FIRSTSERVICE CORP
Form 10-Q
August 14, 2001

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2001

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______ to ______

Commission File Number 0-24762

FIRSTSERVICE CORPORATION
(Exact name of Registrant as specified in its charter)

ONTARIO, CANADA (State or other jurisdiction of incorporation or organization)	NOT APPLICABLE (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 [X] or No [ ]

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 - 12,838,393 as of July 31, 2001

Multiple Voting Shares - 662,847 as of July 31, 2001

FIRSTSERVICE CORPORATION

FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 2001

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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 period ended June 30 2001	
		(NOTE 3)	
Revenues		$136,575	$10
Cost of revenues		89,358	6
Selling, general and administrative expenses		28,457	2
Depreciation		2,752	
Amortization		204	
Interest		2,668	
Earnings before income taxes and minority interest		13,136	
Income taxes		4,595	
Earnings before minority interest		8,541	
Minority interest share of earnings		1,451	
Net earnings before extraordinary item		$7,090	$
Extraordinary loss on early retirement of debt, net of income tax benefit of $578		797	
Net earnings		$6,293	$
EARNINGS PER SHARE			
Net earnings before extraordinary item:	Basic	$0.53	
	Diluted	$0.49	
Net earnings:	Basic	$0.47	
	Diluted	$0.44	
Weighted average shares outstanding:	Basic	13,395	1
(in thousands)	Diluted	14,400	1

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

FIRSTSERVICE CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands of U.S. dollars) - in accordance with U.S. generally accepted accounting principles.

	June 30 2001	M

	(UNAUDITED) (NOTE 3)	(
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$9,254	
Accounts receivable, net	92,230	
Inventories	9,656	
Prepaids and other assets	11,403	
Deferred income taxes	1,178	
	123,721	
Other receivables	5,707	
Fixed assets	43,593	
Other assets	2,472	
Deferred income taxes	1,349	
Intangible assets	3,355	
Goodwill	157,770	
	214,246	
	$337,967	
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$23,565	
Accrued liabilities	32,270	
Income taxes payable	5,214	
Unearned revenue	14,536	
Long-term debt - current (note 4)	3,042	
Deferred income taxes	278	
	78,905	
LONG-TERM LIABILITIES		
Long-term debt less current portion (note 4)	157,676	
Deferred income taxes	4,276	
	161,952	
Minority interest	10,154	
SHAREHOLDERS' EQUITY		
Capital stock	56,197	
Receivables pursuant to share purchase plan	(3,196)	
Retained earnings	34,265	
Cumulative other comprehensive loss	(310)	
	86,956	
	$337,967	

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.

	Three month p ended June 2001
	(NOTE 3)
CASH PROVIDED BY (USED IN)	
OPERATING ACTIVITIES	
Net earnings	$6,293
Items not affecting cash:	
Depreciation and amortization	2,956
Deferred income taxes	(159)
Minority interest share of earnings	1,451
Extraordinary loss on early retirement of debt	1,375
Other	110
	12,026
Changes in operating assets and liabilities:	
Accounts receivable	(9,449)
Inventories	87
Prepaids and other assets	(458)
Accounts payable and other current liabilities	(1,083)
Unearned revenue	4,731
Net cash provided by operating activities	5,854
INVESTING ACTIVITIES	
Acquisition of businesses, net of cash acquired	(1,190)
Purchase of minority shareholders' interest	-
Purchases of fixed assets, net	(4,993)
Decrease in intangibles and other assets	53
Increase in other receivables	(470)
Net cash used for investing	(6,600)
FINANCING ACTIVITIES	
Increase in long-term debt, net	6,439
Financing fees paid	(2,561)
Issuance of Subordinate Voting Shares, net of repurchases	1,334
Dividends paid to minority shareholders of subsidiaries	(70)
Net cash provided by financing	5,142
Effect of exchange rate changes on cash	(257)
Increase in cash and cash equivalents during the period	4,139
Cash and cash equivalents, beginning of period	5,115
Cash and cash equivalents, end of period	$9,254

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

FIRSTSERVICE CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2001
(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 residential, corporate and public sector customers in the United States and Canada. The Company's operations are conducted through two operating divisions, Property Services and Business Services. The Property Services division includes Residential Property Management, Integrated Security Services and Consumer Services and represented approximately 80% of the Company's revenues for the year ended March 31, 2001. The Business Services division provides customer support & fulfillment and business process outsourcing services to corporations and government agencies.

