

QUEST RESOURCE HOLDING CORP

FORM 10-Q (Quarterly Report)

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**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 March 31, 2014

Commission file number: 001-36451

Quest Resource Holding Corporation
(Exact Name of Registrant as Specified in Its Charter)

Nevada
(State or Other Jurisdiction of
Incorporation or Organization)

51-0665952
(I.R.S. Employer
Identification No.)

6175 Main Street, Suite 420
Frisco, Texas 75034
(Address of Principal Executive Offices and Zip Code)

(972) 464-0004
(Registrant's Telephone Number, Including Area Code)

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

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

As of May 1, 2014, there were outstanding 97,030,266 shares of the registrant's common stock, \$0.001 par value.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	March 31, 2014 (Unaudited)	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,082,168	\$ 2,676,984
Accounts receivable, less allowance for doubtful accounts of \$360,938 and \$319,735 as of March 31, 2014 and December 31, 2013, respectively	21,593,210	20,849,140
Inventory	7,584	3,251
Prepaid expenses and other assets	545,687	401,537
Total current assets	23,228,649	23,930,912
Property and equipment, net	582,617	645,485
Goodwill	58,337,290	58,337,290
Intangible assets, net	16,832,292	17,636,964
Security deposits and other assets	95,560	95,892
Total assets	<u>\$ 99,076,408</u>	<u>\$100,646,543</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Line of credit	\$ 4,750,000	\$ 2,750,000
Accounts payable	21,416,280	23,589,755
Accrued liabilities	2,042,833	2,673,770
Deferred revenue	342,913	234,899
Long-term debt and capital lease obligations—current portion	16,224	16,096
Convertible notes payable—short term	—	25,000
Total current liabilities	28,568,250	29,289,520
Long-term capital lease obligations, less current maturities	28,987	33,067
Long-term senior secured convertible notes—related parties, net of discount \$4,205,292 and \$4,656,934 as of March 31, 2014 and December 31, 2013, respectively	17,794,708	17,343,066
Total liabilities	<u>46,391,945</u>	<u>46,665,653</u>
Commitments and Contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value, 10,000,000 shares authorized, no shares issued or outstanding as of March 31, 2014 and December 31, 2013, respectively	—	—
Common stock, \$0.001 par value, 200,000,000 shares authorized, 95,837,766 and 95,814,565 shares issued and outstanding as of March 31, 2014 and December 31, 2013, respectively	95,838	95,815
Additional paid-in capital	119,602,750	119,410,777
Accumulated deficit	(67,014,125)	(65,525,702)
Total stockholders' equity	52,684,463	53,980,890
Total liabilities and stockholders' equity	<u>\$ 99,076,408</u>	<u>\$100,646,543</u>

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

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	For the Three Months Ended March 31,	
	2014	2013
Revenue	\$ 38,160,050	\$ 313,489
Cost of revenue	34,827,635	39,693
Gross profit	<u>3,332,415</u>	<u>273,796</u>
Operating expenses:		
Selling, general and administrative	2,993,708	2,258,802
Depreciation and amortization	951,663	14,980
Total operating expenses	<u>3,945,371</u>	<u>2,273,782</u>
Operating loss	(612,956)	(1,999,986)
Other expense:		
Interest expense	(875,467)	(308,414)
Financing cost for senior secured convertible notes—related parties	—	(1,465,000)
Total other expense, net	<u>(875,467)</u>	<u>(1,773,414)</u>
Loss before taxes and equity income	(1,488,423)	(3,773,400)
Equity in Quest Resource Management Group, LLC income	—	475,796
Loss before taxes	(1,488,423)	(3,297,604)
Income tax expense	—	—
Net loss	<u>\$ (1,488,423)</u>	<u>\$ (3,297,604)</u>
Net loss applicable to common stockholders	<u>\$ (1,488,423)</u>	<u>\$ (3,297,604)</u>
Net loss per share		
Basic and diluted	<u>\$ (0.02)</u>	<u>\$ (0.06)</u>
Weighted average number of common shares outstanding		
Basic and diluted	<u>95,821,525</u>	<u>57,961,106</u>

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

QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE THREE MONTHS ENDED MARCH 31, 2014
(UNAUDITED)

	<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Accumulated Deficit</u>	<u>Total Stockholders' Equity</u>
	<u>Shares</u>	<u>Par Value</u>			
Balances, December 31, 2013	95,814,565	\$ 95,815	\$119,410,777	\$(65,525,702)	\$53,980,890
Stock-based compensation expense	—	—	162,995	—	162,995
Shares issued upon conversion of note	23,201	23	28,978	—	29,001
Net loss	—	—	—	(1,488,423)	(1,488,423)
Balances, March 31, 2014	<u>95,837,766</u>	<u>\$ 95,838</u>	<u>\$119,602,750</u>	<u>\$(67,014,125)</u>	<u>\$52,684,463</u>

The accompanying notes are an integral part of this consolidated statement.

QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three Months Ended March 31,	
	2014	2013
Cash flows from operating activities:		
Net loss	\$ (1,488,423)	\$ (3,297,604)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	69,567	14,980
Amortization of intangibles	882,096	—
Amortization of debt discount and deferred financing costs	451,642	259,690
Equity in Quest Resource Management Group, LLC income	—	(475,796)
Provision (benefit) for doubtful accounts	41,338	(436)
Stock-based compensation	162,995	784,105
Financing costs for senior convertible notes—related parties	—	1,465,000
Changes in operating assets and liabilities:		
Accounts receivable	(785,408)	59,600
Inventory	(4,333)	1,383
Prepaid expenses and other assets	(144,150)	(9,049)
Security deposits and other assets	332	63,626
Accounts payable	(2,173,475)	38,577
Accrued liabilities	(626,936)	57,912
Deferred revenue	108,014	88,749
Net cash used in operating activities	<u>(3,506,741)</u>	<u>(949,263)</u>
Cash flows from investing activities:		
Purchase of property and equipment	(6,698)	(4,114)
Capitalized software development	(77,425)	—
Distributions received from Quest Resource Management Group, LLC	—	300,000
Net cash (used in) provided by investing activities	<u>(84,123)</u>	<u>295,886</u>
Cash flows from financing activities:		
Proceeds from senior related party secured convertible note	—	500,000
Proceeds from line of credit	2,000,000	—
Repayments capital lease obligations	(3,952)	(18,226)
Net cash provided by financing activities	<u>1,996,048</u>	<u>481,774</u>
Net decrease in cash and cash equivalents	<u>(1,594,816)</u>	<u>(171,603)</u>
Cash and cash equivalents at beginning of period	2,676,984	485,728
Cash and cash equivalents at end of period	<u>\$ 1,082,168</u>	<u>\$ 314,125</u>
Supplemental cash flow information:		
Cash paid for interest	\$ 423,826	\$ 56,269
Supplemental non-cash flow activities:		
Common stock issued for conversion of notes payable, including accrued interest	29,001	61,461
Common stock issued for services and loan fees	—	50,780
Common stock issued for warrants—cashless exercise	—	21,698,338
Discount to senior convertible note—related party	—	500,000

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

**QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

1. The Company and Description of Business and Future Liquidity Needs

The accompanying consolidated financial statements include the accounts of Quest Resource Holding Corporation (“QRHC”), formerly Infinity Resources Holdings Corp., and its subsidiaries, Earth911, Inc. (“Earth911”), Quest Resource Management Group, LLC (“Quest”), Landfill Diversion Innovations, LLC, and Youchange, Inc. (“YouChange”) (collectively, “QRHC”, the “Company”, “we”, “us”, or “our company”). On October 28, 2013, we changed our name to Quest Resource Holding Corporation, increased our shares of common stock authorized for issuance to 200,000,000, and changed our trading symbol to “QRHC.”

On July 16, 2013, we acquired the membership interests of Quest held by Quest Resource Group LLC (“QRG”), comprising 50% of Quest (the “Quest Interests”). Prior to July 16, 2013, our wholly owned subsidiary, Earth911, held the remaining 50% membership interest of Quest. Upon acquisition of the Quest Interests, we assigned the Quest Interests to Earth911 so that Earth911 now owns Quest and Quest is now our indirectly wholly owned subsidiary. We consolidated Quest in these financial statements for the quarter ended March 31, 2014.

Operations – We are an environmental solutions company that serves as a single-source provider of full service recycling and waste stream management solutions, as well as an environmental program services and information provider. We offer innovative, cost-effective, one-stop reuse, recycling, and waste disposal management programs designed to provide regional and national customers with a single point of contact for managing a variety of recyclables and disposables. We also own the *Earth911.com* website, offering original online environmental related content about reuse, recycling, and disposal of waste and recyclables, and we own a comprehensive online database of local recycling and proper disposal options. Our principal offices are located in Frisco, Texas.

Liquidity – During 2013, we restructured and relocated the operations of Earth911 and YouChange to reduce future operating expenses and streamline management. We expect the acquisition of the Quest Interests to provide increased cash flow from operations. In addition, we plan to increase working capital by increasing sales, maintaining efficient operating expenses, and through other initiatives.

