmental exposure relating to historical operations and develop policies and procedures, including periodic audits of our terminals and tank cleaning facilities, in an effort to avoid circumstances that could lead to future environmental exposure.

As a handler of hazardous substances, we are potentially subject to strict, joint and several liability for investigating and rectifying the consequences of spills and other environmental releases of such substances either under the Comprehensive Environmental Response Compensation and Liability Act of 1980, as amended by the Superfund Amendments and Reauthorization Act of 1986 ( CERCLA ) or comparable state laws. From time to time, we have incurred remedial costs and regulatory penalties with respect to chemical or wastewater spills and releases at our facilities and, notwithstanding the existence of our environmental management program, we cannot assure that such obligations will not be incurred in the future, nor that such liabilities will not result in a material adverse effect on our financial condition, results of operations or our business reputation. As the result of environmental studies conducted at our facilities in conjunction with our environmental management program, we have identified environmental contamination at certain sites that will require remediation.

We have also been named a potentially responsible party ( PRP ), or have otherwise been alleged to have some level of responsibility, under CERCLA or similar state laws for cleanup of off-site locations at which our waste, or material transported by us, has allegedly been disposed of. We have asserted defenses to such actions and have not incurred significant liability in the CERCLA cases settled to date. While we believe that we will not bear any material liability in any current or future CERCLA matters, there can be no assurance that we will not in the future incur material liability under CERCLA or similar laws. See Certain Considerations Environmental Risk Factors for a discussion of certain risks of our being associated with transporting hazardous substances.

We are currently solely responsible for remediation of the following two federal Superfund sites:

Bridgeport, New Jersey. During 1991, CLC entered into a Consent Decree with the EPA filed in the U.S. District Court for the District of New Jersey, U.S. v. Chemical Leaman Tank Lines, Inc., Civil Action No. 91-2637 (JFG) (D.N.J.), with respect to its site located in Bridgeport, New Jersey, requiring CLC to remediate groundwater contamination. The Consent Decree required CLC to undertake Remedial Design and Remedial Action ( RD/RA ) related to the groundwater operable unit of the cleanup.

In August 1994, the EPA issued a Record of Decision, selecting a remedy for the wetlands operable unit at the Bridgeport site at a cost estimated by the EPA to be approximately \$7 million. In October 1998, the EPA issued an administrative order that requires CLC to implement the EPA's wetlands remedy. In April 1998, the federal and state natural resource damages trustees indicated their

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intention to bring claims against CLC for natural resource damages at the Bridgeport site. CLC has finalized a consent decree with the state and federal trustees and has resolved the natural resource damages claims. In addition, the EPA has investigated contamination in site soils. No decision has been made as to the extent of soil remediation to be required, if any.

CLC initiated litigation against its insurers to recover its costs in connection with environmental cleanups at its sites. In a case captioned Chemical Leaman Tank Lines, Inc. v. Aetna Casualty & Surety Co., et al., Civil Action No. 89-1543 (SSB) (D.N.J.), Chemical Leaman sought from its insurers reimbursement of substantially all past and future environmental cleanup costs at the Bridgeport site. In a case captioned The Aetna Casualty and Surety Company v. Chemical Leaman Tank Lines, Inc., et al., Civil Action No. 94-CV-6133 (E.D. Pa.), Chemical Leaman sought from its insurers reimbursement of substantially all past and future environmental cleanup costs at its other sites. In an agreement dated as of November 18, 1999, Chemical Leaman favorably resolved these outstanding insurance claims. In early 2000, we received settlement proceeds of approximately \$11.0 million.

West Caln Township, PA. The EPA has alleged that CLC disposed of hazardous materials at the William Dick Lagoons Superfund Site in West Caln, Pennsylvania. On October 10, 1995, CLC entered into a Consent Decree with the EPA which required CLC to:

- (1) pay the EPA for installation of an alternate water line to provide water to area residents;
- (2) perform an interim groundwater remedy at the site; and
- (3) conduct soil remediation. US v. Chemical Leaman Tank Lines, Inc., Civil Action No. 95-CV-4264 (RJB) (E.D. Pa.).

CLC has paid all costs associated with installation of the waterline. CLC has completed a hydro-geologic study, and has commenced activities for the design of a groundwater treatment plant to pump and treat groundwater. The EPA anticipates that CLC will operate the plant for about five years, at which time the EPA will evaluate groundwater conditions and determine whether a final groundwater remedy is necessary. Field sampling for soil remediation has been completed and activities for the design of a soil remediation system have commenced. The Consent Decree does not cover the final groundwater remedy or other site remedies or claims, if any, for natural resource damages.

