

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

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2002

COMMISSION FILE NUMBER: 1-13011

COMFORT SYSTEMS USA, INC.
(Exact name of registrant as specified in its charter)

DELAWARE
(State or Other Jurisdiction
of Incorporation or Organization)

76-0526487
(I.R.S. Employer
Identification No.)

777 POST OAK BLVD.
SUITE 500
HOUSTON, TEXAS 77056
(713) 830-9600
(Address and telephone number of Principal Executive Offices)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

TITLE OF EACH CLASS -----	NAME OF EACH EXCHANGE ON WHICH REGISTERED -----
Common Stock, \$.01 par value	New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: NONE

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes [X] No []

As of March 25, 2003, the aggregate market value of the 36,200,882 shares of the registrant's common stock held by non-affiliates of the registrant was \$179,918,384, based on the \$4.97 last sale price of the registrant's common stock on the New York Stock Exchange on June 28, 2002.

As of March 25, 2003, 37,923,494 shares of the registrant's common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Part III (other than the required information regarding executive officers) is incorporated by reference from the registrant's definitive proxy statement, which will be filed with the Commission not later

than 120 days following December 31, 2002.

FORWARD-LOOKING STATEMENTS

This report contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended ("Securities Act") and Section 21E of the Exchange Act. Such forward-looking statements are made only as of the date of this report and involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or achievements of the Company, or industry results, to differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements. Such risks, uncertainties and other important factors include, among others, the lack of a combined operating history and the difficulty of integrating formerly separate businesses, retention of key management, national or regional declines in non-residential construction activity, difficulty in obtaining or increased costs associated with debt financing or bonding, shortages of labor and specialty building materials, seasonal fluctuations in the demand for HVAC systems and the use of incorrect estimates for bidding a fixed price contract. Important factors that could cause actual results to differ are discussed under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Factors Which May Affect Future Results."

PART I

ITEM 1. BUSINESS

Comfort Systems USA, Inc., a Delaware corporation, provides comprehensive heating, ventilation and air conditioning ("HVAC") installation, maintenance, repair and replacement services within the mechanical services industry in 57 cities throughout the United States.

We operate primarily in the commercial and industrial HVAC markets, and perform most of our services within office buildings, retail centers, apartment complexes, manufacturing plants, and healthcare, education and government facilities. In addition to standard HVAC services, we provide specialized applications such as building automation control systems, fire protection, process cooling, electronic monitoring and process piping. Certain locations also perform related activities such as electrical service and plumbing. Approximately 96% of our consolidated 2002 revenues were derived from commercial and industrial customers with approximately 52% of the revenues attributable to installation services in newly constructed facilities and 48% attributable to maintenance, repair and replacement services. Our consolidated 2002 revenues were derived from the following service activities, all of which are in the mechanical services industry, the single industry segment we serve:

SERVICE ACTIVITY	PERCENTAGE OF REVENUE
-----	-----
HVAC.....	73
Plumbing.....	10
Building Automation Control Systems.....	5
Electrical.....	3
Fire Protection.....	2
Other.....	7

Total.....	100

We were originally formed in 1997 through an initial public offering, or IPO, and simultaneous acquisition of 12 companies engaged in our business. From the time we completed our IPO through December 1999, we acquired 107 HVAC and complementary businesses, of which 26 were "tuck-in" operations that were integrated with our existing operations. Since we suspended our acquisition program in late 1999, we have sold or ceased operations at 29 companies through 2002.

Significantly, on March 1, 2002, we sold 19 operations to Emcor Group, Inc. for \$186.25 million, including Emcor's assumption of approximately \$22.1 million of subordinated notes to former owners of certain of the divested companies.

These 19 operations provided \$683.4 million and \$657.9 million of our revenue in 2000 and 2001, respectively. We used the proceeds from this sale to reduce debt. We recognized a

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loss of \$11.8 million and a goodwill impairment charge prior to the sale of \$32.4 million, net of taxes, related to the sold operations. For a further discussion of this sale, see "Item 8 -- Financial Statements and Supplemental Data -- Notes 3 and 4."

Our Internet address is <http://www.csusafix.com>. We make available free of charge on or through our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

INDUSTRY OVERVIEW

We believe that the HVAC industry as a whole generates annual revenues in excess of \$75 billion, over \$40 billion of which is in the commercial and industrial markets. HVAC systems are necessary to virtually all commercial and industrial buildings as well as homes. Because most commercial buildings are sealed, HVAC systems provide the primary method of circulating fresh air in such buildings. In many instances, replacing an aging system with a modern, energy-efficient HVAC system significantly reduces a building's operating costs and improves air quality and the HVAC system effectiveness. Older commercial and industrial facilities often have poor air quality as well as inadequate air conditioning, and older HVAC systems result in significantly higher energy costs than do modern systems. These factors cause many facility owners to consider replacing older systems early.

Many factors positively affect HVAC industry growth, particularly (i) an aging installed base, (ii) increasing efficiency, sophistication and complexity of HVAC systems, (iii) opportunities associated with utility deregulation, (iv) increasing emphasis on indoor air quality, and (v) reduction or elimination of the refrigerants commonly used in older HVAC systems. We believe these factors should increase demand for the reconfiguration or replacement of existing HVAC systems and may also mitigate, to some extent, the effect on the HVAC industry of the cyclical nature inherent in the traditional construction industry.

The HVAC industry can be broadly divided into two service functions:

- installation in newly constructed facilities, which provided approximately 52% of our revenues in 2002, and
- maintenance, repair and replacement, which provided the remaining 48% of our 2002 revenues.

Installation Services. Installation services consist of "design and build" and "plan and spec" projects. In "design and build" projects, the commercial HVAC firm is responsible for designing, engineering and installing a cost-effective, energy-efficient system customized to the specific needs of the building owner. Costs and other project terms are normally negotiated between the building owner or its representative and the HVAC firm. Firms that specialize in "design and build" projects generally have specially-trained HVAC engineers, CAD/CAM design systems and in-house sheet metal and prefabrication capabilities. These firms use a consultative approach with customers and tend to develop long-term relationships with building owners and developers, general contractors, architects and property managers. "Plan and spec" installation refers to projects where a third-party architect or consulting engineer designs the HVAC systems and the installation project is "put out for bid." We believe that "plan and spec" projects usually take longer to complete than "design and build" projects because the system design and installation process generally are not integrated and because the resulting bid process often takes months to complete. Furthermore, in "plan and spec" projects, the HVAC firm is not responsible for project design and other parties must also approve any changes, thereby increasing overall project time and cost.

