FIRSTSERVICE CORP
Form 10-Q
February 13, 2004

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2003

or

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

For the transition period from to
Commission File Number 0-24762

FIRSTSERVICE CORPORATION

(Exact name of Registrant as specified in its charter)

Ontario, Canada	**Not Applicable**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification number, if applicable)

FirstService Building
1140 Bay Street, Suite 4000
Toronto, Ontario, Canada
M5S 2B4
(416) 960-9500
(Address and telephone number of Registrant's principal executive office)

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 ý No o

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes ý No o

Indicate the number of shares outstanding of each of the Registrant's classes of common stock as of the latest practicable date:

Subordinate Voting Shares	13,768,043 as of January 31, 2004
Multiple Voting Shares	662,847 as of January 31, 2004

FIRSTSERVICE CORPORATION

Form 10-Q
for the quarterly period ended December 31, 2003

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PART I FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

FIRSTSERVICE CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited)

(in thousands of U.S. Dollars, except per share amounts) in accordance with U.S. generally accepted accounting principles

	Three month periods ended December 31		Nine month periods ended December 31	
	2003	**2002 (restated see note 3)**	**2003**	**2002 (restated see note 3**
Revenues	**$ 152,099**	$ 126,684	**$ 476,427**	$ 417,929
Cost of revenues	**106,523**	89,664	**325,426**	280,998
Selling, general and administrative expenses	**36,082**	28,840	**103,024**	89,077
Depreciation	**3,647**	3,065	**10,462**	9,144
Amortization	**548**	533	**1,808**	1,356
Operating earnings	**5,299**	4,582	**35,707**	37,354

	Three month periods ended December 31		Nine month periods ended December 31	
Interest	**2,021**	2,082	**6,162**	6,666
Earnings before income taxes and minority interest	**3,278**	2,500	**29,545**	30,688
Income taxes	**978**	810	**8,941**	10,072
Earnings before minority interest	**2,300**	1,690	**20,604**	20,616
Minority interest share of earnings	**290**	355	**3,213**	3,179
Net earnings	**$ 2,010**	$ 1,335	**$ 17,391**	$ 17,437
Earnings per share (note 8):				
Basic	**$ 0.14**	$ 0.10	**$ 1.23**	$ 1.26
Diluted	**0.14**	0.09	**1.21**	1.19

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

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FIRSTSERVICE CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(in thousands of U.S. Dollars) in accordance with U.S. generally accepted accounting principles

	December 31, 2003	March 31, 2003 (restated see note 3)
Assets		
Current assets		
Cash and cash equivalents	**$ 11,257**	$ 5,378
Accounts receivable, net	**103,446**	85,484
Inventories	**15,595**	15,095
Prepaids and other assets	**12,450**	13,617
Deferred income taxes	**2,054**	2,808
	144,802	122,382
Other receivables	**7,453**	5,839
Interest rate swaps	**3,161**	6,279
Fixed assets	**49,174**	46,600
Other assets	**2,846**	2,777
Deferred income taxes	**6**	103
Intangible assets	**36,995**	31,427
Goodwill	**186,209**	173,624
	285,844	266,649

		December 31, 2003		March 31, 2003 (restated see note 3)
	$	**430,646**	$	389,031
Liabilities and shareholders' equity				
Current liabilities				
Accounts payable	$	**27,525**	$	22,564
Accrued liabilities		**44,488**		34,270
Income taxes payable		**949**		1,209
Unearned revenues		**7,009**		8,369
Long-term debt current		**3,367**		3,030
Deferred income taxes		**643**		1,066
		83,981		70,508
Long-term debt non-current		**162,198**		161,889
Deferred income taxes		**22,206**		19,404
Minority interest		**16,076**		13,824
		200,480		195,117
Shareholders' equity				
Capital stock		**61,502**		60,571
Receivables pursuant to share purchase plan		**(2,434)**		(2,434)
Retained earnings		**80,339**		62,948
Cumulative other comprehensive earnings		**6,778**		2,321
		146,185		123,406
	$	**430,646**	$	389,031

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

FIRSTSERVICE CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Unaudited)

(in thousands of U.S. Dollars, except share information) in accordance with U.S. generally accepted accounting principles

	Issued and outstanding shares		Capital stock		Receivables pursuant to share purchase plan		Retained earnings		Cumulative other comprehensive earnings (loss)		Total shareholders' equity
Balance, March 31, 2002 as previously reported	13,775,265	$	57,712	$	(2,630)	$	45,386	$	(626)	$	99,842

	Issued and outstanding shares	Capital stock	Receivables pursuant to share purchase plan	Retained earnings	Cumulative other comprehensive earnings (loss)	Total shareholders' equity
Restatement adjustment				(621)		(621)
Balance, March 31, 2002 as restated (see note 3)	13,775,265	57,712	(2,630)	44,765	(626)	99,221
Comprehensive earnings:						
Net earnings				17,437		17,437
Foreign currency translation adjustments					314	314
Comprehensive earnings						17,751
Subordinate Voting Shares:						
Stock options exercised	104,750	747				747
Purchased for cancellation	(2,000)	(40)				(40)
Balance, December 31, 2002 (restated see note 3)	13,878,015	$ 58,419	$ (2,630)	$ 62,202	$ (312)	$ 117,679

