

OLYMPIC STEEL INC  
Form 10-K  
March 02, 2017

---

---

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

**Form 10-K**

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

For The Year Ended December 31, 2016

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 0-23320

**OLYMPIC STEEL, INC.**

(Exact name of registrant as specified in its charter)

Ohio  
(State or other jurisdiction of

incorporation or organization)

22901 Millcreek Boulevard, Suite 650, Highland Hills, OH  
(Address of principal executive offices)

34-1245650  
(I.R.S. Employer

Identification Number)

44122  
(Zip Code)

Registrant's telephone number, including area code (216) 292-3800

**Securities registered pursuant to Section 12(b) of the Act:**

| <u>Title of each Class</u>      | <u>Name of each Exchange on which registered</u> |
|---------------------------------|--|
| Common Stock, without par value | The NASDAQ Stock Market LLC                      |

**Securities registered pursuant to Section 12(g) of the Act:**

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ( ) No (X)

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ( ) No (X)

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

Yes (X) No ( )

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

Yes (X) No ( )

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. (X)





**TABLE OF CONTENTS**

|  | <b><u>Page</u></b> |
|--|--------------------|
| <b>Part I</b>  |                    |
| Item 1. Business   | 4                  |
| Item 1A. Risk Factors  | 14                 |
| Item 1B. Unresolved Staff Comments   | 22                 |
| Item 2. Properties   | 23                 |
| Item 3. Legal Proceedings  | 24                 |
| Item 4. Mine Safety Disclosures  | 24                 |
| Executive Officers of the Registrant   | 25                 |
| <b>Part II</b>   |                    |
| Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities | 26                 |
| Item 6. Selected Financial Data  | 27                 |
| Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations                        | 28                 |
| Item 7A. Quantitative and Qualitative Disclosures About Market Risk  | 47                 |
| Item 8. Financial Statements and Supplementary Data  | 48                 |
| Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure                         | 77                 |
| Item 9A. Controls and Procedures   | 77                 |
| Item 9B. Other Information   | 77                 |
| <b>Part III</b>  |                    |
| Item 10. Directors, Executive Officers and Corporate Governance  | 78                 |
| Item 11. Executive Compensation  | 78                 |
| Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters              | 78                 |
| Item 13. Certain Relationships and Related Transactions, and Director Independence                                   | 78                 |
| Item 14. Principal Accountant Fees and Services  | 78                 |
| <b>Part IV</b>   |                    |
| Item 15. Exhibits and Financial Statement Schedules  | 79                 |
| Item 16. Form 10-K Summary   | 79                 |
| Signatures   | 80                 |
| Index to Exhibits  | 81                 |

## **PART I**

### **ITEM 1. BUSINESS**

#### **The Company**

We are a leading metals service center that operates in three reportable segments; carbon flat products, specialty metals flat products and tubular and pipe products. The carbon flat products segment and the specialty metals flat products segment are at times consolidated and referred to as the flat products segments. Some of the flat products segments' assets and resources are shared by the carbon and specialty metals segments and both segments' products are stored in the shared facilities and, in some locations, processed on shared equipment. We provide metals processing and distribution services for a wide range of customers. Our carbon flat products segment's focus is on the direct sale and distribution of large volumes of processed carbon and coated flat-rolled sheet, coil and plate products, and fabricated parts. Our specialty metals flat products segment's focus is on the direct sale and distribution of processed aluminum and stainless flat-rolled sheet and coil products, flat bar products and fabricated parts. Through our tubular and pipe products segment, which consists of our Chicago Tube & Iron, or CTI, subsidiary we distribute metal tubing, pipe, bar, valves and fittings and fabricate pressure parts supplied to various industrial markets.

Products that require more value-added processing generally have a higher gross profit. Accordingly, our overall gross profit is affected by, among other things, product mix, the amount of processing performed, the demand for and availability of metals, and volatility in selling prices and material purchase costs. We also perform toll processing of customer-owned metals. We sell certain products internationally, primarily in Canada, Mexico and the Dominican Republic. International sales have increased over the past couple of years to 2.2% of consolidated net sales in 2016, but are still immaterial to our consolidated financial results and to the individual segments' results.

Segment reporting information is contained in Note 15 of Notes to Consolidated Financial Statements, which can be found in Part II, Item 8 of this Annual Report on Form 10-K and which is incorporated herein by reference.

We are incorporated under the laws of the State of Ohio. Our executive offices are located at 22901 Millcreek Boulevard, Suite 650, Highland Hills, Ohio 44122. Our telephone number is (216) 292-3800, and our website address is [www.olysteel.com](http://www.olysteel.com). We are not including the information on our website as a part of, or incorporating it by reference into, this Annual Report on Form 10-K.

## Industry Overview

The metals industry is comprised of three types of entities: metals producers, intermediate metals processors and metals service centers. Metals producers have historically emphasized the sale of metals to volume purchasers and have generally viewed intermediate metals processors and metals service centers as part of their customer base. However, all three types of entities can compete for certain customers who purchase large quantities of metals. Intermediate metals processors tend to serve as processors in large quantities for metals producers and major industrial consumers of processed metals, including automobile and appliance manufacturers.

Services provided by metals service centers can range from storage and distribution of unprocessed metal products to complex, precision value-added metals processing. Metals service centers respond directly to customer needs and emphasize value-added processing of metals pursuant to specific customer demands, such as cutting-to-length, slitting, shearing, roll forming, shape correction and surface improvement, blanking, tempering, plate burning and stamping. These processes produce metals to specified lengths, widths, shapes and surface characteristics through the use of specialized equipment. Metals service centers typically have lower cost structures than, and provide services and value-added processing not otherwise available from, metals producers.

End product manufacturers and other metals users seek to purchase metals on shorter lead times and with more frequent and reliable deliveries than can normally be provided by metals producers. Metals service centers generally have lower labor costs than metals producers and consequently process metals on a more cost-effective basis. In addition, due to this lower cost structure, metals service centers are able to handle orders in quantities smaller than would be economical for metals producers. The benefits to customers purchasing products from metals service centers include lower inventory levels, lower overall cost of raw materials, more timely response and decreased manufacturing time and expense. Customers also benefit from a lower investment in production labor, buildings and equipment, which allows them to focus on the engineering, assembly and marketing of their products. We believe that customers' demands for just-in-time delivery have made the value-added inventory, processing and delivery functions performed by metals service centers increasingly important.

## **Corporate History**

Our company was founded in 1954 by the Siegal family as a general steel service center. Michael Siegal, the son of one of the founders, began his career with us in the early 1970s and has served as our Chief Executive Officer since 1984, and as our Chairman of the Board of Directors since 1994. David Wolfort, our President, joined us as General Manager in 1984. In the late 1980s, our business strategy changed from a focus on warehousing and distributing steel from a single facility with no major processing equipment to a focus on geographic and product growth, customer diversity and value-added processing. An integral part of our growth has been the acquisition and start-up of processing and sales operations, and the investment in processing equipment. In 1994, we completed an initial public offering and, in 1996, we completed a follow-on offering of our common stock. In July 2011, we acquired CTI, a private leading distributor of tubing, pipe, bar, valves, and fittings, which represents our tubular and pipe products segment. Andrew Greiff, our newly appointed Executive Vice President and Chief Operating Officer joined us in 2009 and has managed the Company's rapidly expanding specialty metals business.

## **Business Strategy and Objectives**

We believe that the metals service center and processing industry is driven by the following primary trends: (i) shift by customers to fewer suppliers that are larger and financially strong; (ii) increased customer demand for more frequent deliveries, higher quality products and services; and (iii) globalization of metals industry participants.

In recognition of these industry trends, our focus has been on achieving profitable geographic and product growth through the start-up and acquisition of service centers, processors, fabricators and related businesses, and investments in people, information systems, higher value-added processing equipment and services, while continuing our commitment to expanding and improving our operating efficiencies, sales and servicing efforts.

Our profit improvement program, initiated in 2015 to reduce operating expenses and enhance margins, is now integrated into our operations. This plan included eliminating certain leased properties, lowering transportation, labor and personnel expenses, centralization of certain administrative functions, as well as inventory and purchasing initiatives. We successfully executed on the initiatives of the plan, which has led to reduced operating expenses and improved efficiencies.

We are focused on specific operating objectives including: (i) managing inventory turnover; (ii) managing operating expenses; (iii) maintaining targeted cash turnover rates; (iv) investing in value-added processing and material handling equipment; (v) growing our market share; (vi) investing in technology and business information systems; (vii)



improving safety performance; and (viii) improving on-time delivery and quality performance for our customers.

These operating objectives are supported by:

A set of core values, which are communicated, practiced and measured throughout the Company.

Our “flawless execution” program (Fe), which is an internal recognition program that rewards employees who achieve profitable growth by delivering superior customer service and exceeding customer expectations.

Operational initiatives designed to improve efficiencies and reduce costs by improving three key sub-systems:

*Operating system:* Focused on continuously improving processes through waste and variation elimination using Lean Six Sigma tools and employee certifications.

*Cultural system:* Focused on creating the environment to facilitate change and improve the way we work and create value.

*Management system:* Focused on creating the measurements and governance structure to support continuous improvement.

New information systems and key metric reporting to focus managers on achieving specific operating objectives. Alignment of compensation with the financial objectives and performance of the Company and the achievement of specific financial and operating objectives.

We believe our depth of management, facilities, locations, processing capabilities, inventory, focus on safety, quality and customer service, extensive and experienced sales force, and the strength of our customer and supplier relationships provide a strong foundation for implementation of our strategy and achievement of our objectives. Certain elements of our strategy are set forth in more detail below.

*Investments and Acquisitions.* Historically, we have accelerated our growth through acquisitions and capital investments in facilities and processing equipment. When the results of sales and marketing efforts and our financial justifications indicate that there is sufficient customer demand for a particular product, process or service, we may purchase equipment to satisfy that demand. We also evaluate our existing equipment to ensure that it remains productive, and we upgrade, replace, redeploy or dispose of equipment when necessary. During the five-year period ended December 31, 2012, we spent approximately \$160 million on the CTI acquisition and over \$125 million on capital investments for new facilities and processing equipment in support of our strategic growth initiatives. Since 2013, we continued to invest in processing equipment to support customer demand and to respond to the growing trend among original equipment manufacturers (our customers) to outsource non-core production processes, such as plate processing, machining, welding and fabrication, in order to concentrate on engineering, design and assembly.

Our capital investments during the past three years have primarily consisted of a stretcher leveling line as well as other processing equipment for our expanded value-added customer base in Winder, Georgia, added tube and pipe distribution capabilities from our Cleveland, Ohio and Monterey, Mexico facilities and additional processing equipment in our tubular and pipe products segment.

*Sales and Marketing.* We believe that our commitments to quality, service, just-in-time delivery and field sales personnel have enabled us to build and maintain strong customer relationships. We continuously analyze our customer base to ensure that strategic customers are properly targeted and serviced, while focusing our efforts to supply and successfully service multi-location customers from multi-location Olympic facilities. We service certain customers with carbon and specialty metals flat products and tubular and pipe products through cross-stocking of products in certain facilities.

We offer business solutions to our customers through value-added and value-engineered services. We also provide inventory stocking programs and in-plant Olympic Steel employees located at certain customer locations to help reduce customers' costs. Our owned truck fleet further enhances our just-in-time deliveries based on our customers' requirements.

Our flawless execution (Fe) program is a commitment to provide superior customer service while striving to exceed customer expectations. This program includes tracking on-time delivery and quality performance against objectives, and recognition of employee initiatives to improve efficiencies, streamline processes or reduce operating expenses at each operation.

We believe our large and experienced sales force provides strategic advantages. Our sales force makes direct daily sales calls to customers throughout the continental United States, Canada and Mexico. The continuous interaction between our sales force and active and prospective customers provides us with valuable market information and sales opportunities, including opportunities for outsourcing, improving customer service and increasing sales.

Our sales efforts are further supported by metallurgists, engineers, technical and quality service personnel and product specialists who have specific expertise in carbon and stainless steel, aluminum, alloy plate and steel fabrication as well as tubular and pipe products. We have expanded our sales force to increase market share in all of our segments. Our services for certain customers also include integration into our internal business systems to provide cost efficiencies for both us and our customers.

*Management.* We believe one of our strengths is the depth, knowledge and experience of our management team. In addition to our executive officers, members of our senior management team have a diversity of backgrounds within the metals industry, including management positions at metals producers and other metals service centers. They average 30 years of experience in the metals industry and 23 years with our company.

## **Products, Processing Services and Quality Standards**

We maintain inventory of carbon, stainless and aluminum coil, plate and sheet products, and tubular and pipe products. Coil is in the form of a continuous sheet, typically 36 to 96 inches wide, between 0.015 and 0.625 inches thick, and rolled into 10 to 30 ton coils. Because of the size and weight of these coils and the equipment required to move and process them into smaller sizes, such coils do not meet the requirements, without further processing, of most customers. Plate is typically thicker than coil and is processed by laser, plasma or oxygen burning.

Through our CTI subsidiary, we maintain inventory of round, square, and rectangular mechanical and structural tubing; hydraulic and stainless tubing; boiler tubing; carbon, stainless, and aluminum pipe; and valves and fittings. CTI provides a variety of value added services to its tube and pipe product line, including saw cutting, laser cutting, beveling, threading and grooving. CTI also fabricates pressure components supplied to various industrial markets.

Customer orders are entered or electronically transmitted into computerized order entry systems, and appropriate inventory is selected and scheduled for processing in accordance with the customer's specified delivery date. We attempt to maximize yield and equipment efficiency through the use of computer software and by combining customer orders for processing each coil, plate, tube or pipe to the fullest extent practicable.

Our services include both traditional service center processes of cutting-to-length, slitting, flattening, sawing and shearing and higher value-added processes of blanking, tempering, plate burning, laser cutting, precision machining, welding, fabricating, bending, beveling, polishing, kitting and painting to process metals to specified lengths, widths and shapes pursuant to specific customer orders. Cutting-to-length involves cutting metal along the width of the coil. Slitting involves cutting metal to specified widths along the length of the coil. Shearing is the process of cutting sheet metal. Blanking cuts the metal into specific shapes with close tolerances. Tempering improves the uniformity of the thickness and flatness of the metals through a cold rolling process. Plate and laser processing is the process of cutting metal into specific shapes and sizes. Our forming activities include bending metal. Our machining activities include drilling, milling, tapping, boring and sawing. Tube processing includes tube bending and end finishing. Finishing activities include shot blasting, grinding, edging and polishing. Our fabrication activities include machining, welding, assembly and painting of component parts.

Commencing with 2015, the flat products segment has been separated into two reportable segments; carbon flat products and specialty metals flat products. The flat products segments' assets and resources are shared by the carbon and specialty metals segments and both segments' products are, in some instances, stored in the shared facilities and processed on the shared equipment.

Edgar Filing: OLYMPIC STEEL INC - Form 10-K

The following table sets forth, as of December 31, 2016, the major pieces of processing equipment in operation by segment:

| Processing Equipment | Consolidated | Tubular  | Total |
|----------------------|--------------|----------|-------|
|                      | Flat         | and Pipe |       |
|                      | Products     | Products |       |
| Tempering            | 3            | -        | 3     |
| Stretcher-leveling   | 2            | -        | 2     |
| Cutting-to-length    | 12           | 12       | 24    |
| Slitting             | 10           | -        | 10    |
| Shearing             | 11           | -        | 11    |
| Blanking             | 4            | -        | 4     |
| Plate processing     | 26           | -        | 26    |
| Laser processing     | 27           | 8        | 35    |
| Forming              | 18           | -        | 18    |
| Machining            | 53           | 84       | 137   |
| Painting             | 3            | 1        | 4     |
| Tube processing      | 2            | 39       | 41    |
| Finishing            | 29           | 3        | 32    |
| Total                | 200          | 147      | 347   |

Our quality assurance system, led by certified specialists and engineers, establishes controls and procedures covering all aspects of our products from the time the material is ordered through receipt, processing and shipment to the customer. These controls and procedures encompass periodic supplier and customer audits, workshops with customers, inspection equipment and criteria, preventative actions, traceability and certification. We have quality testing labs at several of our facilities, as well as adjacent to our temper mill facilities in Cleveland, Ohio and Bettendorf, Iowa.

In addition, 25 of our facilities have earned International Organization for Standardization (ISO) 9001:2008 certifications. Our Detroit operation is also TS-16949 certified. CTI has earned The American Society of Mechanical Engineers S Certification and The National Board of Boiler & Pressure Vessel Inspectors R Certification. Our office building in Winder, Georgia has received Leadership in Energy and Environmental Design (LEED) certification.

## Customers and Distribution

We have a diverse customer and geographic base, which helps to reduce the inherent risk and cyclicity of our business. Net sales to our top three customers, in the aggregate, approximated 8.9%, 11.6% and 11.1% of our consolidated net sales in 2016, 2015 and 2014, respectively. We serve customers in metals consuming industries, including manufacturers and fabricators of transportation and material handling lift equipment, construction, mining and farm equipment, storage tanks, environmental and energy generation equipment, automobiles, food service and electrical equipment, military vehicles and equipment, as well as general and plate fabricators and metals service centers. The table below shows the percentage of our consolidated net sales to the largest industries for the past three years.

| <b>Industry</b>  | <b>2016</b> | <b>2015</b> | <b>2014</b> |
|--|-------------|-------------|-------------|
| Industrial machinery and equipment manufacturers and their fabricators | 51.3%       | 49.4%       | 50.6%       |
| Automobile manufacturers and their suppliers                           | 9.8%        | 9.6%        | 7.9%        |
| Metals service centers   | 9.7%        | 7.2%        | 9.1%        |
| Residential and commercial construction                                | 8.3%        | 10.2%       | 8.2%        |
| Transportation equipment manufacturers                                 | 6.4%        | 7.1%        | 5.6%        |
| All others <5%   | 14.5%       | 16.5%       | 18.6%       |

While we ship products throughout the United States, most of our customers are located in the midwestern, eastern and southern regions of the United States. Most customers are located within a 250-mile radius of one of our processing facilities, thus enabling an efficient delivery system capable of handling a high frequency of short lead time orders. We transport our products directly to customers via our in-house truck fleet, which further supports the just-in-time delivery requirements of our customers, and third-party trucking firms. Products sold to foreign customers, which have been immaterial to our consolidated results, are shipped either directly from metals producers

to the customer or to an intermediate processor, and then to the customer by rail, truck or ocean carrier. Through our facility in Monterrey, Mexico, we are able to stock material and service our customers in that country with shorter lead times.

We process our metals to specific customer orders as well as for stocking programs. Many of our larger customers commit to purchase on a regular basis at agreed upon or indexed prices for periods ranging from three to twelve months. To help mitigate price volatility risks, these price commitments are generally matched with corresponding supply arrangements, or to a lesser degree by commodities hedging. Customers notify us of specific release dates as processed products are required. Customers typically notify us of release dates anywhere from a just-in-time basis to one month before the release date. Therefore, we are required to carry sufficient inventory to meet the short lead time and just-in-time delivery requirements of our customers. CTI produces pressure parts and other fabricated components primarily for industrial boiler applications representing 1.7% of consolidated net sales in 2016. These products typically take several months to produce due to their size and complexity. Due to the time required for production, we may require progress payments throughout the construction period.

The current global economic environment has resulted in increased supply chain scrutiny by our customers and potential customers. We believe our size, geographic footprint, financial position, and our focus on quality and customer service are advantageous in maintaining our customer base and in securing new customers.

## **Raw Materials**

Our principal raw materials are carbon, coated and stainless steel and aluminum, in the forms of pipe and tube, flat rolled sheet, coil and plate that we typically purchase from multiple primary metals producers. The metals industry as a whole is cyclical and at times pricing and availability of material can be volatile due to numerous factors beyond our control, including general domestic and global economic conditions, domestic and global supply and demand imbalance, competition, lead times from metals producers, fluctuations in the costs of raw materials necessary to produce metals, import duties and tariffs and currency exchange rates. This volatility can significantly affect the availability and cost of raw materials for us.

Inventory management is a key profitability driver in the metals service center industry. We, like many other metals service centers, maintain substantial inventories of metals to accommodate the short lead times and just-in-time delivery requirements of our customers. Accordingly, we purchase metals in an effort to maintain our inventory at levels that we believe to be appropriate to satisfy the anticipated needs of our customers based upon historic buying practices, purchase commitments with customers and market conditions.

Our commitments to purchase metals are generally at prevailing market prices in effect at the time we place our orders. During the past three years, we have entered into pass through nickel and carbon swaps at the request of our customers in order to mitigate our customers' risk of volatility in the price of metals. The swaps are settled with the brokers at maturity and the economic benefit or loss arising from the changes in fair value of the swaps is contractually passed through to the customer. During 2014, we entered into cash flow metals hedges to mitigate our risk of volatility in the price of metals. The cash flow hedges were settled with the brokers at maturity and the economic benefit or loss arising from the changes in fair value of the hedges was recorded to "Cost of Materials Sold" in the Consolidated Statements of Comprehensive Income. All of the metals cash flow hedges settled during 2015, and we have no outstanding metals cash flow hedges as of December 31, 2016.

We have no long-term, fixed-price metals purchase contracts, except for commodity hedges. When metals prices decline, customer demands for lower prices and our competitors' responses to those demands could result in lower sale prices and, consequently, lower gross profits and earnings as we use existing metals inventory. When metals prices increase, competitive conditions will influence how much of the price increase we can pass on to our customers.

## **Suppliers**



We concentrate on developing supply relationships with high-quality domestic and international metals producers, using a coordinated effort to be the customer of choice for business critical suppliers. We employ sourcing strategies that maximize the quality, production lead times and transportation economies of a global supply base. We are an important customer of flat-rolled coil and plate, pipe and tube for many of our principal suppliers, but we are not dependent on any one supplier. We purchase in bulk from metals producers in quantities that are efficient for such producers. This enables us to maintain a continued source of supply at what we believe to be competitive prices. We believe the access to our facilities and equipment, and our high quality customer services and solutions, combined with our long-standing and continuous prompt pay practices, will continue to be an important factor in maintaining strong relationships with metals suppliers.

The metals producing supply base has experienced significant consolidation, with a few suppliers accounting for a majority of the domestic carbon steel market. We purchased approximately 54% and 51% of our total metals requirements from our three largest suppliers in 2016 and 2015, respectively. Although we have no long-term supply commitments, we believe we have good relationships with our metals suppliers. If, in the future, we are unable to obtain sufficient amounts of metals on a timely basis, we may not be able to obtain metals from alternate sources at competitive prices. In addition, interruptions or reductions in our supply of metals could make it difficult to satisfy our customers' just-in-time delivery requirements, which could have a material adverse effect on our business, financial condition, results of operations and cash flows.

## **Competition**

Our principal markets are highly competitive. We compete with other regional and national metals service centers, single location service centers and, to a certain degree, metals producers and intermediate metals processors on a regional basis. We have different competitors for each of our products and within each region. We compete on the basis of price, product selection and availability, customer service, value-added capabilities, quality, financial strength and geographic proximity. Certain of our competitors have greater financial and operating resources than we have.

With the exception of certain Canadian or Mexican operations, foreign-located metals service centers are generally not a material competitive factor in our principal domestic markets.

## Management Information Systems

Information systems are an important component of our strategy. We have invested in technologies and human resources as a foundation for growth. We depend on our Enterprise Resource Planning (ERP) systems for financial reporting, management decision-making, inventory management, order tracking and fulfillment and production optimization. We continue to upgrade and consolidate our systems for optimal use of resources and to assure we are taking advantage of technology offerings.

Our information systems focus on the following core application areas:

*Inventory Management.* Our information systems track the status and cost of inventories by product, location and process on a daily basis. This information is essential to optimize management of inventory.

*Differentiated Services To Customers.* Our information systems support value-added services to customers, including quality control and on-time delivery monitoring and reporting, just-in-time inventory management and shipping services.

*E-Commerce and Advanced Customer Interaction.* We are actively participating in electronic commerce initiatives to reduce processing cost and time. In addition to full electronic data interchange (EDI) capabilities with our customers and vendors, we also have implemented extranet sites for specific customers which are integrated with our internal business systems.

*System and Process Enhancements.* We have completed development of business system solutions to replace our legacy information systems and have successfully implemented new ERP systems at most of our locations and have decommissioned three legacy systems as of December 31, 2016. We continue to implement these new systems to provide standardized business processes, enhanced inventory management, production cost, and sales administrative controls, and reduced technical support requirements. Our business analysts work with our quality team to identify opportunities for efficiency and improved customer service. We collaborate across the metal supply chain, working with metals producers, service providers, customers, and industry-sponsored organizations to develop industry processing standards to drive cost out of the supply chain.

Information security and continuous availability of information processing are of highest priority. Our information professionals employ proven security and monitoring practices and tools. In case of physical emergency or threat, our new ERP systems, accounting systems, internet and communications systems are duplicated at a secure off-site

computing facility or through secure, multi-site cloud providers, with migration of our other systems which are in progress.

## Employees

At December 31, 2016, we employed approximately 1,660 people. Approximately 280 of the hourly plant personnel are represented by nine separate collective bargaining units. The table below shows the expiration dates of the collective bargaining agreements.

| <b>Facility</b>              | <b>Expiration date</b> |
|------------------------------|------------------------|
| Minneapolis plate, Minnesota | March 31, 2017         |
| Detroit, Michigan            | August 31, 2017        |
| Duluth, Minnesota            | December 21, 2017      |
| St. Paul, Minnesota          | May 25, 2018           |
| Milan, Illinois              | August 12, 2018        |
| Locust, North Carolina       | March 4, 2020          |
| Romeoville, Illinois         | May 31, 2020           |
| Minneapolis coil, Minnesota  | September 30, 2020     |
| Indianapolis, Indiana        | January 29, 2021       |

We have never experienced a work stoppage and we believe that our relationship with employees is good. However, any prolonged work stoppages by our personnel represented by collective bargaining units could have a material adverse impact on our business, financial condition, results of operations and cash flows.

## Service Marks, Trade Names and Patents

We conduct our business under the name “Olympic Steel.” A provision of federal law grants exclusive rights to the word “Olympic” to the U.S. Olympic Committee. The U.S. Supreme Court has recognized, however, that certain users may continue to use the word based on long-term and continuous use. We have used the name Olympic Steel since 1954, but are prevented from registering the name “Olympic” and from being qualified to do business as a foreign corporation under that name in certain states. In such states, we have registered under different names, including “Oly Steel” and “Olympia Steel.” Our wholly-owned subsidiary, Olympic Steel Lafayette, Inc., does business in certain states under the names “Olympic Steel Detroit,” “Lafayette Steel and Processing” and “Lafayette Steel.” Our wholly-owned subsidiary, Olympic Steel Iowa, Inc. does business in certain states under the name “Oly Steel Iowa, Inc.”. Our North Carolina operation conducts business under the name “Olympic Steel North Carolina.” Our Integrity Stainless operation conducts business under the name “Integrity Stainless”. Our CTI North Carolina operation conducts business under the name “CTI Power.” Our operation in Monterrey, Mexico operates under the name “Metales de Olympic S. de.R.L. de C.V.”

We also hold a trademark for our stainless steel sheet and plate product “OLY-FLATBRITE,” which has a unique combination of surface finish and flatness.

### **Government Regulation**

Our operations are governed by many laws and regulations, including those relating to workplace safety and worker health, principally the Occupational Safety and Health Act and regulations thereunder. We believe that we are in material compliance with these laws and regulations and do not believe that future compliance with such laws and regulations will have a material adverse effect on our business, financial condition, results of operations and cash flows.

### **Environmental**

Our facilities are subject to certain federal, state and local requirements relating to the protection of the environment. We believe that we are in material compliance with all environmental laws, do not anticipate any material expenditures to meet environmental requirements and do not believe that compliance with such laws and regulations will have a material adverse effect on our business, financial condition, results of operations and cash flows.

### **Seasonality**

Seasonal factors may cause demand fluctuations within the year which could impact our results of operations. Typically, demand in the first half of the year is stronger than the second half of the year, as it contains more ship days and is not impacted by the seasonal shut-downs in July, November and December due to holidays.

## **Effects of Inflation**

Inflation generally affects us by increasing the cost of employee wages and benefits, transportation services, processing equipment, purchased metals, energy and borrowings under our credit facility. General inflation has not had a material effect on our financial results during the past three years.

## **Backlog**

Because we conduct our operations generally on the basis of short-term orders, we do not believe that backlog is a material or meaningful indicator of future performance.

## **Available Information**

We file annual, quarterly, and current reports, proxy statements, and other documents with the SEC under the Securities Exchange Act of 1934. The public may read and copy any materials filed with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Also, the SEC maintains an Internet website that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The public can obtain any documents that are filed by the Company at <http://www.sec.gov>.

In addition, our annual reports on Form 10-K, as well as our quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to all of the foregoing reports, are made available free of charge on or through the "Investor Relations" section of our website at [www.olysteel.com](http://www.olysteel.com) as soon as reasonably practicable after such reports are electronically filed with or furnished to the SEC.

Information relating to our corporate governance at Olympic Steel, including our Business Ethics Policy, information concerning our executive officers, directors and Board committees (including committee charters), and transactions in our securities by directors and officers, is available free of charge on or through the "Investor Relations" section of our website at [www.olysteel.com](http://www.olysteel.com). We are not including the information on our website as a part of, or incorporating it by reference into, this Annual Report on Form 10-K.