Pro forma Three Months Ended March 31, 2013 Operating Results – As discussed above and in Note 10 to these financial statements, we previously accounted for Quest as an equity investment. On July 16, 2013, we acquired the remaining 50% membership interests of Quest and now hold 100% of the membership interests of Quest. The accompanying financial statements consolidate the results of operations of Quest for the quarter ended March 31, 2014.

The following table summarizes our pro forma consolidated operating results for the three months ended March 31, 2013, assuming Quest had been a wholly owned subsidiary and 100% of Quest’s operations were included in the relevant periods:

	Pro Forma Three Months Ended March 31,	
	2013	
	(Unaudited)	
Consolidated operating statement information:		
Net sales	\$	30,964,553
Gross profit		3,571,150
Income (loss) from operations		(924,938)
Net income (loss)		(2,821,808)

2. Summary of Significant Accounting Policies

Principals of Presentation, Consolidation, and Reclassifications

The consolidated financial statements included herein have been prepared by us without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and should be read in conjunction with the audited financial statements for the year ended December 31, 2013. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted, as permitted by the SEC, although we believe the disclosures that are made are adequate to make the information presented herein not misleading.

The accompanying consolidated financial statements reflect, in our opinion, all normal recurring adjustments necessary to present fairly our financial position at March 31, 2014, and the results of our operations and cash flows for the periods presented. We derived the December 31, 2013 consolidated balance sheet data from audited financial statements, but did not include all disclosures required by GAAP.

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Through July 16, 2013, Quest was deemed to be a separate operating unit and as such, there were no intercompany transactions that required elimination at that time. All other intercompany accounts and transactions have been eliminated in consolidation, including transactions between QRHC and Quest subsequent to July 16, 2013. Certain reclassifications have been made to prior year balances to conform to the current year presentation. Interim results are subject to seasonal variations, and the results of operations for the three months ended March 31, 2014 are not necessarily indicative of the results to be expected for the full year.

As Quest, Earth911, and YouChange are operating as ecology based green service companies, we did not deem segment reporting necessary.

Accounting Estimates

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could materially differ from those estimates.

We use significant estimates when accounting for the collectability of accounts receivable, depreciable lives of fixed assets, accruals, assumptions used in the valuation and recognition of share-based payments and warrant liability, the realization of goodwill and intangible assets, deferred tax assets, the equity method investment in Quest, and the application of accounting for the senior secured convertible notes, all of which are discussed in their respective notes to the consolidated financial statements.

Revenue Recognition

We recognize revenue only when all of the following criteria have been met:

- persuasive evidence of an arrangement exists;
- delivery has occurred or services have been rendered;
- the fee for the arrangement is fixed or determinable; and
- collectability is reasonably assured.

Persuasive Evidence of an Arrangement – We document all terms of an arrangement in a quote signed or confirmed by the customer prior to recognizing revenue.

Delivery Has Occurred or Services Have Been Performed – We perform all services or deliver all products prior to recognizing revenue. Services are deemed to be performed when the services are complete.

The Fee for the Arrangement is Fixed or Determinable – Prior to recognizing revenue, a customer's fee is either fixed or determinable under the terms of the quote or accepted customer purchase order.

Collectability Is Reasonably Assured – We assess collectability on a customer by customer basis based on criteria outlined by management.

Quest provides businesses with management programs to reuse, recycle, and dispose of a wide variety of waste streams and recyclables generated by their business. Quest utilizes third-party subcontractors to execute the collection, transport, and recycling or disposal of used motor oil, oil filters, scrap tires, cooking oil, and expired food products. We evaluate the criteria outlined in the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Subtopic 605-45, *Revenue Recognition—Principal Agent Considerations*, in determining whether it is appropriate to record the gross amount of service revenue and related costs or the net amount earned as management fees. Generally, when we are primarily obligated in a transaction, have latitude in establishing prices and selecting suppliers, have credit risk, or have several but not all of these indicators, we record revenue gross and record amounts collected from customers for sales tax on a net basis. In a situation where we are not primarily obligated and amounts earned are determined using a fixed percentage, a fixed-payment schedule, or a combination of the two, we would record the net amounts as management fees earned. Currently, we have no contracts accounted for as management fees.

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Earth911 revenue primarily represents licensing fees that are recognized ratably over the term of the license. We derive some revenue from advertising contracts, which we recognize ratably, over the term that the advertisement appears on our website.

Cash and Cash Equivalents

We consider all highly liquid instruments with a remaining maturity of three months or less when purchased to be cash equivalents.

Fair Value Measurements

ASC Topic 820, *Fair Value Measurements*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820 also specifies a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value as follows:

Level 1: Quoted prices in active markets for identical assets or liabilities;

Level 2: Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3: Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our own estimate of assumptions that market participants would use in pricing the asset or liability.

Fair value accounting has been applied to the valuation of stock-based compensation, warrants issued, intangible assets, and goodwill.

Stock Options – We estimate the fair value of stock options on the grant date in accordance with ASC Topic 718 using the Black-Scholes-Merton valuation model. Significant Level 3 assumptions used in the calculation are as follows:

- We determine the expected term using the simplified method for plain vanilla options by averaging the contractual term and vesting period of the award due to the unavailability of appropriate statistical data required to properly estimate the expected term in accordance with SEC Staff Accounting Bulletin No. 107;
- We measure expected volatility using the historical changes in the market price of our common stock, disregarding identifiable periods of extraordinarily volatile share prices due to certain events that are not expected to recur during the expected term;
- We use the risk-free interest rate to approximate the implied yield on zero-coupon U.S. Treasury bonds with a remaining maturity equal to the expected term of the awards; and
- We base forfeitures on the history of cancellations of options granted by us and our analysis of potential future forfeitures.

Net Loss Per Share

We compute basic net loss per share by dividing net loss attributable to common stockholders by the weighted average number of shares of common stock outstanding during the period. The calculation of basic loss per share gives retroactive effect to the recapitalization related to our reverse acquisition of Earth911. We have other potentially anti-dilutive securities outstanding that are not shown in a diluted net loss per share calculation because their effect in both 2014 and 2013 would be dilutive. These potentially dilutive securities include options, warrants, and convertible promissory notes totaled 15,096,948 and 11,782,240 shares at March 31, 2014 and 2013, respectively.

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

The following table sets forth the computation of basic and diluted loss per share:

	For the Three Months Ended March 31,	
	2014	2013
	(Unaudited)	(Unaudited)
Net loss applicable to common stockholders—numerator for basic and diluted earnings per share	\$ (1,488,423)	\$ (3,297,604)
Weighted—average common shares outstanding—denominator for basic and diluted earnings per share	95,821,525	57,961,106
Net loss per share:		
Basic and diluted	\$ (0.02)	\$ (0.06)

The following table sets forth the anti-dilutive securities excluded from diluted loss per share:

	As of March 31,	
	2014	2013
	(Unaudited)	(Unaudited)
Anti-dilutive securities excluded from diluted loss per share:		
Stock options	4,096,948	3,432,115
Warrants	—	1,381,113
Convertible notes	11,000,000	6,969,012
	<u>15,096,948</u>	<u>11,782,240</u>

Investment in Quest

Investee companies that are not consolidated, but over which we exercise significant influence, are accounted for under the equity method of accounting. Whether or not we exercise significant influence with respect to an investee depends on an evaluation of several factors, including, among others, representation on the investee company's board of directors and ownership level, which is generally a 20% to 50% interest in the voting securities of the investee company. Prior to July 17, 2013, we accounted for the investment in Quest under the equity method of accounting, in which the investee company's accounts were not consolidated within our consolidated balance sheet and statement of operations. We reflect our share of earnings or losses of the investee company in the caption "Equity in Quest Resource Management Group, LLC income" in our consolidated statement of operations. Subsequent to our acquisition of the Quest Interests, we consolidate the operational activity of Quest with QRHC.

Income Taxes

We recognize deferred tax assets and liabilities for the future tax consequences of temporary differences between the book and tax basis of assets and liabilities that will result in taxable or deductible amounts in the future, based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. We establish valuation allowances to reduce a deferred tax asset to the amount expected to be realized. We assess our ability to realize deferred tax assets based on current earnings performance and on projections of future taxable income in the relevant tax jurisdictions. These projections do not include taxable income from the reversal of deferred tax liabilities and do not reflect a general growth assumption but do consider known or pending events, such as the passage of legislation. We review our estimates of future taxable income annually. We first analyze all tax positions to determine if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of any related appeals or litigation processes. After the initial analysis, we measure the tax benefit as the largest amount that is more than 50% likely of being realized upon ultimate settlement. Our income tax returns are subject to adjustment under audit for approximately the last three years.

If we are required to pay interest on the underpayment of income taxes, we recognize interest expense in the first period the interest becomes due according to the provisions of the relevant tax law.

If we are subject to payment of penalties, we recognize an expense for the amount of the statutory penalty in the period when we take the position on the income tax return. If we did not recognize the penalty in the period when we initially took the position, we recognize the expense in the period when we change our judgment about meeting minimum statutory thresholds related to the initial position taken.