	Issued and outstanding shares	Capital stock	Receivables pursuant to share purchase plan	Retained earnings	Cumulative other comprehensive earnings	Total shareholders' equity
Balance, March 31, 2003 as previously reported	14,164,190	$ 60,571	$ (2,434)	$ 63,965	$ 2,321	$ 124,423
Restatement adjustment				(1,017)		(1,017)
Balance, March 31, 2003 as restated (see note 3)	14,164,190	60,571	(2,434)	62,948	2,321	123,406
Comprehensive earnings:						
Net earnings				17,391		17,391
Foreign currency translation adjustments					4,457	4,457
Comprehensive earnings						21,848
Subordinate Voting Shares:						
Stock options exercised	75,500	931				931
Balance, December 31, 2003	14,239,690	$ 61,502	$ (2,434)	$ 80,339	$ 6,778	$ 146,185

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

FIRSTSERVICE CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands of U.S. Dollars) in accordance with U.S. generally accepted accounting principles

	Nine-month periods ended December 31	
	2003	**2002 (restated see note 3)**
Cash provided by (used in)		
Operating activities		
Net earnings	**$ 17,391**	$ 17,437
Items not affecting cash:		
Depreciation and amortization	**12,270**	10,500
Deferred income taxes	**617**	(1,309)
Minority interest share of earnings	**3,213**	3,179
Other	**469**	425
Changes in non-cash working capital:		
Accounts receivable	**(8,976)**	(3,113)
Inventories	**35**	754
Prepaids and other assets	**1,975**	(229)
Accounts payable and other accrued liabilities	**6,134**	2,791
Unearned revenues	**(2,302)**	(3,595)
Net cash provided by operating activities	**30,826**	26,840
Investing activities		
Acquisition of businesses, net of cash acquired	**(14,929)**	(5,396)
Purchases of minority shareholders' interests	**(940)**	(4,204)
Purchases of fixed assets	**(10,555)**	(8,055)
(Purchases) disposals of intangibles and other assets	**(362)**	1,236
Increase in other receivables	**(1,295)**	(121)
Net cash used in investing activities	**(28,081)**	(16,540)
Financing activities		
Increases in long-term debt	**62,389**	10,342
Repayments of long-term debt	**(58,626)**	(16,632)
Financing fees paid	**(399)**	
Issuance of Subordinate Voting Shares, net	**931**	707
Dividends paid to minority shareholders of subsidiaries	**(430)**	(179)
Net cash provided by (used in) financing activities	**3,865**	(5,762)
Effect of exchange rate changes on cash and cash equivalents	**(731)**	142
Increase in cash and cash equivalents during the period	**5,879**	4,680
Cash and cash equivalents, beginning of period	**5,378**	7,332

	Nine-month periods ended December 31	
Cash and cash equivalents, end of period	**$ 11,257**	$ 12,012

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

FIRSTSERVICE CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2003
(Unaudited)
(in thousands of U.S. Dollars, except per share amounts)

1. DESCRIPTION OF THE BUSINESS

FirstService Corporation (the "Company") is a provider of property and business services to commercial, residential and institutional customers in the United States and Canada. The Company's operations are conducted through four segments: Residential Property Management, Integrated Security Services, Consumer Services and Business Services.

2. SUMMARY OF PRESENTATION

The condensed consolidated financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC") for the presentation of interim financial information. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information not misleading. The year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. generally accepted accounting principles.

In the opinion of management, the condensed consolidated financial statements contain all adjustments necessary to present fairly the financial position of the Company as of December 31, 2003, the results of its operations for the three and nine months ended December 31, 2003 and 2002 and cash flows for the nine-month periods ended December 31, 2003 and 2002. All such adjustments are of a normal recurring nature. The results of operations for the nine months ended December 31, 2003 are not necessarily indicative of the results to be expected for the fiscal year ending March 31, 2004. For further information, refer to the consolidated financial statements and footnotes thereto for the fiscal year ended March 31, 2003 contained in the Company's Form 10-K/A as filed with the SEC.

3. RESTATEMENTS

As a result of a detailed review of the accounting for certain intangible assets, including purchase accounting at the times of acquisition and accounting upon the adoption of Statement of Financial Accounting Standards ("SFAS") No. 142, *Goodwill and Other Intangible Assets*, at April 1, 2001, the Company has made certain restatements. In particular, the Company recorded deferred income taxes with respect to franchise intangible assets acquired upon the October 1998 acquisition of California Closet Company, Inc. ("CCC") and the October 1997 acquisition of Paul Davis Restoration, Inc. ("PDR"). In addition, the Company reevaluated the useful lives of the franchise intangible assets associated with CCC and PDR. It was determined that the amortization of franchise rights should follow the pattern of use, specifically the attrition rate of the franchisees that were present at the dates of acquisition. The amortization of trademarks and trade names was determined to be 35 and 25 years for CCC and PDR, respectively. Previously, all of these assets were treated as indefinite life intangible assets.

The following presents the impact on net earnings of the restatement adjustments for the three and nine-month periods ended December 31, 2002.

	Three months ended December 31, 2002	Nine months ended December 31, 2002
Net earnings, as previously reported	$ 1,433	$ 17,733
Adjustments:		
Amortization expense	(205)	(617)
Income tax recovery	87	260
Minority interest	20	61
Net earnings, as restated	$ 1,335	$ 17,437

The consolidated balance sheet as at March 31, 2003 was restated. The recognition of deferred income taxes related to the CCC and PDR franchise intangible assets resulted in an increase to goodwill and an increase to deferred income taxes long-term liability. In addition, the balance sheets were restated to take into account the amortization expense, income tax recovery, minority interest, and effect on retained earnings resulting from the restatement adjustments to net earnings described in the chart above. A reconciliation of the consolidated balance sheet at March 31, 2003 follows.