Maintenance, Repair and Replacement Services. These services include maintaining, repairing, replacing, reconfiguring and monitoring previously installed HVAC systems and building automation controls. The growth and aging of the installed base of HVAC systems and the demand for more efficient,

sophisticated and complex systems and building automation controls have fueled growth in this service line. The increasing sophistication and complexity of these HVAC systems is leading many commercial and industrial building owners and property managers to increase attention to maintenance and to outsource maintenance and repair, often through service agreements with HVAC service providers. In addition, further restrictions have been

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placed on the use of certain types of refrigerants used in HVAC systems, which, along with indoor air quality concerns, may increase demand for the reconfiguration and replacement of existing HVAC systems. State-of-the-art control and monitoring systems feature electronic sensors and microprocessors. These systems require specialized training to install, maintain and repair, and the typical building engineer has not received this training. Increasingly, HVAC systems in commercial and industrial buildings are being remotely monitored through PC-based communications systems to improve energy efficiency and expedite problem diagnosis and correction, thereby allowing us to provide maintenance and repair services at a lower cost.

STRATEGY

We are focusing on strengthening operating competencies and increasing operating margins. The key elements of our operating strategy are:

Achieve Excellence in Core Competencies. We have identified six core competencies, which we believe are critical to attracting and retaining customers, increasing operating income and cash flow and creating additional employment opportunities. The six core competencies are: (i) customer cultivation and intimacy, (ii) design and build expertise, (iii) estimating, (iv) job costing and job measurements, (v) safety, and (vi) service capability.

Achieve Operating Efficiencies. We think we can achieve operating efficiencies and cost savings through purchasing economies, adopting "best practices" operating programs, and focusing on job management to deliver services in a cost-effective and efficient manner. For example, we use our combined purchasing to gain volume discounts on products and services such as HVAC components, raw materials, services, vehicles, advertising, bonding, insurance and employee benefits.

Attract and Retain Quality Employees. We seek to attract and retain quality employees by providing them (i) an enhanced career path from working for a larger company, (ii) additional training, education and apprenticeships to allow talented employees to advance to higher-paying positions, (iii) the opportunity to realize a more stable income, and (iv) attractive benefits packages.

Focus on Commercial and Industrial Markets. We primarily focus on the commercial and industrial markets with particular emphasis on "design and build" installation services and maintenance, repair and replacement services. We believe that the commercial and industrial HVAC markets are attractive because of their growth opportunities, large and diverse customer base, reduced weather exposure as compared to residential markets, attractive margins and potential for long-term relationships with building owners, property managers, general contractors and architects. Approximately 96% of our consolidated 2002 revenues were derived from commercial and industrial customers.

Expand National Service Capabilities. We believe larger regional and national commercial and industrial companies can benefit from consolidating their HVAC needs with fewer HVAC service companies that are capable of providing those services regionally or nationally. In response to this opportunity, we have developed a National Accounts Group with an interactive website and a call center to increase our ability to handle these types of customers. We are devoting increased marketing resources to expanding our customer base in regional and national service coverage.

Increase Emphasis on Facility Automation Services. We believe we can expand our technical capabilities related to building automation control systems including HVAC lighting, building access control and fire alarms. We coordinate these services, manage national account opportunities and implement business development strategies across operating locations with expertise in providing these services.

Leveraging Resources. We believe significant operating efficiencies can be achieved by leveraging resources among our operating locations. For example, we have shifted certain prefabrication activities into centralized locations thereby increasing asset utilization in these centralized locations and redirecting prefabrication employees into other operational areas. We have also transferred our engineering, field and supervisory labor from one operation to another to more fully use our employee base, meet our customers' needs, and share expertise.

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OPERATIONS SERVICES PROVIDED

We provide a wide range of installation, maintenance, repair and replacement services for HVAC and related systems in commercial and industrial properties. We manage our locations on a decentralized basis, with local management maintaining responsibility for day-to-day operating decisions. Our local management is augmented by regional leadership that focuses its efforts on core business competencies, cooperation and coordination between locations, implementing best practices and focusing on major corporate initiatives. In addition to senior management, local personnel generally include design engineers, sales personnel, customer service personnel, installation and service technicians, sheet metal and prefabrication technicians, estimators and administrative personnel. We have centralized certain administrative functions such as insurance, employee benefits, training, safety programs, marketing and cash management to enable our local operating management to focus on pursuing new business opportunities and improving operating efficiencies. We also take advantage of best practices by opportunistically combining certain back office and administrative functions at various locations.

Installation Services. Our installation business related to newly constructed facilities, which comprised approximately 52% of our consolidated 2002 revenues involves the design, engineering, integration, installation and start-up of HVAC, building automation controls and related systems. We provide "design and build" and "plan and spec" installation services for office buildings, retail centers, apartment complexes, manufacturing plants, health care, education and government facilities and other commercial and industrial facilities. In a "design and build" installation, working with the customer, we determine the needed capacity, energy efficiency and type of building automation controls that best suit the proposed facility. Our engineer then estimates the amount of time, labor, materials and equipment needed to build the specified system. The final design, terms, price and timing of the project are then negotiated with the customer or its representatives, after which any necessary modifications are made to the system. In "plan and spec" installation, we participate in a bid process to provide labor, equipment, materials and installation based on plans and engineering provided by a customer or a general contractor.

Once an agreement has been reached, we order the necessary materials and equipment for delivery to meet the project schedule. In many instances, we fabricate the ductwork and piping and assemble certain components for the system based on the mechanical drawing specifications, eliminating the need to subcontract ductwork or piping fabrication. Then we install the system at the project site, working closely with the general contractor. Most of our installation projects last from two weeks to one year and generate revenues from \$50,000 to \$3,000,000 per project. These projects are generally billed periodically as costs are incurred and, in most cases, with retainage of 5% to 10% that is held back until completion and successful start-up of the HVAC system.