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Stock-Based Compensation

We expense all share-based grants to employees, including grants of employee stock options, based on their estimated fair values at grant date, in accordance with ASC Topic 718. We record compensation expense for stock options over the vesting period using the estimated fair value on the date of grant, as calculated using the Black-Scholes-Merton model. We classify all share-based awards as equity instruments and recognize the vesting of the awards ratably over their respective terms. See Note 13 for a description of our share-based compensation plan and information related to awards granted under the plan.

3. Inventories

As of March 31, 2014 and December 31, 2013, finished goods inventories were \$7,584 and \$3,251, respectively, and consisted of composite heaters, with no reserve for inventory obsolescence at either date.

4. Property and Equipment

At March 31, 2014 and December 31, 2013, property and equipment consisted of the following:

	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
	<u>(Unaudited)</u>	
Vehicles	\$ 544,984	\$ 544,984
Computer equipment	796,419	790,987
Office furniture and fixtures	240,929	239,662
Machinery and equipment	458,257	458,257
Leasehold improvements	12,363	12,363
	<u>2,052,952</u>	<u>2,046,253</u>
Less: accumulated depreciation	<u>(1,470,335)</u>	<u>(1,400,768)</u>
	<u>\$ 582,617</u>	<u>\$ 645,485</u>

We lease certain computer equipment under agreements that are classified as capital leases. The cost of equipment under these capital leases was \$50,470 and \$49,163 at March 31, 2014 and December 31, 2013, respectively, and we record it in the consolidated financial statements as property and equipment. Accumulated depreciation of the leased equipment at March 31, 2014 and December 31, 2013 was \$3,365, and \$1,402, respectively.

5. Intangible Assets

The components of intangible assets are as follows:

<u>March 31, 2014</u>	<u>Estimated</u> <u>Useful Life</u>	<u>Gross Carrying</u> <u>Amount</u>	<u>Accumulated</u> <u>Amortization</u>	<u>Net</u>
Finite lived intangible assets:				
Customer relationships	5 years	\$ 12,720,000	\$1,802,000	\$10,918,000
Trademarks	7 years	6,230,000	630,417	5,599,583
Patents	7 years	230,683	225,191	5,492
Software	7 years	77,425	—	77,425
Customer lists	5 years	307,153	75,361	231,792
Total intangible assets		<u>\$ 19,565,261</u>	<u>\$2,732,969</u>	<u>\$16,832,292</u>
Goodwill	Indefinite	\$ 58,337,290		\$58,337,290

We compute amortization using the straight-line method over the estimated useful lives of the assets. The amortization expense related to intangible assets was \$882,096 for the quarter ended March 31, 2014, with no comparable expense for the quarter ended March 31, 2013. We have no indefinite-lived intangible assets other than goodwill. The goodwill is not deductible for tax purposes.

**QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED**

6. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consisted of the following:

	<u>March 31,</u> <u>2014</u> (Unaudited)	<u>December 31,</u> <u>2013</u>
Compensation	\$ 796,663	\$ 1,114,252
Deferred rent obligation	835,804	930,274
Sales and use tax	183,801	484,134
Professional fees	144,826	40,241
Insurance	—	48,663
Accrued interest and other	81,739	56,206
	<u>\$2,042,833</u>	<u>\$ 2,673,770</u>

7. Line of Credit

On December 15, 2010, Quest entered into a Revolving Credit Note and Loan Agreement with Regions Bank (“Regions”), a national banking association. This agreement provides Quest with a loan facility up to \$10,000,000 for working capital with advances generally limited to 60% of eligible accounts receivable from Quest’s largest customer and 85% of all other eligible accounts receivable. The interest on the outstanding principal amount accrues daily and is payable monthly based on a fluctuating interest rate per annum, which is the base rate plus 1.50% (4.75% as of March 31, 2014). The base rate for any day is the greater of (a) the Federal funds rate plus one-half of 1%, (b) Region’s published effective prime rate, or (c) the Eurodollar rate for such day based on an interest period of one month. To secure the amounts due under the agreement, Quest granted Regions a security interest in all of its assets. Quest had \$4,750,000 outstanding and approximately \$5,250,000 available to be borrowed as of March 31, 2014. On May 9, 2014, Quest and Regions had made amendments to the loan to extend the term to May 31, 2015. See Note 15 — Subsequent Events.

8. Convertible Note Payable

During the quarter ended March 31, 2014, \$25,000 of principal and \$4,001 of interest was converted into 23,201 shares of our common stock. We treat the intrinsic value of a beneficial conversion feature inherent to a convertible note payable, which we do not bifurcate, separately from the convertible note payable, and we may not settle in cash upon conversion, as a discount to the convertible note payable. We amortize this discount over the period from the date of issuance to the date the note is due using the effective interest method. If we retire the note payable prior to the end of its contractual term, we expense the unamortized discount in the period of retirement to interest expense. In general, we measure the beneficial conversion feature by comparing the effective conversion price, after considering the relative fair value of detachable instruments included in the financing transaction, if any, to the fair value of the common shares at the commitment date to be received upon conversion.

The following convertible note payable was outstanding as of March 31, 2014 and December 31, 2013:

	<u>March 31,</u> <u>2014</u> (Unaudited)	<u>December 31,</u> <u>2013</u>
Convertible note payable to unrelated parties, issuance date of September 2012	—	\$ 25,000
Total convertible notes payable - short term	<u>—</u>	<u>\$ 25,000</u>

During September 2012, we issued for cash a \$25,000 convertible note to an unrelated, accredited third party. The note matured six months from the date of issuance but could be extended for an additional 30 days at our discretion. The note bore interest at a rate of 10.0% per annum and was convertible at any time, with accrued interest, at the discretion of the investor into shares of our common stock at a rate of \$1.25 per share. Based on our share price at the time we entered into the note agreement, we recognized a beneficial conversion feature of \$17,500 for this convertible note.

**QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED**

9. Long-Term Debt and Capital Lease Obligations

At March 31, 2014 and December 31, 2013, total long-term debt outstanding consisted of the following:

	March 31, 2014 (Unaudited)	December 31, 2013
Secured convertible notes payable to related parties, 7% interest due monthly in arrears, due July 2016, repayment provisions discussed further below (Net of discount of \$4,205,292 and \$4,656,934 as of March 31, 2014 and December 31, 2013, respectively)	\$17,794,708	\$17,343,066
Capital lease obligations, imputed interest at 4.75%, with monthly payments of \$1,507 through November 2016, secured by computer equipment	45,211	49,163
Total	17,839,919	17,392,229
Less: current maturities	(16,224)	(16,096)
Long-term portion	<u>\$17,823,695</u>	<u>\$17,376,133</u>

Convertible Secured Promissory Notes – Quest Acquisition – In connection with our acquisition of Quest on July 16, 2013, we issued convertible secured promissory notes with a total principal amount of \$22,000,000 to the owners of QRG: the Chief Executive Officer of Quest and former President of Quest, who are also related parties of our company. The convertible secured promissory notes (collectively, the “Sellers Notes”) are each secured by a first-priority security interest in a 25% membership interest held by Earth911 in Quest (comprising a total of 50% of the membership interests of Quest), as set forth in security and membership interest pledge agreements, by and between Earth911 and the sellers. The Sellers Notes accrue interest at a rate of 7% per annum and are payable on a monthly basis on the 5th day of the month beginning on September 5, 2013. The principal amount will be due and payable in one installment on July 16, 2016.

The Sellers Notes are convertible at any time, in the sole discretion of the holders, into shares of our common stock at a price of \$2.00 per share. In addition, the Sellers Notes are convertible, in our sole discretion, into shares of our common stock at a price of \$2.00 per share at any time (i) after the two year anniversary of the Notes, (ii) the principal amount of each Sellers Notes has been paid down by \$5,000,000 as a result of the first capital raise, (iii) our common stock trades on the Nasdaq Stock Market, the New York Stock Exchange, or NYSE MKT, and (iv) our common stock has traded at four times the \$2.00 conversion price, as adjusted for any stock splits, reverse stock splits, or both. If the holders converted the Seller’s Notes as of March 31, 2014, the value of the shares upon conversion would have exceeded the note original principal balance by \$1.3 million. Based on our share price at the time we entered into the Sellers Notes agreement, we recognized a beneficial conversion feature of \$5,500,000 and discounted the Sellers Notes. As of March 31, 2014, the unamortized discount on the Sellers Notes was \$4,205,292. The amount of interest expense related to the Sellers Notes for the quarter ended March 31, 2014 was \$379,726. The amount of interest expense related to the amortization of the discount on the Sellers Notes for the quarter ended March 31, 2014 was \$451,642.

Stockbridge Senior Secured Convertible Note – On March 22, 2012, Earth911 entered into a securities purchase agreement with Stockbridge Enterprises, L.P., a related party (“Stockbridge”), pursuant to which Earth911 issued a senior secured convertible note (the “Convertible Note”) and four warrants to Stockbridge. All of the assets of Earth911 secured the Convertible Note. On each of October 10, 2012 and March 29, 2013, the terms of the note and the warrants were amended and additional warrants were issued to Stockbridge (the “Allonge” and the “Second Allonge”). The Convertible Note and warrants were also adjusted for the Earth911 Merger in October 2012. On July 16, 2013, Stockbridge elected to convert \$3,000,000 in principal and \$34,500 of accrued interest into 8,382,597 shares of our common stock.