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 Securities and Exchange Commission for the presentation of interim financial information. Certain information and footnote disclosures normally included in 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.

   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 June 30, 2001 and the results of its operations for the three months ended June 30, 2001 and 2000 and its cash flows for the three months ended June 30, 2001 and 2000. All such adjustments are of a normal recurring nature. The results of operations for the three months ended June 30, 2001 are not necessarily indicative of the results to be expected for the year ending March 31, 2002. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended March 31, 2001 contained in the Company's Form 10-K filed on June 29, 2001.

3. ADOPTION OF NEW ACCOUNTING STANDARDS - Effective April 1, 2001, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 142 - Goodwill and Other Intangible Assets. These standards require the Company to no longer amortize goodwill. This results in a material increase in net earnings and earnings per share.

   The prior period figures have not been restated for the impact of SFAS No. 142. The tables below provide a reconciliation of previously reported earnings to the earnings adjusted for SFAS No. 142.

	Three months ende 2001
Reported net earnings before extraordinary item	$7,090
Goodwill amortization	
Minority interest	
Adjusted net earnings before extraordinary item	$7,090
Reported net earnings	$6,293
Goodwill amortization	
Minority interest	
Adjusted net earnings	$6,293
NET EARNINGS PER SHARE BEFORE EXTRAORDINARY ITEM:	
BASIC	
Reported	$0.53
Goodwill amortization	
Minority interest	
Adjusted	$0.53
DILUTED	
Reported	$0.49
Goodwill amortization	
Minority interest	
Adjusted	$0.49
NET EARNINGS PER SHARE:	
BASIC	
Reported	$0.47
Goodwill amortization	
Minority interest	
Adjusted	$0.47
DILUTED	
Reported	$0.44
Goodwill amortization	
Minority interest	
Adjusted	$0.44

4. LONG-TERM DEBT - On June 29, 2001, the Company amended and restated its lending agreement to allow for the issuance of additional debt. The

amended and restated agreement provides a $140 million 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 allows for borrowing in either U.S. or Canadian currency and bears interest at 1.50% to 3.00% over floating reference rates, depending on certain leverage ratios. At June 30, 2001, the Company had drawn $50.9 million on the Credit Facility, and had $89.1 million of available un-drawn credit.

Also on June 29, 2001, the Company completed a private placement of $100 million of 8.06% fixed-rate Senior Secured Notes (the "Notes"). The Notes have a final maturity of ten years, with equal annual principal repayments beginning at the end of the fourth year, resulting in a seven-year average life.

The Credit Facility and the Notes are pari-passu in terms of security. 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 lending agreement and the Note agreement are substantially the same. The covenants require the Company to maintain certain ratios including leverage, fixed charge coverage, interest coverage and net worth. Other limitations include prohibition from paying dividends, and without prior approval, from undertaking certain mergers, acquisitions and dispositions.

5. COMPREHENSIVE INCOME - Total comprehensive income was $6,166 and $4,231 for the three months ended June 30, 2001 and 2000, respectively. Total comprehensive income includes net earnings, foreign currency exchange adjustments and current income taxes on realized foreign exchange gains for income tax purposes.

6. SEGMENTED INFORMATION - Within the Property Services division, three operating units (Residential Property Management, Integrated Security Services and Consumer Services) provide a variety of services to residential and commercial customers. The Business Services division provides customer support & fulfillment and business process outsourcing services to corporate and institutional clients.

OPERATING SEGMENTS

	Property Services - residential property management	Property Services - integrated security services	Property Services - consumer services	Business Services	C

THREE MONTH PERIOD ENDED JUNE 30, 2001				
Revenues	$56,995	$22,874	$25,613	$31,031
Operating profit	5,961	1,595	5,132	4,297
Total assets	95,311	45,743	61,297	126,303
THREE MONTH PERIOD ENDED JUNE 30, 2000				
Revenues	$46,611	$15,231	$24,527	$18,977
Operating profit	4,638	609	4,430	3,282
Total assets	82,472	32,834	53,987	75,085

GEOGRAPHIC SEGMENTS

	Canada	United States	Consolidated
THREE MONTH PERIOD ENDED JUNE 30, 2001			
Revenues	$47,874	$88,701	$136,575
Total assets	112,632	225,335	337,967
THREE MONTH PERIOD ENDED JUNE 30, 2000			
Revenues	$32,194	$73,197	$105,391
Total assets	67,710	180,575	248,285

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(in U.S. dollars)

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. The Company intends 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. The Company's actual results may differ materially from such statements. Among the factors that could result in such differences are the impact of weather conditions, increased competition, labor shortages, the condition of the United States and Canadian economies and the ability of the Company to make acquisitions at reasonable prices. Although the Company believes that the assumptions underlying its 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. The Company notes that past performance in operations and share price are not necessarily predictive of future performance.