## Forward-Looking Information

This Annual Report on Form 10-K and other documents we file with the SEC contain various forward-looking statements that are based on current expectations, estimates, forecasts and projections about our future performance, business, our beliefs and our management's assumptions. In addition, we, or others on our behalf, may make forward-looking statements in press releases or written statements, or in our communications and discussions with investors and analysts in the normal course of business through meetings, conferences, webcasts, phone calls and conference calls. Words such as "may," "will," "anticipate," "should," "intend," "expect," "believe," "estimate," "project," "plan" and "continue," as well as the negative of these terms or similar expressions are intended to identify forward-looking statements, which are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements are subject to certain risks and uncertainties that could cause our actual results to differ materially from those implied by such statements including, but not limited to, those set forth in Item 1A (Risk Factors) below and the following:

- general and global business, economic, financial and political conditions;
- competitive factors such as the availability, global production levels and pricing of metals, industry shipping and inventory levels and rapid fluctuations in customer demand and metals pricing;
- cyclicality and volatility within the metals industry;
- the strengthening of the U.S. dollar and the related impact on foreign steel pricing, U.S. exports, and foreign imports to the United States;
- the levels of imported steel in the United States and any associated tariffs and duties;
- the availability and costs of transportation and logistical services;
- the successes of our strategic efforts and initiatives to increase sales volumes, maintain or improve working capital turnover and free cash flows, improve our customer service, and achieve cost savings, including our internal program to improve earnings;
- our ability to generate free cash flow through operations and repay debt within anticipated time frames;
- events or circumstances that could impair or adversely impact the carrying value of any of our assets;
- risks and uncertainties associated with intangible assets, including additional impairment charges related to indefinite lived intangible assets;
- events or circumstances that could adversely impact the successful operation of our processing equipment and operations;
- the amounts, successes and our ability to continue our capital investments and strategic growth initiatives, including our business information system implementations;
- the successes of our operational initiatives to improve our operating, cultural and management systems and reduce our costs;
- the ability to comply with the terms of our asset-based credit facility;
- the ability of our customers and third parties to honor their agreements related to derivative instruments;
- customer, supplier and competitor consolidation, bankruptcy or insolvency;
- reduced production schedules, layoffs or work stoppages by our own, our suppliers' or customers' personnel;
- the impacts of union organizing activities and the success of union contract renewals;
- the timing and outcomes of inventory lower of cost or market adjustments and last-in, first-out, or LIFO, income, especially during periods of declining market pricing;
- the ability of our customers (especially those that may be highly leveraged, and those with inadequate liquidity) to maintain their credit availability;



the inflation or deflation existing within the metals industry, as well as our product mix and inventory levels on hand, which can impact our cost of materials sold as a result of the fluctuations in the LIFO inventory valuation;  
the adequacy of our existing information technology and business system software, including duplication and security processes;  
the adequacy of our efforts to mitigate cyber security risks and threats;  
access to capital and global credit markets;  
our ability to pay regular quarterly cash dividends and the amounts and timing of any future dividends;  
our ability to repurchase shares of our common stock and the amounts and timing of repurchases, if any;  
unanticipated developments that could occur with respect to contingencies such as litigation, arbitration and environmental matters, including any developments that would require any increase in our costs for such contingencies; and  
changes in laws or regulations or the manner of their interpretation or enforcement could impact our financial performance and restrict our ability to operate our business or execute our strategies.

Should one or more of these or other risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, intended, expected, believed, estimated, projected or planned. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We undertake no obligation to republish revised forward-looking statements to reflect the occurrence of unanticipated events or circumstances after the date hereof, except as otherwise required by law.

## ITEM 1A. RISK FACTORS

*In addition to the other information in this Annual Report on Form 10-K and our other filings with the SEC, the following risk factors should be carefully considered in evaluating us and our business before investing in our common stock. The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties, not presently known to us or otherwise, may also impair our business. If any of the risks actually occur, our business, financial condition or results of operations could be materially and adversely affected. In that case, the trading price of our common stock could decline, and investors may lose all or part of their investment.*

### Risks Related to our Business

**Volatile metals prices can cause significant fluctuations in our operating results. Our sales and operating income could decrease if metals prices decline or if we are unable to pass producer price increases on to our customers.**

Our principal raw materials are carbon and stainless steel and aluminum flat rolled coil, sheet, plate, pipe and tube that we typically purchase from multiple primary metals producers. The metals industry as a whole is cyclical and, at times, pricing and availability of metals can be volatile due to numerous factors beyond our control, including general domestic and international economic conditions, sales levels, competition, levels of inventory held by other metals service centers, producer lead times, higher raw material costs for the producers of metals, imports, import duties and tariffs and currency exchange rates. This volatility can significantly affect the availability and cost of raw materials for us.

We, like many other metals service centers, maintain substantial inventories of metals to accommodate the short lead times and just-in-time delivery requirements of our customers. Accordingly, we purchase metals in an effort to maintain our inventory at levels that we believe to be appropriate to satisfy the anticipated needs of our customers based upon historic buying practices, supply agreements with customers and market conditions. Our commitments to purchase metals are generally at prevailing market prices in effect at the time we place our orders. We entered into metals hedges, which carry counterparty performance risk, in order to mitigate our risk of volatility in the price of metals. We have no long-term, fixed-price metals purchase contracts, except for metals hedges. Declining metals prices, customer demand for lower prices and our competitors' responses to those demands could result in lower sale prices and, consequently, lower gross profits and potentially inventory lower of cost or market adjustments as we use existing inventory. Significant or rapid declines in metals prices or reductions in sales volumes could adversely impact our ability to remain in compliance with certain financial covenants in our revolving credit facility, as well as result in us incurring inventory or asset impairment charges. When metals prices increase, competitive conditions will influence how much of the price increase we can pass on to our customers. To the extent we are unable to pass on future price increases in our raw materials to our customers, the net sales and profitability of our business could be adversely affected. Changing metals prices therefore could significantly impact our net sales, gross profit, operating

income and net income, and could impair or adversely impact the carrying value of any of our assets.

China is the world's largest producer and consumer of metals and metals products. Its expansion of metals production has significantly affected the global metals industry. The recent economic downturn in China, the slowing of its growth and decreased metals consumption has led to an increased supply of metals in the United States, which result in lower prices for our products. Actions by domestic and foreign producers, including metals companies in China, to further increase production could result in an increased supply of metals in the United States, which could result in lower prices for our products. A decline in metals prices could adversely affect our sales, gross profits and profitability.

**We service industries that are highly cyclical, and any downturn in our customers' demand could reduce our sales, gross profits and profitability.**

We sell our products in a variety of industries, including capital equipment manufacturers for industrial, agricultural and construction use, the automotive industry, the utilities industry, and manufacturers of fabricated metals products. Numerous factors, such as general economic conditions, strengthening of the US dollar, government stimulus or regulation, availability of adequate credit and financing, consumer confidence, significant business interruptions, labor shortages or work stoppages, energy prices, seasonality, customer inventory levels and other factors beyond our control, may cause significant demand fluctuations from one or more of these industries. Any decrease in demand within one or more of these industries may be significant and may last for a lengthy period of time. In periods of economic slowdown or recession in the United States, excess customer or service center inventory or a decrease in the prices that we can realize from sales of our products to customers in any of these industries could result in lower sales, gross profits and profitability.

Approximately 51.3% of our 2016 consolidated net sales were to industrial machinery and equipment manufacturers and their fabrications. Due to the concentration of customers in the industrial machinery and equipment industry, a decline in production levels in that industry could result in lower sales, gross profits and profitability. Approximately 9.8% of our 2016 consolidated net sales were to automotive manufacturers or manufacturers of automotive components and parts, whom we refer to as automotive customers. Historically, due to the concentration of customers in the automotive industry, our gross profits on these sales have generally been less than our gross profits on sales to customers in other industries.

**We may not be able to retain or expand our customer base if the U.S. manufacturing industry erodes or if the U.S. dollar continues to strengthen.**

Our customer base primarily includes manufacturing and industrial firms in the United States, some of which are, or have considered, relocating production operations outside the United States or outsourcing particular functions outside the United States. Some customers have closed because they were unable to compete successfully with foreign competitors. Our facilities are primarily located in the United States and, therefore, to the extent that our customers relocate or move operations where we do not have a presence, we could lose their business.

Some customers have historically manufactured products in the United States for export to foreign markets. As the U.S. dollar has strengthened, products made by U.S. manufacturers have become less attractive to foreign buyers. Fewer purchases by foreign buyers reduces our metals sales to those U.S. manufacturers and adversely affects our sales and results of operations.

**Our success is dependent upon our relationships with certain key customers.**

We have derived and expect to continue to derive a significant portion of our revenues from a relatively limited number of customers. Collectively, our top three customers accounted for approximately 8.9% and 11.6% of our consolidated net sales in 2016 and 2015, respectively. Many of our larger customers commit to purchase on a regular basis at agreed upon prices over periods from three to twelve months. We generally do not have long-term contracts with our customers. As a result, the relationship, as well as particular orders, can generally be terminated with relatively little advance notice. The loss of any one of our major customers or decrease in demand by those customers or credit constraints placed on them could have a material adverse effect on our business, our results of operations and our cash flows.

**An interruption in the sources of our metals supply could have a material adverse effect on our results of operations.**

In recent years, the metals producing supply base has experienced significant consolidation with a few domestic producers accounting for a majority of the domestic metals market. Collectively, we purchased approximately 54% and 51% of our total metals requirements from our three largest suppliers in 2016 and 2015, respectively. The number of available suppliers could be reduced in the future by factors such as further industry consolidation or bankruptcies affecting metals suppliers. Additionally, fewer available suppliers increases the risk of supply disruption through both scheduled and unscheduled supplier outages. We have no long-term supply commitments with our metals suppliers. If, in the future, we are unable to obtain sufficient amounts of metals on a timely basis, we may not be able to obtain metals from alternate sources at competitive prices. In addition, interruptions or reductions in our supply of metals could make it difficult to satisfy our customers' just-in-time delivery requirements, which could have a material adverse effect on our business, financial condition, results of operations and cash flows.

Conversely, the addition of new mill sources and decreased domestic demand could lead to domestic over capacity, which could lead to a decrease in steel prices.

**We depend, in part, on third parties for transportation services, and increases in costs or the availability of transportation could adversely affect our business and operations.**

We ship products throughout the United States via our in-house truck fleet or by third-party trucking firms. Products sold to foreign customers are shipped either directly from metals producers to the customer or to an intermediate processor, and then to the customer by rail, truck or ocean carrier. Our business depends on the transportation of a large number of products. We depend to a certain extent on third parties for transportation of our products as well as delivery of our raw materials.

If any of these providers were to fail to deliver raw materials to us in a timely manner, we may be unable to process and deliver our products in response to customer demand. In addition, if any of these third parties were to cease operations or cease doing business with us, we may be unable to replace them at a reasonable cost. In addition, such failure of a third-party transportation provider could harm our reputation, negatively affect our customer relationships and have a material adverse effect on our financial position and results of operations.

**Our implementation of new information systems could adversely affect our results of operations and cash flows.**

We are in the process of implementing new information systems and eliminating our legacy operating systems. The objective is to standardize and streamline business processes and improve support for our service center and fabrication business. Risks associated with the phased implementation include, but are not limited to:

- a significant deployment of capital and a significant use of management and employee time;
- the possibility that software and implementation vendors may not be able to support the project as planned;
- the possibility that the timelines, costs or complexities related to the new system implementation will be greater than expected;
- the possibility that the software, once fully implemented, does not function as planned;
- the possibility that benefits from the new systems may be less or take longer to realize than expected;
- the possibility that disruptions from the implementation may make it difficult for us to maintain relationships with our customers, employees or suppliers; and
- limitations on the availability and adequacy of proprietary software or consulting, training and project management services, as well as our ability to retain key personnel.

Although we have successfully initiated use of the new systems at most of our locations, we can provide no assurance that the rollout to the remaining locations will be successful or will occur as planned and without disruption to

operations. Difficulties associated with the design and implementation of new information systems could adversely affect our business, our customer service, our results of operations and our cash flows.

**The failure of our key computer-based systems could have a material adverse effect on our business.**

Until our new systems implementations are completed, we maintain separate regional legacy computer-based systems in the operation of our business and we depend on these systems to a significant degree, particularly for inventory management. These systems are vulnerable to, among other things, damage or interruption from fire, flood, tornado and other natural disasters, power loss, computer system and network failures, operator negligence, physical and electronic loss of data or security breaches and computer viruses. Although we have secure back-up systems off-site, the destruction or failure of any one of our computer-based systems for any significant period of time could materially adversely affect our business, financial condition, results of operations and cash flows.

**Risks associated with our growth strategy may adversely impact our ability to sustain our growth.**

Historically, we have grown internally by increasing sales and services to our existing customers, aggressively pursuing new customers and services, building or purchasing new facilities and acquiring and upgrading processing equipment in order to expand the range of customer services and products that we offer. In addition, we have grown through the acquisition of other service centers and related businesses. We intend to actively pursue our growth strategy in the future.

We have completed a number of expansion projects since 2010. Future expansion or construction projects, could have adverse effects on our results of operations due to the impact of the associated start-up costs and the potential for underutilization in the start-up phase of a facility. While we are pursuing potential acquisition targets, we are unable to predict whether or when any prospective acquisition candidate will become available or the likelihood that any acquisition will be completed. Moreover, in pursuing acquisition opportunities, we may compete for acquisition targets with other companies with similar growth strategies that may be larger and have greater financial and other resources than we have. Competition among potential acquirers could result in increased prices for acquisition targets. As a result, we may not be able to consummate acquisitions on satisfactory terms to us, or at all.

The pursuit of acquisitions and other growth initiatives may divert management's time and attention away from day-to-day operations. In order to achieve growth through acquisitions, expansion of current facilities, greenfield construction or otherwise, additional funding sources may be needed and we may not be able to obtain the additional capital necessary to pursue our growth strategy on terms that are satisfactory to us, or at all.

**We depend on our senior management team and the loss of any member could prevent us from implementing our business strategy.**

Our success is dependent upon the management and leadership skills of our senior management team. We have employment agreements, which include non-competition provisions, with our Chief Executive Officer, our President, the President of CTI, our Executive Vice President and Chief Operating Officer and our Chief Financial Officer that expire on January 1, 2018, December 31, 2020, June 30, 2021, July 1, 2020 and January 1, 2021, respectively. The loss of any member of our senior management team or the failure to attract and retain additional qualified personnel could prevent us from implementing our business strategy.

**We may not achieve the expected results of our profit improvement programs or operational initiatives.**

The profit improvement programs initiated in 2015 to reduce operating expenses and enhance margins included eliminating certain leased properties, lowering transportation, labor and personnel expenses, centralization of certain administrative functions, as well as inventory and purchasing initiatives.

In addition, our operational initiatives are designed to improve efficiencies and lower our costs. The initiatives are focused on continuously improving processes through waste and variation elimination using Lean Six Sigma tools and



employee certifications. The risks associated with these initiatives include, but are not limited to:

- a significant use of management and employee time;
- the possibility that the initiatives do not meet expectations; and
- the possibility that the initiatives do not provide the expected or sustained economic results.

Difficulties associated with executing our profit improvement plan and operational initiatives could adversely affect our business, our customer service, our results of operations and our cash flows.

**Processing equipment investments at our existing locations may be unable to achieve expected results, and events or circumstances that could adversely impact the successful operation of new processing equipment and operations could have a material adverse effect on our results of operations.**

We continue to invest in processing equipment to support customer demand. Although we have successfully installed new and used processing equipment in the past, we can provide no assurance that future installations will be successful, or achieve expected results. Risks associated with the installations include, but are not limited to:

- a significant use of management and employee time;
- the possibility that the performance of the equipment does not meet expectations; and
- the possibility that disruptions from the installations may make it difficult for us to maintain relationships with our respective customers, employees or suppliers.

Difficulties associated with the installation of new processing equipment could adversely affect our business, our customer service, our results of operations and our cash flows.

**Customer and third-party credit constraints and credit losses could have a material adverse effect on our results of operations.**

Some of our customers may experience difficulty obtaining and/or maintaining credit availability. In particular, certain customers that are highly leveraged represent an increased credit risk. Some customers have reduced their purchases because of these credit constraints. Moreover, our disciplined credit policies have, in some instances, resulted in lost sales. If we have misjudged our credit estimations and they result in future credit losses, lost sales or lost customers, there could be a material adverse effect on our business, financial condition, results of operations, cash flows and our allowance for doubtful accounts.

**Although we expect to finance our growth initiatives through borrowings under our credit facility, we may have to find additional sources of funding, which could be difficult. Additionally, increased leverage and borrowing rates could adversely impact our business and results of operations.**

We expect to finance our growth initiatives through borrowings under our credit facility, which matures on June 30, 2019. However, our credit facility may not be sufficient or available to finance our growth initiatives, and we may have to find additional sources of financing. It may be difficult for us in the future to obtain the necessary funds and liquidity to run and expand our business.

The borrowings under our credit facility are primarily at variable interest rates. If interest rates in the future were to increase 100 basis points (1.0%) from December 31, 2016 rates and, assuming no change in total debt from December 31, 2016 levels, the additional annual interest expense to us would be approximately \$1.6 million.

**Our information technology systems could be negatively affected by cyber security threats.**

Increased global information technology security requirements, vulnerabilities, threats and a rise in sophisticated and targeted computer crime pose a risk to the security of our systems, networks and the confidentiality, availability and integrity of our data. Despite our efforts to protect sensitive information and confidential and personal data, our facilities and systems and those of our third-party service providers may be vulnerable to security breaches. This could lead to disclosure, modification or destruction of proprietary and other key information, production downtimes and operational disruptions, which in turn could adversely affect our results of operations. We may face greater risks in this area than our competitors as we implement the ERP system because among other things, we must simultaneously

protect both the ERP and legacy systems until the ERP project is complete.

**Labor disruptions at any of our facilities or those of major customers could adversely affect our business, results of operations and financial condition.**

At December 31, 2016, we employed approximately 1,660 people. Approximately 280 of the hourly plant personnel are represented by nine separate collective bargaining units. Any prolonged work stoppages by our personnel represented by collective bargaining units could have a material adverse impact on our business, financial condition, results of operations and cash flows.

In addition, many of our larger customers, including those in the automotive industry, have unionized workforces and some have experienced significant labor disruptions in the past such as work stoppages, slow-downs and strikes. A labor disruption at one or more of our major customers could interrupt production or sales by that customer and cause that customer to halt or limit orders for our products. Any such reduction in the demand for our products could adversely affect our business, financial condition, results of operations and cash flows.

**Our business is highly competitive, and increased competition could reduce our market share and harm our financial performance.**

Our business is highly competitive. We compete with metals service centers and, to a certain degree, metals producers and intermediate metals processors, on a regular basis, primarily on quality, price, inventory availability and the ability to meet the delivery schedules and service requirements of our customers. We have different competitors for each of our products and within each region. Certain of these competitors have financial and operating resources in excess of ours. Increased competition could lower our gross profits or reduce our market share and have a material adverse effect on our financial performance.

**Impairment in the carrying value of intangible assets could result in the incurrence of impairment charges and negatively impact our results of operations.**

The net carrying value of intangibles represents trade names and customer relationships, net of accumulated amortization, related to our tubular and pipe products segment. Indefinitely lived assets are evaluated for impairment annually or whenever events or changes in circumstance indicate that the carrying amounts of these assets may not be recoverable. Amortizable intangible assets are evaluated for impairment whenever events or changes in circumstance indicate that the carrying amounts of these assets may not be recoverable. Impairments to intangible assets may be caused by factors outside our control, such as increased competitive pricing pressures, lower than expected revenue and profit growth rates, changes in discount rates based on changes in the cost of capital (interest rates, etc.), or the loss of a significant customer and could result in the incurrence of impairment charges and negatively impact our results of operations.

**Increases in energy prices would increase our operating costs, and we may be unable to pass all these increases on to our customers in the form of higher prices.**

If our energy costs increase disproportionately to our revenues, our earnings could be reduced. We use energy to process and transport our products. Our operating costs increase if energy costs, including electricity, diesel fuel and natural gas, rise. During periods of higher energy costs, we may not be able to recover our operating cost increases through price increases without reducing demand for our products. In addition, we generally do not hedge our exposure to higher prices via energy futures contracts. Increases in energy and fuel prices will increase our operating costs and may reduce our profitability if we are unable to pass all of the increases on to our customers.

**Participation in multiemployer pension plans carry withdrawal liability risks which could impact our results of operations and financial condition.**

Through our CTI subsidiary, we contribute to one multiemployer pension plan. The risks of participating in the multiemployer plan are different from a single-employer plan in that 1) assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers, 2) if a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers, and 3) if CTI chooses to stop participating in the multiemployer plan, CTI may be required to pay the plan an amount based on the unfunded status of the plan, referred to as a withdrawal liability.

**We are subject to significant environmental, health and safety laws and regulations and related compliance expenditures and liabilities.**

Our businesses are subject to many federal, state and local environmental, health and safety laws and regulations, particularly with respect to the use, handling, treatment, and disposal of substances and waste used or generated in our manufacturing processes. We have incurred and expect to continue to incur expenditures to comply with applicable environmental laws and regulations. Our failure to comply with applicable environmental laws and regulations and permit requirements could result in civil or criminal fines or penalties or enforcement actions, including regulatory or judicial orders enjoining or curtailing operations or requiring corrective measures, installation of pollution control equipment or remedial actions.

We may in the future be required to incur costs relating to the investigation or remediation of property, and for addressing environmental conditions. Some environmental laws and regulations impose liability and responsibility on present and former owners, operators or users of facilities and sites for contamination at such facilities and sites without regard to causation or knowledge of contamination. Consequently, we cannot assure you that existing or future circumstances, the development of new facts or the failure of third parties to address contamination at current or former facilities or properties will not require significant expenditures by us.

We expect to continue to be subject to environmental and health and safety laws and regulations. It is difficult to predict the future interpretation and development of environmental and health and safety laws and regulations or their impact on our future earnings and operations. We anticipate that compliance will continue to require increased capital expenditures and operating costs. Any increase in these costs, or unanticipated liabilities arising for example, out of discovery of previously unknown conditions or more aggressive enforcement actions, could have a material adverse effect on our business, financial condition, results of operations and cash flows.

**Changes in laws or regulations or the manner of their interpretation or enforcement could adversely impact our financial performance and restrict our ability to operate our business or execute our strategies.**

New laws or regulations, or changes in existing laws or regulations, or the manner of their interpretation or enforcement, could increase our cost of doing business and restrict our ability to operate our business or execute our strategies. In particular, there may be significant changes in U.S. laws and regulations and existing international trade agreements by the new U.S. presidential administration that could affect a wide variety of industries and businesses, including those businesses we own and operate. It remains unclear what the new U.S. presidential administration will do, if anything, with respect to existing laws, regulations, or trade agreements. If the new U.S. presidential administration materially modifies U.S. laws and regulations and international trade agreements, our business, financial condition, and results of operations could be affected.

### **Risks Related to Our Common Stock**

**The market price for our common stock may be volatile.**

Historically, there has been volatility in the market price for our common stock. Furthermore, the market price of our common stock could fluctuate substantially in the future in response to a number of factors, including, but not limited to, the risk factors described herein. Examples include:

- changes in commodity prices, especially metals;
- changes in financial estimates or recommendations by stock market analysts regarding us or our competitors;
- the operating and stock performance of other companies that investors may deem comparable;
- developments affecting us, our customers or our suppliers;
- press releases, earnings releases or publicity relating to us or our competitors or relating to trends in the metals service center industry;
- inability to meet securities analysts' and investors' quarterly or annual estimates or targets of our performance;
- sales of our common stock by large shareholders;
- the amount of shares acquired for short-term investments;
- general domestic or international economic, market and political conditions;
- fluctuations in the value of the US dollar;
- changes in the legal or regulatory environment affecting our business; and
- announcements by us or our competitors of significant acquisitions, dispositions or joint ventures, or other material events impacting the domestic or global metals industry.

In the past, the stock market has experienced significant price and volume fluctuations. This volatility has had a significant effect on the market prices of securities issued by many companies for reasons unrelated to their specific operating performance. These factors may adversely affect the trading price of our common stock, regardless of actual operating performance.

In addition, stock markets from time to time experience extreme price and volume fluctuations that may be unrelated or disproportionate to the operating performance of companies. In the past, some shareholders have brought securities class action lawsuits against companies following periods of volatility in the market price of their securities. We may in the future be the target of similar litigation. Securities litigation, regardless of whether our defense is ultimately successful, could result in substantial costs and divert management's attention and resources.

**Our quarterly results may be volatile.**

Our operating results have varied on a quarterly basis during our operating history and are likely to fluctuate significantly in the future. Our operating results may be below the expectations of our investors or stock market analysts as a result of a variety of factors, many of which are outside of our control. Factors that may affect our quarterly operating results include, but are not limited to, the risk factors listed above.

Many factors could cause our revenues and operating results to vary significantly in the future. Accordingly, we believe that quarter-to-quarter comparisons of our operating results are not necessarily meaningful. Investors should not rely on the results of one quarter as an indication of our future performance. Further, it is our practice not to provide forward-looking sales or earnings guidance and not to endorse any analyst's sales or earnings estimates. Nonetheless, if our results of operations in any quarter do not meet analysts' expectations, our stock price could materially decrease.

**Certain provisions in our charter documents and Ohio law could delay or prevent a change in management or a takeover attempt that you may consider to be in your best interest.**

We are subject to Chapter 1704 of the Ohio Revised Code, which prohibits certain business combinations and transactions between an "issuing public corporation" and an "Ohio law interested shareholder" for at least three years after the Ohio law interested shareholder attains 10% ownership, unless the Board of Directors of the issuing public corporation approves the transaction before the Ohio law interest shareholder attains 10% ownership. We are also subject to Section 1701.831 of the Ohio Revised Code, which provides that certain notice and informational filings and special shareholder meeting and voting procedures must be followed prior to consummation of a proposed "control share acquisition." Assuming compliance with the notice and information filings prescribed by the statute, a proposed control share acquisition may be made only if the acquisition is approved by a majority of the voting power of the issuer represented at the meeting and at least a majority of the voting power remaining after excluding the combined voting power of the "interested shares."



Certain provisions contained in our Amended and Restated Articles of Incorporation and Amended and Restated Code of Regulations and Ohio law could delay or prevent the removal of directors and other management and could make a merger, tender offer or proxy contest involving us that you may consider to be in your best interest more difficult. For example, these provisions:

- allow our Board of Directors to issue preferred stock without shareholder approval;
- provide for our Board of Directors to be divided into two classes of directors serving staggered terms;
- limit who can call a special meeting of shareholders; and
- establish advance notice requirements for nomination for election to the Board of Directors or for proposing matters to be acted upon at shareholder meetings.

These provisions may discourage potential takeover attempts, discourage bids for our common stock at a premium over market price or adversely affect the market price of, and the voting and other rights of the holders of our common stock. These provisions could also discourage proxy contests and make it more difficult for you and other shareholders to elect directors other than the candidates nominated by our Board of Directors.

**Principal shareholders who own a significant numbers of shares of our common stock may have interests that conflict with yours.**

Michael D. Siegal, our Chief Executive Officer and Chairman of the Board and our largest shareholder, owned approximately 11.3% of our outstanding common stock as of December 31, 2016. Mr. Siegal may have the ability to significantly influence matters requiring shareholder approval. In deciding how to vote on such matters, Mr. Siegal may be influenced by interests that conflict with yours.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

22

---

**ITEM 2. PROPERTIES**

We believe that our properties are strategically situated relative to our domestic suppliers, our customers and each other, allowing us to support customers from multiple locations. Product is shipped from the most advantageous facility, regardless of where the customer order is taken. The facilities are located in the hubs of major metals consumption markets, and within a 250-mile radius of most of our customers, a distance approximating the one-day driving and delivery limit for truck shipments. During 2016, we terminated leases on certain warehouse facilities in Moses Lake, Washington and Roseville, Minnesota and gave notice to terminate the lease in Oklahoma City, Oklahoma in 2017.