The amended Convertible Note provided for up to \$3,000,000 principal with a maturity date of October 1, 2015, which was extendable under certain circumstances. As of June 30, 2013, the full amount of the principal had been drawn. The annual interest rate was adjusted in October 2012 to 9.0% from the original 6.0%, and was due monthly in arrears. Reflecting the adjustment for the Earth911 Merger, the Convertible Note was convertible into shares of our common stock at \$0.362 per share prior to the maturity date, subject to a downward formula-based adjustment for future issuances of common stock or stock equivalents under certain conditions whereby the issue price was lower than the conversion price in effect immediately prior to such issue or sale (the “Fixed Conversion Price”). As a result of the Earth911 Merger, a United States exchange lists our common stock (a “Triggering Event”); therefore the conversion price was the lower of the Fixed Conversion Price or the average closing bid price during the ten trading days immediately preceding the conversion date.

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

In connection with the Convertible Note, we issued five-year warrants that were subsequently adjusted for the Earth911 Merger and consisted of the following:

- (i) a warrant issued March 2012 to acquire up to 1,381,115 shares of our common stock, exercisable immediately upon execution of the Convertible Note (“Warrant 1-1”);
- (ii) three contingent warrants issued March 2012, exercisable only in the event that all outstanding principal and accrued interest on the Convertible Note was not paid in full at such dates, as follows: a warrant to acquire up to 345,278 shares of our common stock, exercisable at the conclusion of 42 months after the issuance date of the warrant (“Warrant 1-2”); a warrant to acquire up to 345,278 shares of our common stock, exercisable at the conclusion of 45 months after the issuance date of the warrant (“Warrant 1-3”); and a warrant to acquire up to 690,557 shares of our common stock, exercisable at the conclusion of 48 months after the issuance date of the warrant (“Warrant 1-4”);
- (iii) a warrant issued October 2012 upon execution of the Allonge to acquire up to 5,524,461 shares of our common stock, exercisable immediately (“Warrant 1-5”); and
- (iv) a warrant issued March 2013 upon execution of the Second Allonge to acquire up to 500,000 shares of our common stock, exercisable immediately (“Warrant 1-6”).

Warrant 1-1 was exercisable at the lower of \$0.37 per share or the average closing bid price during the ten trading days immediately preceding the exercise date. Warrant 1-5 was exercisable at the lower of \$0.37 per share or the average closing bid price during the ten trading days immediately preceding the exercise date. Warrant 1-6 was exercisable at the lower of \$0.37 per share or the average closing bid price during the ten trading days immediately preceding the exercise date.

Warrant 1-1, Warrant 1-5, and Warrant 1-6 were exercised in March 2013 as part of the Second Allonge using a cashless exercise formula.

If the contingent Warrant 1-2, Warrant 1-3, and Warrant 1-4 had become exercisable, the exercise price would have been the lower of \$0.37 per share or the average closing bid price during the ten trading days immediately preceding the exercise date. The exercise price for all of the warrants was also subject to a downward formula-based adjustment for future issuances of common stock or stock equivalents under certain conditions whereby the issue price is lower than the exercise price in effect immediately prior to such issue or sale. These warrants were cancelled when the Convertible Note was converted on July 16, 2013.

In connection with the issuance of the Convertible Note, Warrant 1-1 and Warrant 1-5 were initially valued and accounted for as a warrant liability of \$18,742,526 and allocated as a discount to the Convertible Note of \$1,500,000 with the remainder of \$17,242,526 expensed as a financing cost. See Note 12 regarding the valuations of the warrant liability.

On March 29, 2013, Stockbridge elected to exercise Warrant 1-1, Warrant 1-5, and Warrant 1-6 with exercisable rights in total to purchase 7,405,576 shares of our common stock at \$0.37 per share under the cashless exercise option of the Second Allonge. The Company determined the net number of shares to issue using the “Cashless Exercise” formula, as amended and restated, as follows:

$$\text{Net Number of Shares to Issue} = \frac{(A \times B) - (A \times C)}{D}$$

For purposes of the foregoing formula as of March 29, 2013:

A = 7,406,576, the total number of warrant shares with respect to which these warrants were then being exercised.

B = \$3.30, the closing price of our common stock plus 10.0% on the date of exercise of the warrant.

C = \$0.37, the warrant exercise price then in effect for the applicable warrant shares at the time of such exercise.

D = \$3.00, the closing price of our common stock on the date of exercise of the warrant.

Based on the cashless exercise formula, on March 29, 2013, Warrant 1-1, Warrant 1-5, and Warrant 1-6 yielded a net number of shares to issue of 7,232,779 with a value of \$21,698,338 based on the \$3.00 closing price of the stock on the date of issue.

10. Investment in Quest Resource Management Group, LLC

Prior to July 16, 2013, we held a 50% ownership interest in Quest, which Earth911 acquired on August 21, 2008. On July 16, 2013, we acquired all of the Quest Interests, held by QRG, comprising 50% of the membership interests of Quest. The purchase price for the Quest Interests consisted of 22,000,000 shares of our common stock issued at a fair market value of \$2.50 per share based on the

**QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED**

closing price of the stock on the date of the transaction and the Sellers Notes in the aggregate principal amount of \$22,000,000. We paid the total purchase price of \$77,000,000 to the owners of QRG and related parties: the Chief Executive Officer of Quest and the President of Quest. After the close of the transaction, the Chief Executive Officer of Quest became the President, Chief Executive Officer, and member of the Board of Directors of our Company. Subsequent to our purchase of the Quest Interests on July 16, 2013, we consolidated 100% of the operating activity of Quest into the operations of our company and reflected the adjustments for the ownership purchase and valuation of goodwill.

Concurrently with our acquisition of the Quest Interests, we assigned the Quest Interests to Earth911, our wholly owned subsidiary, which now holds 100% of Quest. We accounted for the acquisition of Quest under ASC Topic 805; thereby the acquisition accounting for the acquired Quest Interests and the step up basis of the previously owned 50% interest resulted in the following total purchase price for Quest as follows:

Consideration paid for Quest Interest	\$ 77,000,000
Non-controlling interest in the acquiree at the acquisition date fair value	27,050,000
Total consideration	<u>\$104,050,000</u>

We primarily employed two methodologies that yielded substantially the same results to determine the fair value of our preexisting equity interest in Quest, which we re-measured as a non-controlling interest independent of the acquired controlling interest as of the effective date of the acquisition: (i) the amount at which the asset could be bought or sold in a current transaction between willing parties; and (ii) the present value of expected future cash flows of Quest, level 2 and level 3 inputs, respectively.

The purchase price allocation as of July 16, 2013 for the assets, liabilities, intangibles, and goodwill totaling \$104,050,000 was as follows:

Net assets and liabilities	\$ 1,214,804
Customer relationships	12,720,000
Trademarks	6,230,000
Goodwill	83,885,196
	<u>\$104,050,000</u>

In connection with the fair value adjustment to the Investment in Quest due to the acquisition, we recorded in 2013 a gain on investment in Quest of \$23,449,372, the difference between the fair value and the carrying amount of the asset on the date of the acquisition. In addition, we recognized \$26,850,039 of goodwill impairment based on our goodwill impairment testing. We determined that the carrying amount of the reporting unit exceeded the fair value and recorded a goodwill impairment charge. The impact of the goodwill impairment and the gain on investment was a net expense of \$3,400,667 included in the operating loss for the year ended December 31, 2013.

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

The financial condition and operating results of Quest for the relevant periods are presented below:

	Three Months ended March 31,	
	2014	2013
	(Unaudited)	(Unaudited)
Condensed operating statement information:		
Net sales	\$37,972,639	\$30,651,064
Gross profit	3,145,004	3,297,354
Income from operations	21,583	1,075,048
Net income (loss)	(22,065)	951,592

11. Income Taxes

Income taxes are computed using the asset and liability method in accordance with ASC Topic 740. Under the asset and liability method, we determine deferred income tax assets and liabilities based on the differences between the financial reporting and tax bases of assets and liabilities and measure them using currently enacted tax rates and laws. We provide a valuation allowance for the amount of deferred tax assets that, based on available evidence, are not expected to be realized. In our opinion, realization of our net operating loss carry forward is not reasonably assured as of March 31, 2014 and December 31, 2013, and we have recorded a valuation allowance of \$6,991,000 and \$6,582,000 respectively, against deferred tax assets in excess of deferred tax liabilities in the accompanying consolidated financial statements.