RESULTS OF OPERATIONS - THREE MONTHS ENDED JUNE 30, 2001 AND 2000

Revenues increased $31.2 million, or 30%, to $136.6 million in the first quarter of fiscal 2002 from $105.4 million in the first quarter of fiscal 2001. Approximately $22.0 million of the increase is attributable to acquired companies owned less than one year including Herbert A. Watts Ltd. ("Watts"), Security Services and Technologies ("SST") and several smaller tuck-under acquisitions.

Earnings before interest, taxes, depreciation and amortization ("EBITDA") increased 30% to $18.8 million from $14.5 million in the prior year period. The EBITDA margin for the three months ended June 30, 2001 was 13.7%, unchanged versus the prior year.

Depreciation for the quarter ended June 30, 2001 was $2.8 million, up 58% from the prior year quarter due largely to acquisitions. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 142 - Goodwill and Other Intangible Assets, effective April 1, 2001, goodwill is no longer being amortized in the Statement of Earnings.

Interest expense for the quarter increased 19% over prior year levels to $2.7 million as a result of increased borrowings related to acquisitions offset by lower interest rates. All acquisitions completed during the past year have been financed through the Company's credit facilities.

The income tax provision for the second quarter was approximately 35% of earnings before taxes, lower than the 40% recorded in the prior year. Before the adoption of SFAS No. 142, the fiscal 2002 tax rate was 38%.

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Minority interest increased to $1.5 million or 17.0% of earnings before minority interest from $1.1 million or 16.9% in the prior year quarter (adjusted for SFAS No. 142). The 32% increase in minority interest reflects the 31% increase in earnings before minority interest.

Net earnings before the extraordinary item were $7.1 million, up 31% over the prior year period (adjusted for SFAS No. 142), while diluted earnings per share increased 23% to $0.49 from $0.40. The increase in diluted earnings per share reflects a 6% increase in the weighted average share count as a result of shares issued upon the exercise of options and an increase in dilution caused by the 80% increase in the average market price of the Company's shares relative to the prior year.

On June 29, 2001, the Company recorded an extraordinary loss of $797,000 (after taxes) on the early retirement of debt. The loss represented the unamortized portion of financing fees related to the prior credit facility. The prior credit facility was terminated to allow for the issuance of additional senior debt.

Revenues for the Property Services division were $105.5 million, an increase of $19.1 million or 22% over the prior year due to internal growth of approximately 8% as well as several acquisitions. Property Services EBITDA grew 24% to $14.5 million or 13.7% of revenue compared to $11.6 million or 13.5% of revenue in the prior year. The Property Services division is comprised of three service lines - Residential Property Management, Integrated Security Services and Consumer Services.

Residential Property Management revenue was $57.0 million for the quarter, up 22% over the prior year. EBITDA grew 26% to $7.1 million, while EBITDA margins increased to 12.4% from 12.0% last year. Organic revenue growth was 10%, with the balance coming from acquisitions completed in the past 12 months, most notably Aquashield Corporation, a building restoration contractor in South Florida, Arco Management, a residential property manager in New York City, and Dickinson Management, a full-service residential property manager operating in Jupiter and Palm Beach County in Florida.

Integrated Security Services posted revenue of $22.9 million, up 50% over the prior year reflecting the impact of the acquisition of SST, which was acquired in July 2000, together with strong internal growth. EBITDA was $1.9 million, double the prior year's figure, while EBITDA margins improved from 6.2% last year to 8.3% in the current quarter. Margin improvement resulted from a shift in service mix toward higher-margin systems integration, with reduced emphasis on security officer services.