The following table sets forth certain information concerning our principal properties including which segment's products are serviced out of each location:

| Operation           | Location                   | Square Feet | Function  | Owned or Leased | Segment |                  | Pipe and Tube |
|---------------------|----------------------------|-------------|---|-----------------|---------|------------------|---------------|
|                     |                            |             |   |                 | Carbon  | Specialty Metals |               |
| <b>Cleveland</b>    | Bedford Heights, Ohio (1)  | 127,000     | Corporate offices, coil processing and distribution center              | Owned           |         |                  |               |
|                     | Bedford Heights, Ohio (1)  | 121,500     | Coil and plate processing, distribution center and offices              | Owned           |         |                  |               |
|                     | Bedford Heights, Ohio (1)  | 59,500      | Plate processing, distribution center and offices                       | Leased (2)      |         |                  |               |
|                     | Dover, Ohio                | 62,000      | Plate processing, fabrication and distribution center                   | Owned           |         |                  |               |
| <b>Minneapolis</b>  | Plymouth, Minnesota        | 196,800     | Coil and plate processing, distribution center and offices              | Owned           |         |                  |               |
|                     | Plymouth, Minnesota        | 112,200     | Plate processing, fabrication, distribution center and offices          | Owned           |         |                  |               |
| <b>Chambersburg</b> | Chambersburg, Pennsylvania | 157,000     | Plate processing, distribution center and offices                       | Owned           |         |                  |               |
|                     | Chambersburg, Pennsylvania | 150,000     | Plate processing, fabrication, distribution center and offices          | Owned           |         |                  |               |
| <b>Iowa</b>         | Bettendorf, Iowa           | 244,000     | Coil and plate processing, fabrication, distribution center and offices | Owned           |         |                  |               |
|                     | Oklahoma City, Oklahoma    | 33,000      | Distribution center   | Leased (3)      |         |                  |               |
| <b>Winder</b>       | Winder, Georgia            | 285,000     |   | Owned           |         |                  |               |

Edgar Filing: OLYMPIC STEEL INC - Form 10-K

|                       |                               |         | Coil and plate processing,<br>fabrication, distribution center<br>and offices |            |
|-----------------------|-------------------------------|---------|---|------------|
| <b>Detroit</b>        | Detroit, Michigan             | 256,000 | Coil processing, distribution<br>center and offices                           | Owned      |
| <b>Kentucky</b>       | Mt. Sterling,<br>Kentucky     | 100,000 | Plate processing, fabrication<br>and distribution center                      | Owned      |
|                       | Mt. Sterling,<br>Kentucky     | 107,000 | Distribution center and offices   | Owned (4)  |
| <b>Gary</b>           | Gary, Indiana                 | 183,000 | Coil processing, distribution<br>center and offices                           | Owned      |
| <b>Connecticut</b>    | Milford,<br>Connecticut       | 134,000 | Coil processing, distribution<br>center and offices                           | Owned      |
| <b>Chicago</b>        | Schaumburg,<br>Illinois       | 80,500  | Coil and sheet processing,<br>distribution center and offices                 | Owned      |
| <b>North Carolina</b> | Siler City, North<br>Carolina | 74,000  | Plate processing, fabrication,<br>distribution center and offices             | Owned      |
| <b>Streetsboro</b>    | Streetsboro, Ohio             | 66,200  | Coil and sheet processing,<br>distribution center and offices                 | Owned      |
|                       | Latrobe,<br>Pennsylvania      | 43,200  | Coil and sheet processing,<br>distribution center                             | Leased (5) |
| <b>Washington</b>     | Moses Lake,<br>Washington     | 14,000  | Distribution center   | Leased (6) |
| <b>Mexico</b>         | Monterrey, Mexico             | 60,000  | Distribution center   | Leased (7) |

| Operation    | Location               | Square Feet | Function   | Owned or Leased | Segment |                  |               |
|--------------|------------------------|-------------|--|-----------------|---------|------------------|---------------|
|              |                        |             |  |                 | Carbon  | Specialty Metals | Pipe and Tube |
| Chicago      | Romeoville, Illinois   | 363,000     | Corporate offices, fabrication and distribution center | Owned           |         |                  |               |
| St. Paul     | St. Paul, Minnesota    | 132,000     | Distribution center and offices                        | Owned           |         |                  |               |
| Charlotte    | Locust, North Carolina | 127,600     | Distribution center, fabrication and offices           | Owned           |         |                  |               |
| Fond du Lac  | Fond du Lac, Wisconsin | 117,000     | Distribution center and offices                        | Owned           |         |                  |               |
| Indianapolis | Indianapolis, Indiana  | 79,000      | Distribution center and offices                        | Owned           |         |                  |               |
| Quad Cities  | Milan, Illinois        | 57,600      | Distribution center and offices                        | Owned           |         |                  |               |
| Des Moines   | Ankeny, Iowa           | 50,000      | Distribution center and offices                        | Owned           |         |                  |               |
| Duluth       | Proctor, Minnesota     | 45,202      | Distribution center and offices                        | Leased (8)      |         |                  |               |
| Owatonna     | Owatonna, Minnesota    | 23,000      | Production cutting center                              | Owned           |         |                  |               |

(1) The Bedford Heights facilities are all adjacent properties.

(2) This facility is leased from a related party. The lease expires on December 31, 2018, with renewal options.

(3) The lease on this facility expires on July 7, 2017.

(4) 50% of the facility is leased to an unrelated party whose lease expires on December 31, 2017.

(5) The lease on this facility expires on May 1, 2019.

(6) The Moses Lake location is comprised of two different facilities located in Moses Lake and Quincy, Washington.

(7) The facilities are leased on a month-to-month basis.

(8) The lease on this facility expires on August 31, 2021. 75% of the facility is leased to an unrelated party whose lease expires on September 30, 2017 with renewal options.

(9) The lease on this facility expires on April 30, 2019.

In addition to the facilities listed above, our executive office is located in Highland Hills, Ohio and we have leased sales offices located in Media, Pennsylvania; Miami, Florida; and Monterrey, Mexico. Management believes we will be able to accommodate our capacity needs for the immediate future at our existing facilities.

### ITEM 3. LEGAL PROCEEDINGS

We are party to various legal actions that we believe are ordinary in nature and incidental to the operation of our business. In the opinion of management, the outcome of the proceedings to which we are currently a party will not

have a material adverse effect upon our results of operations, financial condition or cash flows.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## EXECUTIVE OFFICERS OF THE REGISTRANT

This information is included in this Annual Report on Form 10-K pursuant to Instruction 3 of Item 401(b) of Regulation S-K. The following is a list of our executive officers and a brief description of their business experience. Each executive officer will hold office until his successor is chosen and qualified.

Michael D. Siegal, age 64, has served as our Chief Executive Officer since 1984 and as Chairman of our Board of Directors since 1994. From 1984 until January 2001, he also served as our President. He has been employed by us in a variety of capacities since 1974. Mr. Siegal serves on the Board of Directors of Cliffs Natural Resources, Inc. He is also the immediate past Board Chair of the Jewish Federations of North America and is currently on the Board of the Development Corporation for Israel and the Jewish Agency for Israel.

David A. Wolfort, age 64, has served as our President since January 2001. He has been a director since 1987. He previously served as Chief Operating Officer from 1995 to 2016 and as Vice President Commercial from 1987 to 1995, after having joined us in 1984 as General Manager. Prior thereto, he spent eight years with a primary steel producer in a variety of sales assignments. Mr. Wolfort is a past director of the Metals Service Center Institute and previously served as Chairman of its Political Action Committee and Governmental Affairs Committee. He is a trustee of the Board of the Musical Arts Association (Cleveland Orchestra) and of Ohio University where he serves as the Chairman of The Board of Trustees and is a member of the Executive Committee. He also serves as a member of the United States Industry Trade Advisory Committee for steel (ITAC).

Andrew S. Greiff, age 55, has served as our Executive Vice President and Chief Operating Officer since August 2016. He previously served as President, Specialty Metals from 2011 to 2016 after having joined us in 2009 as Vice President of Specialty Metals. Prior thereto, Mr. Greiff spent 24 years in various positions within the steel industry and served as the President and CEO of his own steel trading company. Mr. Greiff serves on the board of Hawken School and the MSCI Specialty Metals Product Council.

Richard T. Marabito, age 53, serves as our Chief Financial Officer. He joined us in 1994 as Corporate Controller and served in this capacity until being named Chief Financial Officer in March 2000. He also served as Treasurer from 1994 through 2002 and again from 2010 through 2012. Prior to joining us, Mr. Marabito served as Corporate Controller for a publicly traded wholesale distribution company and was employed by a national accounting firm in its audit department. Mr. Marabito is a Governance board member of the Make-A-Wish Foundation of Ohio, Kentucky and Indiana and also serves as the Chair of its Northeast Ohio regional board. Mr. Marabito serves on the Board of Trustees and as Treasurer for Hawken School in Cleveland, Ohio. He is also a Vice Chair and Executive Committee member of the Metals Service Center Institute and is a past Chair of its Foundation for Education and Research.

Richard A. Manson, age 48, has served as our Vice President and Treasurer since January 2013 and has been employed by us since 1996. From March 2010 through December 2012, he served as our Vice President of Human Resources and Administration. From January 2003 through March 2010, he served as our Treasurer and Corporate Controller. From 1996 through 2002, he served as our Director of Taxes and Risk Management. Prior to joining us, Mr. Manson was employed for seven years by a national accounting firm in its tax department. Mr. Manson is a Board Member and the Treasurer of the West Side Catholic Center. He also serves on the Board of Directors of the Cleveland Catholic Cemeteries Association. Mr. Manson is a certified public accountant and member of the Ohio Society of Certified Public Accountants and the American Institute of Certified Public Accountants.

Donald McNeeley, age 62, has served as the President of CTI, a wholly owned subsidiary of Olympic Steel, Inc., since the acquisition on July 1, 2011. He joined CTI in 1972 and has held several operational and executive positions within the company. After serving as CTI's Vice President of Operations and subsequently Executive Vice President, in 1990, Dr. McNeeley was appointed President and Chief Operating Officer. He is a former Chairman of the Metals Service Center Institute. Dr. McNeeley is an adjunct professor at Northwestern University where he teaches in the graduate engineering program. He serves on the board of directors of Saulsbury Industries in Odessa, Texas, where he chairs the Audit Committee. Dr. McNeeley also serves on the board of directors of Vail Rubber Industries in St. Joseph, Michigan, and is a former director of The Committee for Monetary Research in Greenwich, Connecticut.



**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****Price Range of Common Stock**

Our common stock trades on the Nasdaq Global Select Market under the symbol "ZEUS." The following table sets forth, for each quarter in the two-year period ended December 31, 2016, the high and low sales prices of our common stock as reported by the Nasdaq Global Select Market:

|                | <b>2016</b> |            | <b>2015</b> |            |
|----------------|-------------|------------|-------------|------------|
|                | <b>High</b> | <b>Low</b> | <b>High</b> | <b>Low</b> |
| First quarter  | \$17.50     | \$7.98     | \$18.57     | \$12.86    |
| Second quarter | 27.48       | 15.41      | 20.93       | 10.44      |
| Third quarter  | 31.19       | 17.42      | 17.92       | 6.40       |
| Fourth quarter | 28.67       | 17.14      | 12.60       | 8.98       |

**Holders of Record**

As of February 1, 2017, we estimate there were approximately 43 holders of record and 3,670 beneficial holders of our common stock.

**Dividends**

During 2016, our Board of Directors approved regular quarterly dividends of \$0.02 per share that were paid on March 15, 2016, June 15, 2016, September 15, 2016 and December 15, 2016.

During 2015, our Board of Directors approved regular quarterly dividends of \$0.02 per share that were paid on March 16, 2015, June 15, 2015, September 15, 2015 and December 15, 2015.

We expect to make regular quarterly dividend distributions in the future, subject to the continuing determination by our Board of Directors that the dividend remains in the best interest of our shareholders. Our asset-based credit facility (the ABL Credit Facility) restricts the aggregate amount of dividends and common stock repurchases that we can pay to \$2.5 million annually. Any determinations by the Board of Directors to pay cash dividends in the future will take into account various factors, including our financial condition, results of operations, current and anticipated cash needs, plans for expansion and restrictions under our credit agreement and any agreements governing our future debt. We cannot assure you that dividends will be paid in the future or that, if paid, the dividends will be at the same amount or frequency.

### **Issuer Purchases of Equity Securities**

We did not purchase any of our equity securities during the quarter ended December 31, 2016.

On October 2, 2015, we announced that our Board of Directors authorized a stock repurchase program of up to 550,000 shares of the Company's issued and outstanding common stock, which could include open market repurchases, negotiated block transactions, accelerated stock repurchases or open market solicitations for shares, all or some of which may be effected through Rule 10b5-1 plans. Any of the repurchased shares will be held in our treasury, or canceled and retired as our Board may determine from time to time. Any repurchases of common stock are subject to the covenants contained in the ABL Credit Facility. Our ABL Credit Facility restricts the aggregate amount of dividends and common stock repurchases that we can pay to \$2.5 million annually. Purchases in excess of \$2.5 million require us to (i) maintain availability in excess of 25% of the aggregate revolver commitments or (ii) to maintain availability equal to or greater than 15% of the aggregate revolver commitments and we must maintain a pro-forma ratio of EBITDA minus certain capital expenditures and cash taxes paid to fixed charges of at least 1.00 to 1.00. The timing and amount of any repurchases under the stock repurchase program will depend upon several factors, including market and business conditions, and limitations under the ABL Credit Facility, and repurchases may be discontinued at any time.

### **Recent Sales of Unregistered Securities**

We did not have any unregistered sales of equity securities during the quarter ended December 31, 2016.



**ITEM 6. SELECTED FINANCIAL DATA**

The following table sets forth selected financial and other data of the Company for each of the five years in the period ended December 31, 2016. The data presented should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and notes thereto included elsewhere in this Annual Report on Form 10-K.

|  | <b>For the Years Ended December 31,</b> |             |             |             |             |
|--|---|-------------|-------------|-------------|-------------|
|  | <b>2016</b>                             | <b>2015</b> | <b>2014</b> | <b>2013</b> | <b>2012</b> |
|  | (in thousands, except per share data)   |             |             |             |             |
| <b>Income Statement Data:</b>                  |   |             |             |             |             |
| Net sales                                      | \$1,055,116                             | \$1,175,543 | \$1,436,270 | \$1,263,331 | \$1,383,701 |
| Cost of materials sold                         | 820,040                                 | 942,214     | 1,160,310   | 999,207     | 1,113,852   |
| Gross profit (a)                               | 235,076                                 | 233,329     | 275,960     | 264,124     | 269,849     |
| Operating expenses (b)                         | 229,328                                 | 236,157     | 261,332     | 244,469     | 244,817     |
| Goodwill and intangible asset impairment       | -                                       | 24,951      | 23,836      | -           | 6,583       |
| Operating income (loss)                        | 5,748                                   | (27,779 )   | (9,208 )    | 19,655      | 18,449      |
| Interest and other expense on debt             | 5,273                                   | 5,690       | 6,780       | 6,703       | 8,357       |
| Income (loss) before income taxes              | 420                                     | (33,594 )   | (16,114 )   | 12,924      | 10,139      |
| Net income (loss)                              | (1,078 )                                | (26,777 )   | \$(19,064 ) | \$7,647     | \$2,277     |
| <b>Per Share Data:</b>                         |   |             |             |             |             |
| Net income (loss) - basic (c)                  | \$(0.10 )                               | \$(2.39 )   | \$(1.71 )   | \$0.69      | \$0.21      |
| Net income (loss) - diluted (d)                | (0.10 )                                 | (2.39 )     | (1.71 )     | 0.69        | 0.21        |
| Dividends paid                                 | \$0.08                                  | \$0.08      | \$0.08      | \$0.08      | \$0.08      |
| <b>Shares Outstanding:</b>                     |   |             |             |             |             |
| Weighted average shares - basic                | 11,210                                  | 11,192      | 11,120      | 11,065      | 10,989      |
| Weighted average shares - diluted              | 11,210                                  | 11,192      | 11,120      | 11,074      | 10,995      |
| <b>Balance Sheet Data (as of December 31):</b> |   |             |             |             |             |
| Current assets (e)                             | \$364,940                               | \$308,946   | \$458,709   | \$417,631   | \$422,377   |
| Current liabilities (e)                        | 104,898                                 | 77,060      | 131,977     | 165,633     | 142,442     |
| Working capital (f)                            | 260,042                                 | 231,886     | 326,732     | 251,998     | 279,935     |
| Total assets (e)                               | 556,068                                 | 511,880     | 699,154     | 695,375     | 705,085     |
| Total debt                                     | 166,424                                 | 148,490     | 247,620     | 199,269     | 241,711     |
| Shareholders' equity                           | \$253,390                               | \$254,695   | \$280,781   | \$298,616   | \$289,857   |

(a) Gross profit is calculated as net sales less the cost of materials sold (includes LIFO income of \$1,489 and \$3,347 in 2016 and 2015, respectively, LIFO expense of \$365 in 2014 and LIFO income of \$3,572 in 2013).

- (b) Operating expenses are calculated as total costs and expenses less the cost of materials sold. It does not include the goodwill and intangible asset impairment charge shown separately below.
- (c) Calculated by dividing net income (loss) by weighted average basic shares outstanding.
- (d) Calculated by dividing net income (loss) by weighted average diluted shares outstanding.
- (e) Prospective adjustment of deferred tax assets and liabilities in 2016, prior periods were not retrospectively adjusted.
- (f) Calculated as current assets less current liabilities.

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from the results discussed in the forward-looking statements. Factors that might cause a difference include, but are not limited to, those discussed under Item 1A, Risk Factors in this Annual Report on Form 10-K. The following section is qualified in its entirety by the more detailed information, including our financial statements and the notes thereto, which appears elsewhere in this Annual Report.*

### **Overview**

We are a leading metals service center that operates in three reportable segments; carbon flat products, specialty metals flat products, and tubular and pipe products. We provide metals processing and distribution services for a wide range of customers. Our carbon flat products segment's focus is on the direct sale and distribution of large volumes of processed carbon and coated flat-rolled sheet, coil and plate products and fabricated parts. Our specialty metals flat products segment's focus is on the direct sale and distribution of processed aluminum and stainless flat-rolled sheet and coil products, flat bar products and fabricated parts. In addition, we distribute metal tubing, pipe, bar, valves and fittings and fabricate pressure parts supplied to various industrial markets. Products that require more value-added processing generally have a higher gross profit. Accordingly, our overall gross profit is affected by, among other things, product mix, the amount of processing performed, the demand for and availability of metals, and volatility in selling prices and material purchase costs. We also perform toll processing of customer-owned metals. We sell certain products internationally, primarily in Canada, Mexico and Dominican Republic. International sales are immaterial to our consolidated financial results and to the individual segments' results.

Our results of operations are affected by numerous external factors including, but not limited to: general and global business, economic, financial, banking and political conditions; fluctuations in the value of the U.S. dollar to foreign currencies, competition; metals pricing, demand and availability; energy prices; pricing and availability of raw materials used in the production of metals; global supply, the level of metals imported into the United States, and inventory held in the supply chain; customers' ability to manage their credit line availability; and layoffs or work stoppages by our own, our suppliers' or our customers' personnel. The metals industry also continues to be affected by the global consolidation of our suppliers, competitors and end-use customers.

Like other metals service centers, we maintain substantial inventories of metals to accommodate the short lead times and just-in-time delivery requirements of our customers. Accordingly, we purchase metals in an effort to maintain our inventory at levels that we believe to be appropriate to satisfy the anticipated needs of our customers based upon customer forecasts, historic buying practices, supply agreements with customers and market conditions. Our commitments to purchase metals are generally at prevailing market prices in effect at the time we place our orders.

We have entered into nickel and carbon swaps at the request of our customers in order to mitigate our customers' risk of volatility in the price of metals, and we have entered into metals hedges to mitigate our risk of volatility in the price of metals. We have no long-term, fixed-price metals purchase contracts. When metals prices decline, customer demands for lower prices and our competitors' responses to those demands could result in lower sale prices and, consequently, lower gross profits and earnings as we use existing metals inventory. When metals prices increase, competitive conditions will influence how much of the price increase we can pass on to our customers. To the extent we are unable to pass on future price increases in our raw materials to our customers, the net sales and gross profits of our business could be adversely affected.

## **Reportable Segments**

The Company operates in three reportable segments; carbon flat products, specialty metals flat products and tubular and pipe products. The carbon flat products segment and the specialty metals flat products segment are at times consolidated and referred to as the flat products segment. Some of the flat products segments' assets and resources are shared by the carbon and specialty metals segments and both segments' products are stored in the shared facilities and, in some locations, processed on shared equipment. As such, total assets and capital expenditures are reported in the aggregate for the flat products segments. Due to the shared assets and resources, certain of the flat products segment expenses are allocated between the carbon flat products segment and the specialty metals flat products segment based upon an established allocation methodology. The financial information for 2014 has been recast to reflect the new segment reporting structure.

We follow the accounting guidance that requires the utilization of a “management approach” to define and report the financial results of operating segments. The management approach defines operating segments along the lines used by the chief operating decision maker, or CODM, to assess performance and make operating and resource allocation decisions. Our CODM evaluates performance and allocates resources based primarily on operating income. Our operating segments are based on internal management reporting.

Due to the nature of the products sold in each segment, there are significant differences in the segments’ average selling price and the cost of materials sold. The tubular and pipe products segment generally has the highest average selling price among the three segments followed by the specialty metals flat products and carbon flat products segments. Due to the nature of the tubular and pipe products, we do not report tons sold or per ton information. Gross profit per ton is generally higher in the specialty metals flat products segment than the carbon flat products segment. Gross profit as a percentage of net sales is generally highest in the tubular and pipe products segment, followed by the carbon and specialty metals flat products segments.

Due to the differences in average selling prices, gross profit and gross profit percentage among the segments, a change in the mix of sales could impact total net sales, gross profit, and gross profit percentage. In addition, certain inventory in the tubular and pipe products segment is valued under the LIFO method. Adjustments to the LIFO inventory value are recorded to cost of materials sold and may impact the gross margin and gross margin percentage at the consolidated Company and tubular and pipe products segment levels.

### ***Carbon flat products***

The primary focus of our carbon flat products segment is on the direct sale and distribution of large volumes of processed carbon and coated flat-rolled sheet, coil and plate products and fabricated parts. We act as an intermediary between metals producers and manufacturers that require processed metals for their operations. We serve customers in most metals consuming industries, including manufacturers and fabricators of transportation and material handling equipment, construction and farm machinery, storage tanks, environmental and energy generation equipment, automobiles, military vehicles and equipment, as well as general and plate fabricators and metals service centers. We distribute these products primarily through a direct sales force.

### ***Specialty metals flat products***

The primary focus of our specialty metals flat products segment is on the direct sale and distribution of processed stainless and aluminum flat-rolled sheet and coil products, flat bar products and fabricated parts. We act as an intermediary between metals producers and manufacturers that require processed metals for their operations. We serve customers in various industries, including manufacturers of food service and commercial appliances, agriculture



equipment, transportation and automotive equipment. We distribute these products primarily through a direct sales force.

Combined, the carbon and specialty metals flat products segments have 22 strategically-located processing and distribution facilities in the United States and one in Monterrey, Mexico. Many of our facilities service both the carbon and the specialty metals flat products segments, and certain assets and resources are shared by the segments. Our geographic footprint allows us to focus on regional customers and larger national and multi-national accounts, primarily located throughout the midwestern, eastern and southern United States.

### *Tubular and pipe products*

The tubular and pipe products segment consists of the Chicago Tube and Iron, or CTI, business, acquired in 2011. Through our tubular and pipe products segment, we distribute metal tubing, pipe, bar, valve and fittings and fabricate pressure parts supplied to various industrial markets. Founded in 1914, CTI operates from nine locations in the midwestern and southeastern United States. The tubular and pipe products segment distributes its products primarily through a direct sales force.

### *Corporate expenses*

Corporate expenses are reported as a separate line item for segment reporting purposes. Corporate expenses include the unallocated expenses related to managing the entire Company (i.e., all three segments), including compensation for certain personnel, expenses related to being a publicly traded entity such as board of directors expenses, audit expenses, and various other professional fees.

## Results of Operations

### 2016 Compared to 2015

Our results of operations are impacted by the market price of metals. Over the past 24 months, metals prices have fluctuated significantly and changes to our net sales, cost of materials sold, gross profit, cost of inventory and profitability, are all impacted by industry metals pricing.

During 2015, the hot-rolled carbon coil index pricing declined by approximately 36% as a result of the strengthened U.S. dollar, a historically high level of imported material arriving in the United States, low raw material costs to produce metals and a global oversupply of metals. The pricing environment in 2015 drove our average selling prices down and caused margins to be pressured as the average cost of inventory did not decrease as quickly as the average selling price as we traditionally keep approximately two and a half to three months of inventory on hand.

During the first six months of 2016, the market price of metals increased and fully recovered the decrease experienced during 2015. Metals market pricing peaked in June 2016, and then decreased until November 2016. Metals prices in December 2016 were not as high as the June 2016 prices, but were more than 65% per ton higher than the December 2015 prices. Although prices increased during 2016, the average selling price during 2016 was still lower than the average selling price during 2015. Transactional or “spot” selling prices generally move in tandem with market price changes, while fixed selling prices typically lag and reset quarterly. Similarly, inventory costs (and therefore cost of materials sold) tend to move slower than market selling price changes due to mill lead times and inventory turnover impacting the rate of change in average cost. As sales volumes were relatively flat between the years, lower average selling prices were the driver for our decreased net sales in 2016. When the average selling price decreases, and net sales decreases, the gross profit and operating expenses as a percentage of net sales will generally increase.

The following table sets forth certain consolidated income statement data for the years ended December 31, 2016 and 2015 (dollars shown in thousands):

|                            | <b>2016</b> |                               | <b>2015</b> |                               |
|----------------------------|-------------|-------------------------------|-------------|-------------------------------|
|                            | \$          | <b>% of<br/>net<br/>sales</b> | \$          | <b>% of<br/>net<br/>sales</b> |
| Net sales                  | \$1,055,116 | 100.0                         | \$1,175,543 | 100.0                         |
| Cost of materials sold (a) | 820,040     | 77.7                          | 942,214     | 80.2                          |
| Gross profit (b)           | 235,076     | 22.3                          | 233,329     | 19.8                          |
| Operating expenses (c)     | 229,328     | 21.7                          | 236,157     | 20.1                          |

Edgar Filing: OLYMPIC STEEL INC - Form 10-K

|  |            |        |             |        |
|--|------------|--------|-------------|--------|
| Goodwill and intangible asset impairment (d) | -          | (0.0 ) | 24,951      | 2.1    |
| Operating loss                               | 5,748      | 0.5    | (27,779 )   | (2.4 ) |
| Other loss, net                              | (55 )      | (0.0 ) | (125 )      | (0.0 ) |
| Interest and other expense on debt           | 5,273      | 0.5    | 5,690       | 0.5    |
| Income (loss) before income taxes            | 420        | 0.0    | (33,594 )   | (2.9 ) |
| Income taxes                                 | 1,498      | 0.1    | (6,817 )    | (0.6 ) |
| Net loss                                     | \$(1,078 ) | (0.1 ) | \$(26,777 ) | (2.3 ) |

(a) Includes \$1,489 and \$3,347 of LIFO income for 2016 and 2015, respectively.

(b) Gross profit is calculated as net sales less the cost of materials sold.

(c) Operating expenses are calculated as total costs and expenses less the cost of materials sold. Excludes goodwill and intangible asset impairment shown separately below for comparability purposes.

The 2015 non-cash goodwill and intangible asset impairment charge is separately displayed for operating expense (d) comparability purposes. \$24,451 of the impairment charge is related to the tubular and pipe products segment and \$500 is related to the specialty metals flat products segment.

Net sales decreased \$120.4 million, or 10.2%, to \$1.06 billion in 2016 from \$1.18 billion in 2015. Carbon flat products net sales decreased \$94.4 million, or 12.3%, and were 63.6% of total net sales in 2016 compared to 65.1% in 2015. Specialty metals flat products net sales decreased \$2.6 million, or 1.3%, and were 18.0% of total net sales in 2016 compared to 16.4% in 2015. Tubular and pipe products net sales decreased \$23.4 million, or 10.8%, and were 18.4% of total net sales in 2016 compared to 18.5% of total net sales in 2015. The decrease in sales for the year ended December 31, 2016 was due to a 10.2% decrease in average selling prices as sales volumes were flat between years. Average selling prices decreased in all segments during 2016 compared to 2015 as market pricing for metals was still lower year-over-year. During the year, we increased our market share for all of the product categories that we sell.

Cost of materials sold decreased \$122.2 million, or 13.0%, to \$820.0 million in 2016 from \$942.2 million in 2015. During 2016, we recorded LIFO income of \$1.5 million compared to LIFO income of \$3.3 million recorded in 2015. The decrease in cost of materials sold in 2016 is due to the decreased metals costs of 12.9% during 2016 as sales volumes were flat between years.

As a percentage of net sales, gross profit (as defined in footnote (b) in the table above) increased to 22.3% in 2016 from 19.8% in 2015. Gross profit as a percentage of net sales increased in the carbon flat products segment to 21.2% from 19.2% in 2015 and in the tubular and pipe products segment to 32.6% from 32.5% in 2015. Gross profit as a percentage of net sales increased in the specialty metals flat products segment to 15.7% in 2016 from 8.2% in 2015. LIFO income increased gross profit by 0.1% and 0.3% of net sales in 2016 and 2015, respectively. The increase in gross profit as a percentage of net sales during 2016 was primarily due to the cost of materials sold decreasing more than selling prices in all segments.

Operating expenses (as defined in footnote (c) in the table above) decreased \$6.8 million, or 2.9%, to \$229.3 million in 2016 from \$236.2 million in 2015. As a percentage of net sales, operating expenses increased to 21.7% in 2016 from 20.1% in 2015. Warehouse and processing costs decreased \$5.9 million, or 6.9%, primarily due to reductions in labor hours worked. Administrative costs decreased by \$1.9 million, or 3.0%, primarily related to reductions in labor and personnel expenses and lower variable based incentive compensation. Distribution expense increased by \$0.4 million, or 1.2%, on flat sales volumes. Selling expenses increased \$1.9 million, or 9.0%, as a result of hiring additional sales professionals. Occupancy expenses decreased \$0.8 million as a result of elimination of certain leased warehouse space. Depreciation expense decreased \$0.6 million, or 3.0%, as a result of certain assets being fully depreciated in 2016. Operating expenses in the carbon flat products segment decreased \$7.6 million, operating expenses in the specialty metals products segment increased \$3.0 million, operating expenses in the tubular and pipe products segment decreased \$2.5 million, and Corporate expenses increased \$0.3 million.