The components of net deferred taxes are as follows:

	March 31,	December 31,
	2014	2013
	(Unaudited)	
Deferred tax assets (liabilities):		
Net operating loss	\$ 4,469,000	\$ 4,212,000
Stock-based compensation	2,168,000	2,103,000
Accrued interest expense	202,000	150,000
Allowance for doubtful accounts	64,000	47,000
Deferred lease liability	88,000	70,000
Total deferred tax assets	6,991,000	6,582,000
Less: valuation allowance	(6,991,000)	(6,582,000)
Net deferred taxes	\$ —	\$ —

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

The reconciliation between the income tax expense (benefit) calculated by applying statutory rates to net loss and the income tax benefit reported in the accompanying consolidated financial statements is as follows:

	March 31, 2014 <u>(Unaudited)</u>	December 31, 2013 <u></u>
U.S. federal statutory rate applied to pretax income	\$(506,064)	\$(6,051,780)
Permanent differences	153,558	2,739,048
State taxes and other	(56,494)	1,597,415
Change in valuation allowance	409,000	1,715,317
	<u>\$ —</u>	<u>\$ —</u>

As of December 31, 2013, we had federal income tax net operating loss carry forwards of approximately \$4,212,000, which expire at various dates beginning in 2031. We are subject to limitations existing under Internal Revenue Code Section 382 (Change of Control) relating to the availability of the operating loss.

As of December 31, 2013, we did not recognize any assets or liabilities relative to uncertain tax positions, nor do we anticipate any significant unrecognized tax benefits will be recorded during 2014. We classify interest and penalties on income taxes as interest expense or penalties expense.

Tax positions are positions taken in a previously filed tax return or positions expected to be taken in a future tax return that are reflected in measuring current or deferred income tax assets and liabilities reported in the financial statements. Tax positions include the following:

- an allocation or shift of income between taxing jurisdictions;
- the characterization of income or a decision to exclude reportable taxable income in a tax return; or
- a decision to classify a transaction, entity, or other position in a tax return as tax exempt.

We are potentially subject to tax audits for federal and state tax returns for tax years ended 2013 to 2011. Tax audits by their very nature are often complex and can require several years to complete. Prior to July 13, 2010, as a limited liability company, we were not a tax paying entity for federal and state income tax purposes. Accordingly, we allocated our taxable income or loss to our members in accordance with their respective percentage ownership.

12. Fair Value of Financial Instruments

Our financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities, convertible notes payable, notes payable, and warrant liability. We do not believe that we are exposed to significant interest, currency, or credit risks arising from these financial instruments. With the exception of the warrant liability, the fair values of these financial instruments approximates their carrying values using Level 3 inputs, based on their short maturities or, for long-term debt based on borrowing rates currently available to us for loans with similar terms and maturities. Gains and losses recognized on changes in fair value of convertible notes and warrant liability are reported in other income (expense).

We measured our initial warrant valuation at fair value by applying the Black-Scholes-Merton option valuation model, which utilizes Level 3 inputs. The assumptions used in the Black-Scholes-Merton option valuation for the warrants are as follows: volatility of 66%; risk free interest rate of 1%; expected term of 5 years; and expected dividend yield of 0%. The grant date fair value of the initial warrant valuation described above was \$2.56 per warrant. We base the risk free interest rate on United States Treasury rates with maturity dates approximating the expected term of the warrants. At the time of the initial warrant valuation, we were a private company and common stock transactions were too infrequent, therefore we could not practically estimate the expected volatility of our own stock. Accordingly, we have substituted the historical volatility of a relevant sector index, which we have generated from companies that are publicly traded and do business within the industry we operate.

We measured the March 29, 2013 fair value by utilizing the quoted market price for our common stock and the valuation for the cashless exercise of Warrant 1-1, Warrant 1-5, and Warrant 1-6 in March 2013, which are Level 1 and Level 2 inputs. These inputs of (i) an observable warrant exercise transaction and (ii) publicly traded market price provided a reasonable basis for valuation for the warrants as of March 29, 2013. Based on that valuation using the \$3.00 closing market price and exercisable rights in total to purchase

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

6,905,576 shares of our common stock at \$0.37 per share, Warrant 1-1 and Warrant 1-5 had a net number value of \$20,233,338. Using the same valuation method, Warrant 1-6 had a net number value of \$1,465,000 upon issuance on March 29, 2013. All three warrants were exercised on March 29, 2013. See Note 9 for further discussion regarding the cashless exercise of these warrants.

13. Stockholders' Equity

Preferred Stock – Our authorized preferred stock consists of 10,000,000 shares of preferred stock with a par value of \$0.001, of which no shares have been issued or are outstanding.

Common Stock – Our authorized common stock consists of 200,000,000 shares of common stock with a par value of \$0.001 with 95,837,766 shares and 95,814,565 shares issued and outstanding as of March 31, 2014 and December 31, 2013, respectively.

During the three months ended March 31, 2014, we issued shares of common stock as follows:

	Common Stock Shares	Amount
Note and interest conversions	23,201	\$29,001
	<u>23,201</u>	<u>\$29,001</u>

Common Stock for Services – We issued none and 17,226 shares of common stock to employees and consultants for nil and \$50,780 of services during the three months ended March 31, 2014 and 2013, respectively.

Stock Option Plan – In October 2012, we adopted our 2012 Incentive Compensation Plan, which was subsequently amended in September 2013 (the “2012 Plan”). The 2012 Plan provides for the grant of stock options, stock appreciation rights, restricted stock, restricted stock units, bonus stock, dividend equivalents, other stock-based awards, and performance awards that may be settled in cash, stock, or other property to our officers, directors, employees, and consultants who are natural persons providing bona fide services to us or our subsidiaries and other designated affiliates, which we refer to as “Related Entities.” The purpose of the 2012 Plan is to assist us and our Related Entities in attracting, motivating, retaining, and rewarding high-quality executives and other employees, officers, directors, and individual consultants who provide services to us or our Related Entities, by enabling such persons to acquire or increase a proprietary interest in our company in order to strengthen the mutuality of interests between such persons and our stockholders, and providing such persons with performance incentives to expend their maximum efforts in the creation of stockholder value. The 2012 Plan is administered by the compensation committee of our Board of Directors or a subcommittee thereof formed by the compensation committee, except to the extent our Board of Directors elects to administer the 2012 Plan (subject to limitations described in the 2012 Plan. Our policy is to fulfill any exercise of options from common stock that is authorized and unissued. The maximum number of shares of common stock available for grant under the plan is 7,500,000. Stock compensation expense prior to October 2012 is related to options granted prior to the Earth911 Merger that the 2012 Plan superseded at the time of the Earth911 Merger. The number of shares available for award under the plan is subject to adjustment for certain corporate changes in accordance with the provisions of the plan. Stock-based compensation expense was \$162,995 and \$784,105 for the three months ended March 31, 2014 and 2013, respectively.

Following is a summary of stock option activity subsequent to December 31, 2013 through March 31, 2014:

	Stock Options		
	Number of Shares	Exercise Price Per Share	Weighted- Average Exercise Price Per Share
Outstanding at December 31, 2013	4,141,948	\$2.00 - 3.25	\$ 2.48
Granted	—	—	—
Canceled/Forfeited	(45,000)	\$2.05 - 2.05	\$ 2.05
Outstanding at March 31, 2014	<u>4,096,948</u>	\$2.00 - 3.25	\$ 2.48

As of March 31, 2014, the intrinsic value of options outstanding was \$122,192 and the intrinsic value of options exercisable was \$66,367.

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QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

The following additional information applies to options outstanding at March 31, 2014:

Ranges of Exercise Prices	Outstanding at March 31, 2014	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Exercisable at March 31, 2014	Weighted-Average Exercise Price
\$2.00 - \$3.25	4,096,948	8.2	\$ 2.48	3,199,448	\$ 2.63

At March 31, 2014, the balance of unearned stock-based compensation to be expensed in future periods related to unvested share-based awards, as adjusted for expected forfeitures, was approximately \$988,699.

14. Related Party Transactions

Stockbridge Convertible Note – In March 2012, we issued the Convertible Note to Stockbridge, a related party. In connection with the issuance of the Convertible Note, we issued four warrants (Warrants 1-1 through 1-4) in March 2012. On July 16, 2013, Stockbridge elected to convert \$3,000,000 in principal and \$34,500 of accrued interest of the Convertible Note into 8,382,597 shares of our common stock. With the conversion, the contingent Warrants 1-2, 1-3, and 1-4 were cancelled.

Allonge to the Convertible Note – In October 2012, we amended the Convertible Note. We increased the original principal amount to \$3,000,000 from the original \$1,000,000 amount. We changed the maturity of the note to October 1, 2014. We changed the conversion rate of the Convertible Note to \$.50 per common share prior to the maturity date and \$.25 per common share after the maturity, subject to certain adjustments. In connection with the amendment, we issued Warrant 1-5 in October 2012 and issued 100,000 shares of our common stock.

