

COCA COLA BOTTLING CO CONSOLIDATED /DE/
Form 10-Q
November 08, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2018

Commission File Number 0-9286

COCA COLA BOTTLING CO. CONSOLIDATED

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

56-0950585
(I.R.S. Employer
Identification No.)

4100 Coca Cola Plaza
Charlotte, North Carolina 28211

(Address of principal executive offices) (Zip Code)

(704) 557-4400

(Registrant's telephone number, including area code)

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

| | |
|-------------------------|---------------------------|
| Large accelerated filer | Accelerated filer |
| Non-accelerated filer | Smaller reporting company |
| | Emerging growth company |

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes No

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

| Class | Outstanding at October 28, 2018 |
|--|---------------------------------|
| Common Stock, \$1.00 Par Value | 7,141,447 |
| Class B Common Stock, \$1.00 Par Value | 2,213,018 |

COCA COLA BOTTLING CO. CONSOLIDATED

QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2018

INDEX

| | Page |
|--|------|
| <u>PART I – FINANCIAL INFORMATION</u> | |
| Item 1. <u>Financial Statements (Unaudited)</u> | |
| <u>Consolidated Condensed Statements of Operations</u> | 2 |
| <u>Consolidated Condensed Statements of Comprehensive Income</u> | 3 |
| <u>Consolidated Condensed Balance Sheets</u> | 4 |
| <u>Consolidated Condensed Statements of Changes in Equity</u> | 5 |
| <u>Consolidated Condensed Statements of Cash Flows</u> | 6 |
| <u>Notes to Consolidated Condensed Financial Statements</u> | 7 |
| Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | 34 |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u> | 54 |
| Item 4. <u>Controls and Procedures</u> | 54 |
| <u>PART II – OTHER INFORMATION</u> | |
| Item 1. <u>Legal Proceedings</u> | 55 |
| Item 1A. <u>Risk Factors</u> | 55 |
| Item 6. <u>Exhibits</u> | 56 |
| <u>Signatures</u> | 57 |

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements.

COCA COLA BOTTLING CO. CONSOLIDATED

CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS

(Unaudited)

| (in thousands, except per share data) | Third Quarter | | First Three Quarters | |
|---|---------------|--------------|----------------------|--------------|
| | 2018 | 2017 | 2018 | 2017 |
| Net sales | \$ 1,211,661 | \$ 1,162,526 | \$ 3,510,997 | \$ 3,197,519 |
| Cost of sales | 791,317 | 752,202 | 2,313,728 | 2,039,996 |
| Gross profit | 420,344 | 410,324 | 1,197,269 | 1,157,523 |
| Selling, delivery and administrative expenses | 375,940 | 372,852 | 1,152,183 | 1,056,446 |
| Income from operations | 44,404 | 37,472 | 45,086 | 101,077 |
| Interest expense, net | 12,827 | 10,697 | 37,617 | 30,607 |
| Other income (expense), net | 1,696 | 3,884 | (3,612) | (36,595) |
| Gain on exchange transactions | 10,170 | - | 10,170 | - |
| Income before income taxes | 43,443 | 30,659 | 14,027 | 33,875 |
| Income tax expense | 16,493 | 11,748 | 3,387 | 11,800 |
| Net income | 26,950 | 18,911 | 10,640 | 22,075 |
| Less: Net income attributable to noncontrolling interest | 1,786 | 1,595 | 3,594 | 3,462 |
| Net income attributable to Coca-Cola Bottling Co. Consolidated | \$ 25,164 | \$ 17,316 | \$ 7,046 | \$ 18,613 |
| Basic net income per share based on net income attributable to Coca-Cola Bottling Co. Consolidated: | | | | |
| Common Stock | \$ 2.69 | \$ 1.86 | \$ 0.75 | \$ 2.00 |
| Weighted average number of Common Stock shares outstanding | 7,141 | 7,141 | 7,141 | 7,141 |
| Class B Common Stock | \$ 2.69 | \$ 1.86 | \$ 0.75 | \$ 2.00 |
| Weighted average number of Class B Common Stock shares outstanding | 2,213 | 2,193 | 2,208 | 2,188 |
| Diluted net income per share based on net income attributable to Coca-Cola Bottling Co. Consolidated: | | | | |
| Common Stock | \$ 2.69 | \$ 1.85 | \$ 0.75 | \$ 1.99 |
| Weighted average number of Common Stock shares outstanding – assuming dilution | 9,405 | 9,374 | 9,400 | 9,369 |
| Class B Common Stock | \$ 2.68 | \$ 1.84 | \$ 0.74 | \$ 1.97 |
| Weighted average number of Class B Common Stock shares outstanding – assuming dilution | 2,264 | 2,233 | 2,259 | 2,228 |
| Cash dividends per share: | | | | |
| Common Stock | \$ 0.25 | \$ 0.25 | \$ 0.75 | \$ 0.75 |
| Class B Common Stock | \$ 0.25 | \$ 0.25 | \$ 0.75 | \$ 0.75 |

See accompanying notes to consolidated condensed financial statements.

2

COCA COLA BOTTLING CO. CONSOLIDATED

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

| (in thousands) | Third Quarter | | First Three Quarters | |
|--|---------------|----------|----------------------|----------|
| | 2018 | 2017 | 2018 | 2017 |
| Net income | \$26,950 | \$18,911 | \$10,640 | \$22,075 |
| Other comprehensive income, net of tax: | | | | |
| Defined benefit plans reclassification including pension costs: | | | | |
| Actuarial gains | 703 | 496 | 2,109 | 1,487 |
| Prior service benefits | 4 | 4 | 13 | 13 |
| Postretirement benefits reclassification included in benefits costs: | | | | |
| Actuarial gains | 376 | 398 | 1,128 | 1,194 |
| Prior service costs | (348) | (458) | (1,044) | (1,374) |
| Foreign currency translation adjustment | (1) | 7 | (7) | 23 |
| Other comprehensive income, net of tax | 734 | 447 | 2,199 | 1,343 |
| Comprehensive income | 27,684 | 19,358 | 12,839 | 23,418 |
| Less: Comprehensive income attributable to noncontrolling interest | 1,786 | 1,595 | 3,594 | 3,462 |
| Comprehensive income attributable to Coca-Cola Bottling Co. Consolidated | \$25,898 | \$17,763 | \$9,245 | \$19,956 |

See accompanying notes to consolidated condensed financial statements.

COCA COLA BOTTLING CO. CONSOLIDATED

CONSOLIDATED CONDENSED BALANCE SHEETS

(Unaudited)

| (in thousands, except share data) | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 9,337 | \$ 16,902 |
| Accounts receivable, trade | 432,384 | 396,022 |
| Allowance for doubtful accounts | (9,069) | (7,606) |
| Accounts receivable from The Coca-Cola Company | 62,541 | 65,996 |
| Accounts receivable, other | 28,632 | 38,960 |
| Inventories | 229,892 | 183,618 |
| Prepaid expenses and other current assets | 91,514 | 100,646 |
| Total current assets | 845,231 | 794,538 |
| Property, plant and equipment, net | 998,117 | 1,031,388 |
| Leased property under capital leases, net | 25,208 | 29,837 |
| Other assets | 119,193 | 116,209 |
| Goodwill | 165,903 | 169,316 |
| Distribution agreements, net | 901,831 | 913,352 |
| Customer lists and other identifiable intangible assets, net | 16,941 | 18,320 |
| Total assets | \$ 3,072,424 | \$ 3,072,960 |
| LIABILITIES AND EQUITY | | |
| Current Liabilities: | | |
| Current portion of obligations under capital leases | \$ 8,438 | \$ 8,221 |
| Accounts payable, trade | 186,706 | 197,049 |
| Accounts payable to The Coca-Cola Company | 142,849 | 171,042 |
| Other accrued liabilities | 153,609 | 185,530 |
| Accrued compensation | 57,651 | 72,484 |
| Accrued interest payable | 9,363 | 5,126 |
| Total current liabilities | 558,616 | 639,452 |
| Deferred income taxes | 123,248 | 112,364 |
| Pension and postretirement benefit obligations | 98,738 | 118,392 |
| Other liabilities | 600,310 | 620,579 |
| Obligations under capital leases | 28,840 | 35,248 |
| Long-term debt | 1,194,109 | 1,088,018 |
| Total liabilities | 2,603,861 | 2,614,053 |
| Commitments and Contingencies | | |
| Equity: | | |
| Common Stock, \$1.00 par value: 30,000,000 shares authorized; 10,203,821 shares issued | 10,204 | 10,204 |
| Class B Common Stock, \$1.00 par value: 10,000,000 shares authorized; 2,841,132 and 2,820,836 shares issued, respectively | 2,839 | 2,819 |

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

| | | |
|--|--------------|-------------|
| Capital in excess of par value | 124,228 | 120,417 |
| Retained earnings | 388,750 | 388,718 |
| Accumulated other comprehensive loss | (92,003) | (94,202) |
| Treasury stock, at cost: Common Stock – 3,062,374 shares | (60,845) | (60,845) |
| Treasury stock, at cost: Class B Common Stock – 628,114 shares | (409) | (409) |
| Total equity of Coca-Cola Bottling Co. Consolidated | 372,764 | 366,702 |
| Noncontrolling interest | 95,799 | 92,205 |
| Total equity | 468,563 | 458,907 |
| Total liabilities and equity | \$ 3,072,424 | \$3,072,960 |

See accompanying notes to consolidated condensed financial statements.

COCA COLA BOTTLING CO. CONSOLIDATED

CONSOLIDATED CONDENSED STATEMENTS OF CHANGES IN EQUITY

(Unaudited)

| (in thousands, except share data) | Common Stock | Class B Common Stock | Capital in Excess of Par Value | Retained Earnings | Accumulated Other Comprehensive Loss | Treasury Stock - Common Stock | Treasury Stock | Total Equity of Coca-Cola Bottling Co. Consolidated | Non-controlling Interest | Total Equity |
|---|--------------|----------------------|--------------------------------|-------------------|--------------------------------------|-------------------------------|----------------|---|--------------------------|--------------|
| | | | | | | | Class B | | | |
| Balance on December 31, 2017 | \$10,204 | \$2,819 | \$120,417 | \$388,718 | \$(94,202) | \$(60,845) | \$(409) | \$366,702 | \$92,205 | \$458,907 |
| Net income | - | - | - | 7,046 | - | - | - | 7,046 | 3,594 | 10,640 |
| Other comprehensive income, net of tax | - | - | - | - | 2,199 | - | - | 2,199 | - | 2,199 |
| Cash dividends paid: | | | | | | | | | | |
| Common Stock (\$0.75 per share) | - | - | - | (5,357) | - | - | - | (5,357) | - | (5,357) |
| Class B Common Stock (\$0.75 per share) | - | - | - | (1,657) | - | - | - | (1,657) | - | (1,657) |
| Issuance of 20,296 shares of Class B Common Stock | - | 20 | 3,811 | - | - | - | - | 3,831 | - | 3,831 |
| Balance on September 30, 2018 | \$10,204 | \$2,839 | \$124,228 | \$388,750 | \$(92,003) | \$(60,845) | \$(409) | \$372,764 | \$95,799 | \$468,563 |
| Balance on January 1, 2017 | \$10,204 | \$2,798 | \$116,769 | \$301,511 | \$(92,897) | \$(60,845) | \$(409) | \$277,131 | \$85,893 | \$363,024 |
| Net income | - | - | - | 18,613 | - | - | - | 18,613 | 3,462 | 22,075 |
| Other comprehensive income, net of | - | - | - | - | 1,343 | - | - | 1,343 | - | 1,343 |

| | | | | | | | | | | |
|---|----------|---------|-----------|-----------|------------|------------|---------|-----------|----------|-----------|
| tax | | | | | | | | | | |
| Cash dividends paid: | | | | | | | | | | |
| Common Stock (\$0.75 per share) | - | - | - | (5,356) | - | - | - | (5,356) | - | (5,356) |
| Class B Common Stock (\$0.75 per share) | - | - | - | (1,639) | - | - | - | (1,639) | - | (1,639) |
| Issuance of 21,020 shares of Class B Common Stock | - | 21 | 3,648 | - | - | - | - | 3,669 | - | 3,669 |
| Balance on October 1, 2017 | \$10,204 | \$2,819 | \$120,417 | \$313,129 | \$(91,554) | \$(60,845) | \$(409) | \$293,761 | \$89,355 | \$383,116 |

See accompanying notes to consolidated condensed financial statements.

5

COCA COLA BOTTLING CO. CONSOLIDATED

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(Unaudited)

| (in thousands) | First Three Quarters | |
|--|----------------------|-------------|
| | 2018 | 2017 |
| Cash Flows from Operating Activities: | | |
| Net income | \$10,640 | \$22,075 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation expense | 123,542 | 108,697 |
| Amortization of intangible assets and deferred proceeds, net | 16,954 | 11,596 |
| Deferred income taxes | 9,903 | (24,741) |
| Gain on exchange transactions | (10,170) | - |
| Loss on sale of property, plant and equipment | 6,123 | 3,420 |
| Impairment of property, plant and equipment | 299 | - |
| Fair value adjustment of acquisition related contingent consideration | 1,584 | 23,140 |
| Stock compensation expense | 4,494 | 6,473 |
| Amortization of debt costs | 1,103 | 806 |
| Proceeds from Territory Conversion Fee | - | 87,066 |
| Change in current assets less current liabilities (exclusive of acquisitions) | (120,421) | (19,036) |
| Change in other noncurrent assets (exclusive of acquisitions) | 724 | (13,391) |
| Change in other noncurrent liabilities (exclusive of acquisitions) | (18,762) | (3,746) |
| Other | 17 | 66 |
| Total adjustments | 15,390 | 180,350 |
| Net cash provided by operating activities | \$26,030 | \$202,425 |
| Cash Flows from Investing Activities: | | |
| Additions to property, plant and equipment (exclusive of acquisitions) | \$(113,104) | \$(114,953) |
| Investment in CONA Services LLC | (2,098) | (1,976) |
| Acquisition of distribution territories and regional manufacturing facilities, net of cash acquired and purchase price settlements | 1,811 | (227,769) |
| Proceeds from cold drink equipment | 3,789 | 8,400 |
| Proceeds from the sale of property, plant and equipment | 3,555 | 493 |
| Glacéau distribution agreement consideration | - | (15,598) |
| Prepayment of funds for October 2017 Expansion Transactions | - | (56,498) |
| Net cash used in investing activities | \$(106,047) | \$(407,901) |
| Cash Flows from Financing Activities: | | |
| Payments on Revolving Credit Facility | \$(322,000) | \$(238,000) |
| Borrowings under Revolving Credit Facility | 285,000 | 333,000 |
| Proceeds from issuance of Senior Notes | 150,000 | 125,000 |
| Payment of acquisition related contingent consideration | (18,312) | (11,650) |
| Payment on Term Loan Facility | (7,500) | - |
| Cash dividends paid | (7,014) | (6,995) |
| Principal payments on capital lease obligations | (6,191) | (5,594) |

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

| | | |
|--|------------|------------|
| Debt issuance fees | (1,531) | (213) |
| Net cash provided by financing activities | \$72,452 | \$195,548 |
| Net decrease in cash | \$(7,565) | \$(9,928) |
| Cash at beginning of period | 16,902 | 21,850 |
| Cash at end of period | \$9,337 | \$11,922 |
| Significant noncash investing and financing activities: | | |
| Additions to property, plant and equipment accrued and recorded in accounts payable, trade | \$4,081 | \$13,724 |
| Issuance of Class B Common Stock in connection with stock award | 3,831 | 3,669 |

See accompanying notes to consolidated condensed financial statements.

COCA COLA BOTTLING CO. CONSOLIDATED

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Unaudited)

1. Significant Accounting Policies and New Accounting Pronouncements

The consolidated condensed financial statements include the accounts of Coca Cola Bottling Co. Consolidated and its majority-owned subsidiaries (the “Company”). All significant intercompany accounts and transactions have been eliminated. The consolidated condensed financial statements reflect all adjustments, including normal, recurring accruals, which, in the opinion of management, are necessary for a fair statement of the results for the interim periods presented:

- The financial position as of September 30, 2018 and December 31, 2017.
- The results of operations and comprehensive income for the 13 week periods ended September 30, 2018 (“third quarter” of fiscal 2018 (“2018”)) and October 1, 2017 (“third quarter” of fiscal 2017 (“2017”)), and the 39 week periods ended September 30, 2018 (“first three quarters” of 2018) and October 1, 2017 (“first three quarters” of 2017).
- The changes in equity and cash flows for the first three quarters of 2018 and the first three quarters of 2017.

The consolidated condensed financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial reporting and the instructions to Form 10-Q and Article 10 of Regulation S-X. The accounting policies followed in the presentation of interim financial results are consistent with those followed on an annual basis. These policies are presented in Note 1 to the consolidated financial statements included in the Company’s Annual Report on Form 10-K for 2017 filed with the Securities and Exchange Commission (the “SEC”).

The preparation of consolidated condensed financial statements, in conformity with GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the 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.

Significant Accounting Policies

In the ordinary course of business, the Company has made a number of estimates and assumptions relating to the reporting of results of operations and financial position in the preparation of its consolidated condensed financial

statements in conformity with GAAP. Actual results could differ significantly from those estimates under different assumptions and conditions. The Company included in its Annual Report on Form 10 K for 2017 under the caption “Discussion of Critical Accounting Policies, Estimates and New Accounting Pronouncements” in Part II, “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” a discussion of the Company’s most critical accounting policies, which are those the Company believes to be the most important to the portrayal of its financial condition and results of operations and require management’s most difficult, subjective and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Any changes in critical accounting policies and estimates are discussed with the Audit Committee of the Board of Directors of the Company during the quarter in which a change is contemplated and prior to making such change.

Recently Adopted Pronouncements

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) 2014-09 “Revenue from Contracts with Customers,” (the “revenue recognition standard”). Subsequent to the issuance of ASU 2014-09, the FASB issued several additional accounting standards for revenue recognition to update the effective date of the revenue recognition guidance and to provide additional clarification on the updated standard. The new guidance is effective for annual and interim periods beginning after December 15, 2017. The Company adopted the revenue recognition standard in the first quarter of 2018, as discussed in Note 2.

In January 2016, the FASB issued ASU 2016-01 “Recognition and Measurement of Financial Assets and Financial Liabilities,” which revises the classification and measurement of investments in equity securities and the presentation of certain fair value changes in financial liabilities measured at fair value. The new guidance is effective for annual and interim periods beginning after December 31, 2017. The Company adopted this guidance in the first quarter of 2018 and there was no material impact to the Company’s consolidated condensed financial statements.

In January 2017, the FASB issued ASU 2017-01 “Clarifying the Definition of a Business,” which clarifies the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions or disposals of assets or businesses. The new guidance is effective for annual periods beginning after December 15, 2017, including

interim periods within those periods. The Company adopted this guidance in the first quarter of 2018 and there was no material impact to the Company's consolidated condensed financial statements.

In January 2017, the FASB issued ASU 2017-04 "Simplifying the Test for Goodwill Impairment," which simplifies how an entity is required to test goodwill for impairment by eliminating step 2 from the goodwill impairment test, which measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount. Under the new guidance, entities should instead perform annual or interim goodwill impairment tests by comparing the fair value of a reporting unit with its carrying amount and recognize an impairment charge for the excess of the carrying amount over the fair value of the respective reporting unit. The new guidance is effective for the annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. The Company adopted this guidance in the first quarter of 2018 and there was no material impact to the Company's consolidated condensed financial statements.

In March 2017, the FASB issued ASU 2017-07 "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost," which requires that the service cost component of the Company's net periodic pension cost and net periodic postretirement benefit cost be included in the same line item as other compensation costs arising from services rendered by employees, with the non-service cost components of net periodic benefit cost being classified outside of a subtotal of income from operations. Of the components of net periodic benefit cost, only the service cost component is eligible for asset capitalization. The new guidance is effective for annual periods beginning after December 31, 2017, including interim periods within those annual periods. The Company adopted this guidance in the first quarter of 2018 using the practical expedient which allows entities to use information previously disclosed in their pension and other postretirement benefit plans note as the estimation basis to apply the retrospective presentation requirements in ASU 2017-07.

With the adoption of this guidance in the first quarter of 2018, the Company recorded the non-service cost component of net periodic benefit cost, which totaled \$0.6 million in the third quarter of 2018 and \$2.0 million in the first three quarters of 2018, to other income (expense), net in the consolidated condensed statements of operations. The Company reclassified \$1.3 million from the third quarter of 2017 and \$4.0 million from the first three quarters of 2017 of non-service cost components of net periodic benefit cost and other benefit plan charges from selling, delivery and administrative ("S,D&A") expenses to other income (expense), net in the consolidated condensed statements of operations. The non-service cost component of net periodic benefit cost is included in the Nonalcoholic Beverages segment.

Recently Issued Pronouncements

In February 2018, the FASB issued ASU 2018-02 "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income," which provides the option to reclassify stranded tax effects resulting from the Tax Cuts and Jobs Act (the "Tax Act") from accumulated other comprehensive income to retained earnings. The new guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, and

can be early adopted. The Company is currently evaluating whether it will adopt this guidance.

In February 2016, the FASB issued ASU 2016-02 "Leases," which requires lessees to recognize a right-to-use asset and a lease liability for virtually all leases (other than leases meeting the definition of a short-term lease). The new guidance is effective for fiscal years beginning after December 15, 2018 and interim periods beginning the following fiscal year. The Company anticipates adopting the new accounting standard on December 31, 2018, the first day of fiscal 2019, using the optional transition method, which was approved by the FASB in March 2018 and allows companies the option to use the effective date as the date of initial application on transition and to not adjust comparative period financial information or make the new required disclosures for periods prior to the effective date.

The Company has formed a project team, which is in the process of reviewing its existing lease portfolio, including certain service contracts for embedded leases, to determine the size of the Company's lease portfolio in order to evaluate the impact of this new guidance on the Company's consolidated condensed financial statements. The Company anticipates the impact of adopting this new guidance will be material to its consolidated condensed balance sheets. The impact on the Company's consolidated condensed statements of operations is still being evaluated. As the impact of the new guidance is non-cash in nature, the Company does not anticipate the impact of adopting this new guidance will be material to its consolidated condensed statements of cash flows. Additionally, the Company is evaluating the impacts of ASU 2016-02 beyond accounting, including system, data and process changes required to comply with this standard. The Company anticipates implementing new controls and utilizing a lease accounting software application with the adoption of this new guidance and on a go-forward basis in order to properly approve, track and account for its entire lease portfolio.

2.Revenue Recognition

The Company adopted the revenue recognition standard, including all relevant amendments and practical expedients, in the first quarter of 2018 using the modified retrospective approach for all contracts not completed at the date of initial adoption, considering materiality and applicability. Upon adoption of this guidance, there was no material impact to the Company's consolidated condensed financial statements.

The Company's contracts are derived from customer orders, including customer sales incentives, generated through an order processing and replenishment model. The Company has defined its performance obligations for its contracts as either at a point in time or over time.

The Company offers a range of nonalcoholic beverage products and flavors designed to meet the demands of its consumers, including both sparkling and still beverages. Sparkling beverages are carbonated beverages and the Company's principal sparkling beverage is Coca Cola. Still beverages include energy products and noncarbonated beverages such as bottled water, tea, ready to drink coffee, enhanced water, juices and sports drinks.