In Consumer Services, revenue advanced to $25.6 million, an increase of 4% over last year, while EBITDA increased to $5.5 million, up 8%. The margin was 21.4% compared to 20.7% in the prior year period. Revenue growth was attributable to the Creative Closets Boston acquisition completed in October 2000. Internal revenue growth was flat for two reasons: a planned decline in product sales at California Closets and production timing at the lawn care operations. California Closets has historically provided laminated board and other supplies to franchisees, but has decided to transition away from this practice and instead facilitate direct relationships between franchisees and product suppliers. This has the impact of lowering California Closets revenue and inventory but increasing margins. California Closets system-wide sales were up over the prior year period. Lawn care operations, located in Canada, experienced a slow start to the season due to residual snow cover that lasted into mid-April. As a result, at quarter-end, revenue from lawn care services was two to three weeks behind where it was last year despite gains in customer count. Lawn care operations are expected to get back on schedule in the second and third quarters.

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Revenues for the Business Services division rose to $31.0 million for the third quarter, a 64% increase over the prior year primarily from the impact of the acquisition of Watts. Business Services EBITDA increased to $5.5 million or 17.6% of revenue, compared to $4.0 million and 21.2% of revenue in the prior year. The margin decline is attributable to the change in service mix resulting from the Watts acquisition.

Corporate expenses remained flat at $1.2 million versus the prior year period in the first quarter.

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 commercial swimming pool services in the northern United States and in 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 third and fourth fiscal quarters, from October to March. Residential Property Management (with the exception of swimming pool services), Integrated Security Services, and Business Services generate revenues evenly throughout the fiscal year.

The seasonality of swimming pool services 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

On June 29, 2001, the Company amended and restated its lending agreement to allow for the issuance of additional debt. The amended and restated agreement provides a $140 million committed 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 allows for borrowing in U.S. and / or Canadian currency and bears interest at 1.50% to 3.00% over floating reference rates, depending on certain leverage ratios. Also on June 29, 2001, the Company completed a private placement of $100 million of 8.06% Senior Secured Notes (the "Notes"). The Notes have a final maturity of ten years, with equal annual principal repayments beginning at the end of the fourth year, resulting in a seven-year average life. Covenants and other limitations within the amended lending agreement and the Notes are similar to those contained in the prior lending agreement.

In connection with the Credit Facility and the Notes, the Company incurred legal, agency and placement fees totaling $2.6 million, which will be amortized over the life of the associated debt.

The Company believes these new credit arrangements will provide stability and flexibility to finance acquisitions and working capital requirements for the foreseeable future. Under the new credit arrangements, un-drawn available credit under the Credit Facility was $89.1 million at June 30, 2001. The higher interest rates with the new credit arrangements, relative to the prior lending agreement, offset by recent declines in LIBOR, will result in a slightly higher average interest rate in fiscal 2002.

During the quarter ended June 30, 2001, capital expenditures were $5.0 million. Significant items included $1.6 million for service vehicles, $1.2 million for a building in South Florida for the expansion of Residential Property Management operations, and $1.0 million in computer equipment and software purchases, primarily in Business Services.

Business acquisitions for the quarter totaled $1.2 million, comprised of two Residential Property Management tuck-under acquisitions completed during the quarter. In connection with certain acquisitions, the Company has agreed to pay additional consideration based on operating results of the acquired entities. The payment of any such amounts would be in cash and would result in an increase in the purchase prices for such acquisitions and, as a result, additional goodwill.

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ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

1. a) Exhibits

3.1*	Articles of Incorporation and Amendment
3.2*	By-Laws and Amendments
10.1*	Credit Facility dated April 1, 1999 among the Company and syndicate of bank lenders
10.2**	FirstService Corporation Amended Stock Option Plan # 2
10.3**	FirstService Corporation Amended Share Purchase Plan # 2
10.4***	Amended and Restated Credit Agreement Dated June 21, 2001 among the Company and syndicate of bank lenders
10.5***	Note and Guarantee Agreement - $US100 million 8.06% Guaranteed Senior Secured Notes due 2011

b) Reports on Form 8-K

None.

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* Incorporated by reference to the Company's report on Form 10-Q for the period ended June 30, 1999.

** Incorporated by reference to the Company's report on Form 10-K for the year ended March 31, 2000.

*** Included herein.

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SIGNATURE

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.

Date: August 14, 2001

FIRSTSERVICE CORPORATION

/s/ D. Scott Patterson

D. Scott Patterson
Senior Vice President and Chief Financial Officer
(PRINCIPAL FINANCIAL OFFICER & AUTHORIZED SIGNATORY)