Other Environmental Matters. CLC has been named as PRP under CERCLA and similar state laws at approximately 35 former waste treatment and/or disposal sites including the Helen Kramer Landfill Site where CLC previously settled its liability. In general, CLC is among several PRP s named at these sites. CLC is also named as a co-defendant in two civil toxic tort claims arising from alleged exposure to hazardous substances that were allegedly transported to disposal sites by CLC and other co-defendants. CLC is also incurring expenses resulting from the investigation and/or remediation of certain current and former CLC properties, including its facility in Tonawanda, New York and its former facility in Putnam County, West Virginia, and its facility in Charleston, West Virginia. As a result of our acquisition of CLC, we identified other owned or formerly owned properties that may require investigation and/or remediation, including properties subject to the New Jersey Industrial Sites Recovery Act (ISRA). CLC s involvement at some of the above referenced sites could amount to material liabilities, and there can be no assurance that costs associated with these sites, individually or in the

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aggregate, will not be material. We have established reserves for liabilities associated with the Helen Kramer Landfill, CLC's facility at Tonawanda, New York and CLC's former facility in Putnam County, West Virginia and other matters discussed above.

**6. NEW ACCOUNTING PRONOUNCEMENTS:**

Effective January 1, 2002, the Corporation adopted the provisions of Financial Accounting Standards No 142, Goodwill and Other Intangible Assets (Statement 142). As a result of the adoption of Statement 142, the amortization of goodwill ceased, resulting in an increase in net income for the quarter ended March 31, 2002 of \$0.9 million. Goodwill is subject to an annual impairment test. The Company expects to have its initial impairment test complete by the end of the second quarter. Intangible assets consist mainly of non-compete agreements with lives ranging from 2-5 years, and an intangible pension plan asset. Accumulated amortization of intangible assets are \$1.6 million and \$1.4 million, at March 31, 2002 and December 31, 2001, respectively.

The following table presents net loss on a comparable basis, after adjustment for goodwill amortization (in thousands, except per share amounts):

	<b>March 31, 2002</b>	<b>March 31, 2001</b>
	<u>          </u>	<u>          </u>
Net loss:		
As reported	\$(3,045)	\$(1,030)
Goodwill amortization (net of tax)		952
	<u>          </u>	<u>          </u>
Adjusted net loss	\$(3,045)	\$ (78)
	<u>          </u>	<u>          </u>
Basic and diluted loss per common share:		
As reported	\$ (1.83)	\$ (.71)
	<u>          </u>	<u>          </u>
As adjusted	\$ (1.83)	\$ (.03)
	<u>          </u>	<u>          </u>

**7. SUBSEQUENT EVENTS:**

Pursuant to the terms of an Offering Memorandum and Consent Solicitation Statement, dated April 10, 2002 (the Offering Memorandum), Quality Distribution, Inc. (the Company) commenced an offer (the Exchange Offer) to exchange (the Debt/Equity Exchange), for each \$1,000 in principal amount of its currently outstanding 10% Series B Senior Subordinated Notes due 2006 (the Fixed Rate Notes) and Series B Floating Interest Rate Subordinated Term Securities due 2006 (FIRSTS<sup>SM</sup>) (the FIRSTS and, together with the Fixed Rate Notes, for debt and equity securities (the Debt/Equity Securities) consisting of (i) \$650 principal amount of new 12 1/2% Senior Subordinated Secured Notes due 2008 (the New Notes) to be issued by a wholly owned subsidiary of the Company and which will acquire substantially all of the Company's assets, (B) \$150 principal amount of new 12% Junior Subordinated PIK Notes due 2009 (the Junior PIK Notes) to be issued by the Company and (C) 1.59 Warrants, each to purchase one share of the Company's common stock, par value \$0.01 per share (the Common Stock, at an exercise price of \$10 per share (the Warrants).

The completion of the Debt/Equity Exchange is conditioned upon, among other things, at least \$61.3 million aggregate principal amount of Notes (excluding the \$53.0 million aggregate principal amount of Notes covered by the Lock-Up Agreements described below) being validly tendered (and not properly withdrawn)

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in the Exchange Offer (the \$61.3 Million Threshold ). If the \$61.3 million Threshold is not satisfied, the Debt/Equity Exchange will not occur and eligible holders of Notes who have validly tendered (and not properly withdrawn) their Notes in the Exchange Offer prior to the expiration date will receive in exchange (the Senior Note Exchange ) for their Notes a like principal amount of new 10% Senior Secured Notes due 2008 (the 10% Senior Secured Notes ) to be issued by the Company. The Exchange Offer will expire on May 24, 2002, unless extended.