The Company's products are sold and distributed through various channels, which include selling directly to retail stores and other outlets such as food markets, institutional accounts and vending machine outlets. During the first three quarters of 2018, approximately 66% of the Company's bottle/can sales volume to retail customers was sold for future consumption, while the remaining bottle/can sales volume to retail customers was sold for immediate consumption. All the Company's beverage sales were to customers in the United States. The Company typically collects payment from customers within 30 days from the date of sale.

The Company's sales are divided into two main categories: (i) bottle/can sales and (ii) other sales. Bottle/can sales include products packaged primarily in plastic bottles and aluminum cans. Other sales include sales to other Coca Cola bottlers, "post-mix" products, transportation and equipment maintenance revenue. Post-mix products are dispensed through equipment that mixes fountain syrups with carbonated or still water, enabling fountain retailers to sell finished products to consumers in cups or glasses. Net sales by category were as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--|------------------|----------------|----------------------|------------------|
| | 2018 | 2017 | 2018 | 2017 |
| Bottle/can sales: | | | | |
| Sparkling beverages (carbonated) | \$605,614 | \$582,710 | \$1,787,451 | \$1,670,093 |
| Still beverages (noncarbonated, including energy products) | 413,282 | 384,495 | 1,142,764 | 1,009,508 |
| Total bottle/can sales | 1,018,896 | 967,205 | 2,930,215 | 2,679,601 |
| Other sales: | | | | |

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

| | | | | |
|-----------------------------------|-------------|-------------|-------------|-------------|
| Sales to other Coca-Cola bottlers | 92,139 | 104,619 | 300,819 | 274,317 |
| Post-mix and other | 100,626 | 90,702 | 279,963 | 243,601 |
| Total other sales | 192,765 | 195,321 | 580,782 | 517,918 |
| Total net sales | \$1,211,661 | \$1,162,526 | \$3,510,997 | \$3,197,519 |

Bottle/can sales represented approximately 83% and 84% in the first three quarters of 2018 and the first three quarters of 2017, respectively. The sparkling beverage category represented approximately 61% and 62% of total bottle/can sales during the first three quarters of 2018 and the first three quarters of 2017, respectively.

Bottle/can sales, sales to other Coca Cola bottlers and post-mix sales are recognized when control transfers to a customer, which is generally upon delivery and is considered a single point in time (“point in time”). Point in time sales accounted for approximately 97% of the Company’s net sales in both the first three quarters of 2018 and the first three quarters of 2017. Substantially all of the Company’s revenue is recognized at a point in time and is included in the Nonalcoholic Beverages segment.

Other sales, which include revenue for service fees related to the repair of cold drink equipment and delivery fees for freight hauling and brokerage services, are recognized over time (“over time”). Revenues related to cold drink equipment repair are recognized as the respective services are completed using a cost-to-cost input method. Repair services are generally completed in less than one day but can extend up to one month. Revenues related to freight hauling and brokerage services are recognized as the delivery occurs using a miles driven output method. Generally, delivery occurs and freight charges are recognized in the same day. Over time sales orders open at the end of a financial period are not considered material to the Company’s consolidated condensed financial statements.

The Company participates in various sales programs with The Coca Cola Company, other beverage companies and customers to increase the sale of its products. Programs negotiated with customers include arrangements under which allowances can be earned for attaining agreed-upon sales levels. The cost of these various sales incentives are not considered a separate performance obligation and are included as deductions to net sales.

Revenues do not include sales or other taxes collected from customers.

The majority of the Company's contracts include multiple performance obligations related to the delivery of specifically identifiable products, which generally have a duration of less than one year. For sales contracts with multiple performance obligations, the Company allocates the contract's transaction price to each performance obligation using stated contractual price, which represents the standalone selling price of each distinct good sold under the contract. Generally, the Company's service contracts have a single performance obligation.

The following table represents a disaggregation of revenue from contracts with customers:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--------------------------------------|---------------------|---------------------|----------------------|---------------------|
| | 2018 | 2017 | 2018 | 2017 |
| Point in time net sales: | | | | |
| Nonalcoholic - point in time | \$ 1,168,276 | \$ 1,132,181 | \$ 3,394,253 | \$ 3,112,777 |
| Total point in time net sales | \$ 1,168,276 | \$ 1,132,181 | \$ 3,394,253 | \$ 3,112,777 |
| Over time net sales: | | | | |
| Nonalcoholic - over time | \$ 11,936 | \$ 10,057 | \$ 33,239 | \$ 27,197 |
| Other - over time | 31,449 | 20,288 | 83,505 | 57,545 |
| Total over time net sales | \$ 43,385 | \$ 30,345 | \$ 116,744 | \$ 84,742 |
| Total net sales | \$ 1,211,661 | \$ 1,162,526 | \$ 3,510,997 | \$ 3,197,519 |

The Company sells its products and extends credit, generally without requiring collateral, based on an ongoing evaluation of the customer's business prospects and financial condition. The Company evaluates the collectability of its trade accounts receivable based on a number of factors, including the Company's historic collections pattern and changes to a specific customer's ability to meet its financial obligations. The Company has established an allowance for doubtful accounts to adjust the recorded receivable to the estimated amount the Company believes will ultimately be collected.

The nature of the Company's contracts gives rise to several types of variable consideration, including prospective and retrospective rebates. The Company accounts for its prospective and retrospective rebates using the expected value method, which estimates the net price to the customer based on the customer's expected annual sales volume

projections.

The Company experiences customer returns primarily as a result of damaged or out-of-date product. At any given time, the Company estimates less than 1% of bottle/can sales and post-mix sales could be at risk for return by customers. The Company's reserve for customer returns was \$2.3 million as of September 30, 2018 and was included in the allowance for doubtful accounts in the consolidated condensed balance sheet. Returned product is recognized as a reduction of net sales.

3.Acquisitions and Divestitures

As part of The Coca Cola Company's plans to rebrand its North American bottling territories, the Company and Piedmont Coca Cola Bottling Partnership, a partnership formed by the Company and The Coca Cola Company ("Piedmont"), completed a series of transactions from April 2013 to October 2017 with The Coca Cola Company, Coca Cola Refreshments USA, Inc. ("CCR"), a wholly-owned subsidiary of The Coca Cola Company and Coca Cola Bottling Company United, Inc. ("United"), an independent bottler that is unrelated to the Company, to significantly expand the Company's distribution and manufacturing operations (the "System Transformation"). The System Transformation included the acquisition and exchange of rights to serve distribution territories and related distribution assets, as well as the acquisition and exchange of regional manufacturing facilities and related manufacturing assets.

A summary of the System Transformation transactions (the "System Transformation Transactions") completed by the Company is included in the Company's Annual Report on Form 10 K for 2017. Following is a summary of the System Transformation Transactions for which final post-closing adjustments were completed during the third quarter of 2018 in accordance with the terms

and conditions of the applicable asset purchase agreement or asset exchange agreement for such transactions. As of September 30, 2018, the cash purchase prices or settlement amounts for all System Transformation Transactions have been resolved according to the terms of the transaction agreements. The post-closing adjustments made during the third quarter of 2018 resulted in a \$10.2 million net adjustment to the gain on exchange transactions in the consolidated condensed statements of operations.

Acquisition of Arkansas Distribution Territories and Memphis, Tennessee and West Memphis, Arkansas Regional Manufacturing Facilities in exchange for the Company's Deep South and Somerset Distribution Territories and Mobile, Alabama Manufacturing Facility (the "CCR Exchange Transaction")

On October 2, 2017, the Company (i) acquired from CCR distribution rights and related assets in territories previously served by CCR through CCR's facilities and equipment located in central and southern Arkansas and two regional manufacturing facilities located in Memphis, Tennessee and West Memphis, Arkansas and related manufacturing assets (collectively, the "CCR Exchange Business") in exchange for which the Company (ii) transferred to CCR distribution rights and related assets in territories previously served by the Company through its facilities and equipment located in portions of southern Alabama, southeastern Mississippi, southwestern Georgia and northwestern Florida and in and around Somerset, Kentucky and a regional manufacturing facility located in Mobile, Alabama and related manufacturing assets (collectively, the "Deep South and Somerset Exchange Business"), pursuant to an asset exchange agreement entered into by the Company, certain of its wholly-owned subsidiaries and CCR on September 29, 2017.

At closing, the Company paid CCR \$15.9 million toward the settlement amount for the CCR Exchange Transaction, representing an estimate of the difference between the value of the CCR Exchange Business acquired by the Company and the value of the Deep South and Somerset Exchange Business acquired by CCR. During the fourth quarter of 2017, the Company recorded certain adjustments to this settlement amount as a result of changes in estimated net working capital and other fair value adjustments. The settlement amount was included in accounts payable to The Coca Cola Company in the consolidated condensed balance sheet as of December 31, 2017.

During the third quarter of 2018, all post-closing adjustments were finalized for the CCR Exchange Transaction, resulting in a final settlement amount for the CCR Exchange Transaction of \$26.2 million. A net balance of \$10.3 million related to the settlement amount for the CCR Exchange Transaction remained payable to CCR by the Company as of September 30, 2018. This balance was paid to CCR during the fourth quarter of 2018.

Acquisition of Memphis, Tennessee Distribution Territories (the "Memphis Transaction")

On October 2, 2017, the Company acquired distribution rights and related assets in territories previously served by CCR through CCR's facilities and equipment located in and around Memphis, Tennessee, including portions of

northwestern Mississippi and eastern Arkansas (the “Memphis Territory”), pursuant to an asset purchase agreement entered by the Company and CCR on September 29, 2017 (the “September 2017 APA”). At closing, the Company paid CCR \$39.6 million toward the purchase price for the Memphis Transaction. During the second and third quarters of 2018, all post-closing adjustments were finalized for the Memphis Transaction, resulting in a net increase of \$2.6 million in the cash purchase price, which was paid to CCR during the third quarter of 2018.

Acquisition of Spartanburg and Bluffton, South Carolina Distribution Territories in exchange for the Company’s Florence and Laurel Territories and Piedmont’s Northeastern Georgia Territories (the “United Exchange Transaction”)

On October 2, 2017, the Company and Piedmont completed exchange transactions in which (i) the Company acquired from United distribution rights and related assets in territories previously served by United through United’s facilities and equipment located in and around Spartanburg, South Carolina and a portion of United’s territory located in and around Bluffton, South Carolina (collectively, the “United Distribution Business”) and Piedmont acquired from United similar rights, assets and liabilities, and working capital in the remainder of United’s Bluffton, South Carolina territory, in exchange for which (ii) the Company transferred to United distribution rights and related assets in territories previously served by the Company through its facilities and equipment located in parts of northwestern Alabama, south-central Tennessee and southeastern Mississippi previously served by the Company’s distribution centers located in Florence, Alabama and Laurel, Mississippi (collectively, the “Florence and Laurel Distribution Business”) and Piedmont transferred to United similar rights, assets and liabilities, and working capital of Piedmont’s in territory located in parts of northeastern Georgia (the “Northeastern Georgia Distribution Business”), pursuant to an asset exchange agreement between the Company, certain of its wholly-owned subsidiaries and United dated September 29, 2017 and an asset exchange agreement between Piedmont and United dated September 29, 2017.

At closing, the Company and Piedmont paid United \$3.4 million toward the settlement amount for the United Exchange Transaction, representing an estimate of (i) the difference between the value of the United Distribution Business acquired by the Company and the value of the Florence and Laurel Distribution Business acquired by United, plus (ii) the difference between the value of the portion of

the Bluffton, South Carolina territory acquired by Piedmont and the value of the Northeastern Georgia Distribution Business acquired by United. During the third quarter of 2018, all post-closing adjustments were finalized for the United Exchange Transaction, resulting in an increase of \$2.8 million in the settlement amount, which was included in accounts payable, trade in the consolidated condensed balance sheet as of September 30, 2018. The Company anticipates this balance will be paid to United during the fourth quarter of 2018.

Collectively, the CCR Exchange Transaction, the Memphis Transaction and the United Exchange Transaction are the “October 2017 Transactions,” the CCR Exchange Business, the Memphis Territory and the United Distribution Business are the “October 2017 Acquisitions” and the Deep South and Somerset Exchange Business and the Florence and Laurel Distribution Business are the “October 2017 Divestitures.”

In addition to the October 2017 Transactions summarized above, the Company completed three additional System Transformation Transactions with CCR in 2017 for which all post-closing adjustments have been completed: (i) the acquisition from CCR of distribution rights and related assets for territories in Anderson, Fort Wayne, Lafayette, South Bend and Terre Haute, Indiana on January 27, 2017 (the “January 2017 Transaction”), (ii) the acquisition from CCR of distribution rights and related assets for territories in Indianapolis and Bloomington, Indiana and Columbus and Mansfield, Ohio and regional manufacturing facilities and related assets located in Indianapolis and Portland, Indiana on March 31, 2017 (the “March 2017 Transactions”), and (iii) the acquisition from CCR of distribution rights and related assets for territories in Akron, Elyria, Toledo, Willoughby and Youngstown, Ohio and a regional manufacturing facility and related assets located in Twinsburg, Ohio on April 28, 2017 (the “April 2017 Transactions”).

Post-closing adjustments for the January 2017 Transaction and the March 2017 Transactions were completed during 2017 and post-closing adjustments for the April 2017 Transactions were completed during the second quarter of 2018. During the fourth quarter of 2017, the cash purchase price for the April 2017 Transactions decreased by \$4.7 million as a result of net working capital and other fair value adjustments, which was paid to the Company by The Coca Cola Company during the second quarter of 2018.

The fair value of acquired assets and assumed liabilities of the System Transformation Transactions that closed during 2017 (the “2017 System Transformation Transactions”), as of the acquisition dates, is summarized as follows:

| | January 2017 | March 2017 | April 2017 | October 2017 | Total 2017 System Transformation Transactions |
|----------------|-----------------|---------------|--------------|-----------------|--|
| (in thousands) | Transaction | Transactions | Transactions | Acquisitions | Acquisitions |
| Cash | \$ 107 | \$ 211 | \$ 103 | \$ 191 | \$ 612 |

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

| | | | | | |
|--|-----------|------------|------------|------------|------------|
| Inventories | 5,953 | 20,952 | 14,554 | 14,850 | 56,309 |
| Prepaid expenses and other current assets | 1,155 | 5,117 | 4,068 | 4,573 | 14,913 |
| Accounts receivable from The Coca-Cola Company | 1,042 | 1,807 | 2,552 | 1,447 | 6,848 |
| Property, plant and equipment | 25,708 | 81,638 | 52,263 | 71,589 | 231,198 |
| Other assets (including deferred taxes) | 1,158 | 3,227 | 3,960 | 1,300 | 9,645 |
| Goodwill | 1,544 | 2,527 | 16,941 | 11,442 | 32,454 |
| Distribution agreements | 22,000 | 46,750 | 19,500 | 129,450 | 217,700 |
| Customer lists | 1,500 | 1,750 | 1,000 | 4,950 | 9,200 |
| Total acquired assets | \$ 60,167 | \$ 163,979 | \$ 114,941 | \$ 239,792 | \$ 578,879 |
| Current liabilities (acquisition related contingent consideration) | \$ 1,350 | \$ 2,958 | \$ 1,475 | \$ 1,501 | \$ 7,284 |
| Other current liabilities | 324 | 3,760 | 2,860 | 8,311 | 15,255 |
| Other liabilities (acquisition related contingent consideration) | 26,377 | 49,739 | 25,616 | 20,676 | 122,408 |
| Other liabilities | 43 | 2,953 | 1,792 | 102 | 4,890 |
| Total assumed liabilities | \$ 28,094 | \$ 59,410 | \$ 31,743 | \$ 30,590 | \$ 149,837 |

The fair value of acquired assets and assumed liabilities in the October 2017 Acquisitions as of the acquisition date is summarized as follows:

| (in thousands) | CCR Exchange Business | Memphis Territory | United Exchange Business | Total October 2017 Acquisitions |
|--|-----------------------------|----------------------|--------------------------------|--|
| Cash | \$ 91 | \$ 100 | \$ - | \$ 191 |
| Inventories | 10,667 | 3,354 | 829 | 14,850 |
| Prepaid expenses and other current assets | 3,172 | 1,087 | 314 | 4,573 |
| Accounts receivable from The Coca-Cola Company | 674 | 563 | 210 | 1,447 |
| Property, plant and equipment | 47,484 | 21,321 | 2,784 | 71,589 |
| Other assets (including deferred taxes) | 753 | 547 | - | 1,300 |
| Goodwill | 3,546 | 5,199 | 2,697 | 11,442 |
| Distribution agreements | 80,100 | 35,400 | 13,950 | 129,450 |
| Customer lists | 3,200 | 1,200 | 550 | 4,950 |
| Total acquired assets | \$ 149,687 | \$ 68,771 | \$ 21,334 | \$ 239,792 |
| Current liabilities (acquisition related contingent consideration) | \$ - | \$ 1,501 | \$ - | \$ 1,501 |
| Other current liabilities | 3,497 | 4,323 | 491 | 8,311 |
| Other liabilities (acquisition related contingent consideration) | - | 20,676 | - | 20,676 |
| Other liabilities | 15 | 87 | - | 102 |
| Total assumed liabilities | \$ 3,512 | \$ 26,587 | \$ 491 | \$ 30,590 |

The goodwill for the 2017 System Transformation Transactions is included in the Nonalcoholic Beverages segment and is primarily attributed to operational synergies and the workforce acquired. Goodwill of \$11.4 million, \$3.5 million, \$8.6 million and \$2.7 million is expected to be deductible for tax purposes for the April 2017 Transactions, the CCR Exchange Business, the Memphis Territory and the United Exchange Business, respectively. No goodwill is expected to be deductible for tax purposes for the January 2017 Transaction or the March 2017 Transactions.

The carrying value of assets and liabilities divested in the October 2017 Divestitures is summarized as follows:

| (in thousands) | October 2017 Divestitures |
|---|---------------------------------|
| Cash | \$ 303 |
| Inventories | 13,717 |
| Prepaid expenses and other current assets | 1,199 |
| Property, plant and equipment | 44,380 |
| Other assets (including deferred taxes) | 604 |

| | |
|---|------------|
| Goodwill | 13,073 |
| Distribution agreements | 65,043 |
| Total divested assets | \$ 138,319 |
| | |
| Other current liabilities | \$ 5,683 |
| Pension and postretirement benefit obligation | 16,855 |
| Total divested liabilities | \$ 22,538 |

The October 2017 Divestitures were recorded in the Company's Nonalcoholic Beverages segment prior to divestiture.

System Transformation Transactions Financial Results

The financial results of the System Transformation Transactions have been included in the Company's consolidated condensed financial statements from their respective acquisition or exchange dates. Net sales and income from operations for certain territories and regional manufacturing facilities acquired and divested by the Company during 2017 are impracticable to separately calculate, as the operations were absorbed into territories and facilities owned by the Company prior to the System Transformation, and therefore have been omitted from the results below. Omission of net sales and income from operations for such territories and facilities is not

considered material to the results presented below. The remaining 2017 System Transformation Transactions contributed the following amounts to the Company's consolidated condensed statements of operations:

| (in thousands) | Third Quarter | | First Three Quarters | |
|---|---------------|-----------|----------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Impact to net sales - total 2017 System Transformation Transactions acquisitions | \$308,825 | \$221,034 | \$896,179 | \$454,174 |
| Impact to net sales - October 2017 Divestitures | - | 79,032 | - | 231,301 |
| Total impact to net sales | \$308,825 | \$300,066 | \$896,179 | \$685,475 |
| Impact to income from operations - total 2017 System Transformation Transactions acquisitions | \$11,874 | \$3,176 | \$14,635 | \$13,595 |
| Impact to income from operations - October 2017 Divestitures | - | 7,689 | - | 22,973 |
| Total impact to income from operations | \$11,874 | \$10,865 | \$14,635 | \$36,568 |

The Company incurred transaction related expenses for the System Transformation Transactions of \$5.6 million in the first three quarters of 2017, which were included within S,D&A expenses on the consolidated condensed statements of operations.

System Transformation Transactions Pro Forma Financial Information

The purpose of the pro forma disclosure is to present the net sales and the income from operations of the combined entity as though the 2017 System Transformation Transactions had occurred as of the beginning of 2017. The pro forma combined net sales and income from operations do not necessarily reflect what the combined Company's net sales and income from operations would have been had the acquisitions occurred at the beginning of 2017. The pro forma financial information also may not be useful in predicting the future financial results of the combined company. The actual results may differ significantly from the pro forma amounts reflected herein due to a variety of factors.

The following table represents the Company's unaudited pro forma net sales and unaudited pro forma income from operations for the 2017 System Transformation Transactions.

| (in thousands) | Third Quarter 2017 | | First Three Quarters 2017 | |
|-----------------------------------|--------------------|------------------------|---------------------------|------------------------|
| | Net Sales | Income from Operations | Net Sales | Income from Operations |
| Balance as reported | \$1,162,526 | \$37,472 | \$3,197,519 | \$101,077 |
| Pro forma adjustments (unaudited) | 1,754 | 55 | 231,183 | 4,262 |

| | | | | |
|---|--------------|-----------|--------------|------------|
| Balance including pro forma adjustments (unaudited) | \$ 1,164,280 | \$ 37,527 | \$ 3,428,702 | \$ 105,339 |
|---|--------------|-----------|--------------|------------|

The net sales pro forma and the income from operations pro forma reflect adjustments for (i) the inclusion of historic results of operations for the distribution territories and the regional manufacturing facilities acquired in the System Transformation Transactions for the period prior to the Company's acquisition of the applicable territories or facility, for each period presented and (ii) the elimination of historic results of operations for the October 2017 Divestitures.

4. Inventories

Inventories consisted of the following:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| Finished products | \$ 156,669 | \$ 116,354 |
| Manufacturing materials | 35,703 | 33,073 |
| Plastic shells, plastic pallets and other inventories | 37,520 | 34,191 |
| Total inventories | \$ 229,892 | \$ 183,618 |

5. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consisted of the following:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| Repair parts | \$ 29,535 | \$30,530 |
| Current portion of income taxes | 22,896 | 35,930 |
| Prepaid software | 5,786 | 5,855 |
| Prepayments for sponsorship contracts | 5,644 | 6,358 |
| Commodity hedges at fair market value | 1,047 | 4,420 |
| Other prepaid expenses and other current assets | 26,606 | 17,553 |
| Total prepaid expenses and other current assets | \$ 91,514 | \$ 100,646 |

6. Property, Plant and Equipment, Net

The principal categories and estimated useful lives of property, plant and equipment, net were as follows:

| (in thousands) | September 30, 2018 | December 31, 2017 | Estimated Useful Lives |
|---|-----------------------|----------------------|------------------------|
| Land | \$ 78,478 | \$78,825 | |
| Buildings | 216,821 | 211,308 | 8-50 years |
| Machinery and equipment | 320,447 | 315,117 | 5-20 years |
| Transportation equipment | 373,426 | 351,479 | 4-20 years |
| Furniture and fixtures | 92,000 | 89,559 | 3-10 years |
| Cold drink dispensing equipment | 497,008 | 488,208 | 5-17 years |
| Leasehold and land improvements | 130,257 | 125,348 | 5-20 years |
| Software for internal use | 120,767 | 113,490 | 3-10 years |
| Construction in progress | 13,524 | 25,490 | |
| Total property, plant and equipment, at cost | 1,842,728 | 1,798,824 | |
| Less: Accumulated depreciation and amortization | 844,611 | 767,436 | |
| Property, plant and equipment, net | \$ 998,117 | \$ 1,031,388 | |

Depreciation expense, which includes amortization expense for leased property under capital leases, was \$123.5 million in the first three quarters of 2018 and \$108.7 million in the first three quarters of 2017.