As at March 31, 2003	**As previously reported**	**Restatement adjustment**	**Restated**
Assets			
Current assets			
Cash and cash equivalents	$ 5,378	$	$ 5,378
Accounts receivable	85,484		85,484
Inventories	15,095		15,095
Prepaids and other	13,617		13,617
Deferred income taxes	2,808		2,808
	122,382		122,382
Other receivables	5,839		5,839
Interest rate swap	6,279		6,279
Fixed assets	46,600		46,600
Other assets	2,777		2,777
Deferred income taxes	103		103
Intangible assets	33,539	(2,112)	31,427
Goodwill	164,610	9,014	173,624
	259,747	6,902	266,649
	$ 382,129	$ 6,902	$ 389,031
Liabilities			
Current liabilities			
Accounts payable	$ 22,564	$	$ 22,564
Accrued liabilities	34,270		34,270
Income taxes payable	1,209		1,209
Unearned revenue	8,369		8,369
Long-term debt current	3,030		3,030
Deferred income taxes	1,066		1,066
	70,508		70,508

As at March 31, 2003	As previously reported	Restatement adjustment	Restated
Long-term debt less current portion	161,889		161,889
Deferred income taxes	11,277	8,127	19,404
Minority interest	14,032	(208)	13,824
	187,198	7,919	195,117
Shareholders' equity			
Capital stock	60,571		60,571
Receivables pursuant to share purchase plan	(2,434)		(2,434)
Retained earnings	63,965	(1,017)	62,948
Cumulative other comprehensive earnings	2,321		2,321
	124,423	(1,017)	123,406
	$ 382,129	$ 6,902	$ 389,031

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4. NEW ACCOUNTING STANDARDS

In April 2003, SFAS No. 149, *Amendment of SFAS 133 on Derivative Instruments and Hedging Activities* ("SFAS 149") was issued. SFAS 149 amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS 133, *Accounting for Derivative Instruments and Hedging Activities* ("SFAS 133"). SFAS 149 is effective for contracts entered into or modified after June 30, 2003 and hedging relationships designated after June 30, 2003. SFAS 149 did not have a material impact on the Company's financial condition or results of operations.

In May 2003, SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity* ("SFAS 150") was issued. SFAS 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity, and is effective for financial instruments entered into or modified after May 31, 2003 and otherwise is effective July 1, 2003. SFAS 150 had no impact on the Company's financial condition or results of operations.

In February 2003, FASB Interpretation No. 46, *Consolidation of Variable Interest Entities (an interpretation of ARB No. 51)* ("FIN 46") was issued. In December 2003, FASB issued FASB Interpretation No. 46 (revised December 2003) ("FIN 46R"). FIN 46R addresses consolidation by business enterprises of variable interest entities having certain characteristics and replaces FIN 46. FIN 46R is effective for the Company's annual financial statements for the year ended March 31, 2004. The Company is evaluating the impact of FIN 46R on its results of operations and financial condition.

5. ACQUISITIONS OF BUSINESSES AND PURCHASES OF MINORITY INTERESTS

During the nine-month period, four businesses were acquired in the Company's Consumer Services segment at a cost of $13,794 ($13,451 net of cash acquired). The purchase prices were allocated as follows: goodwill $9,556; intangible assets $7,387; other net assets $(3,492). During the prior year period, four business acquisitions in the amount of $2,880 ($2,405 net of cash acquired) were completed.

Certain vendors, at the time of acquisition, are entitled to receive contingent consideration if the acquired businesses achieve specified earnings levels during the two to four-year periods following the dates of acquisition. Such contingent consideration is issued at the expiration of the contingency period. As at December 31, 2003, there was contingent consideration outstanding of up to $16,500 ($12,700 as at March 31, 2003). The contingencies will expire during the period extending to April 2007. Vendors are entitled to receive interest on contingent consideration issued to them, which interest is calculated from the acquisition date to the payment date at interest rates ranging from 5% to 7%. The contingent consideration will be recorded when the contingencies are resolved and the consideration is issued or becomes issuable, at which time the Company will record the fair value of the consideration issued or issuable, including interest, as additional costs of the acquired businesses. There was $1,478 of contingent consideration issued or issuable during the nine-month period (2002 $2,991) and allocated to goodwill.

During the nine months ended December 31, 2003, the Company purchased minority interests from one (2002 five) minority shareholder(s) for total consideration of $940 (2002 $4,204). The purchase price for the 2003 purchase was allocated as follows: minority interest $656 and goodwill $284.

6. LONG-TERM DEBT

The Company has an amended and restated credit agreement with a syndicate of banks that provides a $90,000 committed senior revolving credit facility (the "Credit Facility") renewable and extendible in 364-day increments, and if not renewed, a two-year final maturity. The Credit Facility was most recently renewed and extended on May 7, 2003. The Credit Facility bears interest at 1.5% to 3.0% over floating reference rates, depending on certain leverage ratios. At December 31, 2003, the Company had drawn $4,500 on the Credit Facility and had letters of credit of $5,730 outstanding.

The Company has outstanding $100,000 of 8.06% fixed-rate Senior Secured Notes (the "8.06% Notes"), held by a group of U.S. institutional investors. The final maturity of the 8.06% Notes is June 29, 2011, with equal annual principal repayments commencing on June 29, 2005.

On October 1, 2003, the Company issued $50,000 of 6.40% fixed-rate Senior Secured Notes (the "6.40% Notes") to a group of U.S. institutional investors. The 6.40% Notes have a final maturity of September 30, 2015 with equal annual principal repayments commencing on September 30, 2012. The proceeds of the 6.40% Notes were used to repay amounts drawn on the Credit Facility. Concurrent with the issuance of the 6.40% Notes, the Company's Credit Facility was reduced to $90,000 from $140,000 resulting in no net change to the Company's overall borrowing capacity.