In conjunction with the Exchange Offer, the Company is soliciting consents from holders of Notes to amend the existing indenture governing the Notes. The proposed amendments would eliminate many of the restrictive covenants contained in the existing indenture and allow, among other things, the Company to complete the Debt/Equity Exchange. The proposed amendments require for adoption the Company's receipt of consents from holders representing at least a majority of the outstanding principal amount of Notes held by persons other than the Company or its affiliates. The adoption of the proposed amendments to the existing indenture is not conditioned on the consummation of the Debt/Equity Exchange.

In connection with the Exchange Offer, on April 10, 2002, the Company entered into lock-up agreements (collectively, the Lock-Up Agreements ) with (i) certain affiliates of Apollo Management, L.P., the Company's controlling stockholder ( Apollo ), (ii) certain affiliates of Ares Management, L.P. ( Ares ) and (iii) certain members of the Company's management (the Management Group ). Apollo, Ares and the Management Group collectively hold \$53.0 million aggregate principal amount, or approximately 37.9%, of Notes.

The Lock-Up Agreements provide that (i) if the \$61.3 Million Threshold is satisfied (but the \$78.3 Million Threshold (as defined below) and certain other conditions are not satisfied or waived) and the Debt/Equity Exchange is consummated pursuant to the terms of the Offering Memorandum, then Apollo, Ares and the Management Group will exchange their Notes for the Debt/Equity Securities, (ii) if at least \$78.3 million aggregate principal amount of Notes (excluding the \$53.0 million aggregate principal amount of Notes covered by the Lock-Up Agreements) are validly tendered (and not properly withdrawn) in the Exchange Offer (the \$78.3 Million Threshold ) and certain other conditions are satisfied or waived, then, in lieu of receiving Debt/Equity Securities, Apollo will exchange its \$29.5 million of Notes for shares of the Company's 13.75% preferred stock, \$0.01 par value per share (the 13.75% Preferred Stock ) and purchase an additional \$10.0 million of 13.75% Preferred Stock, (iii) if Apollo exchanges its Notes for 13.75% Preferred Stock as described in clause (ii) above, then the Management Group, in lieu of receiving Debt/Equity Securities, will exchange its \$1.0 million of Notes for shares of 13.75% Preferred Stock and (iv) if the Senior Note Exchange is consummated, then Apollo, Ares and the Management Group will exchange their \$53.0 million aggregate principal amount of Notes for a like principal amount of 10% Senior Secured Notes. On May 10, 2002, Apollo agreed to waive the \$78.3 million threshold condition upon satisfaction of the \$61.3 million threshold.

The Debt/Equity Securities or the 10% Senior Secured Notes, as applicable, and the 13.75% Preferred Stock will not be registered under the Securities Act of 1933, as amended, and may not be offered or sold in the United States absent registration or an applicable exemption from such registration requirements. This report is neither an offer to exchange, nor the solicitation of an offer to exchange, any Notes for Debt/Equity securities or 10% Senior Secured Notes, as applicable, nor the solicitation of any consents to the proposed amendments to the existing indenture for the Notes.

On April 5, 2002, we entered into a fifth amendment (the Fifth Amendment ) to our credit agreement. The Fifth Amendment will further amend the financial covenants through the date of the final maturity of our credit agreement. Such



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revised covenants will be less restrictive than the previously existing covenants for the period beginning March 31, 2003 through final maturity of our credit agreement. The revised covenants in the Fifth Amendment will only become effective if we are able to satisfy certain conditions. If the Debt/Equity Exchange is consummated as a result of the Exchange Offer, then the conditions to effectiveness will be satisfied. There can be no assurance that the amendments to the financial covenants in the Fifth Amendment will become effective, or that if they do, that we will be able to comply with such revised financial covenants.