We also install process cooling systems and building automation controls and monitoring systems. Process cooling systems are used primarily in industrial facilities to provide heating and/or cooling to precise temperature and climate standards for products being manufactured and for the manufacturing equipment. Building automation control systems are used in HVAC and process cooling systems to maintain pre-established temperature or climate standards for commercial or industrial facilities. Building automation control systems are capable not only of controlling a facility's entire HVAC system, often on a room-by-room basis, but can be programmed to integrate energy management, security, fire, card key access, lighting and overall facility monitoring. This monitoring can be performed on-site or remotely through a PC-based communications system. The monitoring system communicates an exception when a system is operating outside pre-established parameters. Diagnosis of potential problems can be performed from the computer terminal which often can remotely adjust the control system.

Maintenance, Repair and Replacement Services. Our maintenance, repair and replacement services comprised approximately 48% of our consolidated 2002 revenues and include the maintenance, repair, replacement, reconfiguration and monitoring of HVAC systems and industrial process piping. Over two-thirds of our maintenance, repair and replacement revenues were derived from reconfiguring existing HVAC systems for commercial and industrial customers. Reconfiguration often uses consultative expertise similar to that provided in the "design and build" installation market.

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Maintenance and repair services are provided either in response to service calls or under a service agreement. Service calls are coordinated by customer service representatives or dispatchers that use computer and communication technology to process orders, arrange service calls, communicate with customers, dispatch technicians and invoice customers. Service technicians work from service vehicles equipped with commonly used parts, supplies and tools to complete a variety of jobs. Commercial and industrial service agreements usually have terms of one to three years, with automatic annual renewals. We also provide remote monitoring of temperature, pressure, humidity and air flow for HVAC systems. If the system is not operating within the specifications set forth by the customer and cannot be remotely adjusted, a service crew is dispatched to analyze and repair the system.

SOURCES OF SUPPLY

The raw materials and components we use include HVAC system components, ductwork, steel, sheet metal and copper tubing and piping. These raw materials and components are generally available from a variety of domestic or foreign suppliers at competitive prices. Delivery times are typically short for most raw materials and standard components, but during periods of peak demand, may extend to a month or more. Chillers for large units typically have the longest delivery time and generally have lead times of up to six months. The major components of commercial HVAC systems are compressors and chillers that are manufactured primarily by York Heating and Air Conditioning Corporation, Carrier Corporation, Trane Air Conditioning Company and Lennox International. The major suppliers of building automation control systems are Honeywell, Johnson Controls, Siemens, York, Automated Logic, Novar and Andover Control Corporation. We do not have any significant contracts guaranteeing us a supply of raw materials or components.

SALES AND MARKETING

We have a diverse customer base, with no single customer accounting for more than 2% of consolidated 2002 revenues. Management and a dedicated sales force have been responsible for developing and maintaining successful long-term relationships with key customers. Customers generally include building owners and developers and property managers, as well as general contractors, architects and consulting engineers. We intend to continue our emphasis on developing and maintaining long-term relationships with our customers by providing superior, high-quality service in a professional manner.

We have a national sales team focusing on cross-marketing and business development opportunities that we believe are available to us as a regional or national provider of comprehensive commercial and industrial HVAC and related services. We believe we can continue to leverage the diverse technical and marketing strengths at individual locations to expand the services offered in other local markets.

EMPLOYEES

As of December 31, 2002, we had 6,088 employees, including 331 management personnel, 4,853 engineers, service and installation technicians, 253 sales personnel and 651 administrative personnel across our 84 operating locations. We have collective bargaining agreements covering approximately 108 employees. We have not experienced and do not expect any significant strikes or work stoppages and believe our relations with employees covered by collective bargaining agreements are good.

RECRUITING, TRAINING AND SAFETY

Our continued success depends, in part, on our ability to continue to attract, retain and motivate qualified engineers, service technicians, field supervisors and project managers. We believe our success in retaining qualified employees will be based on the quality of our recruiting, training,

compensation, employee benefits programs and opportunities for advancement. We coordinate our recruiting efforts via the Internet and at local technical schools and community colleges where students focus on learning basic industry skills. Additionally, we provide on-the-job training, technical training, apprenticeship programs, attractive benefit packages and career advancement opportunities within our company.

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We have established comprehensive safety programs throughout our operations to ensure that all technicians comply with safety standards we have established and that are established under federal, state and local laws and regulations. Additionally, we have implemented a "best practices" safety program throughout our operations, which provides employees with incentives to improve safety performance and decrease workplace accidents. Regional safety directors establish safety programs and benchmarking to improve safety within their region. Finally, our employment screening process seeks to determine that prospective employees have the requisite skills, sufficient background references and acceptable driving records, if applicable.

RISK MANAGEMENT, INSURANCE AND LITIGATION

The primary risks in our operations are bodily injury, property damage and injured workers' compensation. We retain the risk for worker's compensation, employer's liability, auto liability, general liability and employee group health claims resulting from uninsured deductibles per accident or occurrence. Losses up to the deductible amounts are estimated and accrued based upon known facts, historical trends and industry averages utilizing the assistance of an actuary to determine the best estimate of these obligations.

We are subject to certain claims and lawsuits arising in the normal course of business and maintain various insurance coverages to minimize financial risk associated with these claims. We have estimated and provided accruals for probable losses and legal fees associated with certain of these actions in our consolidated financial statements. We do not believe uninsured losses, if any, resulting from the ultimate resolution of these matters will have a material adverse effect on our financial position or results of operations.

We typically warrant labor for the first year after installation on new HVAC systems and pass through to the customer manufacturers' warranties on equipment. We generally warrant labor for 30 days after servicing of existing HVAC systems. We do not expect warranty claims to have a material adverse effect on our financial position or results of operations.

COMPETITION

The HVAC industry is highly competitive and consists of thousands of local and regional companies. We believe that purchasing decisions in the commercial and industrial markets are based on (i) long-term customer relationships, (ii) quality, timeliness and reliability of services provided, (iii) competitive price, (iv) range of services provided and (v) scale of operation. To improve our competitive position we focus on both the highly consultative "design and build" installation market and the maintenance, repair and replacement market to promote first the development and then the strengthening of long-term customer relationships. In addition, we believe our ability to provide multi-location coverage, access to project financing and specialized technical skills for facilities owners gives us a strategic advantage over smaller competitors who may be unable to provide these services to customers at a competitive price, if at all.