7. Goodwill

A reconciliation of the activity for goodwill for the first three quarters of 2018 and the first three quarters of 2017 is as follows:

| (in thousands) | First Three Quarters | |
|---|----------------------|------------|
| | 2018 | 2017 |
| Beginning balance - goodwill | \$ 169,316 | \$ 144,586 |
| System Transformation Transactions acquisitions | - | 19,035 |
| Measurement period adjustments ⁽¹⁾ | (3,413) | 1,807 |
| Balance held for sale ⁽²⁾ | - | (12,727) |
| Ending balance - goodwill | \$ 165,903 | \$ 152,701 |

⁽¹⁾Measurement period adjustments relate to post-closing adjustments made in accordance with the terms and conditions of the applicable asset purchase agreement or asset exchange agreement for each System Transformation Transaction. See Note 3 to the consolidated condensed financial statements for additional information on the System Transformation Transactions.

⁽²⁾Goodwill of \$12.7 million related to the October 2017 Divestitures was classified as held for sale as of October 1, 2017.

The Company's goodwill resides entirely within the Nonalcoholic Beverages segment. The Company performs its annual impairment test of goodwill as of the first day of the fourth quarter of each fiscal year. During the first three quarters of 2018, the Company did not experience any triggering events or changes in circumstances indicating the carrying amounts of the Company's goodwill exceeded fair values.

8. Distribution Agreements, Net

Distribution agreements, net, which are amortized on a straight line basis and have an estimated useful life of 20 to 40 years, consisted of the following:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|---------------------------------|-----------------------|----------------------|
| Distribution agreements at cost | \$ 945,895 | \$ 939,527 |
| Less: Accumulated amortization | (44,064) | (26,175) |
| Distribution agreements, net | \$ 901,831 | \$ 913,352 |

A reconciliation of the activity for distribution agreements, net for the first three quarters of 2018 and the first three quarters of 2017 is as follows:

| (in thousands) | First Three Quarters | |
|--|----------------------|-----------|
| | 2018 | 2017 |
| Beginning balance - distribution agreements, net | \$913,352 | \$234,988 |
| Conversion to distribution rights from franchise rights ⁽¹⁾ | - | 533,040 |
| System Transformation Transactions acquisitions | - | 36,800 |
| Measurement period adjustment ⁽²⁾ | 4,700 | - |
| Other distribution agreements | 1,668 | 44 |
| Additional accumulated amortization | (17,889) | (11,774) |
| Balance held for sale ⁽³⁾ | - | (63,321) |
| Ending balance - distribution agreements, net | \$901,831 | \$729,777 |

- (1) In connection with the closing of the March 2017 Transactions, the Company, The Coca-Cola Company and CCR entered into a comprehensive beverage agreement (as amended, the “CBA”) on March 31, 2017, and concurrently converted the Company’s franchise rights within the territories in which the Company distributed Coca Cola products prior to beginning the System Transformation to distribution agreements, net on the consolidated condensed financial statements. Prior to this conversion, the Company’s franchise rights resided entirely within the Nonalcoholic Beverages segment.
- (2) Measurement period adjustment relates to post-closing adjustments made in relation to the Memphis Transaction in accordance with the terms and conditions of the September 2017 APA. The adjustment to amortization expense associated with this measurement period adjustment was not material to the consolidated condensed financial statements. See Note 3 to the consolidated condensed financial statements for additional information on the System Transformation Transactions.
- (3) Distribution agreements, net of \$63.3 million related to the October 2017 Divestitures was classified as held for sale as of October 1, 2017.

9.Customer Lists and Other Identifiable Intangible Assets, Net

Customer lists and other identifiable intangible assets, net, which are amortized on a straight line basis and have an estimated useful life of 12 to 20 years, consisted of the following:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| Customer lists and other identifiable intangible assets at cost | \$ 25,288 | \$ 25,288 |
| Less: Accumulated amortization | (8,347) | (6,968) |
| Customer lists and other identifiable intangible assets, net | \$ 16,941 | \$ 18,320 |

A reconciliation of the activity for customer lists and other identifiable intangible assets, net for the first three quarters of 2018 and the first three quarters of 2017 is as follows:

| (in thousands) | First Three Quarters | |
|--|-------------------------|-----------|
| | 2018 | 2017 |
| Beginning balance - customer lists and other identifiable intangible assets, net | \$ 18,320 | \$ 10,427 |
| System Transformation Transactions acquisitions | - | 3,800 |
| Additional accumulated amortization | (1,379) | (965) |
| Ending balance - customer lists and other identifiable intangible assets, net | \$ 16,941 | \$ 13,262 |

10. Other Accrued Liabilities

Other accrued liabilities consisted of the following:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|--|-----------------------|----------------------|
| Accrued insurance costs | \$ 39,299 | \$ 35,433 |
| Employee and retiree benefit plan accruals | 25,950 | 27,024 |
| Accrued marketing costs | 25,875 | 33,376 |
| Current portion of acquisition related contingent consideration | 25,306 | 23,339 |
| Checks and transfers yet to be presented for payment from zero balance cash accounts | 11,900 | 37,262 |
| Accrued taxes (other than income taxes) | 5,811 | 6,391 |
| Current deferred proceeds from Territory Conversion Fee ⁽¹⁾ | 2,286 | 2,286 |
| All other accrued expenses | 17,182 | 20,419 |
| Total other accrued liabilities | \$ 153,609 | \$ 185,530 |

⁽¹⁾Pursuant to a territory conversion agreement entered into by the Company, The Coca Cola Company and CCR in September 2015 (as amended), upon the conversion of the Company's then-existing bottling agreements to the CBA on March 31, 2017, the Company received a one-time fee from CCR, which, after final adjustments made during the second quarter of 2017, totaled \$91.5 million (the "Territory Conversion Fee"). The Territory Conversion Fee was recorded as a deferred liability and will be amortized as a reduction to cost of sales over a period of 40 years. The portion of the deferred liability that is expected to be amortized in the next twelve months was classified as current.

11. Debt

Following is a summary of the Company's debt:

| (in thousands) | Maturity Date | Interest Rate | Interest Paid | Public / Non-public | September 30, 2018 | December 31, 2017 |
|--------------------------------------|------------------|------------------|------------------|------------------------|--------------------------|-------------------------|
| Senior Notes ⁽¹⁾ | 4/15/2019 | 7.00% | Semi-annually | Public | \$ 110,000 | \$ 110,000 |
| Term Loan Facility ⁽¹⁾ | 6/7/2021 | Variable | Varies | Non-public | 292,500 | 300,000 |
| Senior Notes | 2/27/2023 | 3.28% | Semi-annually | Non-public | 125,000 | 125,000 |
| Revolving Credit Facility | 6/8/2023 | Variable | Varies | Non-public | 170,000 | 207,000 |
| Senior Notes | 11/25/2025 | 3.80% | Semi-annually | Public | 350,000 | 350,000 |
| Senior Notes | 3/21/2030 | 3.96% | Quarterly | Non-public | 150,000 | - |
| Unamortized discount on Senior Notes | 4/15/2019 | | | | (143) | (332) |
| Unamortized discount on Senior Notes | 11/25/2025 | | | | (63) | (70) |

| | | |
|-------------------------------|-------------|-------------|
| Debt issuance costs | (3,185) | (3,580) |
| Total debt | 1,194,109 | 1,088,018 |
| Less: Current portion of debt | - | - |
| Long-term debt | \$1,194,109 | \$1,088,018 |

⁽¹⁾Pursuant to the Company's Term Loan Facility (as defined below) and the indenture under which the senior notes due in 2019 were issued, principal payments will be due in the next twelve months. The Company intends to refinance these amounts and has the capacity to do so under its Revolving Credit Facility (as defined below), which is classified as long-term debt. As such, any amounts due in the next twelve months were classified as non-current.

The Company had capital lease obligations of \$37.3 million on September 30, 2018 and \$43.5 million on December 31, 2017. The Company mitigates its financing risk by using multiple financial institutions and only entering into credit arrangements with institutions with investment grade credit ratings. The Company monitors counterparty credit ratings on an ongoing basis.

On June 8, 2018, the Company entered into a second amended and restated credit agreement for a five-year unsecured revolving credit facility (as amended, the "Revolving Credit Facility"), which amended and restated its prior credit agreement dated October 16, 2014. The Revolving Credit Facility has an aggregate maximum borrowing capacity of \$500 million, which may be increased at the Company's option to \$750 million, subject to obtaining commitments from the lenders and satisfying other conditions specified in the credit agreement. Borrowings under the Revolving Credit Facility bear interest at a floating base rate or a floating Eurodollar rate plus an applicable margin, at the Company's option, dependent on the Company's credit ratings at the time of borrowing. At the

Company's current credit ratings, the Company must pay an annual facility fee of 0.15% of the lenders' aggregate commitments under the Revolving Credit Facility. The Revolving Credit Facility has a scheduled maturity date of June 8, 2023.

On March 21, 2018, the Company sold \$150 million aggregate principal amount of senior unsecured notes due 2030 to NYL Investors LLC ("NYL") and certain of its affiliates pursuant to the Note Purchase and Private Shelf Agreement dated March 6, 2018 between the Company, NYL and the other parties thereto (as amended, the "NYL Shelf Facility"). These notes bear interest at 3.96%, payable quarterly in arrears on March 21, June 21, September 21 and December 21 of each year, and will mature on March 21, 2030, unless earlier redeemed by the Company.

In February 2017, the Company sold \$125 million aggregate principal amount of senior unsecured notes due 2023 to PGIM, Inc. ("Prudential") and certain of its affiliates pursuant to the Note Purchase and Private Shelf Agreement dated June 10, 2016 between the Company, Prudential and the other parties thereto (as amended, the "Prudential Shelf Facility"). These notes bear interest at 3.28%, payable semi-annually in arrears on February 27 and August 27 of each year, and will mature on February 27, 2023 unless earlier redeemed by the Company. The Company may request that Prudential consider the purchase of additional senior unsecured notes of the Company under the Prudential Shelf Facility in an aggregate principal amount of up to \$175 million.

In June 2016, the Company entered into a five-year term loan agreement for a senior unsecured term loan facility (as amended, the "Term Loan Facility") in the aggregate principal amount of \$300 million, maturing June 7, 2021. The Company may request additional term loans under the agreement, provided the Company's aggregate borrowings under the Term Loan Facility do not exceed \$500 million. Borrowings under the Term Loan Facility bear interest at a floating base rate or a floating Eurodollar rate plus an applicable margin, at the Company's option, dependent on the Company's credit ratings.

During the third quarter of 2018, the Company amended each of the Revolving Credit Facility, the NYL Shelf Facility, the Prudential Shelf Facility and the Term Loan Facility to (i) align the calculation of the two financial covenants and certain events of default under each agreement and (ii) with regard to the Term Loan Facility, to revise the calculation of the rates at which borrowings bear interest to conform with the calculation of such rates under the Revolving Credit Facility.

The Revolving Credit Facility, the NYL Shelf Facility, the Prudential Shelf Facility and the Term Loan Facility include two financial covenants: a consolidated cash flow/fixed charges ratio and a consolidated funded indebtedness/cash flow ratio, each as defined in the respective agreements. The Company was in compliance with these covenants as of September 30, 2018. These covenants do not currently, and the Company does not anticipate they will, restrict its liquidity or capital resources.

The indentures under which the Company's public debt was issued do not include financial covenants but do limit the incurrence of certain liens and encumbrances as well as indebtedness by the Company's subsidiaries in excess of certain amounts.

All outstanding long-term debt has been issued by the Company and none has been issued by any of its subsidiaries. There are no guarantees of the Company's debt.

12. Derivative Financial Instruments

The Company is subject to the risk of increased costs arising from adverse changes in certain commodity prices. In the normal course of business, the Company manages these risks through a variety of strategies, including the use of derivative instruments. The Company does not use derivative instruments for trading or speculative purposes. All derivative instruments are recorded at fair value as either assets or liabilities in the Company's consolidated condensed balance sheets. These derivative instruments are not designated as hedging instruments under GAAP and are used as "economic hedges" to manage certain commodity price risk. Derivative instruments held are marked to market on a monthly basis and recognized in earnings consistent with the expense classification of the underlying hedged item. Settlements of derivative agreements are included in cash flows from operating activities on the Company's consolidated condensed statements of cash flows.

The Company uses several different financial institutions for commodity derivative instruments to minimize the concentration of credit risk. While the Company would be exposed to credit loss in the event of nonperformance by these counterparties, the Company does not anticipate nonperformance by these parties.

The following table summarizes pre-tax changes in the fair value of the Company's commodity derivative financial instruments and the classification of such changes in the consolidated condensed statements of operations.

| (in thousands) | Classification of Gain (Loss) | Third Quarter | | First Three Quarters | |
|-------------------|---|---------------|---------|----------------------|---------|
| | | 2018 | 2017 | 2018 | 2017 |
| Commodity hedges | Cost of sales | \$(260) | \$2,042 | \$(2,776) | \$2,066 |
| Commodity hedges | Selling, delivery and administrative expenses | (209) | 1,359 | (363) | 475 |
| Total gain (loss) | | \$(469) | \$3,401 | \$(3,139) | \$2,541 |

The following table summarizes the fair values and classification in the consolidated condensed balance sheets of derivative instruments held by the Company:

| (in thousands) | Balance Sheet Classification | September 30, 2018 | December 31, 2017 |
|---------------------------------------|---|--------------------|-------------------|
| Assets: | | | |
| Commodity hedges at fair market value | Prepaid expenses and other current assets | \$ 1,047 | \$ 4,420 |
| Commodity hedges at fair market value | Other assets | 234 | - |
| Total assets | | \$ 1,281 | \$ 4,420 |

The Company has master agreements with the counterparties to its derivative financial agreements that provide for net settlement of derivative transactions. Accordingly, the net amounts of derivative assets are recognized in either prepaid expenses and other current assets or other assets in the Company's consolidated condensed balance sheets and the net amounts of derivative liabilities are recognized in other accrued liabilities or other liabilities in the consolidated condensed balance sheets. The following table summarizes the Company's gross derivative assets and gross derivative liabilities in the consolidated condensed balance sheets:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|------------------------------|--------------------|-------------------|
| Gross derivative assets | \$ 15,633 | \$ 4,481 |
| Gross derivative liabilities | 14,352 | 61 |

The following table summarizes the Company's outstanding commodity derivative agreements:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|---|--------------------|-------------------|
| Notional amount of outstanding commodity derivative agreements | \$ 143,282 | \$ 59,564 |
| Latest maturity date of outstanding commodity derivative agreements | | |

| December 2019 | December 2018 |
|------------------|------------------|
|------------------|------------------|

13.Fair Values of Financial Instruments

GAAP requires assets and liabilities carried at fair value to be classified and disclosed in one of the following categories:

- Level 1: Quoted market prices in active markets for identical assets or liabilities.
- Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.
- Level 3: Unobservable inputs that are not corroborated by market data.

The following methods and assumptions were used by the Company in estimating the fair values of its financial instruments. There were no transfers of assets or liabilities between levels in any period presented.

| Financial Instrument | Fair Value Level | Method and Assumptions |
|---|------------------|--|
| Deferred compensation plan assets and liabilities | Level 1 | The fair value of the Company's non-qualified deferred compensation plan for certain executives and other highly compensated employees is based on the fair values of associated assets and liabilities, which are held in mutual funds and are based on the quoted market value of the securities held within the mutual funds. |
| Commodity hedging agreements | Level 2 | The fair values of the Company's commodity hedging agreements are based on current settlement values at each balance sheet date. The fair values of the commodity hedging agreements at each balance sheet date represent the estimated amounts the Company would have received or paid upon termination of these agreements. The Company's credit risk related to the derivative financial instruments is managed by requiring high standards for its counterparties and periodic settlements. The Company considers nonperformance risk in determining the fair value of derivative financial instruments. |
| Non-public variable rate debt | Level 2 | The carrying amounts of the Company's non-public variable rate debt approximate their fair values due to variable interest rates with short reset periods. |
| Non-public fixed rate debt | Level 2 | The fair values of the Company's non-public fixed rate debt are based on estimated current market prices. |
| Public debt securities | Level 2 | The fair values of the Company's public debt securities are based on estimated current market prices. |
| Acquisition related contingent consideration | Level 3 | The fair values of acquisition related contingent consideration are based on internal forecasts and the weighted average cost of capital ("WACC") derived from market data. |

The following tables summarize, by assets and liabilities, the carrying amounts and fair values by level of the Company's deferred compensation plan, commodity hedging agreements, debt and acquisition related contingent consideration:

| (in thousands) | September 30, 2018 | | | | |
|--|--------------------|------------------|--------------------|--------------------|--------------------|
| | Carrying Amount | Total Fair Value | Fair Value Level 1 | Fair Value Level 2 | Fair Value Level 3 |
| | | | | | |
| Assets: | | | | | |
| Deferred compensation plan assets | \$36,291 | \$36,291 | \$36,291 | \$- | \$- |
| Commodity hedging agreements | 1,281 | 1,281 | - | 1,281 | - |
| Liabilities: | | | | | |
| Deferred compensation plan liabilities | 36,291 | 36,291 | 36,291 | - | - |
| Non-public variable rate debt | 462,031 | 462,500 | - | 462,500 | - |
| Non-public fixed rate debt | 274,697 | 256,200 | - | 256,200 | - |

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

| | | | | | |
|--|---------|---------|---|---------|---------|
| Public debt securities | 457,381 | 457,800 | - | 457,800 | - |
| Acquisition related contingent consideration | 363,836 | 363,836 | - | - | 363,836 |

| (in thousands) | December 31, 2017 | | | | |
|--|-------------------|------------|---------------|---------------|---------------|
| | Carrying | Total | Fair | Fair | Fair |
| | Amount | Fair Value | Value Level 1 | Value Level 2 | Value Level 3 |
| Assets: | | | | | |
| Deferred compensation plan assets | \$33,166 | \$33,166 | \$33,166 | \$- | \$- |
| Commodity hedging agreements | 4,420 | 4,420 | - | 4,420 | - |
| Liabilities: | | | | | |
| Deferred compensation plan liabilities | 33,166 | 33,166 | 33,166 | - | - |
| Non-public variable rate debt | 506,398 | 507,000 | - | 507,000 | - |
| Non-public fixed rate debt | 124,829 | 126,400 | - | 126,400 | - |
| Public debt securities | 456,791 | 475,100 | - | 475,100 | - |
| Acquisition related contingent consideration | 381,291 | 381,291 | - | - | 381,291 |

Under the CBA, the Company is required to make quarterly sub-bottling payments to CCR on a continuing basis for the grant of exclusive rights to distribute, promote, market and sell specified covered beverages and beverage products in the distribution territories acquired in the System Transformation, excluding territories the Company acquired in an exchange transaction. This

acquisition related contingent consideration is valued using a probability weighted discounted cash flow model based on internal forecasts and the WACC derived from market data, which are considered Level 3 inputs. Each reporting period, the Company adjusts its acquisition related contingent consideration liability related to the distribution territories to fair value by discounting future expected sub-bottling payments required under the CBA using the Company's estimated WACC.

These future expected sub-bottling payments extend through the life of the related distribution assets acquired in each distribution territory, which is generally 40 years. As a result, the fair value of the acquisition related contingent consideration liability is impacted by the Company's WACC, management's estimate of the amounts that will be paid in the future under the CBA, and current sub-bottling payments (all Level 3 inputs). Changes in any of these Level 3 inputs, particularly the underlying risk-free interest rate used to estimate the Company's WACC, could result in material changes to the fair value of the acquisition related contingent consideration and could materially impact the amount of noncash expense (or income) recorded each reporting period.

The acquisition related contingent consideration is the Company's only Level 3 asset or liability. A reconciliation of the Level 3 activity is as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|---|---------------|-----------|----------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Beginning balance - Level 3 liability | \$374,537 | \$319,102 | \$381,291 | \$253,437 |
| Increase due to System Transformation Transactions acquisitions | - | - | - | 46,086 |
| Measurement period adjustments ⁽¹⁾ | (1,279) | - | 813 | - |
| Payment of acquisition related contingent consideration | (7,049) | (5,094) | (18,312) | (11,650) |
| Reclassification to current payables | - | 150 | (1,540) | (2,080) |
| (Favorable)/unfavorable fair value adjustment | (2,373) | (5,225) | 1,584 | 23,140 |
| Ending balance - Level 3 liability | \$363,836 | \$308,933 | \$363,836 | \$308,933 |

⁽¹⁾Measurement period adjustments relate to post-closing adjustments made in relation to the April 2017 Transactions and the October 2017 Transactions in accordance with the terms and conditions of the applicable asset purchase agreement or asset exchange agreement. See Note 3 to the consolidated condensed financial statements for additional information on the System Transformation Transactions.

The fair value adjustments to the acquisition related contingent consideration liability during the first three quarters of 2018 were primarily driven by changes to the risk-free interest rate and the projected future operating results of the distribution territories acquired as part of the System Transformation subject to sub-bottling fees, partially offset by cash payments. The fair value adjustments to the acquisition related contingent consideration liability during the first three quarters of 2017 were primarily driven by a change in the risk-free interest rate. These adjustments were recorded in other income (expense), net in the consolidated condensed statements of operations.

The anticipated amount the Company could pay annually under the acquisition related contingent consideration arrangements for the System Transformation Transactions is expected to be in the range of \$25 million to \$47 million.

14. Other Liabilities

Other liabilities consisted of the following:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|--|-----------------------|----------------------|
| Non-current portion of acquisition related contingent consideration | \$ 338,530 | \$357,952 |
| Accruals for executive benefit plans | 128,079 | 125,791 |
| Non-current deferred proceeds from Territory Conversion Fee | 85,734 | 87,449 |
| Non-current deferred proceeds from Legacy Facilities Credit ⁽¹⁾ | 30,568 | 29,881 |
| Other | 17,399 | 19,506 |
| Total other liabilities | \$ 600,310 | \$620,579 |

⁽¹⁾In December 2017, The Coca Cola Company agreed to provide the Company a one-time fee, which, after final adjustments made during the third quarter of 2018, totaled \$44.3 million (the “Legacy Facilities Credit”). The Legacy Facilities Credit compensated the Company for the net economic impact of changes made by The Coca Cola Company to the authorized pricing on sales of covered beverages produced at the manufacturing facilities owned by Company prior to the System Transformation and sold to The Coca Cola Company and certain U.S. Coca Cola bottlers pursuant to new pricing mechanisms included in the regional

manufacturing agreement entered into by the Company and The Coca Cola Company on March 31, 2017, as amended. The Company immediately recognized the portion of the Legacy Facilities Credit applicable to a regional manufacturing facility in Mobile, Alabama which the Company transferred to CCR as part of the CCR Exchange Transaction. The remaining balance of the Legacy Facilities Credit will be amortized as a reduction to cost of sales over a period of 40 years.

15. Commitments and Contingencies

Manufacturing Cooperatives

The Company is a shareholder of South Atlantic Canners, Inc. (“SAC”), a manufacturing cooperative in Bishopville, South Carolina. All of SAC’s shareholders are Coca Cola bottlers and each has equal voting rights. The Company accounts for SAC as an equity method investment. The Company receives a fee for managing the day-to-day operations of SAC pursuant to a management agreement. Proceeds from management fees received from SAC were \$6.8 million in the first three quarters of 2018 and \$6.9 million in the first three quarters of 2017.