**8. GEOGRAPHIC SEGMENTS**

The Company's operations are located primarily in the United States, Canada, and Mexico. Inter-area sales are not significant to the total revenue of any geographic area. Information about the Company's operations in different geographic areas for the quarters ended March 31, 2002 and March 31, 2001, is as follows:

	March 31, 2001		
	U.S.	INTERNATIONAL	ELIMINATIONS CONSOLIDATED
Operating revenues	\$ 124,293	\$ 6,510	\$ 130,803
Net operating income	8,641	117	8,758
Identifiable assets	432,585	26,630	(14,196) 445,019
Depreciation and amortization	7,785	863	8,648
Capital expenditures	6,194	425	6,619

	March 31, 2002		
	U.S.	INTERNATIONAL	ELIMINATIONS CONSOLIDATED
Operating revenues	\$ 120,057	\$ 4,869	\$ 124,926
Net operating income	6,952	135	7,087
Identifiable assets	432,604	12,413	(1,557) 443,460
Depreciation and amortization	7,414	699	8,113
Capital expenditures	2,926	13	2,939

**9. GUARANTOR SUBSIDIARIES:**

The 10% Series B Senior Subordinated Notes and Series B Floating Interest Rate Subordinated Term Notes issued in June 1998 and due 2006 are unconditionally guaranteed on a senior unsecured basis pursuant to guarantees by all the Company's direct and indirect domestic subsidiaries, except Bulknet (The Guarantors). Each of the Company's direct and indirect subsidiaries is 100% owned. All non-domestic subsidiaries including Levy Transport Ltd. are non-guarantor subsidiaries.

The Company conducts substantially all of its business through and derives virtually all its income from its subsidiaries. Therefore, the Company's ability to make required principal and interest payments with respect all to the Company's indebtedness, including the Notes and other obligations, depends on the earnings of subsidiaries and its ability to receive funds from its subsidiaries through dividend and other payments. The subsidiary guarantors are wholly owned subsidiaries of the Company and have fully and unconditionally guaranteed the Notes on a joint and several basis.

The Company has not presented separate financial statements and other disclosures concerning subsidiary guarantors because management has determined such information is not material to the holders of the Notes.

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The following condensed consolidating financial information presents:

1. Balance Sheets as of March 31, 2002 and December 31, 2001.
2. Statements of Operations for the three months ended March 31, 2002 and 2001.
3. Statements of Cash Flows for the three months ended March 31, 2002 and 2001.
4. The parent company and combined guarantor subsidiaries.
5. Elimination entries necessary to consolidate the parent company and all its subsidiaries.

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QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
CONSOLIDATING BALANCE SHEET  
MARCH 31, 2002  
(Unaudited)  
(In thousands)

	<u>Parent</u>	<u>Guarantor Subs</u>	<u>Non Guarantor Subs</u>	<u>Eliminations</u>	<u>Consolidated</u>
<b>ASSETS</b>					
Current Assets:					
Cash	\$	\$ 602	\$ 1,285	\$	\$ 1,887
Accounts receivable, net		88,510	2,360		90,870
Inventories		850	225		1,075
Prepaid expense and other Current assets		16,901	729		17,630
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total current assets		106,863	4,599		111,462
Property and equipment, net		155,920	15,144		171,064
Intangibles & goodwill, net		151,793	806		152,599
Other assets	100,000	8,331	4	(100,000)	8,335
Investment in subsidiaries	217,478			(217,478)	
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
	\$ 317,478	\$ 422,907	\$ 20,553	\$ (317,478)	\$ 443,460
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>

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QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
CONSOLIDATING BALANCE SHEET  
MARCH 31, 2002  
(Unaudited) (In thousands, continued)

	Parent	Guarantor Subs	Non-Guarantor Subs	Elim's	Consolidated
<b>Current Liabilities:</b>					
Current maturities of indebtedness	\$ 2,679	\$	\$	\$	\$ 2,679
Accounts payable and accrued expense		54,725	1,965		56,690
Inter-company		3,988	(3,988)		
Independent contractors payable		7,142	(17)		7,125
Other current liabilities		5,255			5,255
Income taxes payable		659	418		1,077
	<u>2,679</u>	<u>71,769</u>	<u>(1,622)</u>	<u>(100,000)</u>	<u>72,826</u>
Bank debt, less current maturities	294,011		5,000		299,011
Subordinated debt, less current maturities	140,000	100,000		(100,000)	140,000
Other long term liabilities		11,023			11,023
Environmental liabilities		34,874			34,874
Deferred income taxes		(1,064)	2,262		1,198
Accrued loss and damage claims		1,907			1,907
	<u>\$ 436,690</u>	<u>\$ 218,509</u>	<u>\$ 5,640</u>	<u>\$ (100,000)</u>	<u>\$ 560,839</u>
Minority interest in subsidiaries		1,833			1,833
Mandatorily redeemable preferred stock	17,065				17,065
Mandatorily redeemable common stock	1,210				1,210
<b>Stockholders' Equity (Deficit):</b>					
Common stock and Additional paid-in-capital	105,564	140,254	15,082	(155,336)	105,564
Retained earnings	(41,082)	62,311	1,053	(63,364)	(41,082)
Stock recapitalization	(189,589)		(55)	55	(189,589)
Treasury stock	(628)				(628)
Other stockholders' equity	(9,976)		(1,167)	1,167	(9,976)
Note receivable	(1,776)				(1,776)
	<u>(137,487)</u>	<u>202,565</u>	<u>14,913</u>	<u>(217,478)</u>	<u>(137,487)</u>
	<u>\$ 317,478</u>	<u>\$ 422,907</u>	<u>\$ 20,553</u>	<u>\$ (317,478)</u>	<u>\$ 443,460</u>