Second Allonge to the Convertible Note – On March 29, 2013, the terms of the note and the warrants were amended and additional warrants were issued to Stockbridge. Under the amendment on March 29, 2013, Earth911 and Stockbridge entered into the Second Allonge, pursuant to which the parties agreed to (i) change all references to common stock, options, warrants, warrant shares, or convertible securities of Earth911 in the original note documents and the Allonge documents to our common stock, options, warrants, warrant shares, or convertible securities, respectively, and (ii) expand all references to a “Triggering Event” in the original note documents and the Allonge documents to include any exchanges on which our common stock may be listed or quoted for trading. The parties also (i) amended how the fair market value of our common stock, on the date of exercise, would be defined in a formula used to calculate the net number of shares that Stockbridge would receive upon a cashless exercise, (ii) extended the maturity date of the Convertible Note to October 1, 2015, (iii) revised the terms of Warrant 1-5 to apply the conversion rate from the Earth911 to the number of shares of our common stock underlying Warrant 1-5 and the exercise price at which such shares would be issued upon the exercise date, and (iv) amended the exercisable dates of the contingent Warrant 1-2, the contingent Warrant 1-3, and the contingent Warrant 1-4 to be exercisable 42 months, 45 months, and 48 months, respectively, following the issuance date of the contingent warrants. Finally, Stockbridge retroactively agreed to waive its right to effect a partial conversion of the Convertible Note, with such waiver to be effective for a period of 12 months from October 17, 2012.

To effect the changes in the Second Allonge, we issued to Stockbridge an additional warrant to purchase 500,000 shares of our common stock (“Warrant 1-6”). Warrant 1-6 was exercisable at or after the date of the Second Allonge, and was in the same form as Warrant 1-5, as amended by the Second Allonge. Warrant 1-6 would expire five years from the date of issuance.

See Note 9 for a discussion of the Convertible Note and of the exercise of the related exercisable warrants in March 2013.

Acquisition of the Quest Interests – On July 16, 2013, we acquired all of the Quest Interests held by QRG, comprising 50% of the membership interests of Quest. The purchase price for the Quest Interests consisted of 22,000,000 shares of our common stock issued at a fair market value of \$2.50 per share based on the closing price of the stock on the date of the transaction and the Sellers Notes as described in Note 10 in the aggregate principal amount of \$22,000,000. The total purchase price of \$77,000,000 was paid to the owners of QRG who at the time of the transaction were related parties: the Chief Executive Officer of Quest and the President of Quest. After the close of the transaction, the Chief Executive Officer of Quest became the President, Chief Executive Officer and member of the Board of Directors of our company. Unpaid interest related to the Sellers Notes at March 31, 2014 and December 31, 2013 is \$130,795 and \$132,878, respectively.

**QUEST RESOURCE HOLDING CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED**

The Securities Purchase Agreement provides that QRG and its members may not engage or take a financial interest in any Competitive Business within the Restricted Territory (each as defined in the Securities Purchase Agreement) for a period of five years. The Securities Purchase Agreement also provides restrictions with respect to customers of Quest and non-solicitation of employees of Quest for a period of five years. The Securities Purchase Agreement further provides that if there is an event of default on the Sellers Notes, QRG and its members may compete with us and solicit customers, provided that they resign from all positions held with us first.

15. Subsequent Events

Stock and Warrants Issued

On April 18, 2014, we issued an aggregate of 1,192,500 units, or the Units, to several accredited investors, for an aggregate purchase price of \$2,385,000, with each Unit consisting of one share of our common stock and a warrant to purchase one share of our common stock for \$2.00 per share. Each warrant may be exercised by the holder thereof, in such holder's sole discretion, in whole or in part, any time prior to April 1, 2017.

Line of Credit—Regions

On May 9, 2014, Quest entered into a Sixth Amendment to the Loan Agreement with Regions Bank. The Loan Agreement was amended to, among other things, (i) add a \$5.0 million accordion feature, (ii) increase the Borrowing Base, (iii) reduce the Applicable Margin for Eurodollar Rate Loans by 1% per annum, (iv) add an unused fee of 0.25% per annum, (v) extend the maturity date to May 31, 2015, (vi) release the Guaranty of our Chief Executive Officer previously executed in favor of the Lender, (vii) add our company and our wholly owned subsidiary, Earth911, Inc., as Guarantors, (viii) allow for Permitted Acquisitions, and (ix) delete two of the financial covenants and modify the other financial covenants in certain respects.

In connection with the Sixth Amendment, on May 9, 2014, we and Earth911 entered into a Guaranty (the "Guaranty") for the benefit of Regions to guarantee the obligations of Quest under the Loan Agreement and other Loan Documents. In addition, on May 9, 2014, Earth911 entered into a Pledge Agreement with Regions, pursuant to which Earth911 pledged to Regions 50% of the membership interests in Quest held by Earth911 to secure the prompt and complete payment and performance of the obligations of Quest and the Guarantors under the Loan Agreement and other Loan Documents.

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

You should read the following discussion of our financial condition and results of operations in conjunction with the consolidated financial statements and the notes thereto included elsewhere in this Quarterly Report on Form 10-Q and with our audited consolidated financial statements included in our Report on Form 10-K for the year ended December 31, 2013. This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve substantial risks and uncertainties. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), including, but not limited to, statements regarding our expectations, beliefs, intentions, strategies, future operations, future financial position, future revenue, projected expenses, and plans and objectives of management. In some cases, you can identify forward-looking statements by terms such as "anticipate," "believe," "estimate," "expect," "intend," "may," "might," "plan," "project," "will," "would," "should," "could," "can," "predict," "potential," "continue," "objective," or the negative of these terms, and similar expressions intended to identify forward-looking statements. However, not all forward-looking statements contain these identifying words. These forward-looking statements reflect our current views about future events and involve known risks, uncertainties, and other factors that may cause our actual results, levels of activity, performance, or achievement to be materially different from those expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in our Report on Form 10-K for the year ended December 31, 2013. Furthermore, such forward-looking statements speak only as of the date of their issuance. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We were incorporated in Nevada in July 2002 under the name BlueStar Financial Group, Inc. On July 16, 2013, we acquired the issued and outstanding membership interests of Quest Resource Management Group, LLC ("Quest"), held by Quest Resource Group LLC ("QRG"), comprising 50% of Quest (the "Quest Interests"). Our wholly owned subsidiary, Earth911, held the remaining 50% membership interest of Quest for several years which was accounted for under the equity method of investment. Upon our acquisition of the Quest Interests, we assigned the Quest Interests to Earth911 so that Earth911 now owns 100% of Quest. Effective October 28, 2013, we changed our name to Quest Resource Holding Corporation ("QRHC"), increased our shares of common stock authorized for issuance to 200,000,000 and changed our trading symbol to "QRHC."

This "Management's Discussion and Analysis of Financial Condition and Results of Operations" is based on and relates primarily to the operations of Quest Resource Holding Corporation, Quest, and Earth911.

Our Business

We provide businesses with one stop management programs to reuse, recycle, and dispose of a wide variety of waste streams and recyclables generated by their businesses and operate environmentally based social media and online database platforms that contain information and instructions necessary to empower consumers and consumer product companies to recycle or properly dispose of household products and materials. Our comprehensive reuse, recycling, and proper disposal management programs are designed to enable regional and national customers and large local business to have a single point of contact for managing a variety of waste streams and recyclables. Our directory of local recycling and proper disposal options empowers consumers directly and enables consumer product companies to empower their customers by giving them the guidance necessary for the proper recycling or disposal of a wide range of household products and materials, including the "why, where, and how" of recycling.

We believe we offer innovative, cost-effective, one-stop management programs for the reuse, recycling, and proper disposal of a wide variety of recyclables and disposals that provide regional and national customers with a single point of contact for managing these materials. Our services are designed to enable our business customers to capture the commodity value of their waste streams and recyclables, reduce their disposal costs, enhance their management of environmental risks, enhance their legal and regulatory compliance, and create national sustainability initiatives while maximizing the efficiency of their assets. Our services currently focus on the waste streams and recyclables from the fleet and industrial, food service and retail, and solid waste industries. We currently concentrate on programs for recycling motor oil and automotive lubricant recycling, scrap tires, grease and cooking oil, meat rendering, organics, hazardous and non-hazardous waste, regulated medical waste, construction debris, glass, cardboard, paper, metal, and solid waste.

Utilizing what we believe is the nation's most complete directory of local recycling and proper disposal options for almost every household product and material, we empower consumers and enable consumer product companies to empower their customers by providing them with complete information and instructions about the recycling and disposal of a wide range of household products and materials; offer advertisers the opportunity to target a zero-waste lifestyle audience concerned about sustainability, recycling, and environmentally appropriate disposal; and enable product manufacturers to determine recycling availability for substantiating recycling claims and product design. Consumers can access our directory and instructions for any zip code in the United States

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through multiple platforms, including the *Earth911.com* website, our mobile applications for smartphones and tablets, traditional phone lines, social media, and branded recycling locators on client platforms and applications, in addition to engaging with our content and media on leading social platforms such as Facebook, Twitter, Pinterest, Instagram, Tumblr, YouTube, and Google+.