The Credit Facility and the Notes rank equally in terms of seniority. The Company has granted the lenders and Note-holders various security including the following: an interest in all of the assets of the Company including the Company's share of its subsidiaries, an assignment of material contracts and an assignment of the Company's "call rights" with respect to shares of the subsidiaries held by minority interests.

The covenants and other limitations within the amended and restated credit agreement and the Note agreements are substantially the same. The covenants require the Company to maintain certain ratios including leverage, fixed charge coverage, interest coverage and net worth. The Company is limited from undertaking certain mergers, acquisitions and dispositions without prior approval.

7. FINANCIAL INSTRUMENTS

The Company has interest rate swap agreements to exchange the fixed rates on the Notes for variable rates. On the 8.06% Notes, one interest rate swap exchanges the fixed rate on $75,000 of principal for LIBOR + 250.5 basis points and a second exchanges the fixed rate on $25,000 for LIBOR + 445 basis points. The terms of the swaps match the term of the Notes with a maturity of June 29, 2011. On October 2, 2003, the Company entered into two interest rate swap agreements to exchange the fixed rate on the $50 million in 6.40% Notes for a variable rate of LIBOR + 170 basis points. The terms of the swaps match the term of the 6.40% Notes with a maturity of September 30, 2015.

The interest rate swaps are being accounted for as fair value hedges in accordance with SFAS 133. The swaps are carried at fair value on the balance sheet, with gains or losses recognized in earnings. The carrying value of the hedged debt is adjusted for changes in fair value attributable to the hedged interest rate risk; the associated gain or loss is recognized currently in earnings. So long as the hedge is considered highly effective, the net impact on earnings is nil. The fair value of the swaps is determined based on the present value of the estimated future net cash flows using implied rates in the applicable yield curve as of the valuation date. Due to changes in the yield curve, the fair values of the swaps fluctuate and at December 31, 2003, the fair values were a gain of $3,161 (2002 gain of $6,279).

The Company from time to time purchases and sells foreign currencies by using forward contracts, which have not been specifically identified as hedges. The values of these contracts are marked to market with resulting gains and losses included in earnings. At December 31, 2003 the Company had outstanding 4 foreign currency contracts to purchase $Cdn10,817 at a rate of $Cdn1.3522 per $US1.0000 on various dates during the period from March 2004 to December 2004, the fair value of which represented a gain of $Cdn350 ($US270). The purpose of the contracts is to match expected future Canadian dollar denominated expenses at the Canadian Business Services operations to U.S. dollar denominated revenues.

8. EARNINGS PER SHARE

The following table presents a reconciliation of the denominators used in computing earnings per share:

(in thousands)	Three-month period ended December 31		Nine-month period ended December 31	
	2003	**2002**	**2003**	**2002**
Basic earnings per share weighted average shares outstanding	**14,227**	13,876	**14,188**	13,846
Assumed exercise of stock options, net of shares assumed acquired under the Treasury Stock Method	**368**	569	**226**	782
Diluted earnings per share weighted average shares outstanding	**14,595**	14,445	**14,414**	14,628

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9. STOCK-BASED COMPENSATION

The Company has a stock option plan for officers, key full-time employees and directors of the Company and its subsidiaries. Options are granted at the market price for the underlying shares on the date of grant. Each option vests over a four-year period and expires five years from the date granted and allows for the purchase of one Subordinate Voting Share.

In December 2002, SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure an Amendment of SFAS 123* ("SFAS 148") was issued. SFAS 148 provides alternative methods of transition for making a voluntary change to fair value-based accounting for stock-based compensation. The Company continues to account for its stock option plans under the intrinsic value recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees* ("APB 25"), and related interpretations. Effective for interim periods beginning after December 15, 2002, SFAS 148 also requires disclosure of pro forma results on a quarterly basis as if the Company had applied the fair value recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation* ("SFAS 123").

In accordance with APB 25, no stock-based employee compensation cost has been recognized in earnings. The following table illustrates the effect on net earnings and earnings per share if the Company had applied the fair value recognition provisions of SFAS 123, as amended, to all options outstanding under the Company's stock option plan.

	Three-month period ended December 31		Nine-month period ended December 31	
	2003	**2002**	**2003**	**2002**
Net earnings, as reported	**$ 2,010**	$ 1,335	**$ 17,391**	$ 17,437
Less: Total stock-based compensation expense determined under fair value method, net of tax	**(544)**	(545)	**(1,631)**	(1,634)
Pro forma net earnings	**$ 1,466**	$ 790	**$ 15,760**	$ 15,803
Reported earnings per share:				
Basic	**$ 0.14**	$ 0.10	**$ 1.23**	$ 1.26
Diluted	**0.14**	0.09	**1.21**	1.19
Pro forma net earnings per share:				
Basic	**$ 0.10**	$ 0.06	**$ 1.11**	$ 1.14
Diluted	**0.10**	0.05	**1.09**	1.08

During the nine-month period ended December 31, 2003, the Company granted 37,000 stock options that call for settlement by the issuance of Subordinate Voting Shares at a weighted average exercise price of $12.00 per share with an estimated fair value of $4.03 per share (2002 34,000 stock options at a weighted average exercise price of $22.04 per share and an estimated fair value of $7.64 per share). The value of these option grants was estimated at the date of grant using a Black-Scholes pricing model with the following assumptions:

	Nine-month period ended December 31	
	2003	2002
Risk-free interest rate	**3.6%**	5.1%
Expected life in years	**4.4**	4.4
Volatility	**30%**	30%
Dividend yield	**0.0%**	0.0%

10. CONTINGENCIES

The Company is involved in legal proceedings and claims primarily arising in the normal course of its business. In the opinion of management, the Company's liability, if any, would not materially affect its results of operations or financial condition.