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FORM 10-Q  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
CONSOLIDATING BALANCE SHEET  
DECEMBER 31, 2001  
(Unaudited)  
(In thousands)

	<u>Parent</u>	<u>Guarantor Subs</u>	<u>Non-Guarantor Subs</u>	<u>Elim's</u>	<u>Consolidated*</u>
<b>ASSETS</b>					
Current Assets:					
Cash	\$	\$ 1,909	\$ 303	\$	\$ 2,212
Accounts receivable, net		86,017	2,884		88,901
Inventories		874	269		1,143
Prepaid expenses and other current assets		17,166	541		17,707
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total Current Assets		105,966	3,997		109,963
Property and equipment, net		160,998	16,361		177,359
Intangibles & goodwill, net		151,969	806		152,775
Other assets	100,000	8,877	4	(100,000)	8,881
Investment in subsidiaries	227,098			(227,098)	
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
	\$327,098	\$427,810	\$21,168	\$(327,098)	\$448,978
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>

\* Condensed from audited financial statements.

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QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
CONSOLIDATING BALANCE SHEET  
DECEMBER 31, 2001  
(Unaudited, in thousands, continued)

	PARENT	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
<b>Current liabilities:</b>					
Current maturities of indebtedness	\$ 2,677	\$	\$	\$	\$ 2,677
Accounts payable		11,432	1,985		13,417
Inter-company		(1,133)	1,133		
Affiliates and owner-operators payable		4,902	28		4,930
Accrued expenses		49,431			49,431
Income taxes payable		663	429		1,092
<b>Total current liabilities</b>	<b>2,677</b>	<b>65,295</b>	<b>3,575</b>		<b>71,547</b>
Long-term debt, less current maturities	441,179				441,179
Environmental liabilities		36,163			36,163
Other long-term liabilities		113,744		(100,000)	13,744
Deferred income tax		(1,189)	2,459		1,270
<b>Total liabilities</b>	<b>443,856</b>	<b>214,013</b>	<b>6,034</b>	<b>(100,000)</b>	<b>563,903</b>
Mandatorily redeemable common stock	1,210				1,210
Mandatorily redeemable preferred stock	16,499				16,499
Minority interest in subsidiaries		1,833			1,833
<b>Stockholders' Equity (deficit):</b>					
Common stock and additional paid-in capital	105,564	149,653	15,082	(164,735)	105,564
Retained earnings (deficit)	(37,435)	62,311	1,195	(63,506)	(37,435)
Treasury stock	(402)				(402)
Stock recapitalization	(189,589)		(55)	55	(189,589)
Other comprehensive gain (loss)	(10,829)		(1,088)	1,088	(10,829)
Note receivable	(1,776)				(1,776)
<b>Total stockholders' equity (deficit)</b>	<b>(134,467)</b>	<b>211,964</b>	<b>15,134</b>	<b>(227,098)</b>	<b>(134,467)</b>
	<b>\$ 327,098</b>	<b>\$427,810</b>	<b>\$ 21,168</b>	<b>\$(327,098)</b>	<b>\$ 448,978</b>

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FORM 10-Q  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBS CONDENSED CONSOLIDATING STATEMENTS OF INCOME  
THREE MONTHS ENDED MARCH 31, 2002  
(Unaudited) (In thousands)

	Parent	Guarantor Subs	Non-Guarantor Subs	Elim's	Consolidated
Operating Revenues:					
Transportation	\$	\$ 100,216	\$ 4,518	\$	\$ 104,734
Other		19,825	367		20,192
		120,041	4,885		124,926
Operating Expenses:					
Purchased transportation		70,520	596		71,116
Depreciation and amortization		7,373	740		8,113
Other operating expenses		35,039	3,571		38,610
Operating income (loss)		7,109	(22)		7,087
Interest expense, net	9,851		56		9,907
Other (income) expense		(36)			(36)
Equity in earnings (loss) of subsidiaries	4,031			(4,031)	
Income (loss) before taxes	(5,820)	7,073	(78)	(4,031)	(2,856)
Income taxes	(2,775)	2,900	64		189
Net income (loss)	\$(3,045)	\$ 4,173	\$ (142)	\$(4,031)	\$ (3,045)