The goodwill and intangible asset impairment charge in 2015 included a \$16.5 million non-cash goodwill impairment and a \$8.0 million intangible asset impairment for the tubular and pipe products segment as well as a \$0.5 million goodwill impairment for the specialty metals flat products segment. The 2015 goodwill impairment charges fully impaired the goodwill for both the tubular and pipe products segment and the specialty metals flat products segment.

Interest and other expense on debt totaled \$5.3 million in 2016 compared to \$5.7 million in 2015. Our effective borrowing rate, exclusive of deferred financing fees and commitment fees, was 2.4% in 2016 compared to 2.1% in 2015. The decrease in interest and other expense on debt in 2016 was attributable to lower average borrowings during 2016 compared to 2015.

Income before income taxes totaled \$0.4 million in 2016 compared to a loss before income taxes of \$33.6 million in 2015. 2015 loss before income taxes includes goodwill impairment charges of \$17.0 million and a \$8.0 million intangible asset impairment charge.

An income tax provision of 356.7% was recorded for 2016, compared to an income tax benefit of (20.3%) in 2015. The effective tax rate is disproportionately high in 2016 from comparative periods due to low income before taxes relative to items that impact the effective tax rate. The 2016 effective income tax rate was impacted by increased valuation allowances and non-deductible expenses. The 2015 effective income tax rate was impacted by the non-deductibility of the goodwill impairment charges. The income tax benefit for 2015 prior to the goodwill impairment charge was 39.8%. We expect our 2017 income tax rate to approximate 38% to 40%.

Net loss for 2016 totaled \$1.1 million, or \$0.10 per basic and diluted share, compared to net loss of \$26.8 million, or \$2.39 per basic and diluted share, for 2015. The goodwill and intangible asset impairments in 2015 impacted earnings per share by \$1.93 per basic and diluted shares.

**Segment Results of Operations*****Carbon flat products***

The following table sets forth certain income statement data for the carbon flat products segment for the years ended December 31, 2016 and 2015 (dollars shown in thousands, except per ton data):

|                               | <b>2016</b> |                               | <b>2015</b> |                               |
|-------------------------------|-------------|-------------------------------|-------------|-------------------------------|
|                               |             | <b>% of<br/>net<br/>sales</b> |             | <b>% of<br/>net<br/>sales</b> |
| Direct tons sold              | 952,888     |                               | 935,165     |                               |
| Toll tons sold                | 73,880      |                               | 102,360     |                               |
| Total tons sold               | 1,026,768   |                               | 1,037,525   |                               |
| Net sales                     | \$670,983   | 100.0                         | \$765,400   | 100.0                         |
| Average selling price per ton | 653         |                               | 738         |                               |
| Cost of materials sold        | 529,021     | 78.8                          | 618,674     | 80.8                          |
| Gross profit (a)              | 141,962     | 21.2                          | 146,726     | 19.2                          |
| Operating expenses (b)        | 146,333     | 21.8                          | 153,943     | 20.1                          |
| Operating loss                | \$(4,371 )  | (0.6 )                        | \$(7,217 )  | (0.9 )                        |

(a) Gross profit is calculated as net sales less the cost of materials sold.

(b) Operating expenses are calculated as total costs and expenses less the cost of materials sold.

Tons sold decreased 1.0% to 1.03 million tons in 2016 from 1.04 million tons in 2015. Toll tons sold decreased 27.8% to 74 thousand tons in 2016 from 102 thousand tons in 2015. The decrease in tons sold is due to decreased customer demand and lower industry-wide shipments by U.S. service centers in 2016 compared to 2015. Despite the further softening of industry-wide shipments in 2016, we grew our market share in all of the carbon flat product categories we sell.

Net sales decreased \$94.4 million, or 12.3%, to \$671.0 million in 2016 from \$765.4 million in 2015. Average selling prices in 2016 decreased 11.4% to \$653 per ton, compared to \$738 per ton in 2015. The decrease in sales was primarily due to a 11.4% decrease in average selling prices during 2016 as volumes were down only 1%. The decrease in the average selling price is a result of lower prices in the metals industry during 2016 discussed in the overview of

Results of Operations above. We expect market carbon flat metals prices in the first quarter of 2017 to increase over the prices in the fourth quarter of 2016.

Cost of materials sold decreased \$89.7 million, or 14.5%, to \$529.0 million in 2016 from \$618.7 million in 2015. The decrease in cost of materials sold was due to a 13.6% decrease in the average cost of materials sold per ton during 2016 compared to 2015 as volumes were down only 1% between years.

As a percentage of net sales, gross profit (as defined in footnote (a) in the table above) increased to 21.2% in 2016 from 19.2% in 2015. The increase in gross profit percentage in 2016 was primarily due to the cost of materials sold decreasing more than selling prices. The average gross profit per ton sold declined to \$138 in 2016 from \$141 in 2015 due to the significant decline in market prices for metals in 2016.

Operating expenses in 2016 decreased \$7.6 million, or 4.9%, to \$146.3 million from \$153.9 million in 2015 exceeding the sales volume decrease of 1.0%. As a percentage of net sales, operating expenses increased to 21.8% for 2016 from 20.1% in 2015. Operating expenses decreased through reductions in labor and personnel expenses, lower variable based incentive compensation, lower depreciation expense and lower occupancy expense as a result of elimination of certain leased warehouse space offset by an increase in distribution expense and increased selling expenses as a result of hiring additional sales professionals.

Operating loss for 2016 totaled \$4.4 million compared to operating loss of \$7.2 million in 2015.

*Specialty metals flat products*

The following table sets forth certain income statement data for the specialty metals flat products segment for the years ended December 31, 2016 and 2015 (dollars shown in thousands, except per ton data):

|                                | <b>2016</b> |                               | <b>2015</b> |                               |
|--------------------------------|-------------|-------------------------------|-------------|-------------------------------|
|                                |             | <b>% of<br/>net<br/>sales</b> |             | <b>% of<br/>net<br/>sales</b> |
| Direct tons sold               | 82,156      |                               | 72,041      |                               |
| Toll tons sold                 | 129         |                               | 36          |                               |
| Total tons sold                | 82,285      |                               | 72,077      |                               |
| Net sales                      | \$189,930   | 100.0                         | \$192,516   | 100.0                         |
| Average selling price per ton  | 2,308       |                               | 2,671       |                               |
| Cost of materials sold         | 160,185     | 84.3                          | 176,686     | 91.8                          |
| Gross profit (a)               | 29,745      | 15.7                          | 15,830      | 8.2                           |
| Operating expenses (b)         | 19,904      | 10.5                          | 16,904      | 8.8                           |
| Goodwill impairment charge (c) | -           | -                             | 500         | 0.2                           |
| Operating income (loss)        | \$9,841     | 5.2                           | \$(1,574)   | (0.8)                         |

(a) Gross profit is calculated as net sales less the cost of materials sold.

(b) Operating expenses are calculated as total costs and expenses less the cost of materials sold. Excludes goodwill impairment charge shown separately below for comparability purposes.

(c) The 2015 non-cash goodwill impairment charge is separately displayed for operating expense comparability purposes.

Tons sold increased 14.2% to 82 thousand tons in 2016 from 72 thousand tons in 2015. The specialty metals flat products segment increased its market share in both the stainless steel and aluminum products it sells.

Net sales decreased \$2.6 million, or 1.3%, to \$189.9 million in 2016 from \$192.5 million in 2015. Average selling prices in 2016 decreased to \$2,308 per ton, compared to \$2,671 per ton in 2015. The decrease in sales was due to a 13.6% decrease in the average selling price during 2016 offset by a 14.2% increase in sales volume. The decrease in the year-over-year average selling price per ton is a result of lower market prices of stainless steel and aluminum in 2016. Average market prices for nickel (a component of stainless steel) were also lower in 2016 compared to 2015. We expect stainless steel and aluminum market prices in the first quarter of 2017 to increase over the fourth quarter



2016 prices.

Cost of materials sold decreased \$16.5 million, or 9.3%, to \$160.2 million in 2016 from \$176.7 million in 2015. The decrease in cost of materials sold was due to a 20.6% decrease in the average cost of materials sold per ton during 2016 compared to 2015, offset by a 14.2% sales volume increase.

As a percentage of net sales, gross profit (as defined in footnote (a) in the table above) increased to 15.7% in 2016 from 8.2% in 2015. The average gross profit per ton sold totaled \$361 in 2016 compared to \$220 per ton in 2015. The increase in the gross profit percentage is a result of our cost of materials sold decreasing more than the average selling price in 2016 compared to 2015 as inventory turnover improved in 2016.

Operating expenses (as defined in footnote (b) in the table above) increased \$3.0 million, or 17.7%, to \$19.9 million in 2016 from \$16.9 million in 2015. The increase in operating expenses is related to the increased sales volume of 14.2%. As a percentage of net sales, operating expenses increased to 10.5% of net sales in 2016 from 8.8% in 2015. Variable operating expenses, such as distribution, wages and variable based incentive compensation increased as a result of higher sales volumes and improved profitability. In 2015 we recorded a \$0.5 million non-cash goodwill impairment charge as a result of the continued market pressures which fully eliminated the goodwill for the specialty metals flat products segment.

Operating income for 2016 totaled \$9.8 million compared to operating loss of \$1.6 million in 2015.

***Tubular and pipe products***

The following table sets forth certain income statement data for the tubular and pipe products segment for 2016 and 2015 (dollars shown in thousands).

|  | <b>2016</b> |                               | <b>2015</b> |                               |
|--|-------------|-------------------------------|-------------|-------------------------------|
|  | <b>\$</b>   | <b>% of<br/>net<br/>sales</b> | <b>\$</b>   | <b>% of<br/>net<br/>sales</b> |
| Net sales                                    | \$194,203   | 100.0                         | \$217,627   | 100.0                         |
| Cost of materials sold (a)                   | 130,834     | 67.4                          | 146,854     | 67.5                          |
| Gross profit (b)                             | 63,369      | 32.6                          | 70,773      | 32.5                          |
| Operating expenses (c)                       | 55,656      | 28.7                          | 58,190      | 26.8                          |
| Goodwill and intangible asset impairment (d) | -           | -                             | 24,451      | 11.2                          |
| Operating income (loss)                      | \$7,713     | 3.9                           | \$(11,868)  | (5.5)                         |

(a) Includes \$1,489 and \$3,347 of LIFO income in 2016 and 2015, respectively.

(b) Gross profit is calculated as net sales less the cost of materials sold.

(c) Operating expenses are calculated as total costs and expenses less the cost of materials sold.

(d) The 2015 non-cash goodwill and intangible asset impairment charges are separately displayed for operating expense comparability purposes.

Net sales decreased \$23.4 million, or 10.8%, to \$194.2 million in 2016 from \$217.6 million in 2015. The decrease in net sales was due to a 0.8% decrease in sales volume and a 10.0% decrease in average selling prices during 2016. The decrease in volume was due to decreased customer demand and lower industry-wide shipments of pipe and tube products. The decrease in average selling prices were due to lower industry market prices for metals in 2016 compared to 2015.

Cost of materials sold decreased \$16.0 million, or 10.9%, to \$130.8 million in 2016 from \$146.9 million in 2015. The decrease in cost of materials sold was due to a 0.8% decrease in sales volume and a 10.2% decrease in the average cost of materials sold which was impacted by the LIFO income of \$1.5 million in 2016 compared to LIFO income of \$3.3 million in 2015.

As a percentage of net sales, gross profit (as defined in footnote (b) in the table above) remained relatively flat at 32.6% in 2016 compared to 32.5%, in 2015. The LIFO income increased gross profit by 0.8% of net sales in 2016 compared to 1.5% of net sales in 2015.

Operating expenses (as defined in footnote (c) in the table above) decreased \$2.5 million, or 4.4%, to \$55.7 million from \$58.2 million in 2015. As a percentage of net sales, operating expenses increased to 28.7% in 2016 compared to 26.8% in 2015. Variable operating expenses, such as variable performance-based incentive compensation, decreased in 2016 as a result of lower sales and income before impairment charges.

In 2015 we recorded a \$16.5 million non-cash goodwill impairment charge and an \$8.0 million non-cash intangible asset impairment charge. There were no intangible asset impairment charges recorded in 2016.

Operating income for 2016 totaled \$7.7 million, compared to an operating loss of \$11.9 million in 2015. The operating loss for 2015 was the result of the goodwill impairment of \$16.5 million and the asset impairment charge of \$8.0 million.

#### *Corporate expenses*

Corporate expenses increased \$0.3 million, or 4.4%, to \$7.4 million in 2016 compared to \$7.1 million in 2015. The increase in corporate expenses is primarily attributable to our President of Specialty Metals being appointed to the position of Executive Vice President and Chief Operating Officer and the associated transfer of expenses from the Specialty Metals flat products segment to the Corporate expenses in 2016. Corporate expenses include the unallocated expenses related to managing the entire Company (i.e. all three segments), including compensation for certain personnel, expenses related to being a publicly traded entity such as board of directors expenses, audit expenses, and various other professional fees.

**2015 Compared to 2014**

The metals industry experienced a significant decline in the price of metals during 2015 as a result of the strengthened U.S. dollar, a historically high level of imported materials arriving in the United States, low raw material costs to produce metals and a global oversupply of metals. The price of hot-rolled carbon flat steel decreased approximately 41% during 2015. Similarly, the price of stainless steel and aluminum decreased during 2015. The declines in metals shipments and pricing negatively impacted our 2015 sales and earnings. Industry demand also softened in 2015 compared to 2014 as evidenced by lower year over year shipments by metals service centers in the United States. During the second quarter of 2015, we recorded an impairment charge in our tubular and pipe products segment as a result of the continued decline in metals pricing and its impact on the tubular and pipe products segment results. The impairment charge consisted of a \$16.5 million goodwill impairment, which eliminated the remaining goodwill in the tubular and pipe products segment, and a partial impairment of \$8.0 million related to the segment's tradename. The tradename is an indefinitely lived intangible asset with a remaining value of \$15.4 million. In the fourth quarter of 2015, we recorded a \$0.5 million impairment charge, which fully eliminated the goodwill in our specialty metals flat products segment.

The following table sets forth certain consolidated income statement data for the years ended December 31, 2015 and 2014 (dollars shown in thousands):

|  | <b>2015</b> |                               | <b>2014</b> |                               |
|--|-------------|-------------------------------|-------------|-------------------------------|
|  | <b>\$</b>   | <b>% of<br/>net<br/>sales</b> | <b>\$</b>   | <b>% of<br/>net<br/>sales</b> |
| Net sales                                    | \$1,175,543 | 100.0                         | \$1,436,270 | 100.0                         |
| Cost of materials sold (a)                   | 942,214     | 80.2                          | 1,160,310   | 80.8                          |
| Gross profit (b)                             | 233,329     | 19.8                          | 275,960     | 19.2                          |
| Operating expenses (c)                       | 236,157     | 20.1                          | 261,332     | 18.1                          |
| Goodwill and intangible asset impairment (d) | 24,951      | 2.1                           | 23,836      | 1.7                           |
| Operating loss                               | (27,779 )   | (2.4 )                        | (9,208 )    | (0.6 )                        |
| Other loss, net                              | (125 )      | (0.0 )                        | (126 )      | (0.0 )                        |
| Interest and other expense on debt           | 5,690       | 0.5                           | 6,780       | 0.5                           |
| Loss before income taxes                     | (33,594 )   | (2.9 )                        | (16,114 )   | (1.1 )                        |
| Income taxes                                 | (6,817 )    | (0.6 )                        | 2,950       | 0.2                           |
| Net loss                                     | \$(26,777 ) | (2.3 )                        | \$(19,064 ) | (1.3 )                        |

(a) Includes \$3,347 of LIFO income for 2015 and \$365 of LIFO expense for 2014.

(b) Gross profit is calculated as net sales less the cost of materials sold.

(c) Operating expenses are calculated as total costs and expenses less the cost of materials sold. Excludes goodwill and intangible asset impairment shown separately below for comparability purposes.

The non-cash goodwill and intangible asset impairment charge is separately displayed for operating expense (d) comparability purposes. \$24,451 in 2015 and \$23,836 in 2014 of the impairment charge is related to the tubular and pipe products segment and \$500 in 2015 is related to the specialty metals flat products segment.

Net sales decreased \$261 million, or 18.2%, to \$1.18 billion in 2015 from \$1.44 billion in 2014. Carbon flat products net sales decreased \$220 million, or 22.3%, and were 65.1% of total net sales in 2015 compared to 68.6% in 2014. Specialty metals flat products net sales decreased \$14.2 million, or 6.9%, and were 16.4% of total net sales in 2015 compared to 14.4% in 2014. Tubular and pipe products net sales decreased \$26.9 million, or 11.0%, and were 18.5% of total net sales in 2015 compared to 17.0% of total net sales in 2014. The decrease in sales for the year ended December 31, 2015 was due to a 10.2% decrease in sales volume and an 8.9% decrease in average selling prices in 2015 compared to 2014. The decrease in tons sold was due to decreased customer demand, specifically in the heavy equipment, agriculture, mining and energy sectors, and lower industry-wide shipments in 2015 compared to 2014.

Cost of materials sold decreased \$218 million, or 18.8%, to \$942 million in 2015 from \$1.16 billion in 2014. During 2015, we recorded LIFO income of \$3.3 million compared to LIFO expense of \$0.4 million recorded in 2014. The decrease in cost of materials sold in 2015 is primarily due to the decreased sales volume of 10.2%, decreased metals costs of 9.6% during 2015 and the impact of LIFO income during 2015 compared to LIFO expense in 2014.

As a percentage of net sales, gross profit (as defined in footnote (b) in the table above) increased to 19.8% in 2015 from 19.2% in 2014. Gross profit as a percentage of net sales increased in the carbon flat products segment to 19.2% from 18.2% in 2014 and in the tubular and pipe products segment to 32.5% from 28.9% in 2014. Gross profit as a percentage of net sales decreased in the specialty metals flat products segment to 8.2% in 2015 from 12.5% in 2014. LIFO income increased gross profit by 0.3% of net sales in 2015 and had no consolidated gross profit impact in 2014. The increase in gross profit as a percentage of net sales during 2015 was primarily due to the cost of materials sold decreasing more than selling prices in the carbon flat rolled and tubular and pipe products segments, as well as the impact of LIFO income in 2015 compared to LIFO expense in 2014.

Operating expenses (as defined in footnote (c) in the table above) decreased \$25.2 million, or 9.6%, to \$236.2 million in 2015 from \$261.3 million in 2014. As a percentage of net sales, operating expenses increased to 20.1% in 2015 from 18.1% in 2014. Operating expenses decreased in all categories as reported on the Company's Consolidated Statements of Comprehensive Income. During 2015, we executed on our profit improvement plan, which contributed to the cost reductions. Distribution expense decreased by \$5.2 million, or 12.7%, due to the decreased sales volume. Warehouse and processing costs decreased \$6.8 million, or 7.3%, primarily due to reductions in labor and personnel expenses and reduced warehouse consumables expenses related to the 10.2% 2015 volume decrease. Administrative costs decreased by \$7.2 million, or 10.0%, primarily related to reductions in labor and personnel expenses, centralization of certain administrative functions, lower variable based incentive compensation and decreases in travel and entertainment expenses. Selling expenses decreased \$3.6 million, or 14.7%, as a result of decreased variable compensation associated with fewer sales employees and decreased discretionary spending. Occupancy expenses decreased \$0.6 million as a result of decreased heating and snow removal expenses. Depreciation expense decreased \$1.7 million, or 8.8%, as a result of certain assets being fully depreciated in 2014. Operating expenses in the carbon flat products segment decreased \$19.0 million, operating expenses in the specialty metals products segment decreased \$2.4 million, operating expenses in the tubular and pipe products segment decreased \$1.8 million, and Corporate expenses decreased \$0.9 million.

The goodwill and intangible asset impairment charge in 2015 included a \$16.5 million non-cash goodwill impairment and an \$8.0 million intangible asset impairment for the tubular and pipe products segment as well as a \$0.5 million goodwill impairment for the specialty metals flat products segment. The 2015 goodwill impairment charges fully impaired the goodwill for both the tubular and pipe products segment and the specialty metals flat products segment. The goodwill and intangible asset impairment charge in 2014 included a \$23.8 million goodwill impairment for the tubular and pipe products segment.

Interest and other expense on debt totaled \$5.7 million in 2015 compared to \$6.8 million in 2014. Our effective borrowing rate, exclusive of deferred financing fees and commitment fees, was 2.1% in 2015 compared to 2.4% in 2014. The decrease in interest and other expense on debt in 2015 was primarily attributable to lower average borrowings and lower average borrowing rates during 2015 compared to 2014.

For 2015, loss before income taxes totaled \$33.6 million compared to loss before income taxes of \$16.1 million in 2014. 2015 includes goodwill impairment charges of \$17.0 million and a \$8.0 million intangible asset impairment

charge and LIFO income of \$3.3 million. 2014 included a goodwill impairment charge of \$23.8 million related to the tube and pipe segment and LIFO expense of \$0.4 million.

An income tax benefit of (20.3%) was recorded for 2015, compared to an income tax provision of 18.3% in 2014. The 2015 and 2014 effective income tax rates were impacted by the non-deductibility of the goodwill impairment charges. The income tax benefit for 2015 prior to the goodwill impairment charge was 39.8%. The income tax provision for 2014 prior to the goodwill impairment charge was 38.2%.

Net loss for 2015 totaled \$26.8 million, or \$2.39 per basic and diluted share, compared to net loss of \$19.1 million, or \$1.71 per basic and diluted share, for 2014. The goodwill and intangible asset impairments in 2015 impacted earnings per share by \$1.93 per basic and diluted shares. The goodwill impairment in 2014 impacted earnings per basic and diluted shares by \$2.14.

**Segment Results of Operations*****Carbon flat products***

The following table sets forth certain income statement data for the carbon flat products segment for the years ended December 31, 2015 and 2014 (dollars shown in thousands, except per ton data):

|                               | <b>2015</b> |                               | <b>2014</b> |                               |
|-------------------------------|-------------|-------------------------------|-------------|-------------------------------|
|                               |             | <b>% of<br/>net<br/>sales</b> |             | <b>% of<br/>net<br/>sales</b> |
| Direct tons sold              | 935,165     |                               | 1,059,409   |                               |
| Toll tons sold                | 102,360     |                               | 106,725     |                               |
| Total tons sold               | 1,037,525   |                               | 1,166,134   |                               |
| Net sales                     | \$765,400   | 100.0                         | \$985,039   | 100.0                         |
| Average selling price per ton | 738         |                               | 845         |                               |
| Cost of materials sold        | 618,674     | 80.8                          | 805,747     | 81.8                          |
| Gross profit (a)              | 146,726     | 19.2                          | 179,292     | 18.2                          |
| Operating expenses (b)        | 153,943     | 20.1                          | 172,986     | 17.6                          |
| Operating income (loss)       | \$(7,217 )  | (0.9 )                        | \$6,306     | 0.6                           |

(a) Gross profit is calculated as net sales less the cost of materials sold.

(b) Operating expenses are calculated as total costs and expenses less the cost of materials sold.

Tons sold decreased 11.0% to 1.04 million tons in 2015 from 1.17 million tons in 2014. Toll tons sold decreased 4.1% to 102 thousand tons in 2015 from 107 thousand tons in 2014. The decrease in tons sold was due to decreased customer demand, specifically in the heavy equipment, agriculture, mining and energy sectors, and lower industry-wide shipments of carbon flat products in 2015 compared to 2014.

Net sales decreased \$220 million, or 22.3%, to \$765.4 million in 2015 from \$985.0 million in 2014. Average selling prices in 2015 decreased 12.7% to \$738 per ton, compared to \$845 per ton in 2013. The decrease in sales was due to an 11.0% decrease in sales volume and a 12.7% decrease in average selling prices during 2015. The decrease in the average selling price is a result of declining prices in the metals industry during 2015 discussed in the overview of Results of Operations above.



Cost of materials sold decreased \$187.1 million, or 23.2%, to \$618.7 million in 2015 from \$805.7 million in 2014. The decrease in cost of materials sold was due to the volume decrease of 11.0% as well as a 13.7% decrease in the average cost of materials sold per ton during 2015 compared to 2014.

As a percentage of net sales, gross profit (as defined in footnote (a) in the table above) increased to 19.2% in 2015 from 18.2% in 2014. The increase in gross profit percentage in 2015 was primarily due to the cost of materials sold decreasing more than selling prices. The average gross profit per ton sold declined to \$141 in 2015 from \$154 in 2014 due to the significant decline in market prices for metals in 2015.

Operating expenses in 2015 decreased \$19.0 million, or 11.0%, to \$153.9 million from \$173.0 million in 2014 mirroring the sales volume decrease of 11.0%. As a percentage of net sales, operating expenses increased to 20.1% for 2015 from 17.6% in 2014. Operating expenses decreased through reductions in labor and personnel expenses, lower variable based incentive compensation, decreases in travel and entertainment expenses, and lower distribution expense as a result of lower sales volumes.

Operating loss for 2015 totaled \$7.2 million compared to operating income of \$6.3 million in 2014.

*Specialty metals flat products*

The following table sets forth certain income statement data for the specialty metals flat products segment for the years ended December 31, 2015 and 2014 (dollars shown in thousands, except per ton data):

|                                | <b>2015</b> |                               | <b>2014</b> |                               |
|--------------------------------|-------------|-------------------------------|-------------|-------------------------------|
|                                |             | <b>% of<br/>net<br/>sales</b> |             | <b>% of<br/>net<br/>sales</b> |
| Direct tons sold               | 72,041      |                               | 72,917      |                               |
| Toll tons sold                 | 36          |                               | 45          |                               |
| Total tons sold                | 72,077      |                               | 72,962      |                               |
| Net sales                      | \$192,516   | 100.0                         | \$206,692   | 100.0                         |
| Average selling price per ton  | 2,671       |                               | 2,833       |                               |
| Cost of materials sold         | 176,686     | 91.8                          | 180,812     | 87.5                          |
| Gross profit (a)               | 15,830      | 8.2                           | 25,880      | 12.5                          |
| Operating expenses (b)         | 16,904      | 8.8                           | 19,771      | 9.5                           |
| Goodwill impairment charge (c) | 500         | 0.2                           | -           | -                             |
| Operating income (loss)        | \$(1,574 )  | (0.8 )                        | \$6,109     | 3.0                           |

(a) Gross profit is calculated as net sales less the cost of materials sold.

(b) Operating expenses are calculated as total costs and expenses less the cost of materials sold. Excludes goodwill impairment charge shown separately below for comparability purposes.

(c) The non-cash goodwill impairment charge is separately displayed for operating expense comparability purposes.

Tons sold decreased 1.2% to 72 thousand tons in 2015 from 73 thousand tons in 2014. The decrease in tons sold was due to decreased customer demand and lower industry wide shipments of stainless and aluminum flat products.

Net sales decreased \$14.2 million, or 6.9%, to \$192.5 million in 2015 from \$206.7 million in 2014. Average selling prices in 2015 decreased to \$2,671 per ton, compared to \$2,833 per ton in 2014. The decrease in sales was due to a 1.2% decrease in sales volume and a 5.7% decrease in the average selling price during 2015. The decrease in the year over year average selling price per ton is a result of declining market price of nickel and aluminum, which continue to pressure stainless and aluminum pricing.

Cost of materials sold decreased \$4.1 million, or 2.3%, to \$176.7 million in 2015 from \$180.8 million in 2014. The decrease in cost of materials sold was due to the volume decrease of 1.2% and a 1.1% decrease in the average cost of

materials sold per ton during 2015 compared to 2014.

As a percentage of net sales, gross profit (as defined in footnote (a) in the table above) decreased to 8.2% in 2015 from 12.5% in 2014. The average gross profit per ton sold totaled \$220 in 2015 compared to \$355 per ton in 2014. The decrease in the gross profit percentage is a result of the declining price of nickel, which is a large component of stainless steel and aluminum pricing, and the cost of our material not declining as fast as the average sell price due to slower inventory turns in 2015.

Operating expenses (as defined in footnote (b) in the table above) decreased \$2.9 million, or 14.5%, to \$16.9 million in 2015 from \$19.8 million in 2014. The decrease in operating expenses exceeded the decrease in sales volume of 1.2%. As a percentage of net sales, operating expenses decreased to 8.8% of net sales in 2015 from 9.5% in 2014. Variable operating expenses, such as distribution and wages decreased as a result of lower sales volumes. Expenses also decreased as a result of the profit improvement plan initiated in 2015 and the decrease in variable performance-based incentive compensation in 2015 compared to 2014. In 2015 we recorded a \$0.5 million non-cash goodwill impairment charge as a result of the continued market pressures which fully eliminated the goodwill for the specialty metals flat products segment.

Operating loss for 2015 totaled \$1.6 million compared to operating income of \$6.1 million in 2014.