11. GUARANTEE

In connection with a contract, the Company has assumed risks associated with work to be performed by a third party. In the unlikely event of non-performance by the third party, the maximum exposure to the Company would be $7,713.

12. SEGMENTED INFORMATION

The Company has four reportable operating segments. The segments are grouped with reference to the nature of services provided and the types of clients that use those services. The Company assesses each segment's performance based on operating earnings or operating earnings before depreciation and amortization. Residential Property Management provides property management, maintenance, landscaping, painting and restoration and other services to residential community associations in the United States. Integrated Security Services provides security systems installation, maintenance, monitoring and manpower to primarily commercial customers in Canada and the United States. Consumer Services provides franchised and Company-owned property services to consumers in the United States and Canada. Business Services provides customer support and fulfillment and business process outsourcing services to corporate and institutional clients in Canada and the United States. Corporate includes the costs of operating the Company's headquarters.

OPERATING SEGMENTS

	Residential Property Management	Integrated Security Services	Consumer Services	Business Services	Corporate	Consolidated
Three-month period ended December 31, 2003						
Revenues	$ 54,887	$ 32,592	$ 27,483	$ 37,042	$ 95	$ 152,099
Operating earnings	1,639	2,078	1,119	2,283	(1,820)	5,299
Three-month period ended December 31, 2002						
Revenues	$ 46,810	$ 28,253	$ 19,132	$ 32,428	$ 61	$ 126,684
Operating earnings	1,205	1,735	437	2,268	(1,063)	4,582

	Residential Property Management	Integrated Security Services	Consumer Services	Business Services	Corporate	Consolidated

	Residential Property Management	Integrated Security Services	Consumer Services	Business Services	Corporate	Consolidated
Nine-month period ended December 31, 2003						
Revenues	$ 183,828	$ 92,313	$ 93,768	$ 106,248	$ 270	$ 476,427
Operating earnings	11,703	5,433	15,534	8,038	(5,001)	35,707
Nine-month period ended December 31, 2002						
Revenues	$ 163,496	$ 80,779	$ 76,509	$ 96,923	$ 222	$ 417,929
Operating earnings	11,163	5,089	14,357	10,269	(3,524)	37,354

GEOGRAPHIC INFORMATION

	Canada	United States	Consolidated
Three-month period ended December 31, 2003			
Revenues	$ 43,387	$ 108,712	$ 152,099
Total long-lived assets	60,360	212,018	272,378
Three-month period ended December 31, 2002			
Revenues	$ 39,002	$ 87,682	$ 126,684
Total long-lived assets	53,917	187,668	241,585

	Canada	United States	Consolidated
Nine-month period ended December 31, 2003			
Revenues	$ 144,628	$ 331,799	$ 476,427
Nine-month period ended December 31, 2002			
Revenues	$ 136,257	$ 281,672	$ 417,929

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(in U.S. Dollars)

Results of operations three months ended December 31, 2003 and 2002

Revenues for our third quarter of fiscal 2004 were $152.1 million, 20% higher than the prior year's quarter. Internal growth was 9%, while changes in foreign exchange rates and acquisitions contributed 6% and 5%, respectively.

During the quarter, 31% of our revenues were originally denominated in Canadian currency, and the balance in U.S. dollars. Based on average foreign exchange rates, the Canadian dollar was 19.3% stronger relative to the U.S. dollar during the quarter than in the comparable quarter last year. The Company's Canadian dollar denominated revenues and earnings benefit from a stronger Canadian dollar upon conversion to U.S. dollars. This is offset by exchange losses incurred by certain Business Services operations based in Canada that sell services to U.S. clients in U.S. dollars. If exchange rates had stayed constant year-over-year, the current year's second quarter revenues would have been $7.6 million lower and EBITDA[(1)] would have been $0.1 million higher.

(1) EBITDA is defined as net earnings before extraordinary items, minority interest share of earnings, income taxes, interest, depreciation and amortization. EBITDA excludes income taxes and interest, both of which are charges that require cash settlement. EBITDA is not a recognized measure for financial statement presentation under United States generally accepted accounting principles ("U.S. GAAP"). The most directly comparable U.S. GAAP measure is operating earnings. Operating earnings takes into account depreciation and amortization expenses, while EBITDA does not. Management utilizes EBITDA as a measure to assess the performance of its operations, to evaluate acquisition candidates and establish pricing, for performance-based compensation purposes, and within its debt covenants with its lenders. The Company believes EBITDA is a reasonable measure of operating performance because of the low capital intensity of its service operations. The Company believes EBITDA is a financial metric used by many investors to compare companies, especially in the services industry, on the basis of operating results and the ability to incur and service debt. The table below reconciles EBITDA to operating earnings.

	Three months ended December 31	
	2003	**2002**
EBITDA	$ 9,494	$ 8,180
Less: depreciation and amortization	4,195	3,598
Equals: operating earnings	5,299	4,582

	Nine months ended December 31	
	2003	**2002**
EBITDA	$ 47,977	$ 47,854
Less: depreciation and amortization	12,270	10,500
Equals: operating earnings	35,707	37,354

Third quarter EBITDA was $9.5 million, 16% higher than the $8.2 million reported in the prior year quarter. Our EBITDA margin was 6.2% of revenues versus 6.5% of revenues because of higher corporate costs and foreign exchange in Business Services (higher revenues without corresponding EBITDA). Operating earnings for the quarter were $5.3 million, up from $4.6 million in the prior year due to higher revenues offset by higher depreciation and amortization expenses.