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FORM 10-Q  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBS CONDENSED CONSOLIDATING STATEMENTS OF INCOME  
THREE MONTHS ENDED MARCH 31, 2001  
(Unaudited) (In thousands)

	<u>Parent</u>	<u>Guarantor Subs</u>	<u>Non-Guarantor Subs</u>	<u>Elim's</u>	<u>Consolidated</u>
<b>Operating Revenues:</b>					
Transportation	\$	\$ 108,916	\$ 6,160	\$	\$ 115,076
Other		15,286	441		15,727
		<u>124,202</u>	<u>6,601</u>		<u>130,803</u>
<b>Operating Expenses:</b>					
Purchased transportation		73,419	798		74,217
Depreciation and amortization		7,762	886		8,648
Other operating expenses		34,235	4,945		39,180
		<u>8,786</u>	<u>(28)</u>		<u>8,758</u>
Operating income (loss)		8,786	(28)		8,758
Interest expense, net	9,443		(2)		9,441
Other (income) expense		(14)	1		(13)
Equity in earnings (loss) of subsidiaries	5,105			(5,105)	
		<u>8,800</u>	<u>(27)</u>	<u>(5,105)</u>	<u>(670)</u>
Income (loss) before benefit (provision) for income taxes	(4,338)	8,800	(27)	(5,105)	(670)
Benefit (provision) for income taxes	(3,308)	3,608	60		360
	<u>(1,030)</u>	<u>5,192</u>	<u>(87)</u>	<u>(5,105)</u>	<u>(1,030)</u>
Net income (loss)	\$ (1,030)	\$ 5,192	\$ (87)	\$ (5,105)	\$ (1,030)



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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS  
THREE MONTHS ENDED MARCH 31, 2002 (Unaudited) (In thousands)

	<u>Parent</u>	<u>Guarantor Subs</u>	<u>Non-Guarantor Subs</u>	<u>Elim's</u>	<u>Consolidated</u>
Cash provided by (used in)					
Operating activities:					
Net income (loss)	\$(3,045)	\$ 4,173	\$ (142)	\$(4,031)	\$(3,045)
Adjustments for non cash charges	3,045	2,084	3,856		8,985
Changes in assets/liabilities		3,475	(9,534)	4,031	(2,028)
Net cash provided by (used in) operating activities		9,732	(5,820)		3,912
Investing activities:					
Capital expenditures		(1,578)	(1,361)		(2,939)
Proceeds from asset dispositions		(1,549)	2,557		1,008
Net cash provided by (used in) investing activities		(3,127)	1,196		(1,931)
Financing activities:					
Proceeds from issuance of long term debt	(5,771)		5,771		
Payment of obligations	(2,069)		(100)		(2,169)
Issuance of common stock					
Other		(199)	(64)		(263)
Net change in intercompany balances	7,840	(7,840)			
Net cash provided by (used in) financing activities		(8,039)	5,607		(2,432)
Net increase (decrease) in cash		(1,434)	983		(451)
Effect of exchange rate changes on cash		126			126
Cash, beginning of period		1,910	302		2,212
Cash, end of period	\$	\$ 602	\$ 1,285	\$	\$ 1,887

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATING MARCH 31, 2001 (Unaudited) (In thousands)

	<u>Parent</u>	<u>Guarantor Subs</u>	<u>Non-Guarantor Subs</u>	<u>Elim s</u>	<u>Consolidated</u>
Cash provided by (used in)					
Operating activities:					
Net income (loss)	\$(1,030)	\$ 5,192	\$ (87)	\$(5,105)	\$(1,030)
Adjustments for non cash charges	1,030	7,823	904		9,757
Changes in assets/liabilities		(7,271)	2,775	5,105	609
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Net cash provided by operating activities		5,744	3,592		9,336
Investing activities:					
Capital expenditures		(5,998)	(621)		(6,619)
Proceeds from asset dispositions		1,007	115		1,122
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Net cash (used in) investing activities		(4,991)	(506)		(5,497)
Financing activities:					
Proceeds from issuance of long term debt	3,860		(3,860)		
Payment of obligations		(1,251)			(1,251)
Preferred stock redemption	(2,600)				(2,600)
Other		275			275
Net change in inter-company balances	(1,260)	1,260			
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Net cash provided by (used In) financing activities		284	(3,860)		(3,576)
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Net increase (decrease) in cash		1,037	(774)		263
Effect of exchange rate changes on cash		(583)			(583)
Cash, beginning of period		2,242	394		2,636
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Cash, end of period	\$	\$ 2,696	\$ (380)	\$	\$ 2,316
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>