***Tubular and pipe products***

The following table sets forth certain income statement data for the tubular and pipe products segment for 2015 and 2014 (dollars shown in thousands).

|  | <b>2015</b> |                     | <b>2014</b> |                     |
|--|-------------|---------------------|-------------|---------------------|
|  |             | <b>% of<br/>net</b> |             | <b>% of<br/>net</b> |
|  |             | <b>sales</b>        |             | <b>sales</b>        |
| Net sales                                    | \$217,627   | 100.0               | \$244,539   | 100.0               |
| Cost of materials sold (a)                   | 146,854     | 67.5                | 173,751     | 71.1                |
| Gross profit (b)                             | 70,773      | 32.5                | 70,788      | 28.9                |
| Operating expenses (c)                       | 58,190      | 26.8                | 60,603      | 24.8                |
| Goodwill and intangible asset impairment (d) | 24,451      | 11.2                | 23,836      | 9.7                 |
| Operating loss                               | \$(11,868 ) | (5.5 )              | \$(13,651 ) | (5.6 )              |

(a) Includes \$3,347 of LIFO income in 2015 and \$365 of LIFO expense in 2014.

(b) Gross profit is calculated as net sales less the cost of materials sold.

(c) Operating expenses are calculated as total costs and expenses less the cost of materials sold.

(d) The non-cash goodwill and intangible asset impairment charges are separately displayed for operating expense comparability purposes.

Net sales decreased \$26.9 million, or 11.0%, to \$217.6 million in 2015 from \$244.5 million in 2014. The decrease in net sales was due to a 5.7% decrease in the sales volume and a 5.6% decrease in the average selling price during 2015. The decrease in volume was due to decreased customer demand and lower industry-wide shipments of pipe and tube products.

Cost of materials sold decreased \$26.9 million, or 15.5%, to \$146.9 million in 2015 from \$173.8 million in 2014. The decrease in cost of materials sold was due to a 5.7% decrease in sales volume and a 10.4% decrease in the average cost of materials sold which was impacted by the LIFO income of \$3.3 million in 2015 compared to LIFO expense of \$0.4 million in 2014.

As a percentage of net sales, gross profit (as defined in footnote (b) in the table above) increased to 32.5% in 2015 from 28.9%, in 2014. The LIFO income recorded in 2015 increased gross profit by 1.5% of net sales and the LIFO expense recorded in 2014, decreased gross profit by 0.2% of net sales. Gross profit as a percentage of net sales

increased as a result of increased value added processing sales and an increase in the product mix to higher margin sales.

Operating expenses (as defined in footnote (c) in the table above) decreased \$2.4 million, or 4.0%, to \$58.2 million from \$60.6 million in 2014. As a percentage of net sales, operating expenses increased to 26.8% for 2015 compared to 24.8% for 2014. Variable operating expenses, such as distribution and certain selling expenses, decreased as a result of lower sales volume and net sales. Depreciation expense increased as a result of recent investments in processing equipment.

In 2015 we recorded a \$16.5 million non-cash goodwill impairment charge and an \$8.0 million non-cash intangible asset impairment charge. In 2014 we recorded a \$23.8 million non-cash goodwill impairment charge.

Operating loss for 2015 totaled \$11.9 million, compared to an operating loss of \$13.7 million in 2014. The operating loss for 2015 was the result of the goodwill impairment of \$16.5 million and the asset impairment charge of \$8.0 million. The 2014 operating loss was a result of the \$23.8 million goodwill impairment as well as LIFO expense of \$0.4 million.

### *Corporate expenses*

Corporate expenses decreased \$0.9 million, or 10.7%, to \$7.1 million in 2015 compared to \$8.0 million in 2014. The decrease in corporate expenses is primarily attributable to decreases in travel and entertainment expenses and lower variable performance-based compensation in 2015 compared to 2014. Corporate expenses include the unallocated expenses related to managing the entire Company (i.e. all three segments), including compensation for certain personnel, expenses related to being a publicly traded entity such as board of directors expenses, audit expenses, and various other professional fees.

## **Liquidity, Capital Resources and Cash Flows**

Our principal capital requirements include funding working capital needs, purchasing, upgrading and acquiring processing equipment and facilities, making acquisitions and paying dividends. We use cash generated from operations, leasing transactions and borrowings under our credit facility to fund these requirements.

We believe that funds available under our credit facility, lease arrangement proceeds and the sale of equity or debt securities, together with funds generated from operations, will be sufficient to provide us with the liquidity necessary to fund anticipated working capital requirements, capital expenditure requirements, our dividend payments and share repurchases and any business acquisitions over at least the next 12 months. In the future, we may as part of our business strategy, acquire and dispose of assets or other companies in the same or complementary lines of business, or enter into or exit strategic alliances and joint ventures. Accordingly, the timing and size of our capital requirements are subject to change as business conditions warrant and opportunities arise.

## **2016 Compared to 2015**

### *Operating Activities*

During 2016, we used \$9.8 million of cash for operations, of which \$16.8 million was generated from operating activities and \$26.6 million was used for working capital. During 2015, we generated \$107.5 million of cash from operations, of which \$12.4 million was generated from operating activities and \$95.1 million was generated from working capital.

Net cash used for operations totaled \$16.8 million during 2016 and was primarily comprised of depreciation and amortization of \$19.4 million offset by the net change in long-term assets and liabilities of \$1.7 million and the net loss of \$1.1 million. Net cash from operations totaled \$12.4 million during 2015 and was primarily comprised of depreciation and amortization of \$19.9 million and the non-cash goodwill and intangible asset impairment of \$25.0 million, offset by the net loss of \$26.8 million.

Working capital at December 31, 2016 totaled \$260.0 million, a \$28.2 million increase from December 31, 2015. The increase was primarily attributable to a \$47.9 million increase in inventory (resulting from increased inventory purchases at the end of 2016), a \$9.0 million increase in accounts receivable (resulting primarily from higher sales

volume at the end of 2016) offset by a \$23.8 million increase in accounts payable and outstanding checks (resulting from the increased inventory purchases at the end of 2016) and a \$4.9 million increase in accrued payroll and other accrued liabilities.

### ***Investing Activities***

Net cash used for investing activities was \$6.4 million during 2016, compared to \$7.3 million during 2015. In 2016 capital expenditures were primarily attributable to additional processing equipment and facilities maintenance. During 2017, we expect our capital spending to approximate our annual depreciation levels of \$17 million.

### ***Financing Activities***

In 2016, \$17.0 million of cash was generated from financing activities which primarily consisted of \$18.8 million of net borrowings under our ABL Credit Facility. In 2015, \$100.8 million of cash was used for financing activities which primarily consisted of \$98.3 million of net repayments under our ABL facility.

In February 2017, our Board of Directors approved a regular quarterly dividend of \$0.02 per share, which is payable on March 15, 2017 to shareholders of record as of March 1, 2017. Our Board previously approved 2016 regular quarterly dividends of \$0.02 per share, which were paid on each of March 15, 2016, June 15, 2016, September 15, 2016 and December 15, 2016. Dividend distributions in the future are subject to the availability of cash, the \$2.5 million annual limitation on cash dividends under our ABL Credit Facility and continuing determination by our Board of Directors that the payment of dividends remains in the best interest of our shareholders.

### ***Stock Repurchase Program***

On October 2, 2015, we announced that our Board of Directors authorized a stock repurchase program of up to 550,000 shares of the Company's issued and outstanding common stock, which could include open market repurchases, negotiated block transactions, accelerated stock repurchases or open market solicitations for shares, all or some of which may be effected through Rule 10b5-1 plans. Repurchased shares are held in our treasury, or canceled and retired as our Board may determine from time to time. Any repurchases of common stock are subject to the covenants contained in the ABL Credit Facility. Under the ABL Credit Facility, we may repurchase common stock and pay dividends up to \$2.5 million in the aggregate during any trailing twelve months without restrictions. Purchases in excess of \$2.5 million require us to (i) maintain availability in excess of 25% of the aggregate revolver commitments (\$91.3 million at December 31, 2016) or (ii) to maintain availability equal to or greater than 15% of the aggregate revolver commitments (\$54.8 million at December 31, 2016) and we must maintain a pro-forma ratio of EBITDA minus certain capital expenditures and cash taxes paid to fixed charges of at least 1.00 to 1.00. The timing and amount of any repurchases under the stock repurchase program will depend upon several factors, including market and business conditions, and limitations under the ABL Credit Facility, and repurchases may be discontinued at any time. During 2017, we expect to be limited to the \$2.5 million available without restrictions to repurchase common stock and pay dividends.

There were no shares repurchased during 2016. During the fourth quarter of 2015, we repurchased 65,283 shares for a total cost of \$0.7 million.

### ***Debt Arrangements***

Our ABL Credit Facility is collateralized by our accounts receivable and inventory. The ABL Credit Facility consists of a revolving credit line of \$365 million. Revolver borrowings are limited to the lesser of a borrowing base, comprised of eligible receivables and inventories, or \$365 million in the aggregate. The ABL Credit Facility matures on June 30, 2019.

The ABL Credit Facility requires us to comply with various covenants, the most significant of which include: (i) if any commitments or obligations are outstanding and our availability is less than the greater of \$30 million or 10.0% of the aggregate amount of revolver commitments (\$36.5 million at December 31, 2016) then we must maintain a ratio of EBITDA minus certain capital expenditures and cash taxes paid to fixed charges of at least 1.00 to 1.00 for the most recent twelve fiscal month period; (ii) limitations on dividend payments and stock repurchases; and (iii) restrictions on additional indebtedness. We have the option to borrow under our revolver based on the agent's base rate plus a premium ranging from 0.00% to 0.25% or the London Interbank Offered Rate (LIBOR) plus a premium ranging from 1.25% to 3.00%.



As of December 31, 2016, we were in compliance with our covenants and we had approximately \$94.3 million of availability under the ABL Credit Facility.

As of December 31, 2016, \$2.0 million of bank financing fees were included in “Prepaid expenses and other” and “Other long-term assets” on the accompanying Consolidated Balance Sheets. The financing fees are being amortized over the five-year term of the ABL Credit facility and are included in “Interest and other expense on debt” on the accompanying Consolidated Statements of Comprehensive Income.

We entered into a forward starting fixed rate interest rate hedge that commenced June 2013, in order to eliminate the variability of cash interest payments on \$53.2 million of the then outstanding LIBOR-based borrowings under the ABL Credit Facility. The hedge, which matured on June 1, 2016, fixed the rate at 1.21% plus a premium ranging from 1.25% to 1.75%.

As part of the CTI acquisition in July 2011, we assumed approximately \$5.9 million of Industrial Revenue Bond (IRB) indebtedness. The bond matures in April 2018, with the option to provide principal payments annually on April 1st. On April 1, 2016, we paid an optional principal payment of \$0.9 million. Since the IRB is remarketed annually, it is included in “Current portion of long-term debt” on the accompanying Consolidated Balance Sheets. Interest is payable monthly, with a variable rate that resets weekly. As a security for payment of the bonds, we obtained a direct pay letter of credit issued by JPMorgan Chase Bank, N.A. The letter of credit reduces annually by the principal reduction amount. The interest rate at December 31, 2016 was 1.0% for the IRB debt.

CTI entered into an interest rate swap agreement to reduce the impact of changes in interest rates on the above IRB. At December 31, 2016, the effect of the swap agreement on the bond was to fix the rate at 3.46%. The swap agreement matures in April 2018, and is reduced annually by the amount of the optional principal payments on the bond. We are exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreement. However, we do not anticipate nonperformance by the counterparties.

## **2015 Compared to 2014**

### ***Operating Activities***

During 2015, we generated \$107.5 million of cash from operations, of which \$12.4 million was generated from operating activities and \$95.1 million was generated from working capital. During 2014, we used \$39.6 million of cash for operations, of which \$25.4 million was generated from operating activities and \$65.0 million was used for working capital.

Net cash from operations totaled \$12.4 million during 2015 and was primarily comprised of depreciation and amortization of \$19.9 million and the non-cash goodwill and intangible asset impairment of \$25.0 million, offset by the net loss of \$26.8 million. Net cash from operations totaled \$25.4 million during 2014 and was primarily comprised of depreciation and amortization of \$21.8 million and the non-cash goodwill impairment of \$23.8 million, offset by the net loss of \$19.1 million.

Working capital at December 31, 2015 totaled \$231.9 million, a \$94.8 million decrease from December 31, 2014. The decrease was primarily attributable to a \$104.5 million decrease in inventory (resulting from decreased inventory purchases and lower metals cost in 2015 compared to 2014) and a \$30.9 million decrease in accounts receivable (resulting from lower sales volume and selling prices), offset by a \$35.6 million decrease in accounts payable and outstanding checks and a \$18.5 million decrease in accrued payroll and other accrued liabilities. The decrease in prepaid expenses and other and accrued payroll and other accrued liabilities is mainly related to the decrease in metals derivatives.

### ***Investing Activities***

Net cash used for investing activities was \$7.3 million during 2015, compared to \$7.8 million during 2014. In 2015, capital expenditures were primarily attributable to additional processing equipment at our flat products (carbon and specialty metals) and tube and pipe products existing facilities.

### ***Financing Activities***

In 2015, \$100.8 million of cash was used for financing activities which primarily consisted of \$98.3 million of net repayments under our ABL Credit Facility. In 2014, \$46.4 million of cash was generated from financing activities, which primarily consisted of \$49.2 million of net borrowings under our credit facility, including the payoff of our term loan of \$48.9 million upon refinancing and subsequent borrowings under our revolving credit facility, offset by \$1.2 million of additional deferred financing fees incurred as part of the June 30, 2014 amendment to the ABL Credit Facility (as defined below).

Our Board previously approved 2015 and 2014 regular quarterly dividends of \$0.02 per share, which were paid in March, June, September and December of 2015 and 2014.

## Contractual Obligations

The following table reflects our contractual obligations as of December 31, 2016:

| Contractual Obligations<br>(amounts in thousands) | Total      | Less than |            | More than |          |
|---|------------|-----------|------------|-----------|----------|
|   |            | 1 year    | 1-3 years  | 3-5 years | 5 years  |
| Long-term debt obligations (a)                    | \$ 166,424 | \$ 895    | \$ 165,529 | \$-       | \$-      |
| Interest obligations (b)                          | 9,885      | 3,975     | 5,910      | -         | -        |
| Unrecognized tax positions (c)                    | 40         | 14        | 26         | -         | -        |
| Other long-term liabilities (d)                   | 10,422     | 607       | 5,448      | 3,078     | 1,288    |
| Operating leases (e)                              | 26,466     | 6,634     | 10,315     | 6,235     | 3,282    |
| Total contractual obligations                     | \$ 213,237 | \$ 12,125 | \$ 187,228 | \$ 9,313  | \$ 4,570 |

(a) See Note 6 to the Consolidated Financial Statements.

(b) Future interest obligations are calculated using the debt balances and interest rates in effect on December 31, 2016.

(c) See Note 12 to the Consolidated Financial Statements. Classification is based on expected settlement dates and the expiration of certain statutes of limitations.

(d) Primarily consists of retirement liabilities and deferred compensation payable in future years.

(e) See Note 11 to the Consolidated Financial Statements.

## Off-Balance Sheet Arrangements

An off-balance sheet arrangement is any contractual arrangement involving an unconsolidated entity under which a company has (a) made guarantees, (b) a retained or a contingent interest in transferred assets, (c) any obligation under certain derivative instruments or (d) any obligation under a material variable interest in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to a company, or engages in leasing, hedging, or research and development services within a company.

Other than operating leases, which are disclosed above, and derivative instruments discussed in Note 7 to the Consolidated Financial Statements, as of December 31, 2016, we had no material off-balance sheet arrangements.

### **Effects of Inflation**

Inflation generally affects us by increasing the cost of employee wages and benefits, transportation services, processing equipment, purchased metals, energy and borrowings under our credit facility. General inflation, excluding increases in the price of metals and increased distribution expense, has not had a material effect on our financial results during the past three years.

### **Critical Accounting Policies**

This discussion and analysis of financial condition and results of operations is based on our consolidated financial statements, which have been prepared in conformity with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from these estimates under different assumptions or conditions. On an on-going basis, we monitor and evaluate our estimates and assumptions.

We believe the following critical accounting policies affect our more significant judgments and estimates used in preparation of our consolidated financial statements:

#### Allowance for Doubtful Accounts Receivable

We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. The allowance is maintained at a level considered appropriate based on historical experience and specific customer collection issues that we have identified. Estimations are based upon the application of a historical collection rate to the outstanding accounts receivable balance, which remains fairly level from year to year, and judgments about the probable effects of economic conditions on certain customers, which can fluctuate significantly from year to year. We cannot be certain that the rate of future credit losses will be similar to past experience. We consider all available information when assessing the adequacy of our allowance for doubtful accounts each quarter.

#### Inventory Valuation

Inventories are stated at the lower of cost or market and include the costs of the purchased metals, inbound freight, external and internal processing and applicable labor and overhead costs. Costs of our flat product segment's inventories, including flat-rolled sheet, coil and plate products are determined using the specific identification method.

Certain of our tubular and pipe products inventory is stated under the LIFO method. At December 31, 2016, approximately \$43.4 million, or 17.1% of consolidated inventory, was reported under the LIFO method of accounting. The cost of the remainder of tubular and pipe product segment's inventory is determined using a weighted average rolling first-in, first-out method.

#### Intangible Assets

The Company performs an annual impairment test of indefinite-lived intangible assets for the tubular and pipe products segment in the fourth quarter, or more frequently if changes in circumstances or the occurrence of events indicate potential impairment. Events or changes in circumstances that could trigger an impairment review include significant nonperformance relative to the expected historical or projected future operating results, significant changes in the manner of the use of the acquired assets or the strategy for the overall business or significant negative industry

or economic trends. Management uses judgment to determine whether to use a qualitative analysis or a quantitative fair value measurement for each of the Company's reporting units that carry intangible assets.

If a quantitative fair value measurement is used, the fair value of each indefinite-lived intangible asset is compared to its carrying value and an impairment charge is recorded if the carrying value exceeds the fair value. The Company estimates the fair value of indefinite-lived intangible assets using a discounted cash flow methodology. Management's assumptions used for the calculations are based on historical results, projected financial information and recent economic events. Actual results could differ from these estimates under different assumptions or conditions which could adversely affect the reported value of intangible assets.

### Long-Lived Assets

The Company evaluates the recoverability of long-lived assets and the related estimated remaining lives whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Events or changes in circumstances that could trigger an impairment review include significant underperformance relative to the expected historical or projected future operating results, significant changes in the manner of the use of the acquired assets or the strategy for the overall business or significant negative industry or economic trends. The Company records an impairment or change in useful life whenever events or changes in circumstances indicate that the carrying amount may not be recoverable or the useful life has changed.

### Income Taxes

Deferred income taxes on the consolidated balance sheet include, as an offset to the estimated temporary differences between the tax basis of assets and liabilities and the reported amounts on the consolidated balance sheets, the tax effect of operating loss and tax credit carryforwards. If we determine that we will not be able to fully realize a deferred tax asset, we will record a valuation allowance to reduce such deferred tax asset to its net realizable value.

### Revenue Recognition

For both direct and toll shipments, revenue is recognized when title and risk of loss is transferred, which generally occurs upon delivery to our customers. Given the proximity of our customers to our facilities, substantially all of our sales are shipped and received within one day. Sales returns and allowances are treated as reductions to sales and are provided for based on historical experience and current estimates and are immaterial to the consolidated financial statements.

Certain engineered products produced by CTI can take several months to manufacture due to their size and complexity. Substantially all projects are completed within six months. The Company may request advance payments from customers during the production of these products. These payments are included in "Other accrued liabilities" on the Company's Consolidated Balance Sheets. Due to their short-term nature, the Company uses the units of delivery method to account for these contracts. Revenue for the contracts is recognized when the product is shipped and title of the product transfers to the customers. Revenues for these engineered products accounted for approximately 1.7%, 1.8% and 1.7% of our net sales during 2016, 2015 and 2014, respectively.

### **Impact of Recently Issued Accounting Pronouncements**

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No 2016-15, "Classification of certain cash receipts and cash payments". This ASU addresses the following eight specific cash flow issues: Debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies (COLIs) (including bank-owned life insurance policies (BOLIs)); distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. The guidance will be effective for annual reporting periods beginning after December 15, 2017, and interim periods within those fiscal years with early adoption permitted. The adoption of this ASU is not expected to materially impact the Company's consolidated financial statements.

In March 2016, the FASB issued ASU No 2016-09, "Improvements to Employee Share-Based Payment Accounting". This ASU is part of the FASB's Simplification Initiative and has been issued to reduce complexity in the presentation of employee share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The guidance will be effective for annual reporting periods beginning after December 15, 2016 and interim periods within those fiscal years with early adoption permitted. The adoption of this ASU is not expected to materially impact the Company's consolidated financial statements.



In February 2016, the FASB issued ASU No. 2016-02, "Leases", which specifies the accounting for leases. The objective is to establish the principles that lessees and lessors shall apply to report useful information to users of financial statements about the amount, timing and uncertainty of cash flows arising from a lease. This ASU introduces the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous guidance. The guidance will be effective for annual reporting periods beginning after December 15, 2018 and interim periods within those fiscal years with early adoption permitted. We are in the process of evaluating the impact of the future adoption of this standard on our consolidated financial statements.

In November 2015, the FASB issued ASU No. 2015-17, "Balance Sheet Classification of Deferred Taxes." This ASU is part of the FASB's Simplification Initiative and has been issued to reduce complexity in the presentation of deferred taxes. This new guidance eliminates the requirement for entities that present a classified statement of financial position to classify deferred tax assets and liabilities as current and noncurrent, and instead require that they classify all deferred tax assets and liabilities as noncurrent. As a result, each jurisdiction will now only have one net noncurrent deferred tax asset or liability. However, the guidance does not change the existing requirement that only permits offsetting within a jurisdiction. Companies are still prohibited from offsetting deferred tax liabilities from one jurisdiction against deferred tax assets of another jurisdiction. This ASU is effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years, with early adoption permitted. The guidance may be applied either prospectively, for all deferred tax assets and liabilities, or retrospectively (i.e., by reclassifying the comparative balance sheet). If applied prospectively, entities are required to include a statement that prior periods were not retrospectively adjusted. If applied retrospectively, entities are also required to include quantitative information about the effects of the change on prior periods. The prospective adoption of this guidance on January 1, 2016 did not have a material impact on our consolidated financial statements and the prior periods were not retrospectively adjusted.

In April 2015, the FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs." This ASU is part of the FASB's Simplification Initiative and has been issued to reduce the complexity in the presentation of debt issuance costs. This new guidance requires companies to present debt issuance costs the same way they currently present debt discounts, as a direct deduction from the carrying value of that debt liability. The guidance is limited to simplifying the presentation of debt issuance costs and does not impact the recognition and measurement guidance for debt issuance costs. This ASU is effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years, with early adoption permitted. The amendments of ASU No. 2015-03 must be applied retrospectively, where the balance sheet of each presented individual period is adjusted to indicate the period-specific impact of using the new guidance. The FASB considered that because both debt issuance costs and debt discounts are amortized using the effective interest method, there would be no effect on the income statement upon adoption of the amendments. The adoption of this guidance on January 1, 2016 did not have an impact on our consolidated financial statements because it does not apply to revolving credit agreements.

In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements – Going Concern". This ASU contains new guidance on management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. Management must evaluate whether it is probable that known conditions or events, considered in the aggregate, would raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. If such conditions or events are identified, the standard requires management's mitigation plans to alleviate the doubt or a statement of the substantial doubt about the entity's ability to continue as a going concern to be disclosed in the financial statements. This ASU is effective for fiscal years and interim periods beginning after December 15, 2016, with early adoption permitted. The adoption of this ASU did not impact our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." This ASU is a joint project initiated by the FASB and the International Accounting Standards Board to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. generally accepted accounting principles and International Financial Reporting Standards that will: remove inconsistencies and weaknesses in revenue requirements; provide a more robust framework for addressing revenue issues; improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets; provide more useful information to users of financial statements through improved disclosure requirements; and simplify the preparation of financial statements by reducing the number of requirements to which an entity must refer. As originally proposed, the guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The adoption of this ASU is not expected to materially impact the Company's consolidated financial statements. In August 2015, the FASB issued ASU No. 2015-14, "Revenue from Contracts with Customers." This ASU deferred the effective date of ASU No. 2014-09 by one year.

## ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our principal raw materials are carbon, coated and stainless steel, and aluminum, pipe and tube, flat rolled coil, sheet and plate that we typically purchase from multiple primary metals producers. The metals industry as a whole is cyclical and, at times, pricing and availability of metals can be volatile due to numerous factors beyond our control, including general domestic and international economic conditions, the levels of metals imported into the United States, labor costs, sales levels, competition, levels of inventory held by other metals service centers, consolidation of metals producers, new global capacity by metals producers, higher raw material costs for the producers of metals, import duties and tariffs and currency exchange rates. This volatility can significantly affect the availability and cost of raw materials for us.

We, like many other metals service centers, maintain substantial inventories of metals to accommodate the short lead times and just-in-time delivery requirements of our customers. Accordingly, we purchase metals in an effort to maintain our inventory at levels that we believe to be appropriate to satisfy the anticipated needs of our customers based upon historic buying practices, supply agreements with customers and market conditions. Our commitments to purchase metals are generally at prevailing market prices in effect at the time we place our orders. We have no long-term, fixed-price metals purchase contracts. When metals prices increase, competitive conditions will influence how much of the price increase we can pass on to our customers. To the extent we are unable to pass on future price increases in our raw materials to our customers, the net sales and profitability of our business could be adversely affected. When metals prices decline, customer demands for lower prices and our competitors' responses to those demands could result in lower sale prices and, consequently, lower gross profits and inventory lower of cost or market adjustments as we sell existing inventory. Significant or rapid declines in metals prices or reductions in sales volumes could adversely impact our ability to remain in compliance with certain financial covenants in our credit facility, as well as result in us incurring inventory or intangible asset impairment charges. Changing metals prices therefore could significantly impact our net sales, gross profits, operating income and net income.

Rising metals prices result in higher working capital requirements for us and our customers. Some customers may not have sufficient credit lines or liquidity to absorb significant increases in the price of metals. While we have generally been successful in the past in passing on producers' price increases and surcharges to our customers, there is no guarantee that we will be able to pass on price increases to our customers in the future. Declining metals prices have generally adversely affected our net sales and net income, while increasing metals prices have generally favorably affected our net sales and net income.

Approximately 51%, 49% and 51% of our consolidated net sales in 2016, 2015 and 2014, respectively, were directly related to industrial machinery and equipment manufacturers and their fabricators.

Inflation generally affects us by increasing the cost of employee wages and benefits, transportation services, processing equipment, energy and borrowings under our credit facility. General inflation has not had a material effect

on our financial results during the past three years.

We are exposed to the impact of fluctuating metals prices and interest rate changes. During 2016, 2015 and 2014, we entered into metals swaps at the request of customers. While these derivatives are intended to be effective in helping us manage risk, they have not been designated as hedging instruments. For certain customers, we enter into contractual relationships that entitle us to pass-through the economic effect of trading positions that we take with other third parties on our customers' behalf. In 2014, we entered into carbon swaps in order to mitigate the volatility in the price of metals. The carbon swaps were accounted for as cash flow hedges and all of them settled in 2015. We had no outstanding metals cash flow hedges at December 31, 2016.

Our primary interest rate risk exposure results from variable rate debt. If interest rates in the future were to increase 100 basis points (1.0%) from December 31, 2016 rates and, assuming no change in total debt from December 31, 2016 levels, the additional annual interest expense to us would be approximately \$1.6 million. We have the option to enter into 30- to 180-day fixed base rate LIBOR loans under the ABL Credit Facility. The Company assumed an interest rate swap agreement on the \$5.9 million of CTI IRB. The swap agreement matures in April 2018, but the notional amount may be reduced annually by the amount of the optional principal payments on the IRB. The Company is exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreements. However, the Company does not anticipate nonperformance by the counterparties.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

**Olympic Steel, Inc.**

**Index to Consolidated Financial Statements**

|  | <u>Page</u> |
|--|-------------|
| Report of Independent Registered Public Accounting Firm  | 49          |
| Management's Report on Internal Control Over Financial Reporting                                       | 50          |
| Consolidated Statements of Comprehensive Income for the Years Ended December 31, 2016, 2015 and 2014   | 51          |
| Consolidated Balance Sheets as of December 31, 2016 and 2015   | 52          |
| Consolidated Statements of Cash Flows for the Years Ended December 31, 2016, 2015 and 2014             | 53          |
| Supplemental Disclosures of Cash Flow Information for the Years Ended December 31, 2016, 2015 and 2014 | 54          |
| Consolidated Statements of Shareholders' Equity for the Years Ended December 31, 2016, 2015 and 2014   | 55          |
| Notes to Consolidated Financial Statements for the Years Ended December 31, 2016, 2015 and 2014        | 56          |

## Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of Olympic Steel, Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Olympic Steel, Inc. and its subsidiaries at December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 15(a)(2) presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements and financial statement schedule, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express opinions on these financial statements, on the financial statement schedule and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

Cleveland, Ohio

March 2, 2017

## MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2016. In making this assessment, our management used the criteria established in *Internal Control - Integrated Framework (2013)*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our assessment, we concluded that, as of December 31, 2016, our internal control over financial reporting was effective based on those criteria.