Interest expense was $2.0 million versus $2.1 million recorded in the prior year quarter. The average interest rate during the quarter was 5.3%, approximately 20 basis points higher than last year's quarter. We continued to benefit from low floating reference rates during the quarter. Substantially all of our indebtedness was at variable interest rates during the quarter. We monitor interest rates closely and we intend to fix a portion of our debt if economic indicators warrant.

The consolidated income tax rate declined to approximately 29.8% of earnings before income taxes and minority interest from 32.4% in the prior year's quarter. The reduction in tax rate is primarily the result of efficiencies generated from the cross-border tax structure we implemented in fiscal 2000.

Net earnings for the quarter were $2.0 million, compared to $1.3 million in the prior year quarter, as a result of higher operating earnings from each business segment.

Our Residential Property Management segment reported revenues of $54.9 million for the quarter, up $8.1 million or 17% versus the prior year quarter. Internal growth in core contractual management revenues was 11%, and an additional 6% of growth came from acquisitions completed during the last twelve months. Residential Property Management EBITDA was $2.2 million, up slightly relative to the prior year quarter. Margins declined due to underperformance in our restoration operations and slightly higher insurance costs. Foreign exchange rates did not impact revenue or EBITDA growth.

The revenues of our Integrated Security Services segment rose 15% to $32.6 million. Internal growth was 5%, while foreign exchange on our Canadian operations accounted for the balance of the revenue increase. Integrated Security Services EBITDA was $2.6 million, an increase of 22% over the $2.1 million reported one year ago, and margins improved 50 basis points to 7.9%. The margin improvement was the result of higher gross profit margins on systems installations.

Consumer Services revenues were $27.5 million, an increase of 44% over the prior year period. Internal growth represented 22% of the revenue gain, while acquisitions accounted for 17% and foreign exchange accounted for 5%. EBITDA at Consumer Services was $2.6 million compared to $1.3 million reported in the prior year period. Approximately half of the EBITDA increase was from acquisitions.

Third quarter revenues in Business Services were $37.0 million, an increase of 14% over the fiscal 2003 period. Internal growth accounted for 3% of the revenue increase, while foreign exchange represented the balance. Business Services EBITDA was $3.9 million, up slightly from the $3.7 million reported one year ago. Under-utilization of fulfillment warehouse capacity continued to negatively impact the quarter's margins, but new client wins have slowly begun to increase our utilization, and this is expected to continue. Foreign exchange, while causing reported revenues to increase, had only a nominal impact on EBITDA because margins at our Canadian operations that sell services to U.S. clients in U.S. dollars contracted.

Corporate expenses for the quarter totaled $1.8 million. The $0.8 million increase relative to the prior year was due to foreign exchange of $0.3 million (most Corporate costs are denominated in Canadian dollars) and to increased compensation expense.

Results of operations nine months ended December 31, 2003 and 2002

Revenues for the nine-month period were $476.4 million, 14% higher than revenues reported in the same period one year ago. Internal growth accounted for 6% of the revenue increase, while acquisitions and changes in foreign exchange rates each accounted for 4% of the increase.

During the nine-month period, 30% of our revenues were originally denominated in Canadian currency, and the balance in U.S. dollars. Based on the average foreign exchange rates in effect during the period, the Canadian dollar was 14.4% stronger relative to the U.S. dollar during the period than in the comparable period last year. The Company's Canadian dollar denominated revenues and earnings benefit from a stronger Canadian dollar upon conversion to U.S. dollars. This is offset by exchange losses incurred by certain Business Services operations based in Canada that sell services to U.S. clients in U.S. dollars. If exchange rates had stayed constant year-over-year, the current year period's revenues would have been $18.2 million lower and EBITDA would have been $0.2 million higher.

For the nine months ended December 31, 2003, EBITDA was $48.0 million, up $0.1 million versus the prior year period. The flat comparison was the result of lower profitability in the first quarter, especially in the Business Services segment, offset by improving results in the second and third quarters. Operating earnings were $35.7 million, down $1.6 million versus the prior year entirely due to higher depreciation and amortization expense primarily from fixed and intangible assets acquired in business acquisitions.

Net earnings for the nine-month period were $17.4 million, identical to the comparable period. Net earnings was flat despite the reduction in operating earnings because of lower interest expense due to lower floating interest rates and a decline in our income tax rate.

Residential Property Management reported year-to-date revenues of $183.8 million, reflecting growth of 12% relative to the prior year. Internal growth was 8%, with the balance attributable to acquisitions. Revenue growth came from core property management client wins and ancillary services. EBITDA was $14.9 million, up from $14.0 million in the prior year period.

Integrated Security Services revenues for the nine-month period were $92.3 million, up 14% versus the prior year. Approximately 7% of the revenue increase was a result of internal growth in our US operations, while the balance of the increase related to changes in foreign exchange rates. EBITDA was $6.8 million, up from $6.2 million in the prior year period, while the margin declined slightly to 7.4%.

Consumer Services revenues were $93.8 million, up 23% relative to the prior year period. Internal growth for the period was 13%, acquisitions contributed 5% and foreign exchange rate changes also contributed 5%. EBITDA was $18.3 million, up 11% from $16.5 million, while margins declined from 21.6% in last year's period to 19.6% this year. The margin decline was revenue mix related, since Company-owned operations, such as recently-acquired branchises, contribute lower margins and do not have a seasonal peak in the first half of the year.

Business Services reported year-to-date revenues of $106.2 million, an increase of 10% relative to last year. Foreign exchange accounted for 8% of the increase, while internal growth represented 2%. While revenues contracted early in the year, production started on several new clients in the second quarter to effect the year to date increase. EBITDA was $12.5 million versus $14.6 million reported one year ago, due to excess fulfillment capacity and lower margins on new business. Capacity utilization and corresponding margins are expected to increase slowly over the next few quarters.