We believe that we are larger than most of our competitors which are generally small, owner-operated companies that typically operate in a limited geographic area. However, there are larger companies, divisions of utility companies and equipment manufacturers that provide HVAC services in some of the same service lines and geographic locations we serve. Some of these competitors and potential competitors have greater financial resources than we do to finance development opportunities and support their operations. We believe our smaller competitors generally compete with us based on price and their long-term relationships with local customers. Our larger competitors compete with us on those factors but may also provide attractive financing and comprehensive service and product packages.

VEHICLES

We operate a fleet of various owned or leased service trucks, vans and support vehicles. We believe these vehicles generally are well maintained and sufficient for our current operations.

GOVERNMENTAL REGULATION AND ENVIRONMENTAL MATTERS

Our operations are subject to various federal, state and local laws and regulations, including: (i) licensing requirements applicable to engineering, construction and service technicians, (ii) building and HVAC codes and zoning ordinances, (iii) regulations relating to consumer protection, including those governing residential service agreements and (iv) regulations relating to worker safety and protection of the environment. We believe we have all required licenses to conduct our operations and are in substantial compliance with applicable regulatory requirements. If we fail to comply with applicable regulations we could be subject to substantial fines or revocation of our operating licenses.

Many state and local regulations governing the HVAC services trades require individuals to hold permits and licenses. In some cases, a required permit or license held by a single individual may be sufficient to authorize specified activities for all of our service technicians who work in the state or county that issued the permit or license. We are implementing a policy to ensure that, where possible, we have two employees who hold any such permits or licenses that may be material to our operations in a particular geographic region.

Our operations are subject to the federal Clean Air Act, as amended, which governs air emissions and imposes specific requirements on the use and handling of chlorofluorocarbons, or CFCs, and certain other refrigerants. Clean Air Act regulations require the certification of service technicians involved in the service or repair of equipment containing these refrigerants and also regulate the containment and recycling of these refrigerants. These requirements have increased our training expenses and expenditures for containment and recycling equipment. The Clean Air Act is intended ultimately to eliminate the use of CFCs in the United States and to require alternative refrigerants to be used in replacement HVAC systems. We do not believe these regulations on CFCs will materially affect our business on the whole because although they require us to incur modest ongoing training costs, they also encourage our potential customers to update their HVAC systems.

EXECUTIVE OFFICERS

We have five executive officers.

William F. Murdy, age 61, has served as our Chairman of the Board and Chief Executive Officer since June 2000. Prior to this he was Interim President and Chief Executive Officer of Club Quarters, a privately-owned chain of membership hotels. From January 1998 through July 1999, Mr. Murdy served as President, Chief Executive Officer and Chairman of the Board of LandCare USA, a publicly-traded commercial landscape and tree services company. He was primarily responsible for organizing LandCare USA and its listing as a publicly-traded company on the New York Stock Exchange in July 1998. LandCare USA was acquired in July 1999 by another publicly-traded company specializing in services to homeowners and commercial facilities. From 1989 through December 1997, Mr. Murdy was President and Chief Executive Officer of General Investment and Development Company, a privately-held real estate operating company. From 1981 to 1989, Mr. Murdy served as the Managing General Partner of the Morgan Stanley Venture Capital Fund. From 1974 to 1981, Mr. Murdy served as the Senior Vice President and Chief Operating Officer, among other positions, of Pacific Resources, Inc., a publicly-traded company involved primarily in petroleum refining and marketing.

Norman C. Chambers, age 53, has served as our President and as a director since November 2002. Prior to this, Mr. Chambers was Chief Operating Officer of Capstone Turbine Corporation, a small cap distributive generation technology company. From April 2000 to September 2001, Mr. Chambers served as President and Chief Executive Officer of Petrocosm Corporation, a privately held e-commerce business serving as a procurement portal for the energy industry. From June 1985 to April 2000, Mr. Chambers served in various positions with the Halliburton Companies. His responsibilities included construction, service, and business development at the Halliburton Company, including President of Halliburton Energy Development, Senior Vice President of the Halliburton Company and Managing Director of Brown & Root.

J. Gordon Beittenmiller, age 44, has served as our Executive Vice President, Chief Financial Officer and a director since May 1998, and was our Senior Vice President, Chief Financial Officer and a director from

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February 1997 to April 1998. From 1994 to February 1997, Mr. Beittenmiller was Corporate Controller of Keystone International, Inc., a publicly-traded multi-national manufacturer of industrial valves and actuators, and served Keystone in other financial positions from 1991 to 1994. From 1987 to 1991, he was Vice President-Finance of Critical Industries, Inc., a publicly-traded manufacturer and distributor of specialized safety equipment. From 1982 to 1987, he held various positions with Arthur Andersen LLP. Mr. Beittenmiller is a Certified Public Accountant.

William George III, age 38, has served as our Senior Vice President, General Counsel and Secretary since May 1998, and was our Vice President, General Counsel and Secretary from March 1997 to April 1998. From October 1995 to February 1997, Mr. George was Vice President and General Counsel of American Medical Response, Inc., a publicly-traded healthcare transportation company. From September 1992 to September 1995, Mr. George practiced corporate and antitrust law at Ropes & Gray, a Boston, Massachusetts law firm.

Milburn Honeycutt, age 39, has served as our Senior Vice President-Finance since March 2002, and was our Vice President and Corporate Controller from February 1997 to February 2002. He was promoted to Senior Vice President in September 2000. From 1994 to January 1997, Mr. Honeycutt was Financial Accounting Manager -- Corporate Controllers Group for Browning-Ferris Industries, Inc., a publicly-traded multi-national waste services company. From 1986 to 1994, he held various positions with Arthur Andersen LLP and was a Certified Public Accountant.

ITEM 2. PROPERTIES

We lease the real property and buildings from which we operate. Our facilities consist of offices, shops, maintenance and warehouse facilities. Generally, leases range from five to ten years and are on terms we believe to be commercially reasonable. In many instances these leases are with the former owners (some of whom continue to work for us) of companies we purchased from 1997 through 1999. These leases were entered into in connection with the acquisition of the companies these individuals owned. To the extent we renew these leases or otherwise change them, we enter into such agreements on an arm's-length basis. Leased premises range in size from approximately 1,000 square feet to 130,000 square feet. To maximize available capital, we generally intend to continue to lease the majority of our properties. We believe that our facilities are sufficient for our current needs.