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PART 1 FINANCIAL INFORMATION  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES

ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS  
FIRST QUARTER 2002 COMPARED TO THE FIRST QUARTER 2001

RESULTS OF OPERATIONS

Our revenue is principally a function of the volume of shipments by the bulk chemical industry, our market share as opposed to that of our competitors and the amount spent on tank truck transportation as opposed to other modes of transportation such as rail. The volume of shipments of chemical products are in turn affected by many other industries, including consumer and industrial products, automotive, paint and coatings, and paper, and tend to vary with changing economic conditions. Additionally we also provide leasing, tank cleaning, and intermodal services presented as other revenue.

The principal components of our operating costs include purchased transportation, salaries, wages, benefits, annual tractor and trailer maintenance costs, insurance and fuel costs. We believe our use of affiliates and owner-operators provides a more flexible cost structure, increases our asset utilization and increases our return on invested capital.

We have historically focused on maximizing cash flow and return on invested capital. Our affiliate program has greatly reduced the amount of capital needed for us to maintain and grow our terminal network. In addition, the extensive use of owner-operators reduces the amount of capital needed to operate our fleet of tractors, which have shorter economic lives than trailers. These factors have allowed us to concentrate our capital spending on our trailer fleet where we can achieve superior returns on invested capital through our transportation operations and leasing to third parties and affiliates.

Through several strategic asset purchases during 2001, we were further able to expand our service capabilities and our geographic coverage. We intend to continue providing these services and expand upon existing customer relationships by providing our supplementary services as well as increasing the fleet size in these markets.

THREE MONTHS ENDED MARCH 31, 2002 COMPARED TO THREE MONTHS ENDED MARCH 31, 2001

For the quarter ended March 31, 2002, revenues totaled \$124.9 million, a 4.5% decrease from revenues of \$130.8 million for the same period in 2001. This decrease is primarily attributable to lower fuel surcharges of \$3.6 million and 1.5 fewer service days. Operating revenue excluding surcharges on a per service day basis was flat first quarter ended March 31, 2002 compared to the same period in 2001.

The decline in demand in the last several quarters is reflective of the softness in the manufacturing sector over the same period. The first quarter of 2002 showed signs that the demand in base business has begun to stabilize. The overall decline in base business demand in the first quarter 2002 over same quarter last year, accompanied by flat pricing environment were offset partially by growth in new business as a result of successful competitive bids, plus several strategic asset purchases in the latter half of 2001. For the quarter ended March 31, 2002, operating income totaled \$7.1 million, a decrease of \$1.7 million compared to \$8.8 million for the same period in 2001. This decline is primarily the result of lower revenue discussed above, plus

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higher insurance expense in 2002. Significant insurance increases began in September 2001 when the Company entered into a new insurance policy period. These factors were partially offset by an increase in operating income of \$.9 million as a result of the elimination of amortization of goodwill in 2002 due to the adoption of FAS 142.

The operating ratio for the quarter ended March 31, 2002 was 94.3% compared to 93.3% for the same period in 2001.

Interest expense, net, increased to \$9.9 million in the quarter ended March 31, 2002, from \$9.4 million in the quarter ended March 31, 2001. This increase is the result of increased borrowings in the current year, plus costs associated with several amendments to our credit facility in 2001.

The pre-tax loss for the quarter ended March 31, 2002 totaled \$2.9 million compared to a \$0.7 million loss for the same period in 2001 as a result of the items discussed above.

Benefit (provision) for income tax decreased from \$0.4 million to \$0.2 million due to the relative impact of non-deductible items on the different pre-tax amounts and the non-recognition of tax benefits.

For the quarter ended March 31, 2002, the Company's net loss was \$3.0 million compared with a \$1.0 million loss for the same period last year as a result of the items discussed above.

Basic weighted average shares decreased to 1,996,000 in the first quarter of 2002 from 2,021,000 at March 31, 2001. As of March 31, 2002, a total of 1,991,726 shares were outstanding.

**LIQUIDITY AND CAPITAL RESOURCES**

The Company's primary sources of liquidity are funds provided by operations and borrowings under various credit arrangements with financial institutions.

Net cash provided by operating activities totaled \$3.9 million for the three months ended March 31, 2002, versus \$9.3 million for the same period in 2001. The change in cash provided by operations was due to the timing of cash receipts related to accounts payable and payments of trade and other payables.