The Company is obligated to purchase 17.5 million cases of finished product from SAC on an annual basis through June 2024. The Company purchased 22.2 million cases and 22.6 million cases of finished product from SAC in the first three quarters of 2018 and the first three quarters of 2017, respectively.

The Company is also a shareholder of Southeastern Container (“Southeastern”), a plastic bottle manufacturing cooperative from which the Company is obligated to purchase at least 80% of its requirements of plastic bottles for certain designated territories. The Company accounts for Southeastern as an equity method investment.

The following table summarizes the Company’s purchases from these manufacturing cooperatives:

| (in thousands) | Third Quarter | | First Three Quarters | |
|---|---------------|----------|----------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Purchases from SAC | \$38,569 | \$37,267 | \$117,729 | \$111,408 |
| Purchases from Southeastern | 32,379 | 29,344 | 92,613 | 80,301 |
| Total purchases from manufacturing cooperatives | \$70,948 | \$66,611 | \$210,342 | \$191,709 |

The Company guarantees a portion of SAC’s debt, which expires at various dates through 2021. The amounts guaranteed were \$23.9 million as of both September 30, 2018 and December 31, 2017. The Company does not anticipate SAC will fail to fulfill its commitment related to the debt. The Company further believes SAC has sufficient

assets, including production equipment, facilities and working capital, and the ability to adjust selling prices of its products to adequately mitigate the risk of material loss from the Company's guarantee.

In the event SAC fails to fulfill its commitments under the related debt, the Company would be responsible for payments to the lenders up to the level of the guarantee. The following table summarizes the Company's maximum exposure under this guarantee if SAC had borrowed up to its aggregate borrowing capacity:

| (in thousands) | September 30, 2018 |
|--|-----------------------|
| Maximum guaranteed debt | \$ 23,938 |
| Equity investments ⁽¹⁾ | 8,175 |
| Maximum total exposure, including equity investments | \$ 32,113 |

⁽¹⁾Recorded in other assets on the Company's consolidated condensed balance sheets.

The Company holds no assets as collateral against the SAC guarantee, the fair value of which is immaterial to the Company's consolidated condensed financial statements. The Company monitors its investments in SAC and would be required to write down its investment if an impairment was identified and the Company determined it to be other than temporary. No impairment of the Company's investments in SAC was identified as of September 30, 2018, and there was no impairment identified in 2017.

Other Commitments and Contingencies

The Company has standby letters of credit, primarily related to its property and casualty insurance programs. These letters of credit totaled \$35.6 million as of both September 30, 2018 and December 31, 2017.

The Company participates in long-term marketing contractual arrangements with certain prestige properties, athletic venues and other locations. As of September 30, 2018, the future payments related to these contractual arrangements, which expire at various dates through 2033, amounted to \$160.0 million.

The Company is involved in various claims and legal proceedings which have arisen in the ordinary course of its business. Although it is difficult to predict the ultimate outcome of these claims and legal proceedings, management believes that the ultimate disposition of these matters will not have a material adverse effect on the financial condition, cash flows or results of operations of the Company. No material amount of loss in excess of recorded amounts is believed to be reasonably possible as a result of these claims and legal proceedings.

The Company is subject to audits by tax authorities in jurisdictions where it conducts business. These audits may result in assessments that are subsequently resolved with the authorities or potentially through the courts. Management believes the Company has adequately provided for any assessments likely to result from these audits; however, final assessments, if any, could be different than the amounts recorded in the consolidated condensed financial statements.

16. Income Taxes

The Company's effective income tax rate, as calculated by dividing income tax expense by income before income taxes, was 24.1% for the first three quarters of 2018 and 34.8% for the first three quarters of 2017. The decrease in the effective tax rate was primarily driven by the corporate rate reduction due to the Tax Act and its impact on prior estimates and lower income before income taxes, which was offset by an increase in certain non-deductible expenses.

The Company's effective income tax rate, as calculated by dividing income tax expense by income before income taxes minus net income attributable to noncontrolling interest, was 32.5% for the first three quarters of 2018 and 38.8% for the first three quarters of 2017.

Shortly after the Tax Act was enacted, the SEC issued guidance under Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act ("SAB 118") to address the application of GAAP and direct taxpayers to consider the impact of the Tax Act as "provisional" when a registrant does not have the necessary information available, prepared or analyzed (including computations) in reasonable detail to complete the accounting for the change in tax law. In accordance with SAB 118, the Company recognized a provisional tax benefit related to the re-measurement of its net deferred tax liability of \$69.0 million as of December 31, 2017. During the third quarter of 2018, the Company recorded an additional provisional tax benefit of \$1.9 million attributable to the re-measurement of its net deferred tax liability in connection with the filing of its 2017 federal income tax return.

The ultimate impact may differ from the provisional amounts, possibly materially, due to, among other things, the significant complexity of the Tax Act, anticipated additional regulatory guidance or related interpretations that may be issued by the Internal Revenue Service (the "IRS"), changes in accounting standards, legislative actions, future actions by states within the U.S. and changes in estimates, analysis, interpretations and assumptions made by the Company.

The Company had uncertain tax positions, including accrued interest, of \$3.0 million on September 30, 2018 and \$2.4 million on December 31, 2017, all of which would affect the Company's effective tax rate if recognized. While it is expected the amount of uncertain tax positions may change in the next 12 months, the Company does not expect such change would have a significant impact on the consolidated condensed financial statements.

Prior tax years beginning in year 2002 remain open to examination by the IRS, and various tax years beginning in year 1998 remain open to examination by certain state tax jurisdictions.

17. Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) ("AOCI(L)") is comprised of adjustments relative to the Company's pension and postretirement medical benefit plans and foreign currency translation adjustments required for a subsidiary of the Company that performs data analysis and provides consulting services outside the United States.

A summary of AOCI(L) for the third quarter of 2018 and the third quarter of 2017 is as follows:

| (in thousands) | July 1, 2018 | Pre-tax Activity | Tax Effect | September 30, 2018 |
|---|-----------------|---------------------|---------------|-----------------------|
| Net pension activity: | | | | |
| Actuarial loss | \$(77,212) | \$ 934 | \$(231) | \$(76,509) |
| Prior service costs | (34) | 6 | (2) | (30) |
| Net postretirement benefits activity: | | | | |
| Actuarial loss | (22,767) | 499 | (123) | (22,391) |
| Prior service costs | 1,048 | (462) | 114 | 700 |
| Recognized loss due to October 2017 Divestitures ⁽¹⁾ | 6,220 | - | - | 6,220 |
| Foreign currency translation adjustment | 8 | (2) | 1 | 7 |
| Total | \$(92,737) | \$ 975 | \$(241) | \$(92,003) |

⁽¹⁾Recognized loss due to the divestiture of the Deep South and Somerset Exchange Business and the Florence and Laurel Distribution Business during the fourth quarter of 2017.

| (in thousands) | July 2, 2017 | Pre-tax Activity | Tax Effect | October 1, 2017 |
|---|-----------------|---------------------|---------------|--------------------|
| Net pension activity: | | | | |
| Actuarial loss | \$(71,402) | \$ 807 | \$(311) | \$(70,906) |
| Prior service costs | (52) | 7 | (3) | (48) |
| Net postretirement benefits activity: | | | | |
| Actuarial loss | (23,315) | 648 | (250) | (22,917) |
| Prior service costs | 2,763 | (745) | 287 | 2,305 |
| Foreign currency translation adjustment | 5 | 11 | (4) | 12 |
| Total | \$(92,001) | \$ 728 | \$(281) | \$(91,554) |

A summary of AOCI(L) for the first three quarters of 2018 and the first three quarters of 2017 is as follows:

| (in thousands) | December 31, 2017 | Pre-tax Activity | Tax Effect | September 30, 2018 |
|---|----------------------|---------------------|---------------|-----------------------|
| Net pension activity: | | | | |
| Actuarial loss | \$(78,618) | \$ 2,800 | \$(691) | \$(76,509) |
| Prior service costs | (43) | 18 | (5) | (30) |
| Net postretirement benefits activity: | | | | |
| Actuarial loss | (23,519) | 1,497 | (369) | (22,391) |
| Prior service costs | 1,744 | (1,386) | 342 | 700 |
| Recognized loss due to October 2017 Divestitures ⁽¹⁾ | 6,220 | - | - | 6,220 |
| Foreign currency translation adjustment | 14 | (10) | 3 | 7 |
| Total | \$(94,202) | \$ 2,919 | \$(720) | \$(92,003) |

⁽¹⁾Recognized loss due to the divestiture of the Deep South and Somerset Exchange Business and the Florence and Laurel Distribution Business during the fourth quarter of 2017.

| (in thousands) | January 1, 2017 | Pre-tax Activity | Tax Effect | October 1, 2017 |
|---|--------------------|---------------------|---------------|--------------------|
| Net pension activity: | | | | |
| Actuarial loss | \$(72,393) | \$2,421 | \$ (934) | \$(70,906) |
| Prior service costs | (61) | 21 | (8) | (48) |
| Net postretirement benefits activity: | | | | |
| Actuarial loss | (24,111) | 1,944 | (750) | (22,917) |
| Prior service costs | 3,679 | (2,237) | 863 | 2,305 |
| Foreign currency translation adjustment | (11) | 37 | (14) | 12 |
| Total | \$(92,897) | \$2,186 | \$ (843) | \$(91,554) |

A summary of the impact of AOCI(L) on certain statements of operations line items is as follows:

| (in thousands) | Third Quarter 2018 | | | Foreign Currency Translation Adjustment | Total |
|---|--------------------|--------------------|----------|--|-------|
| | Net | | | | |
| | Pension | Net Postretirement | Activity | | |
| Cost of sales | \$217 | \$ 6 | | \$ - | \$223 |
| Selling, delivery and administrative expenses | 723 | 31 | | (2) | 752 |
| Subtotal pre-tax | 940 | 37 | | (2) | 975 |
| Income tax expense | 233 | 9 | | (1) | 241 |
| Total after tax effect | \$707 | \$ 28 | | \$ (1) | \$734 |

| (in thousands) | Third Quarter 2017 | | | Foreign Currency Translation Adjustment | Total |
|---|--------------------|--------------------|----------|--|-------|
| | Net | | | | |
| | Pension | Net Postretirement | Activity | | |
| Cost of sales | \$171 | \$ (21) | | \$ - | \$150 |
| Selling, delivery and administrative expenses | 643 | (76) | | 11 | 578 |
| Subtotal pre-tax | 814 | (97) | | 11 | 728 |
| Income tax expense | 314 | (37) | | 4 | 281 |
| Total after tax effect | \$500 | \$ (60) | | \$ 7 | \$447 |

| (in thousands) | First Three Quarters 2018 | | | Foreign Currency Translation Adjustment | Total |
|---|---------------------------|--------------------|----------|--|---------|
| | Net | | | | |
| | Pension | Net Postretirement | Activity | | |
| Cost of sales | \$648 | \$ 19 | | \$ - | \$667 |
| Selling, delivery and administrative expenses | 2,170 | 92 | | (10) | 2,252 |
| Subtotal pre-tax | 2,818 | 111 | | (10) | 2,919 |
| Income tax expense | 696 | 27 | | (3) | 720 |
| Total after tax effect | \$2,122 | \$ 84 | | \$ (7) | \$2,199 |

| (in thousands) | First Three Quarters 2017 | | | Foreign Currency Translation Adjustment | Total |
|---|---------------------------|--------------------|----------|--|---------|
| | Net | | | | |
| | Pension | Net Postretirement | Activity | | |
| Cost of sales | \$648 | \$ 19 | | \$ - | \$667 |
| Selling, delivery and administrative expenses | 2,170 | 92 | | (10) | 2,252 |
| Subtotal pre-tax | 2,818 | 111 | | (10) | 2,919 |
| Income tax expense | 696 | 27 | | (3) | 720 |
| Total after tax effect | \$2,122 | \$ 84 | | \$ (7) | \$2,199 |

| | | | | |
|---|---------|---------|---------|---------|
| Cost of sales | \$497 | \$ (64 |) \$ - | \$433 |
| Selling, delivery and administrative expenses | 1,945 | (230 |) 37 | 1,752 |
| Subtotal pre-tax | 2,442 | (294 |) 37 | 2,185 |
| Income tax expense | 942 | (114 |) 14 | 842 |
| Total after tax effect | \$1,500 | \$ (180 |) \$ 23 | \$1,343 |

18. Capital Transactions

During the first quarter of each year, the Compensation Committee of the Company's Board of Directors (the "Committee") determines whether any shares of the Company's Class B Common Stock should be issued to J. Frank Harrison, III, in connection with his services for the prior year as Chairman of the Board of Directors and Chief Executive Officer of the Company, pursuant to a performance unit award agreement approved in 2008 (the "Performance Unit Award Agreement"). The Performance Unit Award Agreement expires at the end of 2018, with the final potential award to be issued in the first quarter of 2019 in connection with Mr. Harrison's services during 2018.

As permitted under the terms of the Performance Unit Award Agreement, a number of shares were settled in cash in 2018 and 2017 to satisfy tax withholding obligations in connection with the vesting of the performance units. The remaining number of shares increased the total shares of Class B Common Stock outstanding. A summary of the awards issued in 2018 and 2017 is as follows:

| | Fiscal Year | |
|---|-------------|---------|
| | 2018 | 2017 |
| | March | March |
| Date of approval for award | 6, 2018 | 7, 2017 |
| Fiscal year of service covered by award | 2017 | 2016 |
| Shares settled in cash to satisfy tax withholding obligations | 16,504 | 18,980 |
| Increase in Class B Common Stock shares outstanding | 20,296 | 21,020 |
| Total Class B Common Stock awarded | 36,800 | 40,000 |

Compensation expense for the awards issued pursuant to the Performance Unit Award Agreement, recognized on the closing share price of the last trading day prior to the end of the fiscal period, was as follows:

| (in thousands, except share price) | First Three Quarters | |
|---|----------------------|-----------|
| | 2018 | 2017 |
| Total compensation expense | \$4,494 | \$ 6,473 |
| Share price for compensation expense | \$ 182.28 | \$ 215.75 |
| | September | |
| | 28, | September |
| Share price date for compensation expense | 2018 | 29, 2017 |

During the second quarter of 2018, the Committee and the Company's stockholders approved a long-term performance equity plan (the "Long-Term Performance Equity Plan"), which will compensate J. Frank Harrison, III based on the Company's performance and will succeed the Performance Unit Award Agreement upon its expiration. Awards granted under the Long-Term Performance Equity Plan will be earned based on the Company's attainment during a performance period of certain performance measures, each as specified by the Committee. These awards may be settled in cash and/or shares of Class B Common Stock, based on the average of the closing prices of shares of Common Stock during the last twenty trading days of the performance period. Compensation expense for the Long-Term Performance Equity Plan, which is included in S,D&A expenses on the consolidated condensed statements of operations, was \$1.5 million for the first three quarters of 2018.

19. Pension and Postretirement Benefit Obligations

Pension Plans

There are two Company-sponsored pension plans. The primary Company-sponsored pension plan was frozen as of June 30, 2006 and no benefits accrued to participants after this date. The second Company-sponsored pension plan (the “Bargaining Plan”) is for certain employees under collective bargaining agreements. Benefits under the Bargaining Plan are determined in accordance with negotiated formulas for the respective participants. Contributions to the plans are based on actuarially determined amounts and are limited to the amounts currently deductible for income tax purposes.

The components of net periodic pension cost were as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|------------------------------------|---------------|---------|----------------------|----------|
| | 2018 | 2017 | 2018 | 2017 |
| Service cost | \$1,412 | \$150 | \$4,237 | \$450 |
| Interest cost | 2,856 | 2,978 | 8,568 | 8,936 |
| Expected return on plan assets | (3,853) | (3,399) | (11,557) | (10,197) |
| Recognized net actuarial loss | 934 | 807 | 2,800 | 2,421 |
| Amortization of prior service cost | 6 | 7 | 18 | 21 |
| Net periodic pension cost | \$1,355 | \$543 | \$4,066 | \$1,631 |

The Company contributed \$20.0 million to the two Company sponsored pension plans during the third quarter of 2018 and does not anticipate making additional contributions during the fourth quarter of 2018.

Postretirement Benefits

The Company provides postretirement benefits for a portion of its current employees. The Company recognizes the cost of postretirement benefits, which consist principally of medical benefits, during covered employees' periods of active service. The Company does not pre-fund these benefits and has the right to modify or terminate certain of these benefits in the future.

The components of net periodic postretirement benefit cost were as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--|---------------|---------|----------------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| Service cost | \$502 | \$572 | \$1,507 | \$1,716 |
| Interest cost | 696 | 910 | 2,088 | 2,732 |
| Recognized net actuarial loss | 499 | 648 | 1,497 | 1,944 |
| Amortization of prior service cost | (462) | (745) | (1,386) | (2,237) |
| Net periodic postretirement benefit cost | \$1,235 | \$1,385 | \$3,706 | \$4,155 |

Multi-Employer Benefits

Certain employees of the Company whose employment is covered under collective bargaining agreements participate in a multi-employer pension plan, the Employers-Teamsters Local Union Nos. 175 and 505 Pension Fund (the "Teamsters Plan"). The Company makes monthly contributions to the Teamsters Plan on behalf of such employees. The collective bargaining agreements covering the Teamsters Plan expire at various times by April 2020. The Company expects these agreements will be re-negotiated.

The risks of participating in the Teamsters Plan are different from single-employer plans as contributed assets are pooled and may be used to provide benefits to employees of other participating employers. If a participating employer stops contributing to the Teamsters Plan, the unfunded obligations of the Teamsters Plan may be borne by the remaining participating employers. If the Company chooses to stop participating in the Teamsters Plan, the Company could be required to pay the Teamsters Plan a withdrawal liability based on the underfunded status of the Teamsters Plan. The Company does not anticipate withdrawing from the Teamsters Plan.

In 2015, the Company increased its contribution rates to the Teamsters Plan, with additional increases occurring annually, as part of a rehabilitation plan, which was incorporated into the renewal of collective bargaining agreements with the unions effective April 28, 2014 and adopted by the Company as a rehabilitation plan effective January 1,

2015. This was a result of the Teamsters Plan being certified by its actuary as being in “critical” status for the plan year beginning January 1, 2013.

20. Related Party Transactions

The Coca Cola Company

The Company’s business consists primarily of the production, marketing and distribution of nonalcoholic beverages of The Coca Cola Company, which is the sole owner of the formulas under which the primary components of its soft drink products, either concentrate or syrup, are manufactured.

As of September 30, 2018, The Coca Cola Company owned approximately 27% of the Company’s total outstanding Common Stock and Class B Common Stock on a consolidated basis, representing approximately 5% of the total voting power of the Company’s Common Stock and Class B Common Stock voting together. As long as The Coca Cola Company holds the number of shares of Common Stock it currently owns, it has the right to have a designee proposed by the Company for nomination to the Company’s Board of Directors, and J. Frank Harrison, III, the Chairman of the Board and Chief Executive Officer of the Company, and trustees of certain trusts established for the benefit of certain relatives of J. Frank Harrison, Jr. have agreed to vote the shares of the Company’s Class B Common Stock which they control, representing approximately 86% of the total voting power of the Company’s combined Common Stock and Class B Common Stock, in favor of such designee. The Coca Cola Company does not own any shares of the Company’s Class B Common Stock.

The following table and the subsequent descriptions summarize the significant transactions between the Company and The Coca-Cola Company:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--|---------------|-----------|----------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Payments made by the Company to The Coca-Cola Company for: | | | | |
| Concentrate, syrup, sweetener and other purchases | \$341,949 | \$317,040 | \$904,244 | \$806,256 |
| Customer marketing programs | 34,005 | 27,855 | 110,062 | 102,095 |
| Cold drink equipment parts | 7,958 | 6,881 | 22,188 | 18,968 |
| Glacéau distribution agreement consideration | - | - | - | 15,598 |
| Payments made by The Coca-Cola Company to the Company for: | | | | |
| Proceeds from Territory Conversion Fee | \$- | \$- | \$- | \$87,066 |
| Marketing funding support payments | 22,632 | 22,074 | 65,325 | 62,235 |
| Fountain delivery and equipment repair fees | 10,199 | 9,286 | 29,899 | 26,138 |
| Facilitating the distribution of certain brands and packages to other Coca-Cola bottlers | 1,937 | 1,773 | 7,663 | 6,881 |
| Presence marketing funding support on the Company's behalf | 1,108 | 2,707 | 6,203 | 3,844 |
| Cold drink equipment | - | - | 3,789 | 8,400 |

Coca-Cola Refreshments USA, Inc.

The Company previously had a production arrangement with CCR to buy and sell finished products at cost and transported products for CCR to the Company's and other Coca-Cola bottlers' locations. Following the completion of the October 2017 Transactions discussed in Note 3, the Company no longer transacts with CCR other than making quarterly sub-bottling payments, as discussed below. The following table summarizes purchases and sales under these arrangements between the Company and CCR prior to the closing of the October 2017 Transactions:

| (in thousands) | 2017 | |
|--------------------|---------------|----------------------|
| | Third Quarter | First Three Quarters |
| Purchases from CCR | \$20,157 | \$110,451 |
| Gross sales to CCR | 11,873 | 72,930 |

Pursuant to the CBA, the Company is required to make quarterly sub-bottling payments to CCR on a continuing basis for the grant of exclusive rights to distribute, promote, market and sell the authorized brands of The Coca-Cola Company and related products in the territories acquired in the System Transformation, excluding territories the Company acquired in an exchange transaction. These sub-bottling payments are based on gross profit derived from sales of certain beverages and beverage products that are sold under the same trademarks that identify a covered beverage, beverage product or certain cross-licensed brands. Sub-bottling payments to CCR were

\$18.3 million during the first three quarters of 2018 and \$11.7 million during the first three quarters of 2017. The following table summarizes the liability recorded by the Company to reflect the estimated fair value of contingent consideration related to future sub-bottling payments to CCR:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| Current portion of acquisition related contingent consideration | \$ 25,306 | \$23,339 |
| Non-current portion of acquisition related contingent consideration | 338,530 | 357,952 |
| Total acquisition related contingent consideration | \$ 363,836 | \$381,291 |

Glacéau Distribution Termination Agreement

On January 1, 2017, the Company obtained the rights to market, promote, distribute and sell glacéau vitaminwater, glacéau smartwater and glacéau vitaminwater zero drops in certain geographic territories including the District of Columbia and portions of Delaware, Maryland and Virginia, pursuant to an agreement entered into by the Company, The Coca-Cola Company and CCR in June 2016. Pursuant to the agreement, the Company made a payment of \$15.6 million to The Coca-Cola Company during the first quarter of 2017, which represented a portion of the total payment made by The Coca-Cola Company to terminate a distribution arrangement with a prior distributor in this territory.

Coca Cola Bottlers' Sales and Services Company, LLC ("CCBSS")

Along with all other Coca Cola bottlers in the United States, the Company is a member of CCBSS, a company formed in 2003 for the purpose of facilitating various procurement functions and distributing certain specified beverage products of The Coca Cola Company with the intention of enhancing the efficiency and competitiveness of the Coca Cola bottling system in the United States.

CCBSS negotiates the procurement for the majority of the Company's raw materials, excluding concentrate, and the Company receives a rebate from CCBSS for the purchase of these raw materials. The Company had rebates due from CCBSS of \$13.9 million on September 30, 2018 and \$11.2 million on December 31, 2017, which were classified as accounts receivable, other in the consolidated condensed balance sheets.