We lease our executive and administrative offices in Houston, Texas.

ITEM 3. LEGAL PROCEEDINGS

We are subject to certain claims and lawsuits arising in the ordinary course of business and maintain various insurance coverages to minimize financial risk associated with these claims. We have estimated and provided accruals for probable losses and legal fees associated with certain of these actions in our consolidated financial statements. In the opinion of our management, uninsured losses, if any, resulting from the ultimate resolution of these matters will not have a material adverse effect on our financial position or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The following table sets forth the reported high and low sales prices of our Common Stock for the quarters indicated as traded at the New York Stock

Exchange. Our Common Stock is traded under the symbol FIX:

	HIGH	LOW
	-----	-----
First Quarter, 2001.....	\$2.78	\$2.125
Second Quarter, 2001.....	\$4.24	\$ 1.80
Third Quarter, 2001.....	\$4.40	\$ 2.15
Fourth Quarter, 2001.....	\$3.70	\$ 2.29
First Quarter, 2002.....	\$4.45	\$ 3.63
Second Quarter, 2002.....	\$4.97	\$ 3.90
Third Quarter, 2002.....	\$4.80	\$ 3.04
Fourth Quarter, 2002.....	\$3.58	\$ 2.65
January 1 -- March 25, 2003.....	\$3.45	\$ 2.52

As of March 25, 2003, there were approximately 542 stockholders of record of our Common Stock, and the last reported sale price on that date was \$2.63 per share.

We have never declared or paid a dividend on our Common Stock. We currently expect to retain future earnings to repay debt and finance growth and, consequently, do not intend to declare any dividend on our Common Stock for the foreseeable future. In addition, our revolving credit agreement restricts our ability to pay dividends without the lenders' consent. Our Restricted Voting Common Stock converts to Common Stock upon sale and under certain other conditions.

RECENT SALES OF UNREGISTERED SECURITIES

During 2002, we did not issue any unregistered shares of our Common Stock.

ITEM 6. SELECTED FINANCIAL DATA

The following selected historical financial data has been derived from the audited financial statements of the Company. The historical financial statement data reflects the acquisitions of businesses accounted for as purchases as of their respective acquisition dates. The selected historical financial data below should be read in conjunction with the historical Consolidated Financial Statements and related notes.

	YEAR ENDED DECEMBER 31,				
	1998	1999	2000	2001	2002
	-----	-----	-----	-----	-----
	(IN THOUSANDS)				
STATEMENT OF OPERATIONS DATA:					
Revenues.....	\$553,330	\$801,747	\$902,289	\$882,861	\$ 819,282
Operating income (loss).....	\$ 46,434	\$ 52,502	\$ (21,487)	\$ 13,426	\$ 13,867
Income (loss) from continuing operations.....	\$ 23,069	\$ 23,091	\$ (29,898)	\$ (1,033)	\$ 5,479
Discontinued operations --					
Operating results, net of tax.....	\$ 11,944	\$ 19,231	\$ 13,045	\$ 14,157	\$ (36)
Estimated loss on disposition, including tax.....	\$ --	\$ --	\$ --	\$ --	\$ (12,002)
Cumulative effect of change in accounting principle, net of tax.....	\$ --	\$ --	\$ --	\$ --	\$ (202,521)
Net income (loss).....	\$ 35,013	\$ 42,322	\$ (16,853)	\$ 13,124	\$ (209,080)
Income (loss) per Share:					
Basic --					
Income (loss) from continuing operations.....	\$ 0.70	\$ 0.60	\$ (0.80)	\$ (0.03)	\$ 0.15
Discontinued operations --					
Income (loss) from operations.....	\$ 0.36	\$ 0.50	\$ 0.35	\$ 0.38	\$ --
Estimated loss on disposition.....	\$ --	\$ --	\$ --	\$ --	\$ (0.32)
Cumulative effect of change in accounting principle.....	\$ --	\$ --	\$ --	\$ --	\$ (5.39)

Net income (loss).....	\$ 1.06	\$ 1.10	\$ (0.45)	\$ 0.35	\$ (5.56)
	=====	=====	=====	=====	=====
Diluted --					
Income (loss) from continuing operations.....	\$ 0.69	\$ 0.61	\$ (0.80)	\$ (0.03)	\$ 0.14
Discontinued operations --					
Income (loss) from operations.....	\$ 0.35	\$ 0.48	\$ 0.35	\$ 0.38	\$ --
Estimated loss on disposition.....	\$ --	\$ --	\$ --	\$ --	\$ (0.31)
Cumulative effect of change in accounting principle.....	\$ --	\$ --	\$ --	\$ --	\$ (5.28)
	-----	-----	-----	-----	-----
Net income (loss).....	\$ 1.04	\$ 1.09	\$ (0.45)	\$ 0.35	\$ (5.45)
	=====	=====	=====	=====	=====

BALANCE SHEET DATA:

Working capital.....	\$249,371	\$310,292	\$309,472	\$279,063	\$ 75,740
Total assets.....	\$789,293	\$934,530	\$929,008	\$876,625	\$ 366,535
Total debt, excluding discount.....	\$203,066	\$262,035	\$246,394	\$182,028	\$ 15,234
Total stockholders' equity.....	\$379,932	\$418,965	\$400,239	\$413,821	\$ 205,086

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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes included elsewhere in this Form 10-K. Also see "Forward-Looking Statements" discussion.

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INTRODUCTION

We are a national provider of comprehensive heating, ventilation and air conditioning ("HVAC") installation, maintenance, repair and replacement services within the mechanical services industry. We operate primarily in the commercial and industrial HVAC markets and perform most of our services within office buildings, retail centers, apartment complexes, manufacturing plants, and healthcare, education and government facilities. In addition to standard HVAC services, we provide specialized applications such as building automation control systems, fire protection, process cooling, electronic monitoring and process piping. Certain locations also perform related activities such as electrical service and plumbing. The segment of the HVAC industry we serve can be broadly divided into two service functions: installation in newly constructed facilities, which provided approximately 52% of our revenues in 2002, and maintenance, repair and replacement, which provided the remaining 48% of our 2002 revenues.