Cash used by investing activities totaled \$1.9 million for the three month period ended March 31, 2002, compared to \$5.5 million used for the comparable 2001 period. Capital was used primarily to acquire replacement revenue equipment and for significant upgrades to the Company's computer infrastructure and new dispatch system in 2001 and 2002.

Cash used for financing activities totaled \$2.4 million during the three month period ended March 31, 2002, compared to \$3.6 million used in the comparable period in 2001. This difference is due to the purchase of CLC preferred stock from a minority shareholder in 2001 (\$2.6 million).

The Company has a \$285 million credit facility with a group of banks maturing at various times from June of 2004 to 2006. Additionally, the Company has a revolving credit facility in the amount of \$75 million until June 9, 2004, restricted to \$70.4 million in the Fourth Amendment. As of March 31, 2002, the Company has available \$18.2 million under this revolving credit facility. The Company also has \$100.0 million in 10% senior subordinated notes due in 2006 and \$40.0 million in floating interest rate subordinated term securities also due in 2006.

Our credit agreements include financial covenants, recently modified, which require minimum or maximum ratios to be maintained. Our credit agreement was

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amended (the Fourth Amendment) on December 14, 2001. The new financial covenants are less restrictive than the previously existing covenants and cover the calendar quarters through December 31, 2002. The Company currently believes that it will be in compliance with the covenants through December 31, 2002. In addition, the Fourth Amendment restricts the future availability of the revolving credit facility to an incremental \$15 million above the balance at the date of the agreement, plus places restrictions on the amount of capital expenditures allowed.

On April 5, 2002, the Company entered into a fifth amendment (the Fifth Amendment ) to the credit agreement. The Fifth Amendment relates to the financial covenants which are unlikely to be met beginning with the quarter ending March 31, 2003 and will further amend those financial covenants through the date of the final maturity of the credit agreement. The revised covenants in the Fifth Amendment will only become effective if we are able to satisfy certain conditions. If the Debt/Equity Exchange is consummated as a result of the Exchange Offer, then the conditions to effectiveness will be satisfied. (See note 7 for discussion of the Exchange Offer.) There can be no assurance that the amendments to the financial covenants in the Fifth Amendment will become effective, or that if they do, that the Company will be able to comply with such revised financial covenants. As of March 31, 2002, no default exists relative to any financial covenant. However, continued compliance with these requirements could be effected by changes relating to economic factors, market uncertainties, or other events as described under FORWARD-LOOKING STATEMENTS AND RISK FACTORS.

The Company's management believes that borrowings under the credit agreement, together with available cash and internally generated funds, will be sufficient to fund the Company's cash obligations for the remainder of 2002.

**FORWARD-LOOKING STATEMENTS AND RISK FACTORS**

Some of the statements contained in this report discuss future expectations and contain projections of results of operations or financial condition or state other forward-looking information. Those statements are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from those contemplated by the statements. Please see the risk factors set forth in the Company's 2001 Form 10-K which identify important risk factors such as the Company's high leverage, dependence on affiliates and owner-operators, environmental risks and claims exposure.

The forward-looking information is based on various factors and was derived using numerous assumptions. Important factors that could cause our actual results to be materially different from the forward-looking statements include general economic conditions, cost and availability of diesel fuel, adverse weather conditions and competitive rate fluctuations. Future financial and operating results of QDI may fluctuate as a result of these and other risk factors as detailed from time to time in company filings with the Securities and Exchange Commission.

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FORM 10-Q

ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.  
QUALITY DISTRIBUTION, INC. AND SUBSIDIARIES

See note 4 Derivatives

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FORM 10-Q

PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

Reference is made to Item 2 on page 17 of the Company's Form 10-K for the year ended December 31, 2001. There have been no material changes in the Company's legal proceedings since this filing.

ITEM 4. Submission of Matters to a Vote of Security Holders None

ITEM 6. (a) Exhibits: None

(b) Reports on Form 8-K: None

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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.

QUALITY DISTRIBUTION, INC.

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May 10, 2002

/S/ THOMAS L. FINKBINER

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THOMAS L. FINKBINER, (PRESIDENT AND  
CHIEF EXECUTIVE OFFICER  
(DULY AUTHORIZED OFFICER)

May 10, 2002

/S/ DENNIS R. FARNSWORTH

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DENNIS R. FARNSWORTH (SENIOR VICE  
PRESIDENT AND CHIEF FINANCIAL OFFICER)  
(PRINCIPAL FINANCIAL OFFICER)