In addition, the Company pays an administrative fee to CCBSS for its services. The Company incurred administrative fees to CCBSS of \$2.2 million in the first three quarters of 2018 and \$2.0 million in the first three quarters of 2017, which were classified as S,D&A expenses in the consolidated condensed statements of operations.

National Product Supply Group ("NPSG")

The Company is a member of the NPSG, an organization comprised of The Coca Cola Company and other Coca Cola bottlers who are regional producing bottlers ("RPBs") in The Coca Cola Company's national product supply system, pursuant to a national product supply governance agreement executed in October 2015 with The Coca Cola Company and other RPBs (the "NPSG Governance Agreement"). The stated objectives of the NPSG include, among others, (i) Coca Cola system strategic infrastructure investment and divestment planning (ii) network optimization of all plant to distribution center sourcing and (iii) new product/packaging infrastructure planning.

Under the NPSG Governance Agreement, the NPSG members established certain governance mechanisms, including a governing board (the "NPSG Board") comprised of a representative of (i) the Company, (ii) The Coca Cola Company and (iii) each other RPB. As of September 30, 2018, the NPSG Board consisted of The Coca Cola Company, the Company and seven other RPBs. The NPSG Board makes and/or oversees and directs certain key decisions regarding the NPSG, including decisions regarding the management and staffing of the NPSG and the funding for its ongoing operations.

Pursuant to the decisions of the NPSG Board made from time to time and subject to the terms and conditions of the NPSG Governance Agreement, each RPB is required to make investments in its respective manufacturing assets and implement Coca Cola system strategic investment opportunities consistent with the NPSG Governance Agreement.

The Company is also obligated to pay a certain portion of the costs of operating the NPSG. The Company incurred NPSG operating costs of \$0.9 million in the first three quarters of 2018 and \$0.8 million in the first three quarters of 2017, which were classified as S,D&A expense in the consolidated condensed statements of operations.

CONA Services LLC (“CONA”)

The Company is a member of CONA, an entity formed with The Coca Cola Company and certain other Coca Cola bottlers pursuant to a limited liability company agreement executed in January 2016 (as amended, the “CONA LLC Agreement”) to provide business process and information technology services to its members.

Under the CONA LLC Agreement, the business and affairs of CONA are managed by a board of directors comprised of representatives of its members (the “CONA Board”). All directors are entitled to one vote, regardless of the percentage interest in CONA held by each member. The Company currently has the right to designate one of the members of the CONA Board and has a percentage interest in CONA of approximately 20%. Most matters to be decided by the CONA Board require approval by a majority of a quorum of the directors, provided that the approval of 80% of the directors is required to, among other things, require members to make additional capital contributions, approve CONA’s annual operating and capital budgets, and approve capital expenditures in excess of certain agreed upon amounts. Each CONA member is required to make capital contributions to CONA if and when approved by the CONA Board.

The Company made capital contributions to CONA of \$2.1 million in the first three quarters of 2018 and \$2.0 million in the first three quarters of 2017, which were classified as other assets in the consolidated condensed balance sheets. No CONA member may transfer its membership interest (or any portion thereof) except to a purchaser of the member’s bottling business (or any portion thereof) and as permitted under the member’s comprehensive beverage agreement with The Coca Cola Company.

The CONA LLC Agreement further provides that, if CCR grants any major North American Coca Cola bottler other than a CONA member rights to (i) manufacture, produce and package or (ii) market, promote, distribute and sell Coca Cola products, CCR will

require the bottler to become a CONA member, to implement the CONA System in the bottler's operations and to enter into a master services agreement with CONA.

The Company is also party to an amended and restated master services agreement with CONA (the "CONA MSA"), pursuant to which CONA agreed to make available, and the Company became authorized to use, the Coke One North America system (the "CONA System"), a uniform information technology system developed to promote operational efficiency and uniformity among North American Coca Cola bottlers. As part of making the CONA System available, CONA provides the Company with certain business process and information technology services, including the planning, development, management and operation of the CONA System in connection with the Company's direct store delivery and manufacture of products (collectively, the "CONA Services").

The Company is also authorized under the CONA MSA to use the CONA System in connection with its distribution, promotion, marketing, sale and manufacture of beverages it is authorized to distribute or manufacture under the CBA, the Company's regional manufacturing agreement or any other agreement with The Coca Cola Company, subject to the provisions of the CONA LLC Agreement and any licenses or other agreements relating to products or services provided by third parties and used in connection with the CONA System.

In exchange for the Company's rights to use the CONA System and receive the CONA Services under the CONA MSA, it is charged service fees by CONA. Currently, the service fees are based on the number of physical cases of beverages the Company distributed or manufactured during the applicable period in the portion of its territories where the CONA Services have then been implemented.

Upon the earlier of (i) all members of CONA beginning to use the CONA System in all territories in which they distribute and manufacture Coca Cola products (excluding certain territories of CCR that are expected to be sold to bottlers that are neither members of CONA nor users of the CONA System), or (ii) December 31, 2018, the service fees will be changed to be an amount per physical case of beverages distributed or manufactured in any portion of the Company's territories equal to the aggregate costs incurred by CONA to maintain and operate the CONA System and provide the CONA Services divided by the total number of cases distributed or manufactured by all of the members of CONA, subject to certain exceptions and provided that the aggregate costs related to CONA's manufacturing functionality will be borne solely amongst the CONA members who have rights to manufacture beverages of The Coca Cola Company.

The Company is obligated to pay the service fees under the CONA MSA even if it is not using the CONA System for all or any portion of its distribution and manufacturing operations. The Company incurred CONA services fees of \$15.5 million in the first three quarters of 2018 and \$9.2 million in the first three quarters of 2017.

Related Party Leases

The Company leases its headquarters office facility and an adjacent office facility in Charlotte, North Carolina from Beacon Investment Corporation, of which J. Frank Harrison, III is the majority stockholder and Morgan H. Everett is a minority stockholder. The annual base rent the Company is obligated to pay under this lease agreement is subject to adjustment for increases in the Consumer Price Index and the lease expires on December 31, 2021.

The Company leases the Snyder Production Center and an adjacent sales facility in Charlotte, North Carolina from Harrison Limited Partnership One, which is directly and indirectly owned by trusts of which J. Frank Harrison, III, Chairman of the Board of Directors and Chief Executive Officer of the Company, and Sue Anne H. Wells, a director of the Company, are trustees and beneficiaries and of which Morgan H. Everett, Vice President and a director of the Company, is a permissible, discretionary beneficiary. The annual base rent the Company is obligated to pay under this lease agreement is subject to an adjustment for an inflation factor and the lease expires on December 31, 2020.

A summary of the principal balance outstanding under these related party capital leases is as follows:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|--------------------------|-----------------------|----------------------|
| Company headquarters | \$ 10,597 | \$ 12,771 |
| Snyder Production Center | 9,033 | 11,612 |

A summary of rental payments related to these capital leases is as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--------------------------|---------------|---------|----------------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| Company headquarters | \$1,110 | \$1,091 | \$3,346 | \$3,294 |
| Snyder Production Center | 1,049 | 1,018 | 3,147 | 3,055 |

21. Net Income Per Share

The following table sets forth the computation of basic net income per share and diluted net income per share under the two-class method:

| (in thousands, except per share data) | Third Quarter | | First Three Quarters | |
|---|---------------|----------|----------------------|----------|
| | 2018 | 2017 | 2018 | 2017 |
| Numerator for basic and diluted net income per Common Stock and Class B Common Stock share: | | | | |
| Net income attributable to Coca-Cola Bottling Co. Consolidated | \$25,164 | \$17,316 | \$7,046 | \$18,613 |
| Less dividends: | | | | |
| Common Stock | 1,787 | 1,785 | 5,357 | 5,356 |
| Class B Common Stock | 556 | 548 | 1,657 | 1,639 |
| Total undistributed earnings | \$22,821 | \$14,983 | \$32 | \$11,618 |
| Common Stock undistributed earnings – basic | | | | |
| Common Stock undistributed earnings – basic | \$17,422 | \$11,463 | 24 | \$8,893 |
| Class B Common Stock undistributed earnings – basic | 5,399 | 3,520 | 8 | 2,725 |
| Total undistributed earnings – basic | \$22,821 | \$14,983 | \$32 | \$11,618 |
| Common Stock undistributed earnings – diluted | | | | |
| Common Stock undistributed earnings – diluted | \$17,327 | \$11,414 | 24 | \$8,855 |
| Class B Common Stock undistributed earnings – diluted | 5,494 | 3,569 | 8 | 2,763 |
| Total undistributed earnings – diluted | \$22,821 | \$14,983 | \$32 | \$11,618 |
| Numerator for basic net income per Common Stock share: | | | | |
| Dividends on Common Stock | \$1,787 | \$1,785 | \$5,357 | \$5,356 |
| Common Stock undistributed earnings – basic | 17,422 | 11,463 | 24 | 8,893 |
| Numerator for basic net income per Common Stock share | \$19,209 | \$13,248 | \$5,381 | \$14,249 |
| Numerator for basic net income per Class B Common Stock share: | | | | |
| Dividends on Class B Common Stock | \$556 | \$548 | \$1,657 | \$1,639 |
| Class B Common Stock undistributed earnings – basic | 5,399 | 3,520 | 8 | 2,725 |
| Numerator for basic net income per Class B Common Stock share | \$5,955 | \$4,068 | \$1,665 | \$4,364 |

Numerator for diluted net income per Common Stock share:

| | | | | |
|---|----------|----------|---------|----------|
| Dividends on Common Stock | \$1,787 | \$1,785 | \$5,357 | \$5,356 |
| Dividends on Class B Common Stock assumed converted to Common Stock | 556 | 548 | 1,657 | 1,639 |
| Common Stock undistributed earnings – diluted | 22,821 | 14,983 | 32 | 11,618 |
| Numerator for diluted net income per Common Stock share | \$25,164 | \$17,316 | \$7,046 | \$18,613 |

Numerator for diluted net income per Class B Common Stock share:

| | | | | |
|---|---------|---------|---------|---------|
| Dividends on Class B Common Stock | \$556 | \$548 | \$1,657 | \$1,639 |
| Class B Common Stock undistributed earnings – diluted | 5,494 | 3,569 | 8 | 2,763 |
| Numerator for diluted net income per Class B Common Stock share | \$6,050 | \$4,117 | \$1,665 | \$4,402 |

| (in thousands, except per share data) | Third Quarter | | First Three Quarters | |
|---|---------------|--------|----------------------|--------|
| | 2018 | 2017 | 2018 | 2017 |
| Denominator for basic net income per Common Stock and Class B Common Stock share: | | | | |
| Common Stock weighted average shares outstanding – basic | 7,141 | 7,141 | 7,141 | 7,141 |
| Class B Common Stock weighted average shares outstanding – basic | 2,213 | 2,193 | 2,208 | 2,188 |
| Denominator for diluted net income per Common Stock and Class B Common Stock share: | | | | |
| Common Stock weighted average shares outstanding – diluted (assumes conversion of Class B Common Stock to Common Stock) | 9,405 | 9,374 | 9,400 | 9,369 |
| Class B Common Stock weighted average shares outstanding – diluted | 2,264 | 2,233 | 2,259 | 2,228 |
| Basic net income per share: | | | | |
| Common Stock | \$2.69 | \$1.86 | \$0.75 | \$2.00 |
| Class B Common Stock | \$2.69 | \$1.86 | \$0.75 | \$2.00 |
| Diluted net income per share: | | | | |
| Common Stock | \$2.69 | \$1.85 | \$0.75 | \$1.99 |
| Class B Common Stock | \$2.68 | \$1.84 | \$0.74 | \$1.97 |

NOTES TO TABLE

- (1) For purposes of the diluted net income per share computation for Common Stock, all shares of Class B Common Stock are assumed to be converted; therefore, 100% of undistributed earnings is allocated to Common Stock.
- (2) For purposes of the diluted net income per share computation for Class B Common Stock, weighted average shares of Class B Common Stock are assumed to be outstanding for the entire period and not converted.
- (3) The denominator for diluted net income per share for Common Stock and Class B Common Stock includes the dilutive effect of shares relative to the Performance Unit Award Agreement.
- (4) The Company does not have anti-dilutive shares.

22. Supplemental Disclosures of Cash Flow Information

Changes in current assets and current liabilities affecting cash flows were as follows:

| (in thousands) | First Three Quarters | |
|--|----------------------|--------------|
| | 2018 | 2017 |
| Accounts receivable, trade, net | \$(34,899) | \$(109,023) |
| Accounts receivable from The Coca-Cola Company | (2,083) | 1,548 |
| Accounts receivable, other | 10,328 | (8,308) |

| | | |
|---|-------------|-------------|
| Inventories | (46,274) | (19,254) |
| Prepaid expenses and other current assets | 8,951 | (281) |
| Accounts payable, trade | 3,749 | 67,058 |
| Accounts payable to The Coca-Cola Company | (15,222) | 45,722 |
| Other accrued liabilities | (33,712) | 7,924 |
| Accrued compensation | (15,496) | (10,062) |
| Accrued interest payable | 4,237 | 5,640 |
| Change in current assets less current liabilities (exclusive of acquisitions) | \$(120,421) | \$(19,036) |

23.Segments

The Company evaluates segment reporting in accordance with the FASB Accounting Standards Codification 280, Segment Reporting, each reporting period, including evaluating the reporting package reviewed by the Chief Operation Decision Maker (“CODM”). The Company has concluded the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer, as a group, represent the CODM. In conjunction with the completion of the System Transformation Transactions in October 2017 and integration of acquired operations, management continues to assess whether changes are necessary to the Company’s reportable segments.

The Company believes four operating segments exist. Nonalcoholic Beverages represents the vast majority of the Company's consolidated revenues, income from operations and assets. The additional three operating segments do not meet the quantitative thresholds for separate reporting, either individually or in the aggregate, and therefore have been combined into "All Other."

The Company's segment results are as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|---|--------------------|--------------------|----------------------|--------------------|
| | 2018 | 2017 | 2018 | 2017 |
| Net sales: | | | | |
| Nonalcoholic Beverages ⁽¹⁾ | \$1,180,212 | \$1,142,238 | \$3,427,492 | \$3,139,974 |
| All Other ⁽¹⁾ | 93,493 | 81,439 | 273,490 | 220,734 |
| Eliminations ⁽²⁾ | (62,044) | (61,151) | (189,985) | (163,189) |
| Consolidated net sales | \$1,211,661 | \$1,162,526 | \$3,510,997 | \$3,197,519 |
| Income from operations: | | | | |
| Nonalcoholic Beverages | \$39,361 | \$33,867 | \$32,705 | \$90,254 |
| All Other | 5,043 | 3,605 | 12,381 | 10,823 |
| Consolidated income from operations | \$44,404 | \$37,472 | \$45,086 | \$101,077 |
| Depreciation and amortization: | | | | |
| Nonalcoholic Beverages | \$44,050 | \$41,151 | \$133,095 | \$114,166 |
| All Other | 2,539 | 2,095 | 7,401 | 6,127 |
| Consolidated depreciation and amortization | \$46,589 | \$43,246 | \$140,496 | \$120,293 |

⁽¹⁾In order to correct an error in the prior year segment presentation, the Company revised net sales by \$39.2 million for the third quarter of 2017 and \$96.4 million for the first three quarters of 2017 to reflect sales in the Nonalcoholic Beverages segment which were previously attributed to All Other. Total net sales remain unchanged in prior periods and these revisions were not considered material to the prior periods presented.

⁽²⁾The entire net sales elimination for each period presented represents net sales from All Other to the Nonalcoholic Beverages segment. Sales between these segments are recognized at either fair market value or cost depending on the nature of the transaction.

Item 2. 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 of Coca Cola Bottling Co. Consolidated (together with its majority-owned subsidiaries, the "Company," "we" or "our") should be read in conjunction with the consolidated condensed financial statements of the Company and the accompanying notes to the consolidated condensed financial statements.

The Company's fiscal year generally ends on the Sunday closest to December 31 of each year. The consolidated condensed financial statements presented are:

- The financial position as of September 30, 2018 and December 31, 2017.
- The results of operations and comprehensive income for the 13 week periods ended September 30, 2018 ("third quarter" of fiscal 2018 ("2018")) and October 1, 2017 ("third quarter" of fiscal 2017 ("2017")), and the 39 week periods ended September 30, 2018 ("first three quarters" of 2018) and October 1, 2017 ("first three quarters" of 2017).
- The changes in equity and cash flows for the first three quarters of 2018 and the first three quarters of 2017.

The consolidated condensed financial statements include the consolidated operations of the Company and its majority-owned subsidiaries including Piedmont Coca Cola Bottling Partnership ("Piedmont"), the Company's only subsidiary with a significant noncontrolling interest. This noncontrolling interest consists of The Coca Cola Company's interest in Piedmont, which was 22.7% for all periods presented.

Our Business and the Nonalcoholic Beverage Industry

Coca Cola Bottling Co. Consolidated, a Delaware corporation, distributes, markets and manufactures nonalcoholic beverages in territories spanning 14 states and the District of Columbia. The Company was incorporated in 1980 and, together with its predecessors, has been in the nonalcoholic beverage manufacturing and distribution business since 1902. We are the largest independent Coca Cola bottler in the United States. Approximately 94% of our total bottle/can sales volume to retail customers consists of products of The Coca Cola Company, which include some of the most recognized and popular beverage brands in the world. We also distribute products for several other beverage brands including Dr Pepper, Sundrop and Monster Energy. Our purpose is to honor God, to serve others, to pursue excellence and to grow profitably. Our stock is traded on the NASDAQ Global Select Market under the symbol "COKE."

We offer a range of nonalcoholic beverage products and flavors designed to meet the demands of our consumers, including both sparkling and still beverages. Sparkling beverages are carbonated beverages and the Company's principal sparkling beverage is Coca Cola. Still beverages include energy products and noncarbonated beverages such as bottled water, tea, ready to drink coffee, enhanced water, juices and sports drinks.

Our sales are divided into two main categories: (i) bottle/can sales and (ii) other sales. Bottle/can sales include products packaged primarily in plastic bottles and aluminum cans. Other sales include sales to other Coca Cola bottlers, “post-mix” products, transportation revenue and equipment maintenance revenue. Post-mix products are dispensed through equipment that mixes fountain syrups with carbonated or still water, enabling fountain retailers to sell finished products to consumers in cups or glasses.

Net sales by product category were as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--|--------------------|--------------------|----------------------|--------------------|
| | 2018 | 2017 | 2018 | 2017 |
| Bottle/can sales: | | | | |
| Sparkling beverages (carbonated) | \$605,614 | \$582,710 | \$1,787,451 | \$1,670,093 |
| Still beverages (noncarbonated, including energy products) | 413,282 | 384,495 | 1,142,764 | 1,009,508 |
| Total bottle/can sales | 1,018,896 | 967,205 | 2,930,215 | 2,679,601 |
| Other sales: | | | | |
| Sales to other Coca-Cola bottlers | 92,139 | 104,619 | 300,819 | 274,317 |
| Post-mix and other | 100,626 | 90,702 | 279,963 | 243,601 |
| Total other sales | 192,765 | 195,321 | 580,782 | 517,918 |
| Total net sales | \$1,211,661 | \$1,162,526 | \$3,510,997 | \$3,197,519 |

The nonalcoholic beverage market is highly competitive for both sparkling and still beverages. Our competitors include bottlers and distributors of nationally and regionally advertised and marketed products, as well as bottlers and distributors of private label beverages. Our principal competitors include local bottlers of Pepsi-Cola and, in some regions, local bottlers of Dr Pepper, Royal Crown and/or 7 Up products.

The principal methods of competition in the nonalcoholic beverage industry are point-of-sale merchandising, new product introductions, new vending and dispensing equipment, packaging changes, pricing, price promotions, product quality, retail space management, customer service, frequency of distribution and advertising. We believe we are competitive in our territories with respect to these methods of competition.

Business seasonality results primarily from higher unit sales of the Company's products in the second and third quarters of the fiscal year. We believe that we and other manufacturers from whom we purchase finished goods have adequate production capacity to meet sales demand for sparkling and still beverages during these peak periods. Sales volume can also be impacted by weather conditions. Fixed costs, such as depreciation expense, are not significantly impacted by business seasonality.

Executive Summary

During the third quarter of 2018, our Company made meaningful progress towards the strategic priorities we set during the second quarter of 2018, even in the midst of continued challenges in the commodities and transportation markets. Our pricing actions delivered over 4% revenue growth versus the third quarter of 2017 on relatively flat volume of almost 87 million physical cases. Our performance during the third quarter of 2018 brings our year-to-date volume growth to 5.9% and our year-to-date revenue growth to 9.8%. Our organic case volume decline in the third quarter of 2018 was 0.4% versus the third quarter of 2017, and our year-to-date organic case volume growth was 0.3% versus the prior year period. Beginning in the fourth quarter of 2018, we will have cycled all of the transactions completed during our system transformation initiative, and results should be comparable on a year-over-year basis. As discussed last quarter, the mid-week July 4th holiday resulted in volume being split between the second and third quarters in 2018. Additionally, Hurricane Florence impacted our operations in much of our coastal territory in September, although identified incremental costs due to the storm were immaterial.

Integral to the strategic priorities we set during the second quarter of 2018, we implemented numerous pricing actions throughout our territory in the third quarter of 2018 to address our increased input costs. Gross margin in the third quarter of 2018 was 60 basis points lower than the third quarter of 2017 (34.7% in the third quarter of 2018 versus 35.3% in the third quarter of 2017), which reflects significant and sequential improvement over the gross margin declines we experienced in the first half of 2018. The primary drivers of the year-over-year margin decline remain (in order of significance): (i) rising commodity costs, (ii) the volume shift to lower-margin still products, and (iii) newly acquired territories generally experiencing margins lower than our legacy territories. We continue to refine our pricing strategies and focus on driving operating efficiencies in our supply chain to improve margin performance and address the rising input costs across the consumer products landscape.

Selling, delivery and administrative (“S,D&A”) expenses in the third quarter of 2018 increased approximately \$3.0 million, or 0.8%, as compared to the third quarter of 2017. Notably, our S,D&A expenses as a percent of revenue declined to 31.0% in the third quarter of 2018 from 32.1% in the third quarter of 2017. We believe this leveraging of operating expenses was the result of our actions taken during the second quarter of 2018 and our strong revenue performance in the third quarter of 2018. These improvements were partially offset by the expenses associated with our continuing territory integration efforts. While we are pleased with our operating expense performance in the third quarter, we will continue to refine and optimize our operating model across our Company to drive improvements in efficiency and profitability.

Income from operations was \$44.4 million in the third quarter of 2018, increasing from \$37.5 million in the third quarter of 2017. We have completed our system transformation transactions and are nearing steady state from an IT system perspective. As such, we incurred \$2.7 million less in system transformation expenses in the third quarter of 2018, as compared to the third quarter of 2017. We are encouraged with our progress in operating income performance and recognize we have additional improvement opportunities.

During the third quarter of 2018, we spent \$10.4 million on system transformation expenses, which primarily related to the implementation of our integrated CONA information systems platform. We anticipate spending between \$6 million and \$8 million on system transformation expenses in the fourth quarter of 2018 and expect to see these expenses continue to decrease over the next few quarters.