The effectiveness of our internal control over financial reporting as of December 31, 2016 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which appears herein.



**Olympic Steel, Inc.****Consolidated Statements of Comprehensive Income****For The Years Ended December 31,**

(in thousands, except per share data)

|   | <b>2016</b>        | 2015        | 2014        |
|---|--------------------|-------------|-------------|
| Net sales   | <b>\$1,055,116</b> | \$1,175,543 | \$1,436,270 |
| Costs and expenses  |                    |             |             |
| Cost of materials sold (excludes items shown separately below)                | <b>820,040</b>     | 942,214     | 1,160,310   |
| Warehouse and processing  | <b>79,521</b>      | 85,411      | 92,170      |
| Administrative and general  | <b>63,054</b>      | 64,987      | 72,219      |
| Distribution  | <b>36,490</b>      | 36,073      | 41,312      |
| Selling   | <b>23,060</b>      | 21,158      | 24,799      |
| Occupancy   | <b>8,718</b>       | 9,492       | 10,052      |
| Depreciation  | <b>17,596</b>      | 18,147      | 19,891      |
| Amortization  | <b>889</b>         | 889         | 889         |
| Goodwill and intangible asset impairment                                      | -                  | 24,951      | 23,836      |
| Total costs and expenses  | <b>1,049,368</b>   | 1,203,322   | 1,445,478   |
| Operating income (loss)   | <b>5,748</b>       | (27,779 )   | (9,208 )    |
| Other loss, net   | <b>(55 )</b>       | (125 )      | (126 )      |
| Income (loss) before interest and income taxes                                | <b>5,693</b>       | (27,904 )   | (9,334 )    |
| Interest and other expense on debt  | <b>5,273</b>       | 5,690       | 6,780       |
| Income (loss) before income taxes   | <b>420</b>         | (33,594 )   | (16,114 )   |
| Income tax provision (benefit)  | <b>1,498</b>       | (6,817 )    | 2,950       |
| Net loss  | <b>\$(1,078 )</b>  | \$(26,777 ) | \$(19,064 ) |
| Gain (loss) on cash flow hedges   | <b>114</b>         | (1,816 )    | 12          |
| Tax effect of hedges  | <b>(44 )</b>       | 699         | (125 )      |
| Reclassification of loss included in net income, net of tax of \$804 for 2015 | -                  | 1,596       | -           |
| Total comprehensive loss  | <b>\$(1,008 )</b>  | \$(26,298 ) | \$(19,177 ) |
| Net loss per share - basic  | <b>\$(0.10 )</b>   | \$(2.39 )   | \$(1.71 )   |
| Weighted average shares outstanding - basic                                   | <b>11,210</b>      | 11,192      | 11,120      |
| Net loss per share - diluted  | <b>\$(0.10 )</b>   | \$(2.39 )   | \$(1.71 )   |
| Weighted average shares outstanding - diluted                                 | <b>11,210</b>      | 11,192      | 11,120      |
| Dividends declared per share of common stock                                  | \$0.08             | \$0.08      | \$0.08      |

*The accompanying notes are an integral part of these statements.*



**Olympic Steel, Inc.****Consolidated Balance Sheets****As of December 31,**

(in thousands)

|  | <b>2016</b>      | <b>2015</b> |
|--|------------------|-------------|
| <b>Assets</b>  |                  |             |
| Cash and cash equivalents  | <b>\$2,315</b>   | \$1,604     |
| Accounts receivable, net   | <b>101,902</b>   | 92,877      |
| Inventories, net (includes LIFO debit of \$8,045 and \$6,555 as of December 31, 2016 and 2015, respectively) | <b>254,526</b>   | 206,645     |
| Prepaid expenses and other   | <b>6,197</b>     | 7,820       |
| Total current assets   | <b>364,940</b>   | 308,946     |
| Property and equipment, at cost  | <b>374,242</b>   | 372,129     |
| Accumulated depreciation   | <b>(218,476)</b> | (205,591)   |
| Net property and equipment   | <b>155,766</b>   | 166,538     |
| Intangible assets, net   | <b>23,869</b>    | 24,757      |
| Other long-term assets   | <b>11,493</b>    | 11,639      |
| Total assets   | <b>\$556,068</b> | \$511,880   |
| <b>Liabilities</b>   |                  |             |
| Current portion of long-term debt  | <b>\$1,825</b>   | \$2,690     |
| Accounts payable   | <b>79,458</b>    | 55,685      |
| Accrued payroll  | <b>8,445</b>     | 6,884       |
| Other accrued liabilities  | <b>15,170</b>    | 11,801      |
| Total current liabilities  | <b>104,898</b>   | 77,060      |
| Credit facility revolver   | <b>164,599</b>   | 145,800     |
| Other long-term liabilities  | <b>10,062</b>    | 9,829       |
| Deferred income taxes  | <b>23,119</b>    | 24,496      |
| Total liabilities  | <b>302,678</b>   | 257,185     |
| Commitments and contingencies (Note 11)  |                  |             |
| <b>Shareholders' Equity</b>  |                  |             |
| Preferred stock, without par value, 5,000 shares authorized, no shares issued or outstanding                 | -                | -           |
| Common stock, without par value, 20,000 shares authorized, 10,963 and 10,955 shares issued and outstanding   | <b>128,619</b>   | 128,129     |
| Treasury stock, at cost, 57 and 65 shares held   | <b>(609 )</b>    | (699 )      |
| Accumulated other comprehensive loss   | -                | (70 )       |
| Retained earnings  | <b>125,380</b>   | 127,335     |
| Total shareholders' equity   | <b>253,390</b>   | 254,695     |
| Total liabilities and shareholders' equity   | <b>\$556,068</b> | \$511,880   |

*The accompanying notes are an integral part of these balance sheets.*

**Olympic Steel, Inc.****Consolidated Statements of Cash Flows****For The Years Ended December 31,**

(in thousands)

|   | <b>2016</b>       | 2015        | 2014        |
|---|-------------------|-------------|-------------|
| Cash flows from (used for) operating activities:  |                   |             |             |
| Net loss  | <b>\$(1,078 )</b> | \$(26,777 ) | \$(19,064 ) |
| Adjustments to reconcile net income (loss) to net cash from operating activities -            |                   |             |             |
| Depreciation and amortization   | <b>19,402</b>     | 19,873      | 21,840      |
| Goodwill and intangible asset impairment  | -                 | 24,951      | 23,836      |
| (Gain) loss on disposition of property and equipment  | <b>(376 )</b>     | 15          | 248         |
| Stock-based compensation  | <b>534</b>        | 1,759       | 2,074       |
| Other long-term assets  | <b>(638 )</b>     | 44          | (766 )      |
| Other long-term liabilities   | <b>(1,074 )</b>   | (7,500 )    | (2,754 )    |
|   | <b>16,770</b>     | 12,365      | 25,414      |
| Changes in working capital:   |                   |             |             |
| Accounts receivable   | <b>(9,025 )</b>   | 30,927      | (8,516 )    |
| Inventories   | <b>(47,881 )</b>  | 104,463     | (24,737 )   |
| Prepaid expenses and other  | <b>1,620</b>      | 13,808      | (7,648 )    |
| Accounts payable  | <b>28,619</b>     | (21,923 )   | (24,090 )   |
| Change in outstanding checks  | <b>(4,846 )</b>   | (13,644 )   | (10,670 )   |
| Accrued payroll and other accrued liabilities   | <b>4,930</b>      | (18,511 )   | 10,663      |
|   | <b>(26,583 )</b>  | 95,120      | (64,998 )   |
| Net cash from (used for) operating activities   | <b>(9,813 )</b>   | 107,485     | (39,584 )   |
| Cash flows from (used for) investing activities:  |                   |             |             |
| Capital expenditures  | <b>(6,824 )</b>   | (7,317 )    | (7,834 )    |
| Proceeds from disposition of property and equipment   | <b>376</b>        | 3           | 68          |
| Net cash used for investing activities  | <b>(6,448 )</b>   | (7,314 )    | (7,766 )    |
| Cash flows from (used for) financing activities:  |                   |             |             |
| Credit facility revolver borrowings   | <b>307,298</b>    | 311,372     | 632,726     |
| Credit facility revolver repayments   | <b>(288,499)</b>  | (409,662)   | (534,711)   |
| Term loan repayments  | -                 | -           | (48,854 )   |
| Industrial revenue bond repayments  | <b>(865 )</b>     | (840 )      | (810 )      |
| Credit facility fees and expenses   | <b>(131 )</b>     | (127 )      | (1,218 )    |
| Proceeds from exercise of stock options (including tax benefits) and employee stock purchases | <b>46</b>         | 30          | 147         |
| Repurchase of common stock  | -                 | (699 )      | -           |
| Dividends paid  | <b>(877 )</b>     | (879 )      | (878 )      |
| Net cash from (used for) financing activities   | <b>16,972</b>     | (100,805)   | 46,402      |

Cash and cash equivalents:

|                   |                |         |         |
|-------------------|----------------|---------|---------|
| Net change        | <b>711</b>     | (634 )  | (948 )  |
| Beginning balance | <b>1,604</b>   | 2,238   | 3,186   |
| Ending balance    | <b>\$2,315</b> | \$1,604 | \$2,238 |

*The accompanying notes are an integral part of these statements.*

**Olympic Steel, Inc.**

**Supplemental Disclosures of Cash Flow Information**

**For The Years Ended December 31,**

(in thousands)

|                                    | <b>2016</b>    | 2015    | 2014    |
|------------------------------------|----------------|---------|---------|
| <i>Cash paid during the period</i> |                |         |         |
| Interest paid                      | <b>\$4,300</b> | \$5,083 | \$5,793 |
| Income taxes paid                  | <b>\$982</b>   | \$565   | \$4,658 |

*The accompanying notes are an integral part of these statements*

**Olympic Steel, Inc.****Consolidated Statements of Shareholders' Equity****For The Years Ended December 31,**

(in thousands)

|   | <b>Common<br/>Stock</b> | <b>Treasury<br/>Stock</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Loss</b> | <b>Retained<br/>Earnings</b> | <b>Total<br/>Equity</b> |
|---|-------------------------|---------------------------|---|------------------------------|-------------------------|
| Balance at December 31, 2013                                      | \$124,118               | \$ -                      | \$ (437 )   | \$174,935                    | \$298,616               |
| Net loss  | \$-                     | \$ -                      | \$ -  | \$(19,064 )                  | \$(19,064 )             |
| Payment of dividends  | -                       | -                         | -   | (878 )                       | (878 )                  |
| Exercise of stock options and employee stock purchases (7 shares) | 147                     | -                         | -   | -                            | 147                     |
| Stock-based compensation  | 2,074                   | -                         | -   | -                            | 2,074                   |
| Changes in fair value of hedges                                   | -                       | -                         | (113 )  | -                            | (113 )                  |
| Other   | -                       | -                         | 1   | (2 )                         | (1 )                    |
| Balance at December 31, 2014                                      | \$126,339               | \$ -                      | \$ (549 )   | \$154,991                    | \$280,781               |
| Net loss  | \$-                     | \$ -                      | \$ -  | \$(26,777 )                  | \$(26,777 )             |
| Repurchase of common stock  | -                       | (699 )                    | -   | -                            | (699 )                  |
| Payment of dividends  | -                       | -                         | -   | (879 )                       | (879 )                  |
| Exercise of stock options and employee stock purchases (2 shares) | 30                      | -                         | -   | -                            | 30                      |
| Stock-based compensation  | 1,759                   | -                         | -   | -                            | 1,759                   |
| Changes in fair value of hedges                                   | -                       | -                         | 479   | -                            | 479                     |
| Other   | 1                       | -                         | -   | -                            | 1                       |
| Balance at December 31, 2015                                      | \$128,129               | \$ (699 )                 | \$ (70 )  | \$127,335                    | \$254,695               |
| <b>Net loss</b>   | <b>\$-</b>              | <b>\$ -</b>               | <b>\$ -</b>   | <b>\$(1,078 )</b>            | <b>\$(1,078 )</b>       |
| <b>Payment of dividends</b>                                       | <b>-</b>                | <b>-</b>                  | <b>-</b>  | <b>(877 )</b>                | <b>(877 )</b>           |
| <b>Employee stock purchases (3 shares)</b>                        | <b>46</b>               | <b>-</b>                  | <b>-</b>  | <b>-</b>                     | <b>46</b>               |
| <b>Stock-based compensation</b>                                   | <b>444</b>              | <b>90</b>                 | <b>-</b>  | <b>-</b>                     | <b>534</b>              |
| <b>Changes in fair value of hedges</b>                            | <b>-</b>                | <b>-</b>                  | <b>70</b>   | <b>-</b>                     | <b>70</b>               |
| <b>Balance at December 31, 2016</b>                               | <b>\$128,619</b>        | <b>\$ (609 )</b>          | <b>-</b>  | <b>\$125,380</b>             | <b>\$253,390</b>        |

*The accompanying notes are an integral part of these statements.*





**Olympic Steel, Inc.**

**Notes to Consolidated Financial Statements**

**For The Years Ended December 31, 2016, 2015 and 2014**

***1. Summary of Significant Accounting Policies:***

**Nature of Business**

The Company is a leading U.S. metals service center specializing in the processing and distribution of large volumes of carbon, coated, aluminum and stainless steel, flat-rolled coil, sheet and plate products and tubular and pipe products from facilities throughout the United States. The Company operates in three reportable segments; carbon flat products, specialty metals flat products, and tubular and pipe products. The carbon flat products segment and the specialty metals flat products segments are at times consolidated and referred to as the flat products segments. The flat products segments' assets and resources are shared by the carbon and specialty metals segments and both segments' products are stored in the shared facilities and, in some locations, processed on shared equipment. Due to the shared assets and resources, certain of the flat products segment expenses are allocated between the carbon flat products segment and the specialty metals flat products segment based upon an established allocation methodology. Through its carbon flat products segment, the Company sells and distributes large volumes of processed carbon and coated flat-rolled sheet, coil and plate products, and fabricated parts. Through its specialty metals flat products segment, the Company sells and distributes processed aluminum and stainless flat-rolled sheet and coil products, flat bar products and fabricated parts. Through our tubular and pipe products segment, which consists of our Chicago Tube & Iron subsidiary, or CTI, we distribute metal tubing, pipe, bar, valves and fittings and fabricate pressure parts supplied to various industrial markets.

**Principles of Consolidation and Basis of presentation**

The accompanying consolidated financial statements include the accounts of Olympic Steel, Inc. and its wholly-owned subsidiaries (collectively, the Company or Olympic), after elimination of intercompany accounts and transactions.

**Reclassifications and revisions**

Certain prior year amounts in the accompanying consolidated financial statements have been reclassified to conform to the current year's presentation.

### **Accounting Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### **Concentration Risks**

The Company is a major customer of flat-rolled coil and plate and tubular and pipe steel for many of its principal suppliers, but is not dependent on any one supplier. The Company purchased approximately 54%, 51% and 43% of its total steel requirements from its three largest suppliers in 2016, 2015 and 2014, respectively.

The Company has a diversified customer and geographic base, which reduces the inherent risk and cyclicity of its business. The concentration of net sales to the Company's top 20 customers approximated 29%, 31% and 29% of consolidated net sales in 2016, 2015 and 2014, respectively. In addition, the Company's largest customer accounted for approximately 4%, 6% and 6% of consolidated net sales in 2016, 2015 and 2014, respectively. Sales to industrial machinery and equipment manufacturers and their fabricators accounted for 51%, 49% and 51% of consolidated net sales in 2016, 2015 and 2014, respectively.

### **Cash and Cash Equivalents**

Cash equivalents consist of short-term highly liquid investments, with a three month or less maturity, which are readily convertible into cash.

## **Fair Market Value**

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the liability in an orderly transaction between market participants on the measurement date. Valuation techniques must maximize the use of observable inputs and minimize the use of unobservable inputs. To measure fair value, the Company applies a fair value hierarchy that is based on three levels of inputs, of which the first two are considered observable and the last unobservable, as follows:

*Level 1* – Quoted prices in active markets for identical assets or liabilities.

*Level 2* – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

*Level 3* – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Financial instruments, such as cash and cash equivalents, accounts receivable, accounts payable and the credit facility revolver, are stated at their carrying value, which is a reasonable estimate of fair value. The fair value of marketable securities is based on quoted market prices.

## **Accounts Receivable**

The Company's allowance for doubtful accounts is maintained at a level considered appropriate based on historical experience and specific customer collection issues that the Company has identified. Estimations are based upon a calculated percentage of accounts receivable, which remains fairly level from year to year, and judgments about the probable effects of economic conditions on certain customers, which can fluctuate significantly from year to year. The Company cannot guarantee that the rate of future credit losses will be similar to past experience.

## **Inventories**

Inventories are stated at the lower of cost or market and include the costs of purchased metals, inbound freight, external processing and applicable labor and overhead costs. Costs of our carbon and specialty metals flat products segments' inventories, including flat-rolled sheet, coil and plate products are determined using the specific identification method.

Certain of the Company's tubular and pipe products inventory is stated under the last-in, first-out (LIFO) method. At December 31, 2016 and December 31, 2015, approximately \$43.4 million, or 17.1% of consolidated inventory, and \$42.7 million, or 20.7% of consolidated inventory, respectively, was reported under the LIFO method of accounting. The cost of the remainder of tubular and pipe product segment's inventory is determined using a weighted average rolling first-in, first-out (FIFO) method.

On the Consolidated Statements of Comprehensive Income, "Cost of materials sold (exclusive of items shown separately below)" consists of the cost of purchased metals, inbound and internal transfer freight, external processing costs, and LIFO income or expense.

### **Property and Equipment, and Depreciation**

Property and equipment are stated at cost. Depreciation is provided using the straight-line method over the estimated useful lives of the assets ranging from two to 30 years. The Company capitalizes the costs of obtaining or developing internal-use software, including directly related payroll costs. The Company amortizes those costs over five years, beginning when the software is ready for its intended use.

### **Intangible Assets and Recoverability of Long-lived Assets**

The Company performs an annual impairment test of indefinite-lived intangible assets for the tubular and pipe products segment in the fourth quarter, or more frequently if changes in circumstances or the occurrence of events indicate potential impairment. Events or changes in circumstances that could trigger an impairment review include significant nonperformance relative to the expected historical or projected future operating results, significant changes in the manner of the use of the acquired assets or the strategy for the overall business or significant negative industry or economic trends. Management uses judgment to determine whether to use a qualitative analysis or a quantitative fair value measurement for each of the Company's reporting units that carry intangible assets.

If a quantitative fair value measurement is used, the fair value of each indefinite-lived intangible asset is compared to its carrying value and an impairment charge is recorded if the carrying value exceeds the fair value. The Company estimates the fair value of indefinite-lived intangible assets using a discounted cash flow methodology. Management's assumptions used for the calculations are based on historical results, projected financial information and recent economic events. Actual results could differ from these estimates under different assumptions or conditions which could adversely affect the reported value of intangible assets.

The Company evaluates the recoverability of long-lived assets and the related estimated remaining lives whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Events or changes in circumstances that could trigger an impairment review include significant underperformance relative to the expected historical or projected future operating results, significant changes in the manner of the use of the acquired assets or the strategy for the overall business or significant negative industry or economic trends. The Company records an impairment or change in useful life whenever events or changes in circumstances indicate that the carrying amount may not be recoverable or the useful life has changed.

### **Income Taxes**

The Company, on its consolidated balance sheets, records as an offset to the estimated effect of temporary differences between the tax basis of assets and liabilities and the reported amounts in its consolidated balance sheets, the tax effect of operating loss and tax credit carryforwards. If the Company determines that it will not be able to fully realize a deferred tax asset, it will record a valuation allowance to reduce such deferred tax asset to its realizable value. The Company recognizes interest accrued related to unrecognized tax benefits in income tax expense. Penalties, if incurred, would be recognized as a component of administrative and general expense.

### **Revenue Recognition**

For both direct and toll shipments, revenue is recognized when title and risk of loss is transferred, which generally occurs upon delivery to our customers. Given the proximity of the Company's customers to its facilities, substantially all of the Company's sales are shipped and received within one day. Sales returns and allowances are treated as reductions to sales and are provided for based on historical experience and current estimates and are immaterial to the consolidated financial statements.

Certain engineered products produced by the tubular and pipe products segment typically take several months to produce due to their size and complexity. Substantially all projects are completed within nine months. The Company may request advance payments from customers during the production of these products. These payments are included in current short-term liabilities on the Company's Consolidated Balance Sheet. Due to their short-term nature, the Company uses the units of delivery method to account for these contracts. Revenue for the contracts is recognized when the product is shipped and title of the product transfers to the customers. Revenues for these engineered products accounted for approximately 1.7%, 1.8% and 1.7% of our consolidated net sales during 2016, 2015 and 2014, respectively.

#### **Shipping and Handling Fees and Costs**

Amounts charged to customers for shipping and other transportation services are included in net sales. The distribution expense line on the accompanying Consolidated Statements of Comprehensive Income is entirely comprised of all shipping and other transportation costs incurred by the Company in shipping goods to its customers.

## **Stock-Based Compensation**

The Company records compensation expense for stock awards issued to employees and directors. For additional information, see Note 10, Equity Plans.

## **Impact of Recently Issued Accounting Pronouncements**

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No 2016-15, "Classification of certain cash receipts and cash payments". This ASU addresses the following eight specific cash flow issues: Debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies (COLIs) (including bank-owned life insurance policies (BOLIs)); distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. The guidance will be effective for annual reporting periods beginning after December 15, 2017, and interim periods within those fiscal years with early adoption permitted. The adoption of this ASU is not expected to materially impact our consolidated financial statements.

In March 2016, the FASB issued ASU No 2016-09, "Improvements to Employee Share-Based Payment Accounting". This ASU is part of the FASB's Simplification Initiative and has been issued to reduce complexity in the presentation of employee share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The guidance will be effective for annual reporting periods beginning after December 15, 2016 and interim periods within those fiscal years with early adoption permitted. The adoption of this ASU is not expected to materially impact our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases", which specifies the accounting for leases. The objective is to establish the principles that lessees and lessors shall apply to report useful information to users of financial statements about the amount, timing and uncertainty of cash flows arising from a lease. This ASU introduces the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous guidance. The guidance will be effective for annual reporting periods beginning after December 15, 2018 and interim periods within those fiscal years with early adoption permitted. We are in the process of evaluating the impact of the future adoption of this standard on our consolidated financial statements.

In November 2015, the FASB issued ASU No. 2015-17, "Balance Sheet Classification of Deferred Taxes." This ASU is part of the FASB's Simplification Initiative and has been issued to reduce complexity in the presentation of deferred



taxes. This new guidance eliminates the requirement for entities that present a classified statement of financial position to classify deferred tax assets and liabilities as current and noncurrent, and instead require that they classify all deferred tax assets and liabilities as noncurrent. As a result, each jurisdiction will now only have one net noncurrent deferred tax asset or liability. However, the guidance does not change the existing requirement that only permits offsetting within a jurisdiction. Companies are still prohibited from offsetting deferred tax liabilities from one jurisdiction against deferred tax assets of another jurisdiction. This ASU is effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years, with early adoption permitted. The guidance may be applied either prospectively, for all deferred tax assets and liabilities, or retrospectively (i.e., by reclassifying the comparative balance sheet). If applied prospectively, entities are required to include a statement that prior periods were not retrospectively adjusted. If applied retrospectively, entities are also required to include quantitative information about the effects of the change on prior periods. The prospective adoption of this guidance on January 1, 2016 did not have a material impact on the Company's consolidated financial statements and the prior periods were not retrospectively adjusted.

In April 2015, the FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs." This ASU is part of the FASB's Simplification Initiative and has been issued to reduce the complexity in the presentation of debt issuance costs. This new guidance requires companies to present debt issuance costs the same way they currently present debt discounts, as a direct deduction from the carrying value of that debt liability. The guidance is limited to simplifying the presentation of debt issuance costs and does not impact the recognition and measurement guidance for debt issuance costs. This ASU is effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years, with early adoption permitted. The amendments of ASU No. 2015-03 must be applied retrospectively, where the balance sheet of each presented individual period is adjusted to indicate the period-specific impact of using the new guidance. The FASB considered that because both debt issuance costs and debt discounts are amortized using the effective interest method, there would be no effect on the income statement upon adoption of the amendments. The adoption of this guidance on January 1, 2016 did not have an impact on the Company's consolidated financial statements because it does not apply to revolving credit agreements.

In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements – Going Concern". This ASU contains new guidance on management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. Management must evaluate whether it is probable that known conditions or events, considered in the aggregate, would raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. If such conditions or events are identified, the standard requires management's mitigation plans to alleviate the doubt or a statement of the substantial doubt about the entity's ability to continue as a going concern to be disclosed in the financial statements. This ASU is effective for fiscal years and interim periods beginning after December 15, 2016, with early adoption permitted. The adoption of this ASU did not impact the Company's consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." This ASU is a joint project initiated by the FASB and the International Accounting Standards Board to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. generally accepted accounting principles and International Financial Reporting Standards that will: remove inconsistencies and weaknesses in revenue requirements; provide a more robust framework for addressing revenue issues; improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets; provide more useful information to users of financial statements through improved disclosure requirements; and simplify the preparation of financial statements by reducing the number of requirements to which an entity must refer. As originally proposed, the guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The adoption of this ASU is not expected to materially impact our consolidated financial statements. In August 2015, the FASB issued ASU No. 2015-14, "Revenue from Contracts with Customers." This ASU deferred the effective date of ASU No. 2014-09 by one year.

## **2. Accounts Receivable:**

Accounts receivable are presented net of allowances for doubtful accounts and unissued credits of \$2.4 million and \$3.1 million as of December 31, 2016 and 2015, respectively. Bad debt expense totaled \$0.4 million in 2016, \$0.5 million in both 2015 and 2014.

The Company's allowance for doubtful accounts is maintained at a level considered appropriate based on historical experience and specific customer collection issues that the Company has identified. Estimations are based upon a calculated percentage of accounts receivable, which remains fairly level from year to year, and judgments about the probable effects of economic conditions on certain customers, which can fluctuate significantly from year to year. The Company cannot guarantee that the rate of future credit losses will be similar to past experience. The Company considers all available information when assessing the adequacy of its allowance for doubtful accounts.

**3. Inventories:**

Inventories consisted of the following:

| <b>As of December 31,</b><br>(in thousands) | <b>2016</b> | <b>2015</b> |
|---|-------------|-------------|
| Unprocessed                                 | \$203,256   | \$163,942   |
| Processed and finished                      | 51,270      | 42,703      |
| Totals                                      | \$254,526   | \$206,645   |

During 2016 and 2015, the Company recorded \$1.5 million and \$3.3 million, respectively of LIFO income as a result of decreased metals pricing during 2016 and 2015. The LIFO income increased the Company's inventory balance and decreased its cost of materials sold.

If the FIFO method had been in use, inventories would have been \$8.0 million and \$6.6 million lower than reported at December 31, 2016 and 2015, respectively.

#### **4. Property and Equipment:**

Property and equipment consists of the following:

| (in thousands)                  | Depreciable |      | December 31, | December 31, |
|---------------------------------|-------------|------|--------------|--------------|
|                                 | Lives       |      | 2016         | 2015         |
| Land                            | -           |      | \$ 16,001    | \$ 16,001    |
| Land improvements               | 5           | - 10 | 3,133        | 2,799        |
| Buildings and improvements      | 7           | - 30 | 133,010      | 131,294      |
| Machinery and equipment         | 2           | - 15 | 185,676      | 185,555      |
| Furniture and fixtures          | 3           | - 7  | 6,311        | 6,582        |
| Computer software and equipment | 2           | - 5  | 27,848       | 27,350       |
| Vehicles                        | 2           | - 5  | 1,456        | 1,274        |
| Construction in progress        | -           |      | 807          | 1,274        |
|                                 |             |      | 374,242      | 372,129      |
| Less accumulated depreciation   |             |      | (218,476     | ) (205,591   |
| Net property and equipment      |             |      | \$ 155,766   | \$ 166,538   |

Leasehold improvements are included with buildings and improvements and are depreciated over the life of the lease or seven years, whichever is less.

Construction in progress, as of December 31, 2016, primarily consisted of payments for additional processing equipment at our existing facilities that was not yet placed into service and capitalized costs related to the implementation of ERP systems.

#### **5. Goodwill and Intangible Assets:**

In accordance with the Accounting Standards Codification (ASC), an impairment test of indefinitely lived intangible assets is performed at least annually or more frequently if changes in circumstances or the occurrence of events

indicate potential impairment. Events or changes in circumstances that could trigger an impairment review include significant nonperformance relative to the expected historical or projected future operating results, significant changes in the manner of the use of the acquired assets or the strategy for the overall business or significant negative industry or economic trends.

During 2015, the metals industry experienced a significant decline in the price of metals as a result of the strengthened U.S. dollar, a historically high level of imported materials arriving in the United States, low raw material costs to produce metals, and an oversupply of metals. The challenging market conditions negatively impacted the Company's financial performance and the decrease of the Company's market capitalization led the Company to perform the two-step quantitative impairment test during the year by comparing the fair value of the segment carrying goodwill with its carrying value. During the second quarter of 2015, the Company recorded a full impairment to the tubular and pipe products segment's goodwill. In addition, the Company concluded that the indefinitely lived intangible asset, Trade name, was partially impaired and the impairment in the amount of \$8 million was recorded. During the annual impairment analysis in the fourth quarter of 2015 the Company fully impaired the goodwill related to the specialty metals flat products segment as the asset impairment testing determined that the carrying value of the operations was in excess of the fair value and impairments were identified. The determination of fair value of the reporting units used to perform the first step of the impairment test requires judgment and involves significant estimates and assumptions about the expected future cash flows and the impact of market conditions on those assumptions. Due to the inherent uncertainty associated with these estimates, actual results could differ materially from these estimates.