Our corporate costs were $4.9 million for the nine months, $1.5 million higher than in the prior period, primarily as a result of foreign exchange impact of $0.6 million (a majority of corporate costs are denominated in Canadian dollars) but also due to an executive severance in the first quarter and higher compensation costs.

Restatements

On January 27, 2004, we announced that as a result of a detailed review of the accounting for certain intangible assets, including purchase accounting at the times of acquisition and accounting upon the adoption of Statement of Financial Accounting Standards ("SFAS") No. 142, *Goodwill and Other Intangible Assets*, at April 1, 2001, certain restatements would be made. In particular, we recorded deferred income taxes with respect to franchise intangible assets acquired upon the October 1998 acquisition of California Closet Company, Inc. ("CCC") and the October 1997 acquisition of Paul Davis Restoration, Inc. ("PDR"). In addition, we reevaluated the estimated useful lives of the franchise intangible assets associated with CCC and PDR. It was determined that the amortization of franchise rights should follow the pattern of use, specifically the attrition rate of the franchisees that were present at the dates of acquisition. The amortization of trademarks and trade names was determined to be 35 and 25 years for CCC and PDR, respectively. Previously, all of these assets were treated as indefinite life intangible assets.

On February 11, 2004, we filed an amended Form 10-K/A for the year ended March 31, 2003 and amended Forms 10-Q/A for the quarters ended June 30, 2003 and September 30, 2003 to reflect the restatements. The cumulative impact of the restatements upon retained earnings to September 30, 2003 was $1.2 million. On an annual basis, the impact upon net earnings for each of the years ended March 31, 2003 and 2002 was $0.4 million comprised of additional amortization expense of $0.8 million less income tax and minority interest effects of $0.4 million. The annual impact on diluted earnings per share for each of these years was $0.03.

Acquisitions

In October 2003, we completed four acquisitions in our Consumer Services segment. Two acquisitions are California Closets franchises (San Francisco and Toronto) that became our fifth and six Company-owned "branchises". In addition, we acquired two franchise systems Pillar to Post, Inc. ("PTP") and Floor Coverings International, Inc. ("FCI"). PTP is one of the largest franchised home inspection services in North America, with 300 franchisees and approximately $30 million in annual system-wide sales. FCI franchises mobile shop-at-home floor coverings businesses with 100 franchisees and annual system-wide sales of $20 million. The four acquisitions collectively generated approximately $10 million in revenues and $1.8 million in EBITDA in their most recent fiscal years prior to acquisition.

Outlook

The outlook presented on October 21, 2003 with our second quarter results for fiscal 2004 was: revenues $590-$600 million; EBITDA $54.5-$56.0 million; operating earnings $39.5-$41.0 million and diluted earnings per share of $1.27-$1.32. This outlook has been updated to take our results for the third quarter into consideration and to reflect the impact of the restatements. The updated outlook is as follows: revenues $610-$620 million; EBITDA $55.0-$56.0 million; and diluted earnings per share of $1.27-$1.30.

The Company also presented a preliminary outlook for the year ended March 31, 2005, which may be updated once our internal budgeting process is completed, which is expected to be before the end of March 2004. The preliminary outlook is: revenues $650-675 million; EBITDA $60.5-$63.0 million; and diluted earnings per share of $1.40-$1.50. The preliminary outlook takes into account the impact of amortization resulting from the restatements, an average foreign exchange rate of $US0.7800 per $Cdn1.0000, no change in interest rates, and no new acquisitions.

Seasonality and quarterly fluctuations

Certain segments of the Company's operations, which in the aggregate comprise approximately 15% of revenues, are subject to seasonal variations. Specifically, the demand for residential lawn care, exterior painting, and swimming pool management in the northern United States and Canada is highest during late spring, summer and early fall and very low during winter. As a result, these operations generate a large percentage of their annual revenues between April and September. The Company has historically generated lower profits or net losses during its first and fourth fiscal quarters, from October to March. Residential Property Management (with the exception of swimming pool management), Integrated Security Services, and Business Services generate revenues roughly evenly throughout the fiscal year.

The seasonality of swimming pool management and certain Consumer Services operations (exterior painting and lawn care) results in variations in quarterly EBITDA margins. Variations in quarterly EBITDA margins can also be caused by acquisitions, which alter the consolidated service mix. The Company's non-seasonal businesses typically generate a consistent EBITDA margin over all four quarters, while the Company's seasonal businesses experience high EBITDA margins in the first two quarters, offset by negative EBITDA in the last two quarters. As non-seasonal revenues increase as a percentage of total revenues, the Company's quarterly EBITDA margin fluctuations should be reduced.

Liquidity and capital resources

Net cash provided by operating activities for the nine-month period was $30.8 million, up from $26.8 million in the prior year. The most significant factor contributing to the increase in cash flow was more efficient utilization of working capital. We believe that cash from operations and other existing resources will continue to be adequate to satisfy the ongoing working capital needs of the Company.

Net indebtedness as at December 31, 2003 was $151.2 million, down from $153.3 million at March 31, 2003. Net indebtedness is calculated as the current and non-current portion of long-term debt adjusted for interest rate swaps less cash and cash equivalents. Cash from operating activities was generally offset by investing activities (business acquisitions and fixed assets), resulting in a small decline in net indebtedness during the period.

We are in compliance with the covenants within our financing agreements as at December 31, 2003 and, based on our outlooks for the balance of the year and for fiscal 2005, we expect to remain in compliance with the covenants. We had $79.8 million of available un-drawn credit as of December 31, 2003.