Capital spending for the third quarter was approximately \$27.8 million, bringing our year-to-date total capital investments to \$113.1 million. We anticipate capital spending in the range of \$25 million to \$35 million in the fourth quarter of 2018. Diligent capital management processes have been put in place to continue our focus on debt reduction, while investing in the highest impact projects. In addition to our capital spending, the Company contributed \$20 million to fund our pension plans during the third quarter of 2018.

We expect to begin distribution of the fast-growing premium sports drink, BodyArmor, in a portion of our territories in the fourth quarter of 2018. We are excited about the addition of BodyArmor to our powerful portfolio of brands, and, while we do not expect the impact on our 2018 results to be material, we do anticipate our BodyArmor distribution rights will provide ongoing benefits and round out our sports drink portfolio.

System Transformation Transactions

As part of The Coca Cola Company's plans to rebrand its North American bottling territories, the Company completed a series of transactions from April 2013 to October 2017 with The Coca Cola Company, Coca Cola Refreshments USA, Inc. ("CCR"), a wholly-owned subsidiary of The Coca Cola Company, and Coca Cola Bottling Company United, Inc. ("United"), an independent bottler that is unrelated to the Company, to significantly expand the Company's distribution and manufacturing operations (the "System Transformation"). The System Transformation included the acquisition and exchange of rights to serve distribution territories and related distribution assets, as well as the acquisition and exchange of regional manufacturing facilities and related manufacturing assets. A summary of the System Transformation transactions (the "System Transformation Transactions") completed by the Company is included in the Company's Annual Report on Form 10-K for 2017. As of September 30, 2018, the cash purchase prices or settlement amounts for all System Transformation Transactions have been resolved according to the terms of the transaction agreements. The post-closing adjustments made during the third quarter of 2018 resulted in a \$10.2 million net adjustment to the gain on exchange transactions in the consolidated condensed statements of operations.

The financial results of the System Transformation Transactions have been included in the Company's consolidated condensed financial statements from their respective acquisition or exchange dates. Net sales and income from operations for certain territories and regional manufacturing facilities acquired and divested by the Company during 2017 are impracticable to separately calculate, as the operations were absorbed into territories and facilities owned by the Company prior to the System Transformation, and therefore have been omitted from the results below. Omission of net sales and income from operations for such territories and facilities is not considered material to the results presented below. The remaining System Transformation Transactions that closed during 2017 (the "2017 System Transformation Transactions") contributed the following amounts to the Company's consolidated condensed statements of operations:

| (in thousands) | Third Quarter | | First Three Quarters | |
|---|---------------|-----------|----------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Impact to net sales - total 2017 System Transformation Transactions acquisitions | \$308,825 | \$221,034 | \$896,179 | \$454,174 |
| Impact to net sales - October 2017 Divestitures | - | 79,032 | - | 231,301 |
| Total impact to net sales | \$308,825 | \$300,066 | \$896,179 | \$685,475 |
| Impact to income from operations - total 2017 System Transformation Transactions acquisitions | \$11,874 | \$3,176 | \$14,635 | \$13,595 |

| | | | | |
|--|----------|----------|----------|----------|
| Impact to income from operations - October 2017 Divestitures | - | 7,689 | - | 22,973 |
| Total impact to income from operations | \$11,874 | \$10,865 | \$14,635 | \$36,568 |

See Note 3 to the consolidated condensed financial statements for additional information on the October 2017 Divestitures.

Areas of Emphasis

Key priorities for the Company include integration of the territories and regional manufacturing facilities acquired during the System Transformation, revenue management, product innovation and beverage portfolio expansion, distribution cost management and productivity.

Revenue Management: Revenue management requires a strategy that reflects consideration for pricing of brands and packages within product categories and channels, highly effective working relationships with customers and disciplined fact-based decision-making. Revenue management has been and continues to be a key driver which has a significant impact on the Company's results of operations.

Product Innovation and Beverage Portfolio Expansion: Innovation of both new brands and packages has been and is expected to continue to be important to the Company's overall revenue. Recent product introductions from the Company and The Coca Cola Company include new flavor varieties within certain brands such as Sprite Cherry, POWERade Citrus Passionfruit, Monster Ultra Violet, Monster Juice Mango Loco, Peace Tea Georgia Peach, Peace Tea Razzleberry, Minute Maid 5% Berry Punch,

Dunkin' Donuts Mocha Iced Coffee, Dunkin' Donuts French Vanilla Iced Coffee and Coke Zero Sugar. Recent packaging introductions include the 13.7-ounce bottle for Dunkin' Donuts Iced Coffees, 0.5-liter energy drink cans and eight-packs of 16-ounce energy drinks.

Distribution Cost Management: Distribution costs represent the costs of transporting finished goods from Company locations to customer outlets. Total distribution costs, including warehouse costs, were \$458.7 million in the first three quarters of 2018 and \$407.1 million in the first three quarters of 2017. Management of these costs will continue to be a key area of emphasis for the Company.

The Company has three primary delivery systems: (i) bulk delivery for large supermarkets, mass merchandisers and club stores, (ii) advanced sale delivery for convenience stores, drug stores, small supermarkets and on-premises accounts and (iii) full service delivery for its full service vending customers.

Productivity: A key driver in the Company's selling, delivery and administrative ("S,D&A") expense management relates to ongoing improvements in labor productivity and asset productivity.

Results of Operations

Third Quarter Results

Our results of operations for the third quarter of 2018 and the third quarter of 2017 are highlighted in the table below and discussed in the following paragraphs:

| (in thousands) | Third Quarter | | | |
|---|---------------|-------------|----------|----------|
| | 2018 | 2017 | Change | % Change |
| Net sales | \$1,211,661 | \$1,162,526 | \$49,135 | 4.2% |
| Cost of sales | 791,317 | 752,202 | 39,115 | 5.2 |
| Gross profit | 420,344 | 410,324 | 10,020 | 2.4 |
| Selling, delivery and administrative expenses | 375,940 | 372,852 | 3,088 | 0.8 |
| Income from operations | 44,404 | 37,472 | 6,932 | 18.5 |
| Interest expense, net | 12,827 | 10,697 | 2,130 | 19.9 |
| Other income, net | 1,696 | 3,884 | (2,188) | (56.3) |
| Gain on exchange transactions | 10,170 | - | 10,170 | - |
| Income before income taxes | 43,443 | 30,659 | 12,784 | 41.7 |

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

| | | | | |
|--|----------|----------|---------|-------|
| Income tax expense | 16,493 | 11,748 | 4,745 | 40.4 |
| Net income | 26,950 | 18,911 | 8,039 | 42.5 |
| Less: Net income attributable to noncontrolling interest | 1,786 | 1,595 | 191 | 12.0 |
| Net income attributable to Coca-Cola Bottling Co. Consolidated | \$25,164 | \$17,316 | \$7,848 | 45.3% |

Items Impacting Operations and Financial Condition

The following items affect the comparability of the financial results:

Third Quarter 2018

- \$308.8 million in net sales and \$11.8 million of income from operations related to the 2017 System Transformation Transactions;
- \$10.4 million of expenses related to the System Transformation; and
- \$10.2 million net adjustment to the gain on exchange transactions as a result of final post-closing adjustments related to the 2017 System Transformation Transactions.

Third Quarter 2017

- \$221.1 million in net sales and \$3.2 million of income from operations related to the 2017 System Transformation Transactions;
- \$79.0 million in net sales and \$7.7 million of income from operations related to the October 2017 Divestitures;

\$13.2 million of expenses related to the acquisition and transition of the distribution territories and the regional manufacturing facilities acquired as part of the System Transformation; and
 \$5.3 million recorded in other income, net as a result of a favorable fair value adjustment to the Company's contingent consideration liability related to the distribution territories acquired as part of the System Transformation.

Net Sales

Net sales increased \$49.1 million, or 4.2%, to \$1.21 billion in the third quarter of 2018, as compared to \$1.16 billion in the third quarter of 2017. The increase in net sales was primarily attributable to the following (in millions):

| | |
|--------------------|--|
| Third Quarter 2018 | Attributable to: |
| \$ 50.7 | Increase in net sales primarily related to bottle/can sales price per unit to retail customers and the shift in product mix to higher revenue still products in order to meet consumer preferences |
| (12.6) | Decrease in sales volume to other Coca-Cola bottlers |
| 11.0 | Increase in volume of external freight revenue to external customers (other than non-alcoholic beverages) |
| \$ 49.1 | Total increase in net sales |

The Company's bottle/can sales to retail customers accounted for approximately 84% of the Company's total net sales in the third quarter of 2018, as compared to approximately 83% in the third quarter of 2017. Bottle/can net pricing is based on the invoice price charged to customers reduced by promotional allowances. Bottle/can net pricing per unit is impacted by the price charged per package, the sales volume generated for each package and the channels in which those packages are sold.

Product category sales volume of physical cases in the third quarter of 2018 and the third quarter of 2017 as a percentage of total bottle/can sales volume and the percentage change by product category were as follows:

| Product Category | Bottle/Can Sales Volume Third Quarter | | Bottle/Can Sales Volume Increase / (Decrease) |
|---|---------------------------------------|--------|---|
| | 2018 | 2017 | |
| Sparkling beverages | 66.0 % | 65.1 % | 1.3% |
| Still beverages (including energy products) | 34.0 % | 34.9 % | (2.7)% |
| Total bottle/can sales volume | 100.0% | 100.0% | (0.1)% |

Cost of Sales

Cost of sales includes the following: raw material costs, manufacturing labor, manufacturing overhead including depreciation expense, manufacturing warehousing costs, shipping and handling costs related to the movement of finished goods from manufacturing locations to sales distribution centers and the purchase of finished goods. Inputs representing a substantial portion of the Company's total cost of sales include: (i) sweeteners, (ii) packaging materials, including plastic bottles and aluminum cans, and (iii) finished products purchased from other vendors.

Cost of sales increased \$39.1 million, or 5.2%, to \$791.3 million in the third quarter of 2018, as compared to \$752.2 million in the third quarter of 2017. The increase in cost of sales was primarily attributable to the following (in millions):

| | |
|--------------------------|--|
| Third Quarter 2018 | Attributable to: |
| \$ 42.9 | Increase in cost of sales primarily related to, in order of magnitude, commodities, the change in product mix to meet consumer preferences and higher costs in the territories acquired in the System Transformation |
| (12.7) | Decrease in sales volume to other Coca-Cola bottlers |
| 9.8 | Increase in costs related to increased volume of freight revenue to external customers (other than non-alcoholic beverages) |
| (0.9) | Other |
| \$ 39.1 | Total increase in cost of sales |

The Company relies extensively on advertising and sales promotion in the marketing of its products. The Coca Cola Company and other beverage companies that supply concentrates, syrups and finished products to the Company make substantial marketing and advertising expenditures to promote sales in the Company's territories. Certain of the marketing expenditures by The Coca Cola Company and other beverage companies are made pursuant to annual arrangements. The Company also benefits from national advertising programs conducted by The Coca Cola Company and other beverage companies. Total marketing funding support from The Coca Cola Company and other

beverage companies, which includes both direct payments to the Company and payments to customers for marketing programs, was \$33.1 million in the third quarter of 2018, as compared to \$32.5 million in the third quarter of 2017.

The Company's cost of sales may not be comparable to other peer companies, as some peer companies include all costs related to their distribution network in cost of sales. The Company includes a portion of these costs in S,D&A expenses, as described below.

S,D&A Expenses

S,D&A expenses include the following: sales management labor costs, distribution costs from sales distribution centers to customer locations, sales distribution center warehouse costs, depreciation expenses related to sales centers, delivery vehicles and cold drink equipment, point-of-sale expenses, advertising expenses, cold drink equipment repair costs, amortization of intangibles and administrative support labor and operating costs.

S,D&A expenses increased by \$3.0 million, or 0.8%, to \$375.9 million in the third quarter of 2018, as compared to \$372.9 million in the third quarter of 2017. S,D&A expenses as a percentage of net sales increased to 31.0% in the third quarter of 2018 from 32.1% in the third quarter of 2017. The increase in S,D&A expenses was primarily attributable to the following (in millions):

| Third Quarter 2018 | Attributable to: |
|--------------------------|---|
| \$ (3.7) | Decrease in marketing expenses primarily related to sponsorship contracts |
| 2.9 | Increase in employee salaries including bonuses and incentives due to additional personnel added in the System Transformation and normal salary increases |
| 2.6 | Increase in fuel costs related to the movement of finished goods from sales distribution centers to customer locations primarily as a result of territories acquired in the System Transformation |
| 1.2 | Other individually immaterial expense increases primarily related to the System Transformation |
| \$ 3.0 | Total increase in S,D&A expenses |

Shipping and handling costs related to the movement of finished goods from manufacturing locations to sales distribution centers are included in cost of sales. Shipping and handling costs related to the movement of finished goods from sales distribution centers to customer locations, including warehouse costs, are included in S,D&A expenses and totaled \$157.5 million in the third quarter of 2018 and \$147.9 million in the third quarter of 2017.

As a result of the Company adopting Accounting Standards Update 2017-07 “Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost” (“ASU 2017-07”) issued by the Financial Accounting Standards Board in March 2017, the Company reclassified \$1.3 million from the third quarter of 2017 of non-service cost components of net periodic benefit cost and other benefit plan charges from S,D&A expenses to other income, net. The non-service cost component of net periodic benefit cost is included in the Nonalcoholic Beverages segment.

Interest Expense, Net

Interest expense, net, increased \$2.1 million to \$12.8 million in the third quarter of 2018, as compared to \$10.7 million in the third quarter of 2017. The increase was primarily a result of additional borrowings to finance the 2017 System Transformation Transactions and additional borrowings during 2018 to support working capital and capital expenditure needs.

Other Income, Net

A summary of other income, net is as follows:

| (in thousands) | Third Quarter 2018 | 2017 |
|---|-----------------------|----------|
| Favorable fair value adjustment to acquisition related contingent consideration | \$ 2,373 | \$ 5,225 |
| Non-service cost component of net periodic benefit cost | (677) | (1,341) |
| Total other income, net | \$ 1,696 | \$ 3,884 |

Each reporting period, the Company adjusts its contingent consideration liability related to the territories acquired as part of the System Transformation, excluding territories acquired pursuant to an exchange transaction, to fair value. The fair value is determined by discounting future expected sub-bottling payments required under the CBA, using the Company’s estimated weighted average cost of capital (“WACC”), which is impacted by many factors, including long-term interest rates; projected future operating results; and post-closing settlement of cash purchase prices for the territories acquired as part of the System Transformation. These future expected

sub-bottling payments extend through the life of the related distribution asset acquired in the System Transformation, which is generally 40 years. The Company is required to pay the current portion of the sub-bottling fee on a quarterly basis.

The fair value adjustments to the acquisition related contingent consideration liability during the third quarter of 2018 were primarily driven by changes to the risk-free interest rate and the projected future operating results of the distribution territories acquired as part of the System Transformation subject to sub-bottling fees, partially offset by cash payments. The fair value adjustments to the acquisition related contingent consideration liability during the third quarter of 2017 were primarily a result of a change in the risk-free interest rate.

Gain on Exchange Transactions

As a result of final post-closing adjustments for the 2017 System Transformation Transactions made during the third quarter of 2018, the Company recorded a \$10.2 million net adjustment to the gain on exchange transactions.

Income Tax Expense

The Company's effective income tax rate, calculated by dividing income tax expense by income before income taxes, was 38.0% for the third quarter of 2018 and 38.3% for the third quarter of 2017. The decrease in the effective tax rate was primarily driven by higher income before income taxes for the third quarter of 2018 as compared to income before income taxes for the third quarter of 2017 and the corporate rate reduction due to the Tax Cuts and Jobs Act (the "Tax Act") and its impact on prior estimates, which was offset by an increase in certain non-deductible expenses. The Company's effective tax rate, calculated by dividing income tax expense by income before income taxes minus net income attributable to noncontrolling interest, was 39.6% for the third quarter of 2018 and 40.4% for the third quarter of 2017.

Noncontrolling Interest

The Company recorded net income attributable to noncontrolling interest of \$1.8 million in the third quarter of 2018 and \$1.6 million in the third quarter of 2017, each related to the portion of Piedmont owned by The Coca Cola Company.

Other Comprehensive Income, Net of Tax

Other comprehensive income, net of tax was \$0.7 million in the third quarter of 2018 and \$0.4 million in the third quarter of 2017. The increase was primarily a result of actuarial gains on the Company's pension plans.

First Three Quarters Results

Our results of operations for the first three quarters of 2018 and the first three quarters of 2017 are highlighted in the table below and discussed in the following paragraphs:

| (in thousands) | First Three Quarters | | | % |
|--|----------------------|-------------|-------------|---------|
| | 2018 | 2017 | Change | Change |
| Net sales | \$3,510,997 | \$3,197,519 | \$313,478 | 9.8% |
| Cost of sales | 2,313,728 | 2,039,996 | 273,732 | 13.4 |
| Gross profit | 1,197,269 | 1,157,523 | 39,746 | 3.4 |
| Selling, delivery and administrative expenses | 1,152,183 | 1,056,446 | 95,737 | 9.1 |
| Income from operations | 45,086 | 101,077 | (55,991) | (55.4) |
| Interest expense, net | 37,617 | 30,607 | 7,010 | 22.9 |
| Other expense, net | (3,612) | (36,595) | 32,983 | (90.1) |
| Gain on exchange transactions | 10,170 | - | 10,170 | - |
| Income before income taxes | 14,027 | 33,875 | (19,848) | (58.6) |
| Income tax expense | 3,387 | 11,800 | (8,413) | (71.3) |
| Net income | 10,640 | 22,075 | (11,435) | (51.8) |
| Less: Net income attributable to noncontrolling interest | 3,594 | 3,462 | 132 | 3.8 |
| Net income attributable to Coca-Cola Bottling Co. Consolidated | \$7,046 | \$18,613 | \$(11,567) | (62.1)% |

Items Impacting Operations and Financial Condition

The following items affect the comparability of the financial results:

First Three Quarters 2018

- \$896.2 million in net sales and \$14.6 million of income from operations related to the 2017 System Transformation Transactions;
- \$32.7 million of expenses related to the System Transformation;
- \$10.2 million net adjustment to the gain on exchange transactions as a result of final post-closing adjustments related to the 2017 System Transformation Transactions;
- \$4.8 million recorded in S,D&A expenses related to severance and outplacement expenses incurred to optimize labor expense; and
- \$3.1 million pre-tax unfavorable mark-to-market adjustments related to the Company's commodity hedging program.

First Three Quarters 2017

- \$454.2 million in net sales and \$13.6 million of income from operations related to the 2017 System Transformation Transactions;
- \$231.3 million in net sales and \$23.0 million of income from operations related to the October 2017 Divestitures;
- \$32.4 million of expenses related to the acquisition and transition of the distribution territories and the regional manufacturing facilities acquired as part of the System Transformation Transactions;
- \$23.1 million recorded in other expense, net as a result of an unfavorable fair value adjustment to the Company's contingent consideration liability related to the distribution territories acquired as part of the System Transformation; and
- \$9.4 million recorded in other expense, net for net working capital and other fair value adjustments related to the System Transformation Transactions completed in January 2016 (the "January 2016 Transactions") that were made beyond one year from the acquisition date.

Net Sales

Net sales increased \$313.5 million, or 9.8%, to \$3.51 billion in the first three quarters of 2018, as compared to \$3.20 billion in the first three quarters of 2017. The increase in net sales was primarily attributable to the following (in millions):

First
Three

Quarters

| | |
|----------|--|
| 2018 | Attributable to: |
| \$ 168.4 | Net sales increase related to increased volume, primarily related to the 2017 System Transformation Transactions |
| 86.4 | Increase in net sales primarily related to bottle/can sales price per unit to retail customers and the shift in product mix to higher revenue still products in order to meet consumer preferences |
| 26.5 | Increase in sales volume to other Coca-Cola bottlers |
| 25.2 | Increase in volume of external freight revenue to external customers (other than non-alcoholic beverages) |
| 7.0 | Other |
| \$ 313.5 | Total increase in net sales |

The Company's bottle/can sales to retail customers accounted for approximately 83% of the Company's total net sales in the first three quarters of 2018, as compared to approximately 84% in the first three quarters of 2017.

Product category sales volume as a percentage of total bottle/can sales volume and the percentage change by product category were as follows:

| Product Category | Bottle/Can Sales Volume First Three Quarters | | Bottle/Can Sales Volume Increase | |
|---|---|--------|--|---|
| | 2018 | 2017 | | |
| Sparkling beverages | 68.7 % | 67.9 % | 7.2 | % |
| Still beverages (including energy products) | 31.3 % | 32.1 % | 3.3 | % |
| Total bottle/can sales volume | 100.0% | 100.0% | 5.9 | % |

The Company's products are sold and distributed through various channels, which include selling directly to retail stores and other outlets such as food markets, institutional accounts and vending machine outlets. During the first three quarters of 2018, approximately 66% of the Company's bottle/can sales volume to retail customers was sold for future consumption, while the remaining bottle/can sales volume to retail customers was sold for immediate consumption.

The following table summarizes the percentage of the Company's total bottle/can sales volume to its largest customers, as well as the percentage of the Company's total net sales that such volume represents:

| | First Three Quarters | |
|---|----------------------|------|
| | 2018 | 2017 |
| Approximate percentage of the Company's total bottle/can sales volume: | | |
| Wal-Mart Stores, Inc. | 19% | 19% |
| The Kroger Company | 11% | 9% |
| Food Lion, LLC | 6% | 6% |
| Total approximate percentage of the Company's total bottle/can sales volume | 36% | 34% |
| Approximate percentage of the Company's total net sales: | | |
| Wal-Mart Stores, Inc. | 14% | 14% |
| The Kroger Company | 8% | 7% |
| Food Lion, LLC | 4% | 4% |
| Total approximate percentage of the Company's total net sales | 26% | 25% |

Cost of Sales

Cost of sales increased \$273.7 million, or 13.4%, to \$2.31 billion in the first three quarters of 2018, as compared to \$2.04 billion in the first three quarters of 2017. The increase in cost of sales was primarily attributable to the following (in millions):

| First Three Quarters | Attributable to: |
|----------------------|---|
| 2018 | |
| \$ 118.4 | Increase in cost of sales primarily related to, in order of magnitude, commodities, the change in product mix to meet consumer preferences, higher costs in the territories acquired in the System Transformation and higher transportation costs |
| 103.0 | Cost of sales increase related to increased volume, primarily related to the 2017 System Transformation Transactions |

| | |
|----------|---|
| 29.7 | Increase in sales volume to other Coca-Cola bottlers |
| 22.6 | Increase in costs related to increased volume of freight revenue to external customers (other than non-alcoholic beverages) |
| \$ 273.7 | Total increase in cost of sales |

Total marketing funding support from The Coca Cola Company and other beverage companies, which includes both direct payments to the Company and payments to customers for marketing programs, was \$96.9 million in the first three quarters of 2018, as compared to \$89.4 million in the first three quarters of 2017.