Goodwill, by reportable segment, was as follows as of December 31, 2016 and 2015:

| (in thousands)                  | Specialty<br>Metals | Tubular<br>and<br>Pipe<br>Products | Total     |
|---------------------------------|---------------------|------------------------------------|-----------|
|                                 | Flat<br>Products    | Pipe<br>Products                   |           |
| Balance as of December 31, 2014 | \$ 500              | \$ 16,451                          | \$ 16,951 |
| Acquisitions                    | -                   | -                                  | -         |
| Impairments                     | (500 )              | (16,451 )                          | (16,951)  |
| Balance as of December 31, 2015 | \$ -                | \$ -                               | \$ -      |
| Acquisitions                    | -                   | -                                  | -         |
| Impairments                     | -                   | -                                  | -         |
| Balance as of December 31, 2016 | \$ -                | \$ -                               | \$ -      |

All of the Company's intangible assets were recorded in connection with its July 1, 2011 acquisition of CTI. The intangible assets were evaluated on the premise of highest and best use to a market participant, primarily utilizing the income approach valuation methodology. The useful life of the CTI trade name was determined to be indefinite primarily due to its history and reputation in the marketplace, the Company's expectation that the CTI trade name will continue to be used throughout the life of CTI, and the conclusion that there are currently no other factors identified that would limit its useful life. The useful life of the CTI customer relationships was determined to be fifteen years, based primarily on the consistent and predictable revenue source associated with the existing CTI customer base, the present value of which extends through the fifteen year amortization period. The Company will continue to evaluate the useful life assigned to our amortizable customer relationships in future periods.

During 2016, a step zero test was performed for the indefinitely lived intangible assets and no indication of impairment was present. Due to the impairment of the tubular and pipe segment's goodwill in the second quarter of 2015, a triggering event occurred for the intangible assets subject to amortization and an impairment test was completed. The test revealed no impairment to the Company's intangible assets subject to amortization.

Intangible assets, net, consisted of the following as of December 31, 2016 and 2015:

| (in thousands)                                   | As of December 31, 2016     |                             |             | Intangible<br>Assets,<br>Net |
|--|-----------------------------|-----------------------------|-------------|------------------------------|
|  | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Impairments |                              |
| Customer relationships - subject to amortization | \$ 13,332                   | \$ (4,888 )                 | \$ -        | \$ 8,444                     |
| Trade name - not subject to amortization         | 15,425                      | -                           | -           | 15,425                       |

\$28,757 \$ (4,888 ) \$ - \$ 23,869

| (in thousands)                                   | <b>As of December 31, 2015</b> |                             |             |                              |
|--|--------------------------------|-----------------------------|-------------|------------------------------|
|  | Gross<br>Carrying<br>Amount    | Accumulated<br>Amortization | Impairments | Intangible<br>Assets,<br>Net |
| Customer relationships - subject to amortization | \$13,332                       | \$ (4,000 )                 | \$ -        | \$ 9,332                     |
| Trade name - not subject to amortization         | 23,425                         | -                           | (8,000 )    | 15,425                       |
|  | \$36,757                       | \$ (4,000 )                 | \$ (8,000 ) | \$ 24,757                    |

The Company estimates that amortization expense for its intangible assets subject to amortization will be \$0.9 million per year in each of the next five years.

**6. Debt:**

The Company's debt is comprised of the following components:

| (in thousands)  | <b>As of</b>        |                     |
|---|---------------------|---------------------|
|   | <b>December 31,</b> | <b>December 31,</b> |
|   | <b>2016</b>         | <b>2015</b>         |
| Asset-based revolving credit facility due June 30, 2019 | \$ 164,599          | \$ 145,800          |
| Industrial revenue bond due April 1, 2018               | 1,825               | 2,690               |
| Total debt  | 166,424             | 148,490             |
| Less current amount                                     | (1,825 )            | (2,690 )            |
| Total long-term debt                                    | \$ 164,599          | \$ 145,800          |

The Company's existing asset-based credit facility (the ABL Credit Facility) is collateralized by the Company's accounts receivable and inventory. The ABL Credit Facility consists of a revolving credit line of \$365 million. Revolver borrowings are limited to the lesser of a borrowing base, comprised of eligible receivables and inventories, or \$365 million in the aggregate. The ABL Credit Facility matures on June 30, 2019.

The ABL Credit Facility requires the Company to comply with various covenants, the most significant of which include: (i) until maturity of the ABL Credit Facility, if any commitments or obligations are outstanding and the Company's availability is less than the greater of \$30 million or 10.0% of the aggregate amount of revolver commitments (\$36.5 million at December 31, 2016), then the Company must maintain a ratio of EBITDA minus certain capital expenditures and cash taxes paid to fixed charges of at least 1.00 to 1.00 for the most recent twelve fiscal month period; (ii) limitations on dividend payments and common stock repurchases; and (iii) restrictions on additional indebtedness. The Company has the option to borrow under its revolver based on the agent's base rate plus a premium ranging from 0.00% to 0.25% or the London Interbank Offered Rate (LIBOR) plus a premium ranging from 1.25% to 3.00%.

As of December 31, 2016, the Company was in compliance with its covenants and had approximately \$94.3 million of availability under the ABL Credit Facility.

As of December 31, 2016, \$2.0 million of bank financing fees were included in "Prepaid expenses and other" and "Other long-term assets" on the accompanying Consolidated Balance Sheets. The financing fees are being amortized over the five-year term of the ABL Credit facility and are included in "Interest and other expense on debt" on the accompanying Consolidated Statements of Comprehensive Income.



As part of the CTI acquisition in July 2011, the Company assumed approximately \$5.9 million of Industrial Revenue Bond (IRB) indebtedness. The bond matures in April 2018, with the option to provide principal payments annually on April 1st. On April 1, 2016, the Company paid an optional principal payment of \$0.9 million. Since the IRB is remarketed annually, it is included in "Current portion of long-term debt" on the accompanying Consolidated Balance Sheets. Interest is payable monthly, with a variable rate that resets weekly. As a security for payment of the bonds, the Company obtained a direct pay letter of credit issued by JPMorgan Chase Bank, N.A. The letter of credit reduces annually by the principal reduction amount. The interest rate at December 31, 2016 was 1.0% for the IRB debt.

CTI entered into an interest rate swap agreement to reduce the impact of changes in interest rates on the above IRB. At December 31, 2016, the effect of the swap agreement on the bond was to fix the rate at 3.46%. The swap agreement matures in April 2018, and is reduced annually by the amount of the optional principal payments on the bond. The Company is exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreement. However, the Company does not anticipate nonperformance by the counterparties.

In June 2012, the Company entered into a forward starting fixed rate interest rate hedge that commenced June 2013, in order to eliminate the variability of cash interest payments on \$53.2 million of the then outstanding LIBOR-based borrowings under the ABL Credit Facility. The hedge, which matured on June 1, 2016, fixed the rate at 1.21% plus a premium ranging from 1.25% to 1.75%.

**Scheduled Debt Maturities, Interest, Debt Carrying Values**

The Company's principal payments over the next three years are detailed in the table below:

| <b>(in thousands)</b>    | <b>2017</b> | <b>2018</b> | <b>2019</b> | <b>Total</b> |
|--------------------------|-------------|-------------|-------------|--------------|
| ABL Credit Facility      | \$-         | \$-         | \$164,599   | \$164,599    |
| Industrial revenue bond  | 895         | 930         | -           | 1,825        |
| Total principal payments | \$895       | \$930       | \$164,599   | \$166,424    |

The overall effective interest rate for all debt, exclusive of deferred financing fees and deferred commitment fees, amounted to 2.4%, 2.1% and 2.4% in 2016, 2015 and 2014, respectively. Interest paid totaled \$4.3 million, \$5.1 million and \$5.8 million for the years ended December 31, 2016, 2015 and 2014, respectively. Average total debt outstanding was \$152.5 million, \$211.2 million and \$234.7 million in 2016, 2015 and 2014, respectively.

**7. Derivative Instruments:***Metals swaps*

During 2016, 2015 and 2014, the Company entered into nickel swaps indexed to the London Metal Exchange (LME) price of nickel with third-party brokers. In 2014, the Company entered into carbon swaps indexed to the New York Mercantile Exchange (NYMEX) price of U.S. Midwest Domestic Hot-Rolled Coil Steel with third-party brokers. The nickel and carbon swaps are treated as derivatives for accounting purposes and are included in "Other accrued liabilities" and "Prepaid expenses and other" on the Consolidated Balance Sheet at December 31, 2016 and 2015. The Company entered into the swaps to mitigate its customers' risk of volatility in the price of metals. The outstanding nickel swaps have one to five months remaining and there are no outstanding carbon swaps as of December 31, 2016. The swaps are settled with the brokers at maturity. The economic benefit or loss arising from the changes in fair value of the swaps is contractually passed through to the customer. The primary risk associated with the metals swaps is the ability of customers or third-party brokers to honor their agreements with the Company related to derivative instruments. If the customer or third-party brokers are unable to honor their agreements, the Company's risk of loss is the fair value of the metals swaps.

While these derivatives are intended to help the Company manage risk, they have not been designated as hedging instruments. The periodic changes in fair value of the metals and embedded customer derivative instruments are included in "Cost of materials sold" in the Consolidated Statements of Comprehensive Income. The Company

recognizes derivative positions with both the customer and the third party for the derivatives and classifies cash settlement amounts associated with them as part of “Cost of materials sold” in the Consolidated Statements of Comprehensive Income. The cumulative change in fair value of the metals swaps that have not yet settled are included in “Other accrued liabilities”, and the embedded customer derivatives are included in “Accounts receivable, net” on the Consolidated Balance Sheets at December 31, 2016 and 2015.

In 2014, the Company entered into cash flow metals hedges to mitigate its risk of volatility in the price of metals. The cash flow metals hedges are indexed to the NYMEX price of U.S. Midwest Domestic Hot-Rolled Coil Steel with third-party brokers. There were no cash flow metals hedges outstanding as of December 31, 2016 or 2015. The metals hedges were accounted for as cash flow hedges. The impact of the mark-to-market adjustment on settled hedges is recorded in “Cost of materials sold” in the accompanying Consolidated Statements of Comprehensive Income. The impact for the twelve months ended December 31, 2015 was \$2.4 million of expense.

*Interest rate swap*

CTI entered into an interest rate swap to reduce the impact of changes in interest rates on its IRB. The swap agreement matures April 2018, the same time as the IRB, but the notional amount is reduced annually by the optional principal payments on the IRB. Although the Company is exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreement, the Company anticipates performance by the counterparties. The interest rate swap is not treated as a hedging instrument for accounting purposes.

The periodic changes in fair value of the interest rate swap and cash settlement amounts associated with the interest rate swap are included in “Interest and other expense on debt” in the Consolidated Statements of Comprehensive Income.

*Fixed rate interest rate hedge*

In June 2012, the Company entered into a forward starting fixed rate interest rate hedge commencing June 2013 in order to eliminate the variability of cash interest payments on \$53.2 million of the then outstanding LIBOR-based borrowings under the ABL Credit Facility. The hedge, which matured on June 1, 2016, fixed the rate at 1.21% plus a premium ranging from 1.25% to 1.75%. The fixed rate interest rate hedge was accounted for as a cash flow hedging instrument for accounting purposes.

There was no net impact from the nickel swaps or embedded customer derivative agreements to the Company’s Consolidated Statements of Comprehensive Income for the years ended December 31, 2016, 2015 and 2014. The table below shows the total impact to the Company’s Consolidated Statements of Comprehensive Income through “Net income (loss)” of the derivatives for the years ended December 31, 2016, 2015 and 2014.

| (in thousands)                 | <b>Net Gain (Loss)</b> |             |             |
|--------------------------------|------------------------|-------------|-------------|
|                                | <b>Recognized</b>      |             |             |
|                                | <b>2016</b>            | <b>2015</b> | <b>2014</b> |
| Interest rate swap (CTI)       | \$(66 )                | \$(77 )     | \$(100)     |
| Fixed interest rate swap (ABL) | (98 )                  | (365 )      | (472)       |
| Cash flow metals hedges        | -                      | (2,400)     | (312)       |
| Metals swaps                   | 68                     | (2,304)     | 934         |
| Embedded customer derivatives  | (68 )                  | 2,304       | (934)       |
| Total loss                     | \$(164)                | \$(2,842)   | \$(884)     |

**8. Fair Value of Assets and Liabilities:**

The Company’s financial instruments include cash and cash equivalents, short-term trade receivables, derivative instruments, accounts payable and debt instruments. For short-term instruments, other than those required to be reported at fair value on a recurring basis and for which additional disclosures are included below, management concluded the historical carrying value is a reasonable estimate of fair value because of the short period of time between the origination of such instruments and their expected realization.

During 2016 and 2015, there were no transfers of financial assets between Levels 1, 2 or 3 fair value measurements. There have been no changes in the methodologies used at December 31, 2016 and December 31, 2015. Following is a description of the valuation methodologies used for assets and liabilities measured at fair value as of December 31, 2016 and December 31, 2015:

*Metals swaps and embedded customer derivatives* – Determined by using Level 2 inputs that include the price of nickel indexed to the LME and the price of Hot Rolled Coil Steel indexed to the NYMEX. The fair value is determined based on quoted market prices and reflects the estimated amounts the Company would pay or receive to terminate the nickel swaps.

*Interest rate swap* – Based on the present value of the expected future cash flows, considering the risks involved, and using discount rates appropriate for the maturity date. Market observable Level 2 inputs are used to determine the present value of future cash flows.

The following table presents information about the Company's assets and liabilities that were measured at fair value on a recurring basis and indicates the fair value hierarchy of the valuation techniques utilized by the Company:

| (in thousands)                                  | <b>Value of Items<br/>Recorded at Fair Value<br/>As of December 31,<br/>2016</b> |                    |                    |               |
|---|--|--------------------|--------------------|---------------|
|   | <b>Level<br/>1</b>   | <b>Level<br/>2</b> | <b>Level<br/>3</b> | <b>Total</b>  |
| <b>Assets:</b>                                  |  |                    |                    |               |
| Embedded customer derivatives                   | \$-  | \$ 113             | \$ -               | \$ 113        |
| <b>Total assets at fair value</b>               | <b>\$-</b>   | <b>\$ 113</b>      | <b>\$ -</b>        | <b>\$ 113</b> |
| <b>Liabilities:</b>                             |  |                    |                    |               |
| Metals swaps                                    | \$-  | \$ 113             | \$ -               | \$ 113        |
| Interest rate swap (CTI)                        | -  | 36                 | -                  | 36            |
| <b>Total liabilities recorded at fair value</b> | <b>\$-</b>   | <b>\$ 149</b>      | <b>\$ -</b>        | <b>\$ 149</b> |

| (in thousands)                                      | <b>Value of Items Not Recorded at<br/>Fair Value<br/>As of December 31, 2016</b> |                  |                    |                  |
|---|--|------------------|--------------------|------------------|
|   | <b>Level<br/>1</b>   | <b>Level 2</b>   | <b>Level<br/>3</b> | <b>Total</b>     |
| <b>Liabilities:</b>                                 |  |                  |                    |                  |
| IRB   | \$1,825  | \$-              | \$ -               | \$1,825          |
| ABL Credit Facility                                 | -  | 164,599          | -                  | 164,599          |
| <b>Total liabilities not recorded at fair value</b> | <b>\$1,825</b>   | <b>\$164,599</b> | <b>\$ -</b>        | <b>\$166,424</b> |

The value of the items not recorded at fair value represent the carrying value of the liabilities.

| (in thousands)                    | <b>Value of Items<br/>Recorded at Fair Value<br/>As of December 31,<br/>2015</b> |                    |                    |               |
|-----------------------------------|--|--------------------|--------------------|---------------|
|                                   | <b>Level<br/>1</b>   | <b>Level<br/>2</b> | <b>Level<br/>3</b> | <b>Total</b>  |
| <b>Assets:</b>                    |  |                    |                    |               |
| Embedded customer derivatives     | \$-  | \$ 384             | \$ -               | \$ 384        |
| <b>Total assets at fair value</b> | <b>\$-</b>   | <b>\$ 384</b>      | <b>\$ -</b>        | <b>\$ 384</b> |
| <b>Liabilities:</b>               |  |                    |                    |               |
| Metals swaps                      | \$-  | \$ 384             | \$ -               | \$ 384        |

|   |            |              |            |              |
|---|------------|--------------|------------|--------------|
| Interest rate swap (CTI)                        | -          | 102          | -          | 102          |
| Fixed interest rate swap (ABL)                  | -          | 114          | -          | 114          |
| <b>Total liabilities recorded at fair value</b> | <b>\$-</b> | <b>\$600</b> | <b>\$-</b> | <b>\$600</b> |

| (in thousands)                                      | <b>Value of Items Not Recorded at Fair Value</b> |                  |                |                  |
|---|--|------------------|----------------|------------------|
|   | <b>As of December 31, 2015</b>                   |                  |                |                  |
|   | <b>Level 1</b>                                   | <b>Level 2</b>   | <b>Level 3</b> | <b>Total</b>     |
| <b>Liabilities:</b>                                 |  |                  |                |                  |
| IRB   | \$2,690  | \$-              | \$-            | \$2,690          |
| ABL Credit Facility                                 | -  | 145,800          | -              | 145,800          |
| <b>Total liabilities not recorded at fair value</b> | <b>\$2,690</b>                                   | <b>\$145,800</b> | <b>\$-</b>     | <b>\$148,490</b> |

The value of the items not recorded at fair value represent the carrying value of the liabilities.

The fair value of the IRB is determined using Level 1 inputs. The carrying value and the fair value of the IRB that qualify as financial instruments were \$1.8 million and \$2.7 million at December 31, 2016 and 2015, respectively.

The fair value of the ABL Credit Facility is determined using Level 2 inputs. The carrying value of the ABL Credit Facility was \$164.6 million and \$145.8 million at December 31, 2016 and 2015, respectively. The Level 2 fair value of the Company's long-term debt was estimated using prevailing market interest rates on debt with similar creditworthiness, terms and maturities.

**9. Accumulated Other Comprehensive Loss:**

In June 2012, the Company entered into a forward starting fixed rate interest rate hedge commencing July 2013 in order to eliminate the variability of cash interest payments on \$53.2 million of the outstanding LIBOR-based borrowings under the ABL Credit Facility. The hedge matured on June 1, 2016 and the notional amount was reduced monthly by \$0.7 million. The balance as of December 31, 2015 was \$31.4 million. The fixed rate interest rate hedge was accounted for as a cash flow hedging instrument for accounting purposes. The fair value of the interest rate hedge was included in “Accumulated other comprehensive loss” on the Consolidated Balance Sheets at December 31, 2015.

**10. Equity Plans:**

Pursuant to the Amended and Restated Olympic Steel 2007 Omnibus Incentive Plan (Plan), the Company may grant stock options, stock appreciation rights, restricted shares, restricted share units, performance shares, and other stock- and cash-based awards to employees and Directors of, and consultants to, the Company and its affiliates. Under the Plan, 1,000,000 shares of common stock have been authorized cumulatively for equity grants.

On May 1, 2016 and March 1, 2015, the Compensation Committee of the Company’s Board of Directors approved the grant of 3,094 and 4,639 restricted stock units (RSUs), respectively, to each non-employee Director. Subject to the terms of the Plan and the RSU agreement, the RSUs vest after one year of service (from the date of grant). The RSUs are not converted into shares of common stock until the director either resigns or is terminated from the Board of Directors. The fair value of each RSU was estimated to be the closing price of the Company’s common stock on the date of the grant, which was \$22.62 and \$15.09 on May 1, 2016 and March 1, 2015, respectively.

On July 1, 2016, the Company created a new Senior Management Stock Incentive Program (the New Plan) for certain participants. Under the New Plan, each participant is awarded RSUs with a dollar value equal to 10% of the participant’s base salary, up to a maximum of \$17,500. The RSUs have a five-year vesting period and the RSUs will convert into the right to receive shares of common stock upon a participant’s retirement, or earlier upon the participant’s death or disability or upon a change in control of the Company. The carbon and specialty metals flat products segments adopted the New Plan on July 1, 2016 and the tubular and pipe products segment adopted the New Plan on January 1, 2017.

Prior to July 1, 2016, the Company’s Senior Management Compensation Program included an equity component in order to encourage more ownership of common stock by the senior management (the Old Plan). The Old Plan imposed stock ownership requirements upon the participants. Each participant was required to own at least 750 shares of common stock for each year that the participant participated in the Old Plan. Any participant that failed to meet the stock ownership requirements would be ineligible to receive any equity awards under the Company’s equity



compensation plans, including the Plan, until the participant satisfied the ownership requirements. To assist participants in meeting the stock ownership requirements, on an annual basis, if a participant purchased 500 shares of common stock on the open market, the Company awarded that participant 250 shares of common stock. During 2016 and 2015, the Company matched 2,500 and 9,000 shares, respectively. Additionally, any participant who continued to comply with the stock ownership requirements as of the five-year, 10-year, 15-year, 20-year and 25-year anniversaries of the participant's participation in the Senior Management Compensation Program would receive a restricted stock unit award with a dollar value of \$25 thousand, \$50 thousand, \$75 thousand, \$100 thousand and \$100 thousand, respectively. Restricted stock unit awards would convert into the right to receive shares of common stock upon a participant's retirement, or earlier upon the participant's death or disability or upon a change in control of the Company. The carbon and specialty metals flat products segments terminated this plan on July 1, 2016 and the tubular and pipe products segment terminated the plan on January 1, 2017.

As part of the termination of the Old Plan and the transition to the New Plan, participants were paid the RSU grants that were earned to date, or a pro-rata amount of the RSUs earned, depending on the participants' length of time they participated in the plan. After the payment of the RSUs noted above, the remaining liability of approximately \$1.0 million was reversed during 2016 in accordance with ASC No. 718.

During the third quarter of 2016, the Company adopted a formal RSU award program for employees who are promoted to an executive level position. During the quarter, Andrew Greiff received 10,573 RSUs upon his promotion to Executive Vice President and Chief Operating Officer. These RSUs vest on the fifth anniversary of his promotion.

Stock-based compensation income or expense recognized on RSUs is summarized in the following table:

| (in thousands)                                | For the years ended December 31, |          |          |
|---|----------------------------------|----------|----------|
|   | 2016                             | 2015     | 2014     |
| RSU expense before taxes of New Plan          | \$ 42                            | \$ -     | \$ -     |
| RSU (income) expense before taxes of Old Plan | \$ (73 )                         | \$ 1,047 | \$ 1,252 |
| RSU (income) expense after taxes              | 81                               | 631      | 774      |

All pre-tax charges related to RSUs were included in the caption “Administrative and general” on the accompanying Consolidated Statements of Comprehensive Income.

The following table summarizes the activity related to RSUs for the twelve months ended December 31, 2016:

|                                  | Number<br>of<br>Shares | Weighted<br>Average<br>Estimated<br>Fair<br>Value |
|----------------------------------|------------------------|---|
| Outstanding at December 31, 2015 | 287,894                | \$ 22.39  |
| Granted                          | 137,935                | 15.19   |
| Converted into shares            | (3,239 )               | 19.12   |
| Forfeited                        | (1,104 )               | 18.03   |
| Outstanding at December 31, 2016 | 421,486                | \$ 19.92  |
| Vested at December 31, 2016      | 411,794                | \$ 19.89  |

Of the RSUs granted in 2016, 2015 and 2014, 51,075, 47,639 and 21,506, respectively, were used to fund supplemental executive retirement plan contributions. There was no intrinsic value for the RSUs that were converted into shares in 2016, 2015 and 2014.

***11. Commitments and Contingencies:*****Operating Leases**

The Company leases certain warehouses, sales offices, machinery and equipment and vehicles under long-term operating lease agreements. The leases expire at various dates through 2024. In some cases, the leases include options to extend. Rent and lease expense was \$9.1 million, \$8.7 million and \$8.2 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The future annual minimum lease payments as of December 31, 2016 are as follows:

| (in thousands) | 2017    | 2018    | 2019    | 2020    | 2021    | Thereafter | Total    |
|----------------|---------|---------|---------|---------|---------|------------|----------|
| Lease payments | \$6,634 | \$5,804 | \$4,511 | \$3,661 | \$2,574 | \$ 3,282   | \$26,466 |

**Commitments and Contingencies**

The Company is party to various legal actions that it believes are ordinary in nature and incidental to the operation of its business. In the opinion of management, the outcome of the proceedings to which the Company is currently a party will not have a material adverse effect upon its results of operations, financial condition or cash flows. During 2016, the Company paid \$1.7 million related to an arbitration decision for a 2015 foreign steel purchase. The amount was included in "Cost of materials sold" in the Consolidated Statements of Comprehensive Income. We have not incurred any charges of this nature in the comparable periods.

In the normal course of business, the Company periodically enters into agreements that incorporate indemnification provisions. While the maximum amount to which the Company may be exposed under such agreements cannot be estimated, it is the opinion of management that these indemnifications are not expected to have a material adverse effect on the Company's results of operations or financial condition.

At December 31, 2016, approximately 280 of the hourly plant personnel are represented by nine separate collective bargaining units. The table below shows the expiration dates of the collective bargaining agreements.

| <b>Facility</b>              | <b>Expiration date</b> |
|------------------------------|------------------------|
| Minneapolis plate, Minnesota | March 31, 2017         |
| Detroit, Michigan            | August 31, 2017        |
| Duluth, Minnesota            | December 21, 2017      |
| St. Paul, Minnesota          | May 25, 2018           |
| Milan, Illinois              | August 12, 2018        |
| Locust, North Carolina       | March 4, 2020          |
| Romeoville, Illinois         | May 31, 2020           |
| Minneapolis coil, Minnesota  | September 30, 2020     |
| Indianapolis, Indiana        | January 29, 2021       |

## **12. Income Taxes:**

The components of the Company's provision (benefit) for income taxes from continuing operations were as follows:

| (in thousands)                 | <b>As of December 31,</b> |             |             |
|--------------------------------|---------------------------|-------------|-------------|
|                                | <b>2016</b>               | <b>2015</b> | <b>2014</b> |
| Current:                       |                           |             |             |
| Federal                        | \$2,563                   | \$(149 )    | \$4,859     |
| State and local                | 929                       | (752 )      | 657         |
|                                | 3,492                     | (901 )      | 5,516       |
| Deferred                       | (1,994)                   | (5,916)     | (2,566)     |
| Income tax provision (benefit) | \$1,498                   | \$(6,817)   | \$2,950     |

The components of the Company's deferred income taxes at December 31 are as follows:

| (in thousands) | <b>2016</b> | <b>2015</b> |
|----------------|-------------|-------------|
|----------------|-------------|-------------|

Edgar Filing: OLYMPIC STEEL INC - Form 10-K

Deferred tax assets:

|   |          |          |
|---|----------|----------|
| Inventory (excluding LIFO reserve)              | \$2,531  | \$2,986  |
| Net operating loss and tax credit carryforwards | 3,224    | 2,926    |
| Allowance for doubtful accounts                 | 533      | 500      |
| Accrued expenses                                | 7,228    | 7,311    |
| Other   | 169      | 143      |
|   | 13,685   | 13,866   |
| Valuation reserve                               | (2,017 ) | (1,030 ) |
| Total deferred tax assets                       | 11,668   | 12,836   |

Deferred tax liabilities:

|                                |            |            |
|--------------------------------|------------|------------|
| LIFO reserve                   | (5,874 )   | (6,018 )   |
| Property and equipment         | (19,846)   | (22,535)   |
| Intangibles                    | (9,067 )   | (9,396 )   |
| Total deferred tax liabilities | (34,787)   | (37,949)   |
| Deferred tax liabilities, net  | \$(23,119) | \$(25,113) |

The following table summarizes the activity related to the Company's gross unrecognized tax benefits:

| <b>(in thousands)</b>                                  | <b>2016</b> | <b>2015</b> | <b>2014</b> |
|--|-------------|-------------|-------------|
| Balance as of January 1                                | \$38        | \$58        | \$75        |
| Decreases related to prior year tax positions          | -           | (20)        | (17)        |
| Increases related to current year tax positions        | 13          | 13          | 13          |
| Decreases related to lapsing of statute of limitations | (13)        | (13)        | (13)        |
| Balance as of December 31                              | \$38        | \$38        | \$58        |

It is expected that the amount of unrecognized tax benefits will not materially change in the next twelve months. The tax years 2013 through 2015 remain open to examination by major taxing jurisdictions to which the Company is subject.

The Company recognized interest related to uncertain tax positions in income tax expense.