On October 1, 2003, we completed a private placement of $50 million of 6.40% Senior Secured Notes (the "6.40% Notes") due September 30, 2015. The 6.40% Notes have an average life of 10.5 years, with equal annual principal repayments commencing September 30, 2012. Concurrent with the issuance of the 6.40% Notes, we amended our credit facility such that available credit was reduced by $50 million from $140 million to $90 million. Our total borrowing capacity remains unchanged. On October 2, 2003, we entered into interest rate swap agreements to exchange the fixed rate on the 6.40% Notes for a variable rate of LIBOR + 170 basis points.

For the nine months ended December 31, 2003, capital expenditures were $10.6 million. Significant purchases included service vehicle fleet replacement and expansion for the Company-owned Consumer Services and Residential Property Management operations and a call center technology upgrade in Business Services. Capital expenditures for the year are expected to be approximately $12 million, slightly higher than the amount expended during fiscal 2003.

In relation to acquisitions completed during the past three years, we have outstanding contingent consideration totaling $16.5 million as at December 31, 2003 ($12.7 million as at March 31, 2003). The amount of the contingent consideration is not recorded as a liability unless the outcome of the contingency is determined to be beyond a reasonable doubt. The contingent consideration is based on achieving specified earnings levels, and is issued or issuable at the end of the contingency period. When the contingencies are resolved and additional consideration is distributable, we will record the fair value of the additional consideration as additional costs of the acquired businesses.

In those operations where managements are also minority owners, the Company is party to shareholders' agreements. These agreements allow us to "call" the minority position for a predetermined formula price, which is usually equal to the multiple of trailing two-year average earnings paid by the Company for the original acquisition. Minority owners may also "put" their interest to the Company at the same price, with certain limitations. The total value of the minority shareholders' interests, as calculated in accordance with shareholders' agreements, was approximately $30 million at December 31, 2003 (March 31, 2003 $26.0 million). While it is not our intention to acquire outstanding minority interests, this step would materially increase net earnings. On an annual basis, the impact of the acquisition of all minority interests would increase interest expense by $1.1 million, reduce income taxes by $0.3 million and reduce minority interest share of earnings by $3.2 million, resulting in an approximate increase to net earnings of $2.4 million.

Critical accounting policies

There has been no change in the Company's critical accounting policies from those described in our annual report on Form 10-K/A for the year ended March 31, 2003.

New accounting standards

For a discussion of recently issued accounting standards, please refer to note 4 to the accompanying condensed consolidated financial statements.

Forward-looking statements

This quarterly report on Form 10-Q contains or incorporates by reference certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. We intend that such forward-looking statements be subject to the safe harbors created by such legislation. Such forward-looking statements involve risks and uncertainties and include, but are not limited to, statements regarding future events and the Company's plans, goals and objectives. Such statements are generally accompanied by words such as "intend", "anticipate", "believe", "estimate", "expect" or similar statements. Our actual results may differ materially from such statements. Factors that could result in such differences, among others, are:

- Political conditions, including any outbreak or escalation of terrorism or hostilities and the impact thereof on our business.
- U. S. and Canadian economic conditions, especially as they relate to consumer spending and business spending on customer relations and promotion.
- Extreme weather conditions impacting demand for our services or our ability to perform those services.
- Competition in the markets served by the Company.
- Labor shortages or increases in wage rates.
- The effects of changes in interest rates on our cost of borrowing.
- Unexpected increases in operating costs, such as insurance, workers' compensation, health care and fuel prices.
- Changes in government policies at the federal, state/provincial or local level that may adversely impact our firearms registration processing, lawn care, textbook fulfillment or other activities.
- The effects of changes in the Canadian dollar foreign exchange rate in relation to the U.S. dollar on the Company's Canadian dollar denominated revenues and expenses.
- Our ability to make acquisitions at reasonable prices and successfully integrate acquired operations.

Although we believe that the assumptions underlying our forward-looking statements are reasonable, any of the assumptions could prove inaccurate and, therefore, there can be no assurance that the results contemplated in such forward-looking statements will be realized. The inclusion of such forward-looking statements should not be regarded as a representation by the Company or any other person that the future events, plans or expectations contemplated by the Company will be achieved. We note that past performance in operations and share price are not necessarily predictive of future performance.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

During the past three months, there was no material change to our market risk profile, including foreign currency and interest rate risks, as described in Item 7A of the Company's Form 10-K for the fiscal year ended March 31, 2003 as filed with the SEC.

ITEM 4. CONTROLS AND PROCEDURES

a) *Evaluation of disclosure controls and procedures.* The Company's CEO and CFO have evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this report. They have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were adequate and effective to ensure that material information relating to the Company and its consolidated subsidiaries would be made known to them by others within those entities and would be disclosed on a timely basis.

b) *Changes in internal control over financial reporting.* As of the end of the period covered by this report, there were no changes in the Company's internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

c) *Limitations on the effectiveness of controls.* The Company's management, including the CEO and CFO, does not expect that the Company's disclosure controls will prevent all error and 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.

PART II OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

1. a) Exhibits

31.1-31.2	Certifications of CEO and CFO pursuant to Rule 13a-14(a) or 15d-14(a).
32.1-32.2	Certifications of CEO and CFO pursuant to 18 U.S.C. Section 1350, as enacted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

b) Reports on Form 8-K
A Form 8-K report regarding the Company's earnings press release for the third quarter ended December 31, 2003 was filed with the SEC on January 27, 2003.

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.

FIRSTSERVICE CORPORATION

February 13, 2004

/s/ JAY S. HENNICK

Jay S. Hennick
President and Chief Executive Officer
(Principal Executive Officer)

February 13, 2004

/s/ JOHN B. FRIEDRICHSEN

John B. Friedrichsen
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)

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