S,D&A Expenses

S,D&A expenses increased by \$95.7 million, or 9.1%, to \$1.15 billion in the first three quarters of 2018, as compared to \$1.06 billion in the first three quarters of 2017. S,D&A expenses as a percentage of net sales decreased to 32.8% in the first three quarters of 2018 from 33.0% in the first three quarters of 2017. The increase in S,D&A expenses was primarily attributable to the following (in millions):

| First Three Quarters 2018 | Attributable to: |
|------------------------------------|---|
| \$ 44.6 | Increase in employee salaries including bonuses and incentives due to additional personnel added in the System Transformation and normal salary increases |
| 11.3 | Increase in employee benefit costs primarily due to additional group insurance expense, 401(k) employer matching contributions and bargaining pension plan expense for employees added in the System Transformation |
| 7.5 | Increase in depreciation and amortization of property, plant and equipment primarily due to depreciation for vending equipment, fleet, furniture and fixtures acquired in the System Transformation |
| 6.5 | Increase in software expenses primarily due to increased maintenance expense |
| 4.8 | Increase in fuel costs related to the movement of finished goods from sales distribution centers to customer locations primarily as a result of territories acquired in the System Transformation |
| 4.8 | Severance and outplacement expenses incurred to optimize labor expense in the Nonalcoholic Beverages segment |
| 3.1 | Increase in employer payroll taxes primarily due to additional personnel added from the System Transformation |
| 13.1 | Other individually immaterial expense increases primarily related to the System Transformation |
| \$ 95.7 | Total increase in S,D&A expenses |

During the first three quarters of 2018, the Company incurred \$32.7 million of expenses related to the System Transformation, the majority of which were information technologies related costs. The Company anticipates System Transformation expenses for the remainder of 2018 to be in the range of \$6 million to \$8 million.

Shipping and handling costs related to the movement of finished goods from sales distribution centers to customer locations, including warehouse costs, are included in S,D&A expenses and totaled \$458.7 million in the first three quarters of 2018 and \$407.1 million in the first three quarters of 2017.

As a result of the Company adopting ASU 2017 07, the Company reclassified \$4.0 million in the first three quarters of 2017 of non-service cost components of net periodic benefit cost and other benefit plan charges from S,D&A expenses to other expense, net.

Interest Expense, Net

Interest expense, net, increased \$7.0 million to \$37.6 million in the first three quarters of 2018, as compared to \$30.6 million in the first three quarters of 2017. The increase was primarily a result of additional borrowings to finance the 2017 System Transformation Transactions and additional borrowings during the first three quarters of 2018 to support working capital and capital expenditure needs.

Other Expense, Net

A summary of other expense, net is as follows:

| (in thousands) | First Three Quarters | |
|---|-------------------------|------------|
| | 2018 | 2017 |
| Unfavorable fair value adjustment to acquisition related contingent consideration | \$(1,584) | \$(23,140) |
| Non-service cost component of net periodic benefit cost | (2,028) | (4,025) |
| January 2016 Transactions settlement | - | (9,442) |
| Other | - | 12 |
| Total other expense, net | \$(3,612) | \$(36,595) |

The fair value adjustments to acquisition related contingent consideration liability in the first three quarters of 2018 were primarily driven by changes to the risk-free interest rate and the projected future operating results of the distribution territories acquired as part of the System Transformation subject to sub-bottling fees, partially offset by cash payments. The fair value adjustment to the acquisition related contingent consideration liability in the first three quarters of 2017 was primarily a result of a change in the risk-free interest rate.

Gain on Exchange Transactions

As a result of final post-closing adjustments for the 2017 System Transformation Transactions made during the third quarter of 2018, the Company recorded a \$10.2 million net adjustment to the gain on exchange transactions.

Income Tax Expense

The Company's effective income tax rate, calculated by dividing income tax expense by income before income taxes, was 24.1% in the first three quarters of 2018 and 34.8% in the first three quarters of 2017. The decrease in the effective tax rate was primarily driven by the corporate rate reduction due to the Tax Act and its impact on prior estimates and lower income before income taxes, which was offset by an increase in certain non-deductible expenses. The Company's effective tax rate, calculated by dividing income tax expense by income before income taxes minus net income attributable to noncontrolling interest, was 32.5% in the first three quarters of 2018 and 38.8% in the first three quarters of 2017.

Noncontrolling Interest

The Company recorded net income attributable to noncontrolling interest of \$3.6 million in the first three quarters of 2018 and \$3.5 million in the first three quarters of 2017, each related to the portion of Piedmont owned by The Coca Cola Company.

Other Comprehensive Income, Net of Tax

Other comprehensive income, net of tax was \$2.2 million in the first three quarters of 2018 and \$1.3 million in the first three quarters of 2017. The increase was primarily a result of actuarial gains on the Company's pension plans.

Segment Operating Results

The Company evaluates segment reporting in accordance with the Financial Accounting Standards Board Accounting Standards Codification 280, Segment Reporting, each reporting period, including evaluating the reporting package reviewed by the Chief Operation Decision Maker (“CODM”). The Company has concluded the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer, as a group, represent the CODM. In conjunction with the completion of the System Transformation Transactions in October 2017 and integration of acquired operations, management continues to assess whether changes are necessary to the Company’s reportable segments.

The Company believes four operating segments exist. Nonalcoholic Beverages represents the vast majority of the Company’s consolidated revenues, income from operations and assets. The additional three operating segments do not meet the quantitative thresholds for separate reporting, either individually or in the aggregate, and therefore have been combined into “All Other.”

The Company’s segment results are as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--|--------------------|--------------------|----------------------|--------------------|
| | 2018 | 2017 | 2018 | 2017 |
| Net sales: | | | | |
| Nonalcoholic Beverages ⁽¹⁾ | \$1,180,212 | \$1,142,238 | \$3,427,492 | \$3,139,974 |
| All Other ⁽¹⁾ | 93,493 | 81,439 | 273,490 | 220,734 |
| Eliminations ⁽²⁾ | (62,044) | (61,151) | (189,985) | (163,189) |
| Consolidated net sales | \$1,211,661 | \$1,162,526 | \$3,510,997 | \$3,197,519 |
| Income from operations: | | | | |
| Nonalcoholic Beverages | \$39,361 | \$33,867 | \$32,705 | \$90,254 |
| All Other | 5,043 | 3,605 | 12,381 | 10,823 |
| Consolidated income from operations | \$44,404 | \$37,472 | \$45,086 | \$101,077 |

- (1) In order to correct an error in the prior year segment presentation, the Company revised net sales by \$39.2 million for the third quarter of 2017 and \$96.4 million for the first three quarters of 2017 to reflect sales in the Nonalcoholic Beverages segment which were previously attributed to All Other. Total net sales remain unchanged in prior periods and these revisions were not considered material to the prior periods presented.
- (2) The entire net sales elimination for each period presented represents net sales from All Other to the Nonalcoholic Beverages segment. Sales between these segments are recognized at either fair market value or cost depending on the nature of the transaction.

Organic / Adjusted Results

The Company reports its financial results in accordance with U.S. generally accepted accounting principles (“GAAP”). However, management believes that certain non-GAAP financial measures provide users with additional meaningful financial information that should be considered when assessing the Company’s ongoing performance. Further, with the transformation of the Company’s business through System Transformation Transactions with The Coca Cola Company and the conversion of its information technology systems, the Company believes these non-GAAP financial measures allow users to better appreciate the impact of these transactions on the Company’s performance.

Management also uses these non-GAAP financial measures in making financial, operating and planning decisions and in evaluating the Company’s performance. Non-GAAP financial measures should be viewed in addition to, and not as an alternative for, the Company’s reported results prepared in accordance with GAAP. The Company’s non-GAAP financial information does not represent a comprehensive basis of accounting. The following tables reconcile reported GAAP results to organic / adjusted results (non-GAAP):

| (in thousands) | Third Quarter | | First Three Quarters | |
|--|---------------|-------------|----------------------|-------------|
| | 2018 | 2017 | 2018 | 2017 |
| Total bottle/can sales | \$1,018,896 | \$967,205 | \$2,930,215 | \$2,679,601 |
| Total other sales | 192,765 | 195,321 | 580,782 | 517,918 |
| Total net sales | \$1,211,661 | \$1,162,526 | \$3,510,997 | \$3,197,519 |
| Total bottle/can sales | \$1,018,896 | \$967,205 | \$2,930,215 | \$2,679,601 |
| Less: Acquisition/divestiture related sales | 117,684 | 103,171 | 546,284 | 370,992 |
| Organic net bottle/can sales (non-GAAP) ⁽¹⁾ | \$901,212 | \$864,034 | \$2,383,931 | \$2,308,609 |
| Increase in organic net bottle/can sales | 4.3 | % | 3.3 | % |

| (in millions) | Third Quarter | | First Three Quarters | |
|--|---------------|------|----------------------|-------|
| | 2018 | 2017 | 2018 | 2017 |
| Physical case volume | 86.7 | 86.8 | 254.8 | 240.5 |
| Less: Acquisition/divestiture related physical case volume | 10.6 | 10.4 | 48.7 | 35.1 |

Edgar Filing: COCA COLA BOTTLING CO CONSOLIDATED /DE/ - Form 10-Q

| | | | | |
|---|--------|------|-------|-------|
| Organic physical case volume ⁽¹⁾ | 76.1 | 76.4 | 206.1 | 205.4 |
| Increase (decrease) in organic physical case volume | (0.4)% | | 0.3 | % |

Third Quarter 2018

| (in thousands, except per share data) | Net sales | Gross profit | Income from operations | Income before taxes | Net income | Basic net income per share |
|--|--------------|--------------|------------------------|---------------------|------------|----------------------------|
| Reported results (GAAP) | \$ 1,211,661 | \$ 420,344 | \$ 44,404 | \$ 43,443 | \$ 25,164 | \$ 2.69 |
| System Transformation Transactions expenses ⁽²⁾ | - | 112 | 10,417 | 10,417 | 7,834 | 0.83 |
| Gain on exchange transactions ⁽³⁾ | - | - | - | (10,170) | (7,648) | (0.82) |
| Fair value adjustment of acquisition related contingent consideration ⁽⁴⁾ | - | - | - | (2,373) | (1,785) | (0.19) |
| Fair value adjustments for commodity hedges ⁽⁵⁾ | - | 260 | 469 | 469 | 353 | 0.04 |
| Other tax adjustment ⁽⁶⁾ | - | - | - | - | 3,534 | 0.38 |
| Total reconciling items | - | 372 | 10,886 | (1,657) | 2,288 | 0.24 |
| Adjusted results (non-GAAP) | \$ 1,211,661 | \$ 420,716 | \$ 55,290 | \$ 41,786 | \$ 27,452 | \$ 2.93 |

Third Quarter 2017

| (in thousands, except per share data) | Net sales | Gross profit | Income from operations | Income before income taxes | Net income | Basic net income per share |
|--|-------------|--------------|------------------------|----------------------------|------------|----------------------------|
| Reported results (GAAP) | \$1,162,526 | \$410,324 | \$ 37,472 | \$30,659 | \$17,316 | \$ 1.86 |
| System Transformation Transactions expenses ⁽²⁾ | - | 113 | 13,148 | 13,148 | 9,265 | 0.99 |
| Fair value adjustment of acquisition related contingent consideration ⁽⁴⁾ | - | - | - | (5,225) | (2,386) | (0.25) |
| Fair value adjustments for commodity hedges ⁽⁵⁾ | - | (2,042) | (3,401) | (3,401) | (2,187) | (0.24) |
| Other tax adjustment ⁽⁶⁾ | - | - | - | - | (1,690) | (0.18) |
| Total reconciling items | - | (1,929) | 9,747 | 4,522 | 3,002 | 0.32 |
| Adjusted results (non-GAAP) | \$1,162,526 | \$408,395 | \$ 47,219 | \$35,181 | \$20,318 | \$ 2.18 |

First Three Quarters 2018

| (in thousands, except per share data) | Net sales | Gross profit | Income from operations | Income before income taxes | Net income | Basic net income per share |
|--|-------------|--------------|------------------------|----------------------------|------------|----------------------------|
| Reported results (GAAP) | \$3,510,997 | \$1,197,269 | \$ 45,086 | \$14,027 | \$7,046 | \$ 0.75 |
| System Transformation Transactions expenses ⁽²⁾ | - | 339 | 32,738 | 32,738 | 24,619 | 2.63 |
| Gain on exchange transactions ⁽³⁾ | - | - | - | (10,170) | (7,648) | (0.82) |
| Workforce optimization expenses ⁽⁷⁾ | - | - | 4,810 | 4,810 | 3,617 | 0.39 |
| Fair value adjustment of acquisition related contingent consideration ⁽⁴⁾ | - | - | - | 1,584 | 1,191 | 0.13 |
| Amortization of converted distribution rights, net ⁽⁸⁾ | - | 2,231 | 2,231 | 2,231 | 1,678 | 0.18 |
| Fair value adjustments for commodity hedges ⁽⁵⁾ | - | 2,776 | 3,139 | 3,139 | 2,361 | 0.25 |
| Other tax adjustment ⁽⁶⁾ | - | - | - | - | (2,648) | (0.28) |
| Total reconciling items | - | 5,346 | 42,918 | 34,332 | 23,170 | 2.48 |
| Adjusted results (non-GAAP) | \$3,510,997 | \$1,202,615 | \$ 88,004 | \$48,359 | \$30,216 | \$ 3.23 |

First Three Quarters 2017

| (in thousands, except per share data) | Net sales | Gross profit | Income from operations | Income before income taxes | Net income | Basic net income per share |
|--|-------------|--------------|------------------------|----------------------------|------------|----------------------------|
| Reported results (GAAP) | \$3,197,519 | \$1,157,523 | \$101,077 | \$33,875 | \$18,613 | \$ 2.00 |
| System Transformation Transactions expenses ⁽²⁾ | - | 379 | 32,374 | 32,374 | 21,108 | 2.26 |
| January 2016 Transactions settlement ⁽⁹⁾ | - | - | - | 9,442 | 5,816 | 0.62 |
| | - | - | - | 23,140 | 15,087 | 1.62 |

Fair value adjustment of acquisition related
contingent consideration⁽⁴⁾

| | | | | | | |
|---|-------------|-------------|-----------|----------|----------|---------|
| Fair value adjustments for commodity hedges ⁽⁵⁾ | - | (2,066) | (2,541) | (2,541) | (1,657) | (0.18) |
| Other tax adjustment ⁽⁶⁾ | - | - | - | - | (2,156) | (0.23) |
| Total reconciling items | - | (1,687) | 29,833 | 62,415 | 38,198 | 4.09 |
| Adjusted results (non-GAAP) | \$3,197,519 | \$1,155,836 | \$130,910 | \$96,290 | \$56,811 | \$6.09 |

Following is an explanation of non-GAAP adjustments:

- ⁽¹⁾Organic net bottle/can sales and organic physical case volume include results from the Company's distribution territories not impacted by acquisition or divestiture related activity during 2017.
- ⁽²⁾Adjustment reflects expenses related to the System Transformation, which primarily includes information technologies system conversions and professional fees and expenses related to due diligence.
- ⁽³⁾Adjustment reflects gain on exchange transactions as a result of final post-closing adjustments for the 2017 System Transformation Transactions made during the third quarter of 2018.
- ⁽⁴⁾This non-cash, fair value adjustment of acquisition related contingent consideration fluctuates based on factors such as long-term interest rates, projected future results, and final settlements of acquired territory values.

- (5) The Company enters into derivative instruments from time to time to hedge some or all of its projected purchases of aluminum, PET resin, diesel fuel and unleaded gasoline in order to mitigate commodity risk. The Company accounts for commodity hedges on a mark-to-market basis.
- (6) Includes adjustments related to the Tax Act and other items impacting the Company's effective tax rate.
- (7) Adjustment reflects severance and outplacement expenses relating to the Company's optimization of its labor expense.
- (8) Concurrent with entering into the CBA on March 31, 2017, the Company converted its franchise rights for the territories the Company served prior to the System Transformation to distribution rights, to be amortized over an estimated useful life of 40 years. Adjustment reflects the net amortization expense in the first quarter of 2018 associated with the conversion of the Company's franchise rights.
- (9) Adjustment includes a charge within other income (expense), net for net working capital and other fair value adjustments related to the Company's acquisitions in the January 2016 Transactions, as part of the System Transformation, that were made beyond one year from the acquisition date.

Financial Condition

Total assets were \$3.07 billion on September 30, 2018, which was a decrease of \$0.5 million from December 31, 2017. Net working capital, defined as current assets less current liabilities, was \$286.6 million on September 30, 2018, which was an increase of \$131.5 million from December 31, 2017.

Significant changes in net working capital on September 30, 2018 from December 31, 2017 were as follows:

- An increase in accounts receivable, trade of \$36.4 million primarily as a result of the timing of cash receipts.
- A decrease in accounts receivable, other of \$10.3 million primarily as a result of the timing of payments received for marketing funding and rebates.
- An increase in inventories of \$46.3 million primarily as a result of rising commodity costs and expanded product selection offered by the Company.
- A decrease in prepaid and other current assets of \$9.1 million primarily as a result of a decrease in the current portion of income taxes.
- A decrease in accounts payable, trade of \$10.3 million primarily as a result of the timing of payments.
- A decrease in accounts payable to The Coca Cola Company of \$28.2 million primarily as a result of the timing of purchases of raw materials and payments.

- A decrease in other accrued liabilities of \$31.9 million primarily as a result of the timing of payments.
- A decrease in accrued compensation of \$14.8 million primarily as a result of the timing of bonus and incentive payments in the first quarter of the fiscal year.

Liquidity and Capital Resources

Capital Resources

The Company's sources of capital include cash flows from operations, available credit facilities and the issuance of debt and equity securities. The Company has obtained the majority of its long-term debt, other than capital leases, from public markets, private placements and bank facilities. Management believes the Company has sufficient sources of capital available to refinance its maturing debt, finance its business plan, meet its working capital requirements and maintain an appropriate level of capital spending for at least the next 12 months from the issuance of these consolidated condensed financial statements. The amount and frequency of future dividends will be determined by the Company's Board of Directors in light of the earnings and financial condition of the Company at such time, and no assurance can be given that dividends will be declared or paid in the future.

On June 8, 2018, the Company entered into a second amended and restated credit agreement for a five-year unsecured revolving credit facility (as amended, the "Revolving Credit Facility"), which amended and restated its prior credit agreement dated October 16, 2014. The Revolving Credit Facility has an aggregate maximum borrowing capacity of \$500 million, which may be increased at the Company's option to \$750 million, subject to obtaining commitments from the lenders and satisfying other conditions specified in the credit agreement. Borrowings under the Revolving Credit Facility bear interest at a floating base rate or a floating Eurodollar rate, at the Company's option, plus an applicable margin dependent on the Company's credit ratings. At the Company's current credit ratings,

the Company must pay an annual facility fee of 0.15% of the lenders' aggregate commitments under the Revolving Credit Facility. The Revolving Credit Facility has a scheduled maturity date of June 8, 2023. As of September 30, 2018, the Company had borrowed \$170.0 million under the Revolving Credit Facility, and therefore had \$330.0 million borrowing capacity remaining. The Company currently believes all banks participating in the Revolving Credit Facility have the ability to and will meet any funding requests from the Company.

On March 21, 2018, the Company sold \$150 million aggregate principal amount of senior unsecured notes due 2030 to NYL Investors LLC ("NYL") and certain of its affiliates pursuant to the Note Purchase and Private Shelf Agreement dated March 6, 2018 between the Company, NYL and the other parties thereto (as amended, the "NYL Shelf Facility"). These notes bear interest at 3.96%, payable quarterly in arrears on March 21, June 21, September 21 and December 21 of each year, and will mature on March 21, 2030 unless earlier redeemed by the Company. The Company used the proceeds for general corporate purposes.

In February 2017, the Company sold \$125 million aggregate principal amount of senior unsecured notes due 2023 to PGIM, Inc. ("Prudential") and certain of its affiliates pursuant to the Note Purchase and Private Shelf Agreement dated June 10, 2016 between the Company, Prudential and the other parties thereto (as amended, the "Prudential Shelf Facility"). These notes bear interest at 3.28%, payable semi-annually in arrears on February 27 and August 27 of each year, and will mature on February 27, 2023 unless earlier redeemed by the Company. The Company used the proceeds toward repayment of outstanding indebtedness under the Revolving Credit Facility and for other general corporate purposes. The Company may request that Prudential consider the purchase of additional senior unsecured notes of the Company under the Prudential Shelf Facility in an aggregate principal amount of up to \$175 million.

In June 2016, the Company entered into a five-year term loan agreement for a senior unsecured term loan facility (as amended, the "Term Loan Facility") in the aggregate principal amount of \$300 million, maturing June 7, 2021. The Company may request additional term loans under the agreement, provided the Company's aggregate borrowings under the Term Loan Facility do not exceed \$500 million. Borrowings under the Term Loan Facility bear interest at a floating base rate or a floating Eurodollar rate, at the Company's option, plus an applicable margin dependent on the Company's credit ratings.

During the third quarter of 2018, the Company amended each of the Revolving Credit Facility, the NYL Shelf Facility, the Prudential Shelf Facility and the Term Loan Facility to (i) align the calculation of the two financial covenants and certain events of default under each agreement and (ii) with regard to the Term Loan Facility, to revise the calculation of the rates at which borrowings bear interest to conform with the calculation of such rates under the Revolving Credit Facility.

Pursuant to the Term Loan Facility and the indenture under which the senior notes due in 2019 were issued, principal payments will be due in the next twelve months. The Company intends to refinance these amounts and has the capacity to do so under the Revolving Credit Facility, which is classified as long-term debt. As such, any amounts due in the next twelve months were classified as non-current as of September 30, 2018. See Note 11 to the consolidated

condensed financial statements for additional information on the senior notes due in 2019.

The Revolving Credit Facility, the NYL Shelf Facility, the Prudential Shelf Facility and the Term Loan Facility include two financial covenants: a consolidated cash flow/fixed charges ratio and a consolidated funded indebtedness/cash flow ratio, each as defined in the respective agreements. The Company was in compliance with these covenants as of September 30, 2018. These covenants do not currently, and the Company does not anticipate they will, restrict its liquidity or capital resources.

The indentures under which the Company's public debt was issued do not include financial covenants but do limit the incurrence of certain liens and encumbrances as well as indebtedness by the Company's subsidiaries in excess of certain amounts.

All outstanding long-term debt has been issued by the Company and none has been issued by any of its subsidiaries. There are no guarantees of the Company's debt.

The Company's credit ratings are reviewed periodically by the respective rating agencies. Changes in the Company's operating results or financial position could result in changes in the Company's credit ratings. Lower credit ratings could result in higher borrowing costs for the Company or reduced access to capital markets, which could have a material impact on the Company's financial position or results of operations. During the second quarter of 2018, Standard & Poor's reaffirmed the Company's BBB rating and revised the Company's rating outlook to negative from stable. Moody's rating outlook for the Company is currently stable. As of September 30, 2018, the Company's credit ratings were as follows:

| | Long-Term Debt |
|-------------------|----------------|
| Standard & Poor's | BBB |
| Moody's | Baa2 |

Total net debt and capital lease obligations as of September 30, 2018 and December 31, 2017 were as follows:

| (in thousands) | September 30, 2018 | December 31, 2017 |
|---|-----------------------|----------------------|
| Debt | \$ 1,194,109 | \$ 1,088,018 |
| Capital lease obligations | 37,278 | 43,469 |
| Total debt and capital lease obligations | 1,231,387 | 1,131,487 |
| Less: Cash and cash equivalents | 9,337 | 16,902 |
| Total net debt and capital lease obligations ⁽¹⁾ | \$ 1,222,050 | \$ 1,114,585 |

⁽¹⁾The non-GAAP measure “Total net debt and capital lease obligations” is used to provide investors with additional information which management believes is helpful in the evaluation of the Company’s capital structure and financial leverage. This non-GAAP financial information is not presented elsewhere in this report and may not be comparable to the similarly titled measures used by other companies. Additionally, this information should not be considered in isolation or as a substitute for performance measures calculated in accordance with GAAP.