The following table reconciles the U.S. federal statutory rate to the Company's effective tax rate:

|   | <b>2016</b> | <b>2015</b> | <b>2014</b> |
|---|-------------|-------------|-------------|
| U.S. federal statutory rate                   | 35.0%       | 35.0%       | 35.0%       |
| State and local taxes, net of federal benefit | 11.8%       | 1.4%        | (1.6% )     |
| Valuation allowance                           | 205.4%      | 0.0%        | 0.0%        |
| Goodwill impairment                           | 0.0%        | (17.1%)     | (51.8%)     |
| All other, net                                | 104.4%      | 1.0%        | 0.1%        |
| Effective income tax rate                     | 356.6%      | 20.3%       | (18.3%)     |

The Company's effective tax rate is disproportionately high in 2016 from comparative periods due to low income before taxes relative to items that impact the effective tax rate. Other differences reflect permanent differences of \$0.8 million offset by credits and manufacturing deductions of \$0.3 million. During 2016, the Company recorded a valuation allowance of \$0.9 million to reduce certain state deferred tax assets to the amount that is more likely than not to be realized.

Income taxes paid in 2016, 2015 and 2014 totaled \$1.0 million, \$0.6 million and \$4.7 million, respectively. Some subsidiaries of the Company's consolidated group file state tax returns on a separate company basis and have state net operating loss carryforwards expiring over the next seven to 20 years. A valuation allowance is recorded to reduce certain deferred tax assets to the amount that is more likely than not to be realized.

**13. Shares Outstanding and Earnings Per Share:**

Earnings per share have been calculated based on the weighted average number of shares outstanding as set forth below:

| (in thousands, except per share data)                          | <b>For the years ended</b> |             |             |
|--|----------------------------|-------------|-------------|
|  | <b>December 31,</b>        |             |             |
|  | <b>2016</b>                | <b>2015</b> | <b>2014</b> |
| Weighted average basic shares outstanding                      | 11,210                     | 11,192      | 11,120      |
| Assumed exercise of stock options and issuance of stock awards | -                          | -           | -           |
| Weighted average diluted shares outstanding                    | 11,210                     | 11,192      | 11,120      |
| Net income (loss)  | \$(1,078 )                 | \$(26,777 ) | \$(19,064 ) |
| Basic earnings (loss) per share                                | \$(0.10 )                  | \$(2.39 )   | \$(1.71 )   |
| Diluted earnings (loss) per share                              | \$(0.10 )                  | \$(2.39 )   | \$(1.71 )   |
| Anti-dilutive securities outstanding                           | 167                        | 125         | 118         |

**14. Stock Repurchase Program:**

On October 2, 2015, the Company announced that its Board of Directors authorized a stock repurchase program of up to 550,000 shares of the Company's issued and outstanding common stock, which could include open market repurchases, negotiated block transactions, accelerated stock repurchases or open market solicitations for shares, all or some of which may be effected through Rule 10b5-1 plans. Any of the repurchased shares are held in the Company's treasury, or canceled and retired as the Board may determine from time to time. Any repurchases of common stock are subject to the covenants contained in the ABL Credit Facility. Under the ABL Credit Facility, the Company may repurchase common stock and pay dividends up to \$2.5 million in the aggregate during any trailing twelve months without restrictions. Purchases of common stock or dividend payments in excess of \$2.5 million in the aggregate require the Company to (i) maintain availability in excess of 25% of the aggregate revolver commitments (\$91.3 million at December 31, 2016) or (ii) to maintain availability equal to or greater than 15% of the aggregate revolver commitments (\$54.8 million at December 31, 2016) and the Company must maintain a pro-forma ratio of EBITDA minus certain capital expenditures and cash taxes paid to fixed charges of at least 1.00 to 1.00.

There were no shares repurchased during 2016. During the fourth quarter of 2015, the Company repurchased 65,283 shares of outstanding common stock at an average cost of \$10.71 per share.

**15. Segment Information:**

The Company follows the accounting guidance that requires the utilization of a "management approach" to define and report the financial results of operating segments. The management approach defines operating segments along the lines used by the Company's chief operating decision maker (CODM) to assess performance and make operating and resource allocation decisions. Our CODM evaluates performance and allocates resources based primarily on operating income (loss). Our operating segments are based primarily on internal management reporting.

The Company operates in three reportable segments; carbon flat products, specialty metals flat products, and tubular and pipe products. The flat products segments' assets and resources are shared by the carbon and specialty metals segments and both segments' products are stored in the shared facilities and, in some locations, processed on shared equipment. As such, total assets and capital expenditures are reported in the aggregate for the flat products segments. Due to the shared assets and resources, certain of the flat products segment expenses are allocated between the carbon flat products segment and the specialty metals flat products segment based upon an established allocation methodology. Through its carbon flat products segment, the Company sells and distributes large volumes of processed carbon and coated flat-rolled sheet, coil and plate products. Through its specialty metals flat products segment, the Company sells and distributes processed aluminum and stainless flat-rolled sheet and coil products, flat bar products and fabricated parts. Through its tubular and pipe products segment, the Company distributes metal tubing, pipe, bar, valve and fittings and fabricates pressure parts supplied to various industrial markets.



Corporate expenses are reported as a separate line item for segment reporting purposes. Corporate expenses include the unallocated expenses related to managing the entire Company (i.e., all three segments), including compensation for certain personnel, expenses related to being a publicly traded entity such as board of directors expenses, audit expenses, and various other professional fees.

The following table provides financial information by segment and reconciles the Company's operating income by segment to the consolidated income before income taxes for the years ended December 31, 2016, 2015 and 2014. The Company assesses the performance of the segments based on operating income.

| (in thousands)                                 | For the Year Ended |             |             |
|--|--------------------|-------------|-------------|
|  | December 31,       |             |             |
|  | 2016               | 2015        | 2014        |
| Net sales                                      |                    |             |             |
| Carbon flat products                           | \$670,983          | \$765,400   | \$985,039   |
| Specialty metals flat products                 | 189,930            | 192,516     | 206,692     |
| Tubular and pipe products                      | 194,203            | 217,627     | 244,539     |
| Total net sales                                | \$1,055,116        | \$1,175,543 | \$1,436,270 |
| Depreciation and amortization                  |                    |             |             |
| Carbon flat products                           | \$11,690           | \$12,200    | \$14,250    |
| Specialty metals flat products                 | 797                | 698         | 805         |
| Tubular and pipe products                      | 5,896              | 6,036       | 5,624       |
| Corporate                                      | 102                | 102         | 101         |
| Total depreciation and amortization            | \$18,485           | \$19,036    | \$20,780    |
| Operating income                               |                    |             |             |
| Carbon flat products                           | \$(4,371)          | \$(7,217)   | \$6,306     |
| Specialty metals flat products                 | 9,841              | (1,074)     | 6,109       |
| Tubular and pipe products                      | 7,713              | 12,583      | 10,185      |
| Corporate                                      | (7,435)            | (7,120)     | (7,972)     |
| Goodwill and intangible asset impairment (a)   | -                  | (24,951)    | (23,836)    |
| Total operating income (loss)                  | \$5,748            | \$(27,779)  | \$(9,208)   |
| Other loss, net                                | (55)               | (125)       | (126)       |
| Income (loss) before interest and income taxes | 5,693              | (27,904)    | (9,334)     |
| Interest and other expense on debt             | 5,273              | 5,690       | 6,780       |
| Income (loss) before income taxes              | \$420              | \$(33,594)  | \$(16,114)  |

\$24,451 of the goodwill and intangible asset impairment in 2015 related to the tubular and pipe products (a) segment, \$500 related to the specialty metals flat products segment. The goodwill impairment in 2014 related to the tubular and pipe products segment.

| (in thousands)             | 2016    | 2015    | 2014    |
|----------------------------|---------|---------|---------|
| Capital expenditures       |         |         |         |
| Flat products              | \$5,105 | \$4,295 | \$4,540 |
| Tubular and pipe products  | 1,719   | 3,022   | 3,273   |
| Corporate                  | -       | -       | 21      |
| Total capital expenditures | \$6,824 | \$7,317 | \$7,834 |

Assets

Edgar Filing: OLYMPIC STEEL INC - Form 10-K

|                           |           |           |
|---------------------------|-----------|-----------|
| Flat products             | \$363,626 | \$328,295 |
| Tubular and pipe products | 192,088   | 183,129   |
| Corporate                 | 354       | 456       |
| Total assets              | \$556,068 | \$511,880 |

There were no material revenue transactions between the carbon flat products, specialty metals flat products and tubular and pipe products segments for the years ended December 31, 2016, 2015 and 2014.

The Company sells certain products internationally, primarily in Canada, Mexico and Dominican Republic. International sales have been immaterial to the consolidated financial results and to the individual segment's results.

***16. Retirement Plans:***

The Company's retirement plans consist of two 401(k) plans covering certain non-union employees, two separate 401(k) plans covering all union employees, a profit sharing plans, a multi-employer pension plan covering certain CTI employees and a supplemental executive retirement plan (SERP) covering certain executive officers of the Company.

The 401(k) retirement plans allow eligible employees to contribute up to the statutory maximum. The Company's non-union 401(k) matching contribution is determined annually by the Board of Directors and is based on a percentage of eligible employees' earnings and contributions. For the non-union flat rolled segments' 401(k) retirement plan, the Company matched one-half of each eligible employee's contribution, limited to the first 6% of eligible compensation.

For the union flat rolled segments' 401(k) retirement plan, the Company matched one-half of each eligible employee's contribution, limited to the first 6% of eligible compensation.

For the 401(k) retirement plan at our CTI locations, the Company matched one-half of each eligible employee's contribution, limited to the first 6% of eligible compensation.

All union employees now participate in the profit-sharing plan on a discretionary basis, like all non-union employees. Company contributions to the non-union profit-sharing plan are discretionary amounts as determined annually by the Board of Directors.

In 2005, the Board of Directors adopted a SERP, which has been amended from time to time. Contributions to the SERP are based on: (i) a portion of the participants' compensation multiplied by 13%; and (ii) for certain participants a portion of the participants' compensation multiplied by a factor which is contingent upon the Company's return on invested capital. Benefits are subject to a vesting schedule of up to five years.

The Company, through its CTI subsidiary, contributes to one multiemployer pension plan – the Plumbing and Heating Wholesalers Retirement Income Plan for the Benefit of the Shopmen's Division of Pipe Fitters' Association Local Union 597, EIN 36-6511016, Plan Number 001 (the Multiemployer Plan). The risks of participating in the Multiemployer Plan are different from a single-employer plan in that 1) assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers, 2) if a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers, and 3) if CTI chooses to stop participating in the Multiemployer Plan, CTI may be required to pay the plan an amount based on the unfunded status of the plan, referred to as a withdrawal liability.

The most recent Pension Protection Act zone status available is for the plan year beginning January 1, 2016, and the Multiemployer Plan's actuary has certified that the Multiemployer Plan is neither in critical status nor endangered status and that it is in the green zone. The green zone status is based on information that CTI received from the Multiemployer Plan and is certified by the Multiemployer Plan's actuary. Among other factors, plans in the green zone are at least 80 percent funded.

CTI contributes to the Multiemployer Plan under the terms of a collective bargaining agreement that covers certain of its union employees, and which expires May 31, 2020. CTI contributions to the Multiemployer Plan were immaterial for the years ended December 31, 2016 and 2015.

Retirement plan expense, which includes all Company 401(k), profit-sharing, SERP defined contributions and the Multiemployer Plan, amounted to \$2.2 million, \$2.0 million and \$2.2 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The fair values of the Company's SERP assets as of December 31, 2016 are as follows:

|                    | <b>Quoted<br/>Prices<br/>in Active<br/>Markets<br/>Level 1</b> | <b>Observable<br/>Inputs<br/>Level 2</b> | <b>Unobservable<br/>Inputs<br/>Level 3</b> |
|--------------------|--|--|--|
| (in thousands)     |  |  |  |
| Money market funds | -  | 2,403                                    | -  |
| Fixed income       |  | 120                                      |  |
| Mutual funds       | -  | 3,297                                    | -  |
| Total              | <b>\$ -</b>  | <b>\$ 5,820</b>                          | <b>\$ -</b>                                |

***17. Related-Party Transactions:***

The Company's Chief Executive Officer owns 50% of an entity that owns one of the Cleveland warehouses and leases it to the Company at a fair market value annual rental of \$0.2 million. The lease expires on December 31, 2018 with four five-year renewal options.

**Schedule II – Valuation and Qualifying Accounts**

(in thousands)

| Description                            | Balance at<br>Beginning<br>of Period | Additions<br>Charged<br>to |                   | Deductions      | Balance<br>at<br>End of<br>Period |
|--|--------------------------------------|----------------------------|-------------------|-----------------|-----------------------------------|
|  |                                      | Costs<br>and<br>Expenses   | Other<br>Accounts |                 |                                   |
| Year Ended December 31, 2014           |                                      |                            |                   |                 |                                   |
| Allowance for doubtful accounts        | \$ 1,519                             | \$ 467                     | \$ -              | \$ (638)        | ) \$ 1,348                        |
| Tax valuation reserve                  | \$ 1,298                             | \$ 83                      | \$ -              | \$ -            | ) \$ 1,381                        |
| Year Ended December 31, 2015           |                                      |                            |                   |                 |                                   |
| Allowance for doubtful accounts        | \$ 1,348                             | \$ 506                     | \$ -              | \$ (555)        | ) \$ 1,299                        |
| Tax valuation reserve                  | \$ 1,381                             | \$ -                       | \$ -              | \$ (351)        | ) \$ 1,030                        |
| <b>Year Ended December 31, 2016</b>    |                                      |                            |                   |                 |                                   |
| <b>Allowance for doubtful accounts</b> | <b>\$ 1,299</b>                      | <b>\$ 369</b>              | <b>\$ -</b>       | <b>\$ (283)</b> | <b>) \$ 1,385</b>                 |
| <b>Tax valuation reserve</b>           | <b>\$ 1,030</b>                      | <b>\$ 987</b>              | <b>\$ -</b>       | <b>\$ -</b>     | <b>) \$ 2,017</b>                 |

**SUPPLEMENTAL FINANCIAL INFORMATION**

(in thousands, except per share data)

| <b>2016</b>                                   | <b>1st</b> | <b>2nd</b> | <b>3rd</b> | <b>4th</b> | <b>Year</b> |
|---|------------|------------|------------|------------|-------------|
| Net sales                                     | \$258,349  | \$273,608  | \$268,255  | \$254,904  | \$1,055,116 |
| Operating income (loss) (a)                   | 35         | 8,339      | 27         | (2,653 )   | 5,748       |
| Income (loss) before income taxes             | (1,255 )   | 7,007      | (1,288 )   | (4,044 )   | 420         |
| Net income (loss)                             | \$(767 )   | \$3,550    | \$(1,757 ) | \$(2,104 ) | \$(1,078 )  |
| Basic net income (loss) per share             | \$(0.07 )  | \$0.32     | \$(0.16 )  | \$(0.19 )  | \$(0.10 )   |
| Weighted average shares outstanding - basic   | 11,182     | 11,216     | 11,219     | 11,221     | 11,210      |
| Diluted net income (loss) per share           | \$(0.07 )  | \$0.32     | \$(0.16 )  | \$(0.19 )  | \$(0.10 )   |
| Weighted average shares outstanding - diluted | 11,182     | 11,216     | 11,219     | 11,221     | 11,210      |
| Market price of common stock: (c)             |            |            |            |            |             |
| High  | \$17.50    | \$27.48    | \$31.19    | \$28.67    | \$31.19     |
| Low   | 7.98       | 15.41      | 17.42      | 17.14      | 7.98        |

| <b>2015</b>                                   | <b>1st</b> | <b>2nd</b>  | <b>3rd</b> | <b>4th</b> | <b>Year</b> |
|---|------------|-------------|------------|------------|-------------|
| Net sales                                     | \$345,865  | \$315,251   | \$276,922  | \$237,505  | \$1,175,543 |
| Operating income (loss) (b)                   | 3,345      | (24,398 )   | 453        | (7,179 )   | (27,779 )   |
| Income (loss) before income taxes             | 1,751      | (25,895 )   | (1,036 )   | (8,414 )   | (33,594 )   |
| Net income (loss)                             | \$1,069    | \$(22,260 ) | \$(598 )   | \$(4,988 ) | \$(26,777 ) |
| Basic net income (loss) per share             | \$0.10     | \$(1.99 )   | \$(0.05 )  | \$(0.45 )  | \$(2.39 )   |
| Weighted average shares outstanding - basic   | 11,195     | 11,201      | 11,203     | 11,173     | 11,192      |
| Diluted net income (loss) per share           | \$0.10     | \$(1.99 )   | \$(0.05 )  | \$(0.45 )  | \$(2.39 )   |
| Weighted average shares outstanding - diluted | 11,195     | 11,201      | 11,203     | 11,173     | 11,192      |
| Market price of common stock: (c)             |            |             |            |            |             |
| High  | \$18.57    | \$20.93     | \$17.92    | \$12.60    | \$20.93     |
| Low   | 12.86      | 10.44       | 6.40       | 8.98       | 6.40        |

(a) Operating income (loss) includes \$1,489 of LIFO income related to the Company's tubular and pipe products segment.

(b) Operating income (loss) includes \$3,347 of LIFO income related to the Company's tubular and pipe products segment as well as a \$16,451 goodwill impairment charge and a \$8,000 intangible asset impairment charge recorded in the second quarter related to the Company's tubular and pipe products segment and a \$500 goodwill impairment charge recorded in the fourth quarter related to the specialty metals flat products segment.

(c) Represents the high and low sales prices of our common stock as reported by the Nasdaq Global Select Market.



## **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

## **ITEM 9A. CONTROLS AND PROCEDURES**

### **Disclosure Controls and Procedures**

Evaluations required by Rule 13a-15 of the Securities Exchange Act of 1934 of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Annual Report have been carried out under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer. Based upon such evaluations, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2016 in providing reasonable assurance that information required to be disclosed by us in reports filed under the Exchange Act is recorded, processed, summarized and reported within time periods specified in the rules and forms of the SEC.

### **Management's Report on Internal Control Over Financial Reporting**

Management's Report on Internal Control Over Financial Reporting is set forth in Part II, Item 8 of this Annual Report on Form 10-K and is incorporated herein. PricewaterhouseCoopers LLP, the Company's independent registered public accounting firm, has issued an attestation report on our internal control over financial reporting that is set forth in Part II, Item 8 of this Annual Report and is incorporated herein by reference.

### **Changes in Internal Control Over Financial Reporting**

There have been no changes in our internal control over financial reporting during the quarter ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**ITEM 9B. OTHER INFORMATION**

None.

77

---

## **PART III**

### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS OF THE REGISTRANT AND CORPORATE GOVERNANCE**

Information required by Item 10 as to the executive officers is provided in Part I of this Annual Report on Form 10-K and is incorporated by reference into this section. Other information required by Item 10 will be incorporated herein by reference to the information set forth in our definitive proxy statement for our 2017 Annual Meeting of Shareholders.

### **ITEM 11. EXECUTIVE COMPENSATION**

Information required by Item 11 will be incorporated herein by reference to the information set forth in our definitive proxy statement for our 2017 Annual Meeting of Shareholders.

### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information required by Item 12 will be incorporated herein by reference to the information set forth in our definitive proxy statement for our 2017 Annual Meeting of Shareholders.

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

Information required by Item 13 will be incorporated herein by reference to the information set forth in our definitive proxy statement for our 2017 Annual Meeting of Shareholders.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

Information required by Item 14 will be incorporated herein by reference to the information set forth in our definitive proxy statement for our 2017 Annual Meeting of Shareholders.

78

---

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

**(a)(1) The following financial statements are included in Part II, Item 8:**

Report of Independent Registered Public Accounting Firm

Management's Report on Internal Control Over Financial Reporting

Consolidated Statements of Comprehensive Income for the Years Ended December 31, 2016, 2015 and 2014

Consolidated Balance Sheets as of December 31, 2016 and 2015

Consolidated Statements of Cash Flows for the Years Ended December 31, 2016, 2015 and 2014

Supplemental Disclosures of Cash Flow Information for the Years Ended December 31, 2016, 2015 and 2014

Consolidated Statements of Shareholders' Equity for the Years Ended December 31, 2016, 2015 and 2014

Notes to Consolidated Financial Statements for the Years Ended December 31, 2016, 2015 and 2014

**(a)(2) Financial Statement Schedules.**

Schedule II – Valuation and Qualifying Accounts

**(a)(3) Exhibits.** The Exhibits filed herewith are set forth on the Index to Exhibits filed as part of this Annual Report and incorporated herein by reference.

**ITEM 16. FORM 10-K SUMMARY**

None

79

---



Edgar Filing: OLYMPIC STEEL INC - Form 10-K

March 2, 2017

/s/ Michael G. Rippey \*  
Michael G. Rippey, Director

March 2, 2017

/s/ Howard L. Goldstein \*  
Howard L. Goldstein, Director

\* The undersigned, by signing his name hereto, does sign and execute this Annual Report on Form 10-K pursuant to the Powers of Attorney executed by the above-named officers and directors of the Company and filed with the Securities and Exchange Commission on behalf of such officers and directors.

By: /s/ Richard T. Marabito  
Richard T. Marabito, Attorney-in-Fact

March 2, 2017



**OLYMPIC STEEL, INC.****INDEX TO EXHIBITS**

| Exhibit | Description   | Reference  |
|---------|---|--|
| 2.2     | Agreement and Plan of Merger, dated May 18, 2011, by and among OLYAC II, Inc., Olympic Steel, Inc., Chicago Tube and Iron Company, the Stockholders of Chicago Tube and Iron Company listed on Schedule I, and Dr. Donald McNeeley, as the Representative of the Stockholders.                            | Incorporated by reference to Exhibit 2.2 to Company's Form 8-K filed with the Commission on May 20, 2011 (Commission File No. 0-23320).                          |
| 3.1(i)  | Amended and Restated Articles of Incorporation  | Incorporated by reference to Exhibit 3.1(i) to the Registration Statement on Form S-1 (Registration No. 33-73992) filed with the Commission on January 12, 1994. |
| 3.1(ii) | Amended and Restated Code of Regulations  | Incorporated by reference to Exhibit 3.1 to Company's Form 10-Q filed with the Commission on August 6, 2015 (Commission File No. 0-23320).                       |
| 4.25    | Second Amended and Restated Loan and Security Agreement, dated as of June 30, 2014, by and among the Registrant, the financial institutions from time to time party thereto, Bank of America, N.A., as administrative agent, and the other agents from time to time party thereto.                        | Incorporated by reference to Exhibit 4.25 to Registrant's Form 8-K filed with the Commission on July 3, 2014 (Commission File No. 0-23320).                      |
| 4.26    | First Amendment to Second Amended and Restated Loan and Security Agreement, dated as of October 30, 2015, by and among the Registrant, the financial institutions from time to time party thereto, Bank of America, N.A., as administrative agent, and the other agents from time to time party thereto.  | Filed herewith   |
| 4.27    | Second Amendment to Second Amended and Restated Loan and Security Agreement, dated as of December 1, 2016, by and among the Registrant, the financial institutions from time to time party thereto, Bank of America, N.A., as administrative agent, and the other agents from time to time party thereto. | Filed herewith   |
| 10.1 *  | Olympic Steel, Inc. Stock Option Plan   | Incorporated by reference to Exhibit 10.1 to the Registration Statement on Form S-1 (Registration No. 33-73992) filed with the Commission on January 12, 1994.   |
| 10.8 *  | Form of Management Retention Agreement for Senior Executive Officers of the Company   | Incorporated by reference to Exhibit 10.8 to Registrant's Form 10-Q filed with the Commission on August 7, 2000 (Commission File No. 0-23320).                   |
| 10.9 *  |   |  |

Edgar Filing: OLYMPIC STEEL INC - Form 10-K

Form of Management Retention Agreement for Other  
Officers of the Company

Incorporated by reference to Exhibit 10.9 to  
Registrant's Form 10-Q filed with the  
Commission on August 7, 2000 (Commission  
File No. 0-23320).

10.14 \* Olympic Steel, Inc. Executive Deferred Compensation  
Plan dated December 15, 2004

Incorporated by reference to Exhibit 10.14 to  
Registrant's Form 10-K filed with the  
Commission on March 14, 2005 (Commission  
File No. 0-23320).

Edgar Filing: OLYMPIC STEEL INC - Form 10-K

| Exhibit | Description  | Reference  |
|---------|--|--|
| 10.15 * | Form of Non-Solicitation Agreements  | Incorporated by reference to Exhibit 10.15 to Registrant's Form 8-K filed with the Commission on March 4, 2005 (Commission File No. 0-23320).                          |
| 10.16 * | Form of Management Retention Agreement   | Incorporated by reference to Exhibit 10.16 to Registrant's Form 10-Q filed with the Commission on August 8, 2005 (Commission File No. 0-23320).                        |
| 10.17 * | Supplemental Executive Retirement Plan Term Sheet  | Incorporated by reference to Exhibit 99.1 to Registrant's Form 8-K filed with the Commission on January 5, 2006 (Commission File No. 0-23320).                         |
| 10.20 * | Olympic Steel, Inc. Supplemental Executive Retirement Plan   | Incorporated by reference to Exhibit 10.20 to Registrant's Form 8-K filed with the Commission on April 28, 2006 (Commission File No. 0-23320).                         |
| 10.21 * | Amended and Restated Olympic Steel, Inc. 2007 Omnibus Incentive Plan   | Incorporated by reference to Exhibit 4.3 to Registrant's Registration Statement on Form S-8 (Registration No. 333-211023) filed with the Commission on April 29, 2016. |
| 10.27*  | Form of Performance-Earned Restricted Stock Unit (PERS Unit) Agreement for Messrs. Siegal, Wolfort and Marabito. | Incorporated by reference to Exhibit 10.27 to Registrant's Form 10-Q filed with the Commission on May 5, 2009 (Commission File No. 0-23320).                           |
| 10.28*  | Form of Performance-Earned Restricted Stock Unit (PERS Unit) Agreement for Mr. Manson and Ms. Potash.            | Incorporated by reference to Exhibit 10.28 to Registrant's Form 10-Q filed with the Commission on May 5, 2009 (Commission File No. 0-23320).                           |
| 10.30 * | Olympic Steel, Inc. Senior Manager Compensation Plan   | Incorporated by reference to Exhibit 10.30 to Registrant's Form 10-Q filed with the Commission on May 6, 2011 (Commission File No. 0-23320).                           |
| 10.31 * | David A. Wolfort Employment Agreement effective as of January 1, 2016  | Incorporated by reference to Exhibit 10.31 to Registrant's Form 8-K filed with the Commission on December 31, 2015 (Commission File No. 0-23320).                      |
| 10.32 * | Donald McNeeley Employment Agreement effective as of March 31, 2016  | Incorporated by reference to Exhibit 10.32 to Registrant's Form 8-K filed with the Commission on March 31, 2016 (Commission File No. 0-23320).                         |
| 10.33 * | Richard T. Marabito Employment Agreement effective as of November 23, 2016                                       | Incorporated by reference to Exhibit 10.13 to Registrant's Form 8-K filed with the Commission on November 23, 2016 (Commission File No. 0-23320).                      |
| 10.34 * | Form of RSU Agreements for Messrs. Siegal, Wolfort and Marabito.   | Incorporated by reference to Exhibit 10.34 to Registrant's Form 10-K filed with the Commission on February 23, 2012  |



Edgar Filing: OLYMPIC STEEL INC - Form 10-K

| Exhibit | Description  | Reference   |
|---------|--|---|
| 10.35 * | Michael D. Siegal Employment Agreement effective as of December 1, 2012  | Incorporated by reference to Exhibit 10.35 to Registrant's Form 8-K filed with the Commission on November 21, 2012 (Commission File No. 0-23320). |
| 10.36 * | Departure of Directors or Certain Officers; Election of Directors; Appointment of Certain Officers; Compensatory Arrangements of Certain Officers.   | Incorporated by reference to Exhibit 10.36 to Registrant's Form 8-K filed with the Commission on December 30, 2014 (Commission File No. 0-23320). |
| 10.37*  | Amendment to Form of Management Retention Agreement for Senior Executive Officers of the Company   | Incorporated by reference to Exhibit 10.1 to Registrant's Form 10-Q filed with the Commission on May 1, 2015 (Commission File No. 0-23320).       |
| 10.38 * | Andrew S. Greiff Employment Agreement effective as of August 19, 2016  | Incorporated by reference to Exhibit 10.38 to Registrant's Form 8-K filed with the Commission on August 19, 2016 (Commission File No. 0-23320).   |
| 21      | List of Subsidiaries   | Filed herewith  |
| 23      | Consent of Independent Registered Public Accounting Firm   | Filed herewith  |
| 24      | Directors and Officers Powers of Attorney  | Filed herewith  |
| 31.1    | Certification of the Principal Executive Officer of the Company, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  | Filed herewith  |
| 31.2    | Certification of the Principal Financial Officer of the Company, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  | Filed herewith  |
| 32.1    | Written Statement of Michael D. Siegal, Chairman and Chief Executive Officer of the Company pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | Furnished herewith  |
| 32.2    | Written Statement of Richard T. Marabito, Chief Financial Officer of the Company pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002            | Furnished herewith  |
| 101.INS | XBRL Instance Document   |   |
| 101.SCH | XBRL Taxonomy Extension Schema Document  |   |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document  |   |
| 101.DEF | XBRL Taxonomy Extension Definition   |   |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document  |   |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document   |   |

\* This exhibit is a management contract or compensatory plan or arrangement.