Our company was originally formed in 1997 through an initial public offering, or IPO, and simultaneous acquisition of 12 companies engaged in our business. From the time we completed our IPO through December 1999, we acquired 107 HVAC and complementary businesses, of which 26 were "tuck-in" operations that were integrated with our existing operations.

Beginning in the fourth quarter of 1999, we shifted our strategy from an acquisition-based growth strategy to an operating strategy that increased emphasis on improving our operating performance. Since then, we have sold or ceased operations at 29 locations through December 31, 2002. Significantly, on March 1, 2002, we sold 19 operations to Emcor Group, Inc. for \$186.25 million, including Emcor's assumption of approximately \$22.1 million of subordinated notes to former owners of certain of the divested companies. These 19 operations provided \$683.4 million and \$657.9 million of our revenue in 2000 and 2001, respectively. We used the proceeds from this sale to reduce debt. The operating results of companies sold to Emcor have been reported as discontinued operations in the accompanying consolidated statements of operations. We recognized a loss of \$11.8 million and a goodwill impairment charge prior to the sale of \$32.4 million, net of taxes, related to the sold operations. For a further discussion of this sale, see "Item 8 -- Financial Statements and Supplemental Data -- Notes 3 and 4."

In response to the Securities and Exchange Commission's Release No. 33-8040, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies", we identified our critical accounting policies based upon the significance of the accounting policy to our overall financial statement presentation, as well as the complexity of the accounting policy and our use of estimates and subjective assessments. We have concluded that our most critical accounting policy is our revenue recognition policy. As discussed elsewhere in this annual report, our business has two service functions: (i) installation,

which we account for under the percentage of completion method, and (ii) maintenance, repair and replacement, which we account for as the services are performed, or in the case of replacement, under the percentage completion method. In addition, we identified other critical accounting policies related to our allowance for doubtful accounts receivable, the recording of our self-insurance liabilities and the assessment of goodwill impairment. These accounting policies, as well as others, are described in Note 2 to the Consolidated Financial Statements included elsewhere in the Form 10-K.

PERCENTAGE OF COMPLETION METHOD OF ACCOUNTING

Under the percentage of completion method of accounting as provided by American Institute of Certified Public Accountants Statement of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts," contract revenue recognizable at any time during the life of a contract is determined by multiplying expected total contract revenue by the percentage of contract costs incurred at any time to total estimated contract costs. More specifically, as part of the negotiation and bidding process in which we engage in connection with obtaining installation contracts, we estimate our contract costs, which include all direct materials (net of estimated rebates), labor and subcontract costs and indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and depreciation costs. Then, as we perform under those contracts, we measure such costs incurred, compare them to total estimated costs to complete the contract, and recognize a corresponding proportion of contract revenue. As a result, contract

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revenues recognized in the statement of operations can and usually do differ from amounts that can be billed or invoiced to the customer at any point during the contract.

An added complexity to the percentage of completion method of accounting is that changes in job performance, job conditions, estimated profitability and final contract settlements may result in revisions to estimated costs and, therefore, revenues. Such revisions are frequently based on further estimates and subjective assessments, and we recognize these revisions in the period in which they are determined. If such revisions lead us to conclude that we will recognize a loss on a contract, the full amount of the estimated ultimate loss is recognized in the period we reach that conclusion, regardless of the percentage of completion of the contract. Depending on the size of a project, variations from estimated project costs could have a significant impact on our operating results.

ACCOUNTING FOR ALLOWANCE FOR DOUBTFUL ACCOUNTS

We are required to estimate the collectibility of accounts receivable. Inherent in the assessment of the allowance for doubtful accounts are certain judgments and estimates including, among others, the creditworthiness of the customer, our prior collection history with the customer, the ongoing relationships with our customers, the aging of past due balances, our lien rights, if any, in the property where we performed the work, and the availability, if any, of payment bonds applicable to our contract. The estimate of the allowance is based upon the best facts available and estimates are re-evaluated and adjusted as additional information is received.

ACCOUNTING FOR SELF-INSURANCE LIABILITIES

We are self-insured for worker's compensation, employer's liability, auto liability, general liability and employee group health claims resulting from uninsured deductibles per accident or occurrence. Losses up to the deductible amounts are estimated and accrued based upon known facts, historical trends and industry averages utilizing the assistance of an actuary to determine the best estimate of these obligations. We believe such accruals to be adequate. However, insurance liabilities are difficult to assess and estimate due to unknown factors, including the severity of an injury, the determination of our liability in proportion to other parties, timely reporting of occurrences and the effectiveness of safety and risk management programs. Therefore, if actual experience differs from the assumptions and estimates used for recording the liabilities, adjustments may be required and would be recorded in the period that the experience becomes known.

ACCOUNTING FOR GOODWILL AND OTHER INTANGIBLE ASSETS

Effective January 1, 2002, we adopted Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets." This new standard has two effects. First, we are no longer required to amortize goodwill against our operating results on a recurring basis. Second, we are required to regularly test the goodwill on our books to determine whether its value has been impaired, and if it has, immediately write off, as a component of operating income, the amount of the goodwill that is impaired.

More specifically, we are required to assess our goodwill asset amounts for impairment each year, and more frequently if circumstances suggest an impairment may have occurred. The new requirements for assessing whether goodwill assets have been impaired involve market-based information. This information, and its use in assessing goodwill, entails some degree of subjective assessments.

As part of the adoption of SFAS No. 142, we were required to make a one-time determination of any transitional impairment loss by applying the standard's new, more rigorous valuation methodology. The result of this transitional analysis was a \$202.5 million charge net of taxes reflected as a cumulative effect of a change in accounting principle in our statement of operations in the first quarter of 2002. We recorded an additional impairment charge of \$0.2 million as a component of operating results during the fourth quarter of 2002.