Three Months Ended March 31, 2014 Operating Results

The following table summarizes our operating results for the three months ended March 31, 2014 and 2013:

	For the Three Months Ended March 31,	
	2014	2013
	(Unaudited)	(Unaudited)
Revenue	\$ 38,160,050	\$ 313,489
Cost of revenue	34,827,635	39,693
Gross profit	3,332,415	273,796
Operating expenses:		
Selling, general and administrative	2,993,708	2,258,802
Depreciation and amortization	951,663	14,980
Impairment of goodwill	—	—
Total operating expenses	3,945,371	2,273,782
Operating loss	(612,956)	(1,999,986)
Interest expense	(875,467)	(308,414)
Financing cost for senior secured convertible note—related party	—	(1,465,000)
Equity in Quest Resource Management Group, LLC income	—	475,796
Net loss	<u>\$ (1,488,423)</u>	<u>\$ (3,297,604)</u>

Three Months Ended March 31, 2014 compared to Three Months Ended March 31, 2013

Revenue

Revenue for the three months ended March 31, 2014 was \$38.2 million an increase of \$37.9 million over revenue of \$300,000 for the three months ended March 31, 2013. The increase was primarily due to the consolidated recycling and waste service fees and commodity sales revenue of Quest subsequent to our acquisition of the Quest Interests on July 16, 2013, which contributed approximately \$38.0 million in revenue.

Cost of Revenue/Gross Profit

Our cost of revenue of \$34.8 million and \$40,000 for the three months ended March 31, 2014 and 2013, respectively, related primarily to the consolidated cost of recycling and waste disposal services and commodities from Quest's operations subsequent to July 16, 2013. Gross profit increased \$3.1 million to \$3.3 million for the quarter ended March 31, 2014 from \$300,000 for the quarter ended March 31, 2013, representing a 1,117% increase from 2013. The gross profit margin was 8.7% of total 2014 net sales, compared to 87.3% in 2013. The decrease in gross profit margin percentage was primarily due to the majority of 2014 sales was derived from recycling and waste services and commodity sales consolidated subsequent to acquisition of the Quest Interests on July 16, 2013 versus only advertising revenue and recycled electronic sales in 2013.

We expect gross profit margins during 2014 to remain comparable to the quarter ended December 31, 2013 on average with margins that can range from 5%-20% across the various recycling, waste and commodity programs and beyond that range for advertising revenue and consulting. Margins will be affected quarter to quarter by the volumes of waste and recycling materials generated by our clients, frequency of services delivered, service price and commodity index adjustments, cost of contracted services, advertising rates and the sales mix between advertising, consulting, commodities and services in any one reporting period.

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Operating Expenses

For the three months ended March 31, 2014, operating expenses increased \$1.7 million to \$3.9 million from \$2.3 million for the comparable quarter in 2013. This was primarily due to the added consolidated expenses from Quest's operations beginning July 17, 2013 with no comparable expenses in the first quarter of 2013.

Selling, general, and administrative expenses were \$3.0 million and \$2.3 million for the three months ended March 31, 2014 and 2013, respectively, an increase of \$700,000 primarily due to the addition of Quest operating expenses. Operating expenses also included depreciation and amortization of \$900,000 and \$20,000 for the three months ended March 31, 2014 and 2013, respectively, which primarily relates to the increased amortization of \$900,000 from the recognition of \$16.8 million of amortizable intangible assets related to the acquisition of the Quest Interests.

Interest and Other Expenses

For the quarter ended March 31, 2014, total interest and other expenses decreased \$900,000 to \$900,000 from \$1.8 million for the first quarter of 2013 primarily due to financing costs of approximately \$1.5 million attributed to the Convertible Note issued with warrants that we bifurcated and valued separately pursuant to ASC 815, partially offset by interest related to the addition of the two Sellers Notes totaling \$22 million as part of the acquisition of the Quest Interests on July 16, 2013 and the related amortization of the \$5.5 million note discount.

Equity in Quest Income

For the first quarter ended March 31, 2013, equity in Quest income was \$500,000, which decreased to zero in 2014 due to only recognizing equity method income through July 16, 2013.

Net Loss

For the three months ended March 31, 2014, the net loss from operations decreased \$1.8 million to a net loss of \$1.5 million from a net loss of \$3.3 million for the three months ended March 31, 2013. The explanations above detail the majority of the changes related to the net loss on a quarter-to-quarter and year-to-year basis.

Loss Per Share

The loss per share on a basic and diluted basis was (\$0.02) for the three months ended March 31, 2014 compared to a loss per share of (\$0.06) for the comparable quarter in 2013. The weighted average number of shares of common stock outstanding increased from 58.0 million as of March 31, 2013 to 95.8 million as of March 31, 2014. The increase in the share count was primarily a result of our acquisition of the Quest Interests on July 16, 2013.

Our business, including revenue, operating expenses, and operating margins vary depending on commodity prices, the blend of services, the nature of the contract, and volumes. Our business plan contemplates a rapid expansion of our operations, which may place a significant strain on our management, financial, and other resources. Our ability to manage the challenges associated with any expansion of our business and integration of future acquisitions, if any, will depend upon, among other things, our ability to monitor operations, control costs, maintain effective quality control, secure necessary marketing arrangements, expand internal management, implement technical information and accounting systems, and attract, assimilate, and retain qualified management and other personnel. Therefore our profitability in the near future, or ever will be dependent on successful execution of our business plan, along with market and environmental factors.

EBITDAS

We use the non-GAAP measurement of earnings before interest, taxes, depreciation, amortization, and stock-related non-cash charges ("EBITDAS") to evaluate our performance. EBITDAS is a non-GAAP measure that we believe can be helpful in assessing our overall performance as an indicator of operating and earnings quality. We suggest that EBITDAS be viewed in conjunction with our reported financial results or other financial information prepared in accordance with GAAP.

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The following table reflects the EBITDAS for the three months ended March 31, 2014 and 2013:

RECONCILIATION OF NET LOSS TO EBITDAS (UNAUDITED)

	For the Three Months Ended March 31,	
	2014	2013
Net loss	\$ (1,488,423)	\$ (3,297,604)
Interest expense	875,467	308,414
Income tax expense (benefit)	—	—
Depreciation and amortization	951,663	14,980
Stock-based compensation	162,995	784,105
Other expenses	—	1,465,000
EBITDAS	<u>\$ 501,702</u>	<u>\$ (725,105)</u>

Liquidity and Capital Resources

Cash Flows

The following discussion relates to the major components of our cash flows.

Cash Flows from Operating Activities

Cash used in operating activities was \$3.5 million and \$900,000 for the three months ended March 31, 2014 and 2013, respectively. The cash used in the first three months of March 31, 2014 was related to the net loss of \$1.5 million offset by non-cash items of \$1.6 million and the net change in operating assets and liabilities of \$3.6 million. The non-cash items were primarily from depreciation, amortization of intangible assets and debt discounts and financing costs, stock based compensation, equity income in Quest, and impairment of goodwill. The net changes in operating assets and liabilities are primarily related to changes in accounts receivable, accounts payable and accrued liabilities. Our business, including revenue, operating expenses, and operating margins vary depending on commodity prices, the blend of services, the nature of the contract, and volumes. Our operating activities may require additional cash in the future depending on how we expand our operations and until such time as we generate positive cash flow from operations.

Cash Flows from Investing Activities

Cash used in investing activities for the three months ended March 31, 2014 was \$100,000, primarily from costs related to software development. Cash provided from investing activities for the three months ended March 31, 2013 was \$300,000 from distributions received from Quest prior to July 16, 2013.

Cash Flows from Financing Activities

Cash provided by financing activities was \$2.0 million and \$500,000 for the three months ended March 31, 2014 and 2013, respectively, from \$2.0 million of proceeds from our line of credit during the three months ended March 31, 2014 and \$500,000 of proceeds from our senior related party secured convertible note during the three months ended March 31, 2013.

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Capital Resources

As of March 31, 2013, we had \$1.1 million of cash and cash equivalents and a working capital deficit of \$5.4 million. In April 2014, we received \$2.4 million proceeds from the issuance of stock and warrants as described in Note 15. Our primary sources of funds for conducting our business activities are derived from sales of services, commodities, consulting and advertising, from our credit facilities, and from the placement of our equity securities with investors. We require working capital primarily to increase accounts receivable during sales growth, service debt, purchase capital assets, to fund operating expenses, to address unanticipated competitive threats or technical problems, to transition adverse economic conditions, for potential acquisition transactions, and to pursue our following goals:

- expanding sales staff and market reach;
- expanding and developing our IT infrastructure, operations applications, and mobile strategy;
- enhancing, developing, and introducing services and offerings;
- expanding visitors to the *Earth911.com* website and increasing advertising and sponsorship revenue; and
- expanding our customer base for recycling services.

Critical Accounting Estimates and Policies

General

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States, or GAAP. The preparation of our consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to areas that require a significant level of judgment or are otherwise subject to an inherent degree of uncertainty. These areas include carrying amounts of long-lived assets, inventory, deferred financing costs, warrant liability, stock-based compensation expense, and deferred taxes. We base our estimates on historical experience, our observance of trends in particular areas, and information or valuations and various other assumptions that we believe to be reasonable under the circumstances and which form the basis for making judgments about the carrying value of assets and liabilities that may not be readily apparent from other sources. Actual amounts could differ significantly from amounts previously estimated.