The Company is subject to interest rate risk on its floating rate debt, including the Revolving Credit Facility and the Term Loan Facility. Assuming no changes in the Company’s financial structure, if market interest rates average 1% more over the next twelve months than the interest rates as of September 30, 2018, interest expense for the next twelve months would increase by approximately \$4.6 million.

The Company’s only Level 3 asset or liability is the acquisition related contingent consideration liability incurred as a result of the System Transformation Transactions. There were no transfers from Level 1 or Level 2. Fair value adjustments were noncash, and therefore did not impact the Company’s liquidity or capital resources. Following is a summary of the Level 3 activity:

| (in thousands) | Third Quarter | | First Three Quarters | |
|---|---------------|-----------|----------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Beginning balance - Level 3 liability | \$374,537 | \$319,102 | \$381,291 | \$253,437 |
| Increase due to System Transformation Transactions acquisitions | - | - | - | 46,086 |
| Measurement period adjustments ⁽¹⁾ | (1,279) | - | 813 | - |
| Payment of acquisition related contingent consideration | (7,049) | (5,094) | (18,312) | (11,650) |
| Reclassification to current payables | - | 150 | (1,540) | (2,080) |
| (Favorable)/unfavorable fair value adjustment | (2,373) | (5,225) | 1,584 | 23,140 |
| Ending balance - Level 3 liability | \$363,836 | \$308,933 | \$363,836 | \$308,933 |

⁽¹⁾Measurement period adjustments relate to post-closing adjustments made in relation to the April 2017 Transactions and the October 2017 Transactions in accordance with the terms and conditions of the applicable asset purchase agreement or asset exchange agreement. See Note 3 to the consolidated condensed financial statements for additional information on the April 2017 Transactions and the October 2017 Transactions.

Cash Sources and Uses

The primary sources of cash for the Company in the first three quarters of 2018 were debt financings. The primary uses of cash in the first three quarters of 2018 were repayments of debt and additions to property, plant and equipment. The primary sources of cash for the Company in the first three quarters of 2017 were debt financings, the Territory Conversion Fee (as defined below) received from The Coca Cola Company and operating activities. The primary uses of cash in the first three quarters of 2017 were repayments of debt, acquisitions of territories and regional manufacturing facilities as part of the System Transformation and additions to property, plant and equipment. A summary of cash-based activity is as follows:

| (in thousands) | First Three Quarters | |
|---|----------------------|-------------------|
| | 2018 | 2017 |
| Cash Sources: | | |
| Borrowings under Revolving Credit Facility | \$285,000 | \$333,000 |
| Proceeds from issuance of Senior Notes | 150,000 | 125,000 |
| Territory Conversion Fee ⁽¹⁾ | - | 87,066 |
| Adjusted cash provided by operating activities ⁽²⁾ | 26,030 | 141,672 |
| Refund of income tax payments | 23,573 | - |
| System Transformation acquisitions, net of cash acquired and purchase price settlements | 1,811 | - |
| Proceeds from cold drink equipment | 3,789 | 8,400 |
| Proceeds from the sale of property, plant and equipment | 3,555 | 493 |
| Other | 17 | 66 |
| Total cash sources | \$493,775 | \$695,697 |
| Cash Uses: | | |
| Payments on Revolving Credit Facility | \$322,000 | \$238,000 |
| System Transformation acquisitions, net of cash acquired and purchase price settlements | - | 227,769 |
| Additions to property, plant and equipment (exclusive of acquisitions) | 113,104 | 114,953 |
| Prepayment of funds for October 2017 Expansion Transactions | - | 56,498 |
| Pension plans contributions | 20,000 | 11,600 |
| Glacéau distribution agreement consideration | - | 15,598 |
| Payment of acquisition related contingent consideration | 18,312 | 11,650 |
| Payment on Term Loan Facility | 7,500 | - |
| Cash dividends paid | 7,014 | 6,995 |
| Principal payments on capital lease obligations | 6,191 | 5,594 |
| Income tax payments | 3,590 | 14,779 |
| Investment in CONA Services LLC | 2,098 | 1,976 |
| Debt issuance fees | 1,531 | 213 |
| Total cash uses | \$501,340 | \$705,625 |
| Net decrease in cash | \$(7,565) | \$(9,928) |

⁽¹⁾This one-time fee (the “Territory Conversion Fee”) was paid to the Company upon the conversion of the Company’s then-existing bottling agreements to the CBA in March 2017 pursuant to a territory conversion agreement entered into by the Company, The Coca Cola Company and CCR in September 2015, as amended. The Territory Conversion

Fee was equivalent to 0.5 times the EBITDA the Company and its subsidiaries generated during the twelve-month period ended January 1, 2017 from sales in the territories it served prior to the System Transformation of certain beverages owned by or licensed to The Coca Cola Company or Monster Energy Company on which the Company and its subsidiaries pay a facilitation fee to The Coca Cola Company.

- (2) Adjusted cash provided by operating activities excludes amounts received with regard to the Territory Conversion Fee, net income tax payments/refunds and pension plan contributions. This line item is a non-GAAP measure and provides investors with additional information which management believes is helpful in the evaluation of the Company's cash sources and uses. This non-GAAP financial information is not presented elsewhere in this report and may not be comparable to the similarly titled measures used by other companies. Additionally, this information should not be considered in isolation or as a substitute for performance measures calculated in accordance with GAAP.

Cash Flows From Operating Activities

During the first three quarters of 2018, cash provided by operating activities was \$26.0 million, which was a decrease of \$176.4 million as compared to the first three quarters of 2017. The decrease was primarily a result of the non-reoccurrence of the Territory Conversion Fee, which was received during the first quarter of 2017, and changes in net working capital, as discussed above.

Cash Flows From Investing Activities

During the first three quarters of 2018, cash used in investing activities was \$106.0 million, which was a decrease of \$301.9 million as compared to the first three quarters of 2017. The decrease was driven primarily by the Company's completion of its System Transformation Transactions in October 2017.

Additions to property, plant and equipment were \$113.1 million during the first three quarters of 2018. As of September 30, 2018, \$4.1 million of additions to property, plant and equipment were accrued in accounts payable, trade. The Company anticipates additions to property, plant and equipment for the remainder of 2018 will be in the range of \$25 million to \$35 million.

Additions to property, plant and equipment during the first three quarters of 2017 were \$115.0 million. As of October 1, 2017, \$13.7 million of additions to property, plant and equipment were accrued in accounts payable, trade. These additions exclude \$161.2 million in property, plant and equipment acquired in System Transformation Transactions and \$8.4 million in proceeds from cold drink equipment.

Cash Flows From Financing Activities

During the first three quarters of 2018, cash provided by financing activities was \$72.5 million, which was a decrease of \$123.0 million as compared to the first three quarters of 2017. The decrease was primarily driven by a reduced need for capital as a result of the Company's completion of its System Transformation Transactions in October 2017.

The Company had cash payments for acquisition related contingent consideration of \$18.3 million during the first three quarters of 2018 and \$11.7 million during the first three quarters of 2017. The Company anticipates that the amount it could pay annually under the acquisition related contingent consideration arrangements for the distribution territories acquired in the System Transformation, excluding territories the Company acquired in exchange

transactions, will be in the range of \$25 million to \$47 million.

Significant Accounting Policies

See Note 1 and Note 2 to the consolidated condensed financial statements for information on the Company's significant accounting policies.

Off-Balance Sheet Arrangements

The Company is a member of, and has equity ownership in, South Atlantic Cannery, Inc. ("SAC"), a manufacturing cooperative comprised of Coca Cola bottlers, and has guaranteed \$23.9 million of SAC's debt as of September 30, 2018. The Company does not anticipate SAC will fail to fulfill its commitments related to the debt. The Company further believes SAC has sufficient assets, including production equipment, facilities and working capital, and the ability to adjust selling prices of its products to adequately mitigate the risk of material loss from the Company's guarantee.

In the event SAC fails to fulfill its commitments under the related debt, the Company would be responsible for payment to the lenders up to the level of the guarantee. As of September 30, 2018, the Company's maximum exposure under the guarantee, if SAC borrowed up to its aggregate borrowing capacity, would have been \$32.1 million, including the Company's equity interests. See Note 15 to the consolidated condensed financial statements for additional information.

Hedging Activities

The Company uses derivative financial instruments to manage its exposure to movements in certain commodity prices. Fees paid by the Company for derivative instruments are amortized over the corresponding period of the instrument. The Company accounts for its commodity hedges on a mark-to-market basis with any expense or income reflected as an adjustment to cost of sales or S,D&A expenses.

The Company uses several different financial institutions for commodity derivative instruments to minimize the concentration of credit risk. The Company has master agreements with the counterparties to its derivative financial agreements that provide for net

settlement of derivative transactions. The net impact of the commodity hedges on the consolidated condensed statements of operations was as follows:

| (in thousands) | Third Quarter | | First Three Quarters | |
|--------------------------------------|---------------|-----------|----------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Cost of sales - increase/(decrease) | \$640 | \$(2,446) | \$2,843 | \$(3,015) |
| S,D&A expenses - increase/(decrease) | 50 | (1,575) | (305) | (591) |
| Net impact | \$690 | \$(4,021) | \$2,538 | \$(3,606) |

Cautionary Information Regarding Forward-Looking Statements

Certain statements contained in this report, or in other public filings, press releases, or other written or oral communications made by Coca Cola Bottling Co. Consolidated or its representatives, which are not historical facts, are forward-looking statements subject to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements address, among other things, Company plans, activities or events which the Company expects will or may occur in the future and may include express or implied projections of revenue or expenditures statements of plans and objectives for future operations, growth or initiatives statements of future economic performance, including, but not limited to, the state of the economy, capital investment and financing plans, net sales, cost of sales, S,D&A expenses, gross profit, income tax rates, earnings per diluted share, dividends, pension plan contributions, estimated acquisition related contingent consideration payments or statements regarding the outcome or impact of certain new accounting pronouncements and pending or threatened litigation. These statements include:

- the Company's beliefs and estimates regarding the impact of the adoption of certain new accounting pronouncements;
- the Company's expectations that the adoption of Accounting Standards Update 2016-02 "Leases," (i) will have a material impact on its consolidated condensed balance sheets and (ii) will not have a material impact on its consolidated condensed statements of cash flows as the new guidance is non-cash in nature;
- the Company's expectation that certain amounts of goodwill will, or will not, be deductible for tax purposes;
- the Company's belief that, at any given time, less than 1% of bottle/can sales and post-mix sales could be at risk for return by customers;
- the Company's belief that SAC, whose debt the Company guarantees, has sufficient assets and the ability to adjust selling prices of its products to adequately mitigate the risk of material loss from the Company's guarantee and that the cooperative will perform its obligations under its debt commitments;
- the Company's belief that it has, and that other manufacturers from whom the Company purchases finished goods have, adequate production capacity to meet sales demand for sparkling and still beverages during peak periods;
- the Company's belief that the ultimate disposition of various claims and legal proceedings which have arisen in the ordinary course of its business will not have a material adverse effect on its financial condition, cash flows or results of operations and that no material amount of loss in excess of recorded amounts is reasonably possible as a result of these claims and legal proceedings;
- the Company's belief that it is competitive in its territories with respect to the principal methods of competition in the nonalcoholic beverage industry;

- the Company's belief that certain non-GAAP financial measures provide users with additional meaningful financial information that should be considered when assessing the Company's ongoing performance, including information which the Company believes is helpful in the evaluation of its cash sources and uses, capital structure and financial leverage;
- the Company's belief that it has sufficient sources of capital available to refinance its maturing debt, finance its business plan, meet its working capital requirements and maintain an appropriate level of capital spending for at least the next 12 months;
- the Company's belief that all the banks participating in the Revolving Credit Facility have the ability to and will meet any funding requests from the Company;
- the Company's intention to refinance amounts due in the next twelve months under the Term Loan Facility and the indenture under which the senior notes due in 2019 were issued using the capacity under the Revolving Credit Facility;
- the Company's estimate of the useful lives of certain acquired intangible assets and property, plant and equipment;
- the Company's estimate that a 10% increase in the market price of certain commodities included as part of its raw materials over the current market prices would cumulatively increase costs during the next 12 months by approximately \$56.5 million, assuming no change in volume;
- the Company's expectation that amounts due to United relating to the System Transformation exchange transaction between the Company and United will be paid by the Company during the fourth quarter of 2018;
- the Company's expectation that the amount of uncertain tax positions may change over the next 12 months but that such changes will not have a significant impact on the consolidated condensed financial statements;

- the Company's belief that the ultimate impact of the Tax Act could differ from the Company's estimates, possibly materially, due to, among other things, the significant complexity of the Tax Act, anticipated additional regulatory guidance or related interpretations that may be issued by the Internal Revenue Service, changes in accounting standards, legislative actions, future actions by states within the U.S. and changes in estimates, analysis, interpretations and assumptions made by the Company;
- the Company's belief that innovation of both new brands and packages will continue to be important to the Company's overall revenue;
- the Company's estimates of certain inputs used in its calculations, including estimated rates of return, estimates of bad debts and amounts that will ultimately be collected, and estimates of inputs used in the calculation and adjustment of the fair value of its acquisition related contingent consideration liability related to the distribution territories acquired as part of the System Transformation, such as the amounts that will be paid by the Company in the future under the CBA and the Company's WACC;
- the Company's expectation that certain territories of CCR will be sold to bottlers that are neither members of CONA nor users of the CONA System;
- the Company's belief that the range of undiscounted amounts it could pay annually under the acquisition related contingent consideration arrangements for the System Transformation Transactions is expected to be between \$25 million to \$47 million;
- the Company's belief that the covenants in the Revolving Credit Facility, the Term Loan Facility, the Prudential Shelf Facility and the NYL Shelf Facility will not restrict its liquidity or capital resources;
- the Company's belief that other parties to certain of its contractual arrangements will perform their obligations;
- the Company's expectation that it will not make additional contributions to the two Company-sponsored pension plans during the fourth quarter of 2018;
- the Company's expectation that it will not withdraw from its participation in the Employers-Teamsters Local Union Nos. 175 and 505 Pension Fund (the "Teamsters Plan");
- the Company's expectation that the collective bargaining agreements covering the Teamsters Plan that expire at various times through April 2020 will be re-negotiated;
- the Company's belief that System Transformation expenses will be in the range of \$6 million to \$8 million in the fourth quarter of 2018 and will decrease over the next few quarters;
- the Company's belief that additions to property, plant and equipment for the remainder of 2018 are expected to be in the range of \$25 million to \$35 million;
- the Company's belief that, while the addition of BodyArmor products to the Company's portfolio of brands will not have a material impact on the Company's 2018 results, BodyArmor will provide ongoing benefits and round out the Company's sports drink portfolio;
- the Company's belief that it has adequately provided for any assessments likely to result from audits by tax authorities in the jurisdictions in which the Company conducts business;
- the Company's belief that key priorities include territory and manufacturing integration, revenue management, product innovation and beverage portfolio expansion, distribution cost management and productivity; and
 - the Company's hypothetical calculation that, if market interest rates average 1% more over the next twelve months than the interest rates as of September 30, 2018, interest expense for the next twelve months would increase by approximately \$4.6 million, assuming no changes in the Company's financial structure.

These forward-looking statements may be identified by the use of the words "believe," "plan," "estimate," "expect," "anticipate," "probably," "should," "project," "intend," "continue," and other similar terms and expressions. Various risks, uncertainties and other factors may cause the Company's actual results to differ materially from those expressed or implied in any forward-looking statements. Factors, uncertainties and risks that may result in actual results differing from such forward-looking information include, but are not limited to, those listed in Part I, "Item 1A. Risk Factors" of our Annual Report on Form 10-K for 2017, as well as other factors discussed throughout this report, including, without limitation, the factors described under "Significant Accounting Policies" in our consolidated condensed financial statements, or in

other filings or statements made by the Company. All of the forward-looking statements in this report and other documents or statements are qualified by these and other factors, risks and uncertainties.

Caution should be taken not to place undue reliance on the forward-looking statements included in this report. The Company assumes no obligation to update any forward-looking statements, even if experience or future changes make it clear that projected results expressed or implied in such statements will not be realized, except as may be required by law. In evaluating forward-looking statements, these risks and uncertainties should be considered, together with the other risks described from time to time in the Company's other reports and documents filed with the Securities and Exchange Commission.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

The Company is exposed to certain market risks that arise in the ordinary course of business. The Company may enter into derivative financial instrument transactions to manage or reduce market risk. The Company does not enter into derivative financial instrument transactions for trading or speculative purposes. A discussion of the Company's primary market risk exposure and interest rate risk is presented below.

Debt and Derivative Financial Instruments

The Company is subject to interest rate risk on its floating rate debt, including the Revolving Credit Facility and the Term Loan Facility. Assuming no changes in the Company's financial structure, if market interest rates average 1% more over the next twelve months than the interest rates as of September 30, 2018, interest expense for the next twelve months would increase by approximately \$4.6 million. This amount was determined by calculating the effect of the hypothetical interest rate on the Company's variable rate debt. This calculated, hypothetical increase in interest expense for the following twelve months may be different from the actual increase in interest expense from a 1% increase in interest rates due to varying interest rate reset dates on the Company's floating debt.

The Company's acquisition related contingent consideration, which is adjusted to fair value at each reporting period, is also impacted by changes in interest rates. The risk-free interest rate used to estimate the Company's WACC is a component of the discount rate used to calculate the present value of future cash flows due under the CBA. As a result, any changes in the underlying risk-free interest rates will impact the fair value of the acquisition related contingent consideration and could materially impact the amount of noncash expense (or income) recorded each reporting period.

Raw Material and Commodity Price Risk

The Company is also subject to commodity price risk arising from price movements for certain commodities included as part of its raw materials. The Company manages this commodity price risk in some cases by entering into contracts with adjustable prices to hedge commodity purchases. The Company periodically uses derivative commodity instruments in the management of this risk. The Company estimates a 10% increase in the market prices of commodities included as part of its raw materials over the current market prices would cumulatively increase costs during the next 12 months by approximately \$56.5 million assuming no change in volume.

Fees paid by the Company for agreements to hedge commodity purchases are amortized over the corresponding period of the instruments. The Company accounts for commodity hedges on a mark-to-market basis with any expense

or income being reflected as an adjustment to cost of sales or S,D&A expenses.

Effects of Changing Prices

The annual rate of inflation in the United States, as measured by year-over-year changes in the Consumer Price Index (the "CPI"), was 2.1% in 2017 and 2016. Inflation in the prices of those commodities important to the Company's business is reflected in changes in the CPI, but commodity prices are volatile and in recent years have moved at a faster rate of change than the CPI.

The principal effect of inflation in both commodity and consumer prices on the Company's operating results is to increase costs, both of goods sold and S,D&A expenses. Although the Company can offset these cost increases by increasing selling prices for its products, consumers may not have the buying power to cover these increased costs and may reduce their volume of purchases of those products. In that event, selling price increases may not be sufficient to offset completely the Company's cost increases.

Item 4.Controls and Procedures.

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's "disclosure controls and procedures" (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")), pursuant to Rule 13a-15(b) of the Exchange Act. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2018.

There has been no change in the Company's internal control over financial reporting during the quarter ended September 30, 2018 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

The Company is from time to time a party to various lawsuits, claims and other legal proceedings that arise in the ordinary course of business. With respect to all such lawsuits, claims and proceedings, the Company records reserves when it is probable a liability has been incurred and the amount of loss can be reasonably estimated. The Company does not believe that any of these proceedings, individually or in the aggregate, would be expected to have a material adverse effect on its results of operations, financial position or cash flows. The Company maintains liability insurance for certain risks that is subject to certain self-insurance limits.

Item 1A. Risk Factors.

There have been no material changes in the Company's risk factors from those disclosed in Part I, "Item 1A. Risk Factors" in the Company's Annual Report on Form 10 K for 2017.

Item 6. Exhibits.

| Number | Description | Incorporated by Reference or Filed Herewith |
|--------|--|--|
| 3.1 | <u>Restated Certificate of Incorporation of the Company.</u> | Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended July 2, 2017 (File No. 0-9286). |
| 3.2 | <u>Amended and Restated Bylaws of the Company.</u> | Exhibit 3.1 to the Company's Current Report on Form 8-K filed on May 15, 2017 (File No. 0-9286). |
| 4.1 | The registrant, by signing this report, agrees to furnish the Securities and Exchange Commission, upon its request, a copy of any instrument which defines the rights of holders of long-term debt of the registrant and its consolidated subsidiaries which authorizes a total amount of securities not in excess of 10 percent of the total assets of the registrant and its subsidiaries on a consolidated basis. | |
| 10.1 | <u>Amendment No. 1 to Term Loan Agreement, dated July 11, 2018, by and among the Company, JPMorgan Chase Bank, N.A., as administrative agent, and the other lenders party thereto.</u> | Exhibit 10.1 to the Company's Current Report on Form 8-K filed on July 17, 2018 (File No. 0-9286). |
| 10.2 | <u>Amendment No. 1 to Second Amended and Restated Credit Agreement, dated July 11, 2018, by and among the Company, JPMorgan Chase Bank, N.A., as administrative agent, and the other lenders party thereto.</u> | Exhibit 10.2 to the Company's Current Report on Form 8-K filed on July 17, 2018 (File No. 0-9286). |
| 10.3 | <u>First Amendment to Note Purchase and Private Shelf Agreement, dated July 20, 2018, by and among the Company, PGIM, Inc. and the other parties thereto.</u> | Exhibit 10.1 to the Company's Current Report on Form 8-K filed on July 25, 2018 (File No. 0-9286). |
| 10.4 | <u>First Amendment to Note Purchase and Private Shelf Agreement, dated July 20, 2018, by and among the Company, NYL Investors LLC and the other parties thereto.</u> | Exhibit 10.2 to the Company's Current Report on Form 8-K filed on July 25, 2018 (File No. 0-9286). |
| 10.5* | <u>Fifth Amendment to Comprehensive Beverage Agreement, dated August 20, 2018, by and between the Company, The Coca-Cola Company and Coca-Cola Refreshments USA, Inc.</u> | Filed herewith. |
| 31.1 | <u>Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u> | Filed herewith. |
| 31.2 | | Filed herewith. |

Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

| | | |
|-----|---|---|
| 32 | <u>Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u> | Furnished (and not filed) herewith pursuant to Item 601(b)(32)(ii) of Regulation S-K. |
| 101 | Financial statements (unaudited) from the quarterly report on Form 10-Q of Coca Cola Bottling Co. Consolidated for the quarter ended September 30, 2018, filed on November 8, 2018, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Condensed Statements of Operations; (ii) the Consolidated Condensed Statements of Comprehensive Income; (iii) the Consolidated Condensed Balance Sheets; (iv) the Consolidated Condensed Statements of Changes in Equity; (v) the Consolidated Condensed Statements of Cash Flows and (vi) the Notes to the Consolidated Condensed Financial Statements. | |

* Certain portions of this exhibit have been omitted pursuant to a request for confidential treatment filed with the Securities and Exchange Commission.

SIGNATURES

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

COCA COLA BOTTLING CO. CONSOLIDATED
(REGISTRANT)

Date: November 8, 2018 By: /s/ David M. Katz
David M. Katz
Executive Vice President and Chief Financial Officer
(Principal Financial Officer of the Registrant)

Date: November 8, 2018 By: /s/ William J. Billiard
William J. Billiard
Senior Vice President and Chief Accounting Officer
(Principal Accounting Officer of the Registrant)