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RESULTS OF OPERATIONS

	YEAR ENDED DECEMBER 31,					
	2000		2001		2002	
	(IN THOUSANDS)					
Revenues.....	\$902,289	100.0%	\$882,861	100.0%	\$ 819,282	100.0%
Cost of services.....	736,191	81.6%	717,284	81.2%	676,268	82.5%
Gross profit.....	166,098	18.4%	165,577	18.8%	143,014	17.5%
Selling, general and administrative expenses.....	153,563	17.0%	143,675	16.3%	127,051	15.5%
Goodwill amortization and impairment.....	8,678	1.0%	8,238	0.9%	218	--
Restructuring charges.....	25,344	2.8%	238	--	1,878	0.2%
Operating income (loss).....	(21,487)	(2.4)%	13,426	1.5%	13,867	1.7%
Other expense, net.....	(10,508)	(1.2)%	(7,554)	(0.9)%	(3,485)	(0.4)%
Reductions in non-operating assets and liabilities, net.....	(1,095)	(0.1)%	--	--	--	--
Income (loss) before income taxes.....	(33,090)	(3.7)%	5,872	0.7%	10,382	1.3%
Income tax expense (benefit).....	(3,192)		6,905		4,903	
Income (loss) from continuing operations.....	(29,898)	(3.3)%	(1,033)	(0.1)%	5,479	0.7%
Discontinued operations --						
Operating results, net of tax.....	13,045		14,157		(36)	
Estimated loss on disposition, including tax.....	--		--		(12,002)	
Cumulative effect of change in accounting principle, net of tax....	--		--		(202,521)	
Net income (loss).....	\$(16,853)		\$ 13,124		\$(209,080)	

2002 COMPARED TO 2001

Revenues -- Revenues decreased \$63.6 million, or 7.2%, to \$819.3 million in 2002 compared to 2001. The 7.2% decline in revenues was comprised of a 6.5% decline in revenues at ongoing operations and a 0.7% decline in revenues related to operations that were sold or shut down during 2001.

The decline in revenues at ongoing operations in 2002 resulted primarily from the lagged effect of the general economic slowdown that began in 2001. This slowdown led to widespread delays in facility owners' decisions to proceed on

both new and replacement projects, and has also resulted in a more competitive pricing environment. The decline in revenue is also consistent with management's decreased emphasis on revenue growth in favor of improvement in profit margins, operating efficiency, and cash flow. There can be no assurance, however, that this strategy will lead to improved profit margins in the near term. In view of these factors, particularly the decreased economic activity and increased price competition affecting our industry, we may continue to experience only modest revenue growth or revenue declines in upcoming periods. In addition, if general economic activity in the U.S. slows significantly from current levels, we may realize further decreases in revenue and lower operating margins.

Backlog primarily contains installation and replacement project work, and maintenance agreements. These projects generally last less than a year. Service work and short duration projects are generally billed as performed and therefore do not flow through backlog. Accordingly, backlog represents only a portion of our revenues for any given future period, and it represents revenues that are likely to be reflected in our operating results over the next six to twelve months. As a result, we believe the predictive value of backlog information is limited to indications of general revenue direction over the near term, and should not be interpreted as indicative of ongoing revenue performance over several quarters.

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Backlog associated with continuing operations as of December 31, 2002 was \$444.5 million, a 6.9% increase from December 31, 2001 backlog of \$415.7 million. During the fourth quarter, we removed \$16.0 million from backlog that related to a project that we now believe will not proceed. This project was first reflected in backlog in the third quarter of 2001. If this project is excluded from all applicable periods, our backlog reflected an increase of 11.2% from an adjusted December 31, 2001 backlog of \$399.7 million.

Gross Profit -- Gross profit decreased \$22.6 million, or 13.6%, to \$143.0 million in 2002 compared to 2001. As a percentage of revenues, gross profit decreased from 18.8% in 2001 to 17.5% in 2002.

The decline in gross profit for the year as a whole is primarily due to a more competitive pricing environment as a result of the general economic slowdown which began in 2001. This slowdown also resulted in project delays at a number of our operations as decisions to start new construction activities as well as retrofit projects were delayed in the fourth quarter of 2001. These delays significantly affected our revenue volume and profitability during the first part of 2002.

In the fourth quarter of 2002, we began experiencing cost overruns in certain operations as well as reduced activity levels in connection with renewed uncertainty about the economy and international events. These developments continued into the first quarter of 2003. We also undertook restructuring steps at our energy efficiency and national account operations in the first quarter of 2003. With the occurrence of these developments during what is traditionally a period of reduced seasonal activity, we expect we will report a net loss for the first quarter of 2003 that is comparable to the net loss from continuing operations that we reported in the first quarter of 2002. We do expect to be profitable in the second quarter and for 2003 as a whole.

Selling, General and Administrative Expenses ("SG&A") -- SG&A decreased \$16.6 million, or 11.6%, to \$127.1 million in 2002 compared to 2001. As a percentage of revenues, SG&A decreased from 16.3% in 2001 to 15.5% in 2002. During the fourth quarter of 2001, we estimated and recorded bad debt expense of approximately \$3.5 million related to our receivables with Kmart, in light of that company's bankruptcy filing in January 2002. During the second quarter of 2002, we reversed \$0.8 million of the bad debt reserves that were established in the fourth quarter of 2001 related to the Kmart receivables as a result of a settlement with Kmart. Excluding the Kmart charge in 2001 and reversal in 2002, SG&A declined \$12.3 million, or 8.8%, to \$127.9 million, and as a percentage of revenue, from 15.9% in 2001 to 15.6% in 2002. The decrease in SG&A is primarily due to a concerted effort to reduce SG&A throughout our Company. This effort included a reduction in corporate overhead at the end of the first quarter of 2002 in response to our smaller size following the sale of 19 units to Emcor as discussed further below under "Discontinued Operations." Nonrecurring costs associated with this particular reduction were reflected as restructuring charges in March 2002.

SG&A as a percentage of revenues for periods prior to the Emcor transaction

is higher than historical levels because the financial statements do not allocate any corporate overhead to the discontinued operations. As a result, SG&A for continuing operations in those periods includes substantially the full amount of corporate office overhead that was in place to support our larger size prior to the sale of operations to Emcor.

Goodwill Amortization and Impairment -- As discussed above, we no longer amortize goodwill via regular charges to our income statement due to our adoption of SFAS 142. See "Cumulative Effect of Change in Accounting Principle" for further discussion. We recorded an additional goodwill impairment charge of \$0.2 million during the fourth quarter of 2002.