We believe that of our significant accounting policies, the following may involve a higher degree of judgment and complexity:

Long-Lived Assets

We periodically evaluate whether events and circumstances have occurred that may warrant revision of the estimated useful life of property and equipment or whether the remaining balance of property and equipment, or other long-lived assets should be evaluated for possible impairment. Instances that may lead to an impairment include the following: (i) a significant decrease in the market price of a long-lived asset group; (ii) a significant adverse change in the extent or manner in which a long-lived asset or asset group is being used or in its physical condition; (iii) a significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset or asset group, including an adverse action or assessment by a regulator; (iv) an accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset or asset group; (v) a current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset or asset group; or (vi) a current expectation that, more likely than not, a long-lived asset or asset group will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

Upon recognition of an event, as previously described, we use an estimate of the related undiscounted cash flows, excluding interest, over the remaining life of the property and equipment and long-lived assets in assessing their recoverability. We measure impairment loss as the amount by which the carrying amount of the asset(s) exceeds the fair value of the asset(s). We primarily employ the two following methodologies for determining the fair value of a long-lived asset: (i) the amount at which the asset could be bought or sold in a current transaction between willing parties; or (ii) the present value of expected future cash flows grouped at the lowest level for which there are identifiable independent cash flows.

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Beneficial Conversion Features

We treat the intrinsic value of a beneficial conversion feature inherent to a convertible note payable, which we do not bifurcate, do not account for separately from the convertible note payable, and we may not settle in cash upon conversion, as a discount to the convertible note payable. We amortize this discount over the period from the date of issuance to the note due date using the effective interest method. If we retire the note payable prior to the end of its contractual term, we expense the unamortized discount in the period of retirement to interest expense. In general, we measure the beneficial conversion feature by comparing the effective conversion price, after considering the relative fair value of detachable instruments included in the financing transaction, if any, to the fair value of the common shares at the commitment date to be received upon conversion.

Stock Options

We estimate fair value of stock options using the Black-Scholes-Merton valuation model. Significant Level 3 assumptions used in the calculation were determined as follows:

- We determine the expected term under the simplified method using an average of the contractual term and vesting period of the award due to the unavailability of appropriate statistical data required to properly estimate the expected term;
- We measure the expected volatility using the historical weekly changes in the market price of our common stock, disregarding identifiable periods of extraordinarily volatile share prices due to certain events that are not expected to recur during the expected term; and
- We approximate the risk-free interest rate using the implied yield on zero-coupon U.S. Treasury bonds with a remaining maturity equal to the expected term of the awards.

Forfeitures are based on the history of cancellations of warrants granted by us and our analysis of potential future forfeitures.

Accounting for Income Taxes

We use the asset and liability method to account for income taxes. We use significant judgment in determining the provision for income taxes, deferred tax assets and liabilities, and any valuation allowance recorded against net deferred tax assets. In preparing our consolidated financial statements, we are required to estimate income taxes in each of the jurisdictions in which we operate. This process involves estimating the actual current tax liability together with assessing temporary differences resulting from differing treatment of items, such as deferred revenue, depreciation on property, plant and equipment, intangible assets, goodwill, and losses for tax and accounting purposes. These differences result in deferred tax assets, which include tax loss carry-forwards, and liabilities, which are included within our consolidated balance sheets. We then assess the likelihood that deferred tax assets will be recovered from future taxable income, and to the extent that recovery is not likely or there is insufficient operating history, we establish a valuation allowance. To the extent we establish or increase a valuation allowance in a period, we include an adjustment within the tax provision of our consolidated statements of operations. As of December 31, 2013, we had established a full valuation allowance for all deferred tax assets.

As of March 31, 2014 and December 31, 2013, we did not recognize any assets or liabilities relative to uncertain tax positions, nor do we anticipate any significant unrecognized tax benefits will be recorded during the next 12 months. We recognize any interest or penalties related to unrecognized tax benefits in income tax expense. Since there are no unrecognized tax benefits as a result of tax positions taken, there are no accrued penalties or interest.

Recently Issued Accounting Pronouncements

There have been no recent accounting pronouncements or changes in accounting pronouncements during the three months ended March 31, 2014 that are of significance, or potential significance to us.

Off-Balance Sheet Financing

We have no off-balance sheet debt or similar obligations. We have no transactions or obligations with related parties that are not disclosed, consolidated into, or reflected in our reported results of operations or financial position. We do not guarantee any third-party debt.

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Item 3. Quantitative and Qualitative Disclosure About Market Risk

Not applicable.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of March 31, 2014.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting identified in management's evaluation pursuant to Rules 13a-15(d) or 15d-15(d) of the Exchange Act during the period covered by this Quarterly Report on Form 10-Q that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations on Effectiveness of Controls and Procedures

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, misstatements, errors, and instances of fraud, if any, within our Company have been or will be prevented or detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls also can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. We base the design of any system of controls in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, internal controls may become inadequate as a result of changes in conditions, or through the deterioration of the degree of compliance with policies or procedures.

PART II: OTHER INFORMATION

Item 1. Legal Proceedings

We may be subject to legal proceedings in the ordinary course of business. As of the date of this Quarterly Report on Form 10-Q, we are not aware of any legal proceedings to which we are a party that we believe could have a material adverse effect on us.

Item 1A. Risk Factors

Investing in our common stock involves a high degree of risk. Before deciding to invest in our common stock, you should carefully consider each of the risk factors described in “Part I – Item 1A. Risk Factors” in our Report on Form 10-K for the year ended December 31, 2013 and all information set forth in this Quarterly Report on Form 10-Q. Those risks could materially harm our business, financial condition, operating results, cash flow, and prospects. If that occurs, the trading price of our common stock could decline, and you may lose all or part of your investment.

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

(None)

Item 3. Defaults Upon Senior Securities

(None)

Item 4. Mine Safety Disclosures

(Not Applicable)

Item 5. Other Information

(a) (None)

(b) (None)

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Item 6. Exhibits

<u>Exhibit No.</u>	<u>Exhibit</u>
4.1	Registration Rights Agreement, dated as of April 18, 2014 by and between Quest Resource Holding Corporation and the Purchasers named therein (1)
10.19(a)	Sixth Amendment to Loan Agreement, dated as of May 9, 2014, by and between Quest Resource Management Group, LLC and Regions Bank (2)
10.19(b)	Guaranty, dated as of May 9, 2014, by Quest Resource Holding Corporation and Earth911, Inc. for the benefit of Regions Bank (2)
10.19(c)	Pledge Agreement, dated as of May 9, 2014, by and between Earth911, Inc. and Regions Bank (2)
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
32.1	Section 1350 Certification of Chief Executive Officer
32.2	Section 1350 Certification of Chief Financial Officer
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

- (1) Filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on April 18, 2014.
(2) Filed as Exhibits 10.19(a), 10.19(b), and 10.19(c) to the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on May 14, 2014.

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.

QUEST RESOURCE HOLDING CORPORATION

Date: May 15, 2014

By: /s/ Brian S. Dick

Brian S. Dick
President and Chief Executive Officer

Date: May 15, 2014

By: /s/ Laurie L. Latham

Laurie L. Latham
Chief Financial Officer

CERTIFICATION

I, Brian S. Dick, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Quest Resource Holding Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal controls over financial reporting, or caused such internal controls over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 15, 2014

/s/ Brian S. Dick

Brian S. Dick
President and Chief Executive Officer
(Principal Executive Officer)

I, Laurie L. Latham, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Quest Resource Holding Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal controls over financial reporting, or caused such internal controls over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 15, 2014

/s/ Laurie L. Latham

Laurie L. Latham
Chief Financial Officer
(Principal Financial and Accounting Officer)

SECTION 1350 CERTIFICATION OF CHIEF EXECUTIVE OFFICER

In connection with the Quarterly Report on Form 10-Q of Quest Resource Holding Corporation (the "Company") for the quarterly period ended March 31, 2014, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Brian S. Dick, President and Chief Executive Officer of the Company, certify, to the best of my knowledge and belief, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Brian S. Dick

Brian S. Dick
President and Chief Executive Officer
(Principal Executive Officer)

Date: May 15, 2014

This certification accompanies the Quarterly Report on Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of Quest Resource Holding Corporation under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Quarterly Report on Form 10-Q), irrespective of any general incorporation language contained in such filing.

SECTION 1350 CERTIFICATION OF CHIEF FINANCIAL OFFICER

In connection with the Quarterly Report on Form 10-Q of Quest Resource Holding Corporation (the "Company") for the quarterly period ended March 31, 2014, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Laurie L. Latham, Chief Financial Officer of the Company, certify, to the best of my knowledge and belief, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Laurie L. Latham

Laurie L. Latham

Chief Financial Officer

(Principal Financial and Accounting Officer)

Date: May 15, 2014

This certification accompanies the Quarterly Report on Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of Quest Resource Holding Corporation under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Quarterly Report on Form 10-Q), irrespective of any general incorporation language contained in such filing.