Restructuring Charges -- During the first quarter of 2002, we recorded restructuring charges of approximately \$1.9 million. These charges included approximately \$0.8 million for severance costs primarily associated with the reduction in corporate overhead in light of our smaller size following the Emcor transaction. The severance costs related to the termination of 33 employees, all of whom were terminated as of March 31, 2002. In addition, these charges include approximately \$0.7 million for costs associated with decisions to merge or close three smaller divisions and realign regional operating management. These restructuring charges are primarily cash obligations but did include approximately \$0.3 million of non-cash writedowns associated with long-lived assets.

During the first quarter of 2001, we recorded restructuring charges of approximately \$0.2 million, primarily related to contractual severance obligations of two operating presidents in connection with our

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significant restructuring program in the second half of 2000. These restructuring charges are net of a gain of approximately \$0.1 million related to management's decision to sell a small operation during the first quarter of 2001.

Other Expense, Net -- Other expense, net, primarily includes interest expense, and decreased \$4.1 million, or 53.9%, to \$3.5 million in 2002 compared to 2001. A portion of our actual interest expense in both years has been allocated to the discontinued operations caption based upon our net investment in these operations. Therefore, interest expense relating to continuing operations does not reflect the pro forma reduction of interest expense from applying the proceeds from the sale of these operations to reduce debt in any earlier period. Interest expense allocated to the discontinued operations in 2001 and 2002 was \$13.8 million and \$1.5 million, respectively. In addition, first quarter 2002 interest expense in continuing operations includes a non-cash writedown of \$0.6 million, before taxes, of loan arrangement costs in connection with the reduction in our borrowing capacity following the Emcor transaction. Other expense, net, for the second quarter of 2002 also includes a gain of \$0.6 million on the sale of the residential portion of one of our operations. In addition, a gain of \$0.7 million was recorded in the fourth quarter of 2002 related to the extinguishment of subordinated debt which was partially offset by the acceleration of the amortization of deferred debt costs of \$0.4 million in October 2002 when we replaced our existing credit facility.

Income Tax Expense -- Our effective tax rates associated with results from continuing operations for 2001 and 2002 were 117.6% and 47.2%, respectively. As a result of the discontinuation of goodwill amortization in connection with the adoption of SFAS No. 142 effective January 1, 2002, our 2002 effective tax rate no longer reflects a permanent difference between book income and tax income for goodwill amortization that is not deductible for tax purposes.

Discontinued Operations -- On March 1, 2002, we sold 19 operations to Emcor Group. The total purchase price was \$186.25 million, including the assumption by Emcor of approximately \$22.1 million of subordinated notes to former owners of certain of the divested companies.

The transaction with Emcor provided for a post-closing adjustment based on a final accounting, done after the closing of the transaction, of the net assets of the operations that were sold to Emcor. That accounting indicated that the net assets transferred to Emcor were approximately \$7 million greater than a target amount that had been agreed to with Emcor. In the second quarter of 2002, Emcor paid us that amount, and released \$2.5 million that had been escrowed in connection with this element of the transaction.

Of Emcor's purchase price, \$5 million was deposited into an escrow account

to secure potential obligations on our part to indemnify Emcor for future claims and contingencies arising from events and circumstances prior to closing, all as specified in the transaction documents. Of this escrow, \$4 million has been applied in determining the Company's liability to Emcor in connection with the settlement of certain claims as described subsequently in this section. The remaining \$1 million of escrow is available for book purposes to apply to any future claims and contingencies in connection with this transaction, and has not been recognized as part of the Emcor transaction purchase price.

The net cash proceeds of approximately \$164 million received to date from the Emcor transaction have been used to reduce our debt. We paid \$7.3 million of federal taxes related to this transaction in March 2003.

In the fourth quarter of 2002, we recognized a charge of \$1.2 million, net of tax benefits of \$2.7 million, in "Estimated loss on disposition, including tax" in our results of operations in connection with the Emcor transaction. This charge primarily relates to a preliminary agreement to settle claims from Emcor for reimbursement of impaired assets and additional liabilities associated with the operations acquired from us. Under this settlement, we also agreed to partially reimburse Emcor for any loss on the eventual resolution of certain claims involving a project at one of the operations Emcor acquired from us, and we were released from liability on all other outstanding receivables and issues relating to the profitability of projects that were in process at the time Emcor acquired these operations from us. The settlement agreement also includes the use of \$2.5 million of the \$5 million escrow described above to fund settled claims. We further estimated that an additional \$1.5 million of the remaining escrow would be applied against elements of the settlement that will not be fully resolved until a later date, principally the one open project referred to above. Accordingly, for book

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purposes, \$1.0 million of escrow remains available to apply against future claims that may arise from Emcor in connection with this transaction. We recorded a tax benefit of \$1.4 million related to this additional charge. In addition, the \$1.2 million charge recognized during the fourth quarter is also net of a tax credit of \$1.3 million as a result of lower final tax liabilities in connection with the overall Emcor transaction than we originally estimated in the first quarter.

Under SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which took effect for us on January 1, 2002, the operating results of the companies sold to Emcor for all periods presented through the sale, as well as the loss on the sale of these operations, have been presented as discontinued operations in our results of operations. We realized a total loss of \$11.8 million, including related tax expense, in connection with the sale of these operations. As a result of the adoption of SFAS No. 142 "Goodwill and Other Intangible Assets," we also recognized a goodwill impairment charge related to these operations of \$32.4 million, net of taxes, as of January 1, 2002. The reporting of our aggregate initial goodwill impairment charge in connection with adopting SFAS No. 142 is discussed further below under "Cumulative Effect of Change in Accounting Principle."

In March 2002, we also decided to divest of an additional operating company. In the first quarter of 2002, we recorded an estimated loss of \$0.6 million from this planned disposition in "Estimated loss on disposition, including tax" in our results of operations. In the fourth quarter of 2002, we reversed this estimated loss because we decided not to sell this unit.

During the second quarter of 2002, we sold a division of one of our operations. The operating loss for this division for the first two quarters of 2002 of \$0.3 million, net of taxes, has been reported in discontinued operations under "Operating results, net of tax" in our results of operations. We realized a loss of \$0.3 million on the sale of this division. This loss is included in "Estimated loss on disposition, including tax" during the second quarter of 2002 in our results of operations.

Cumulative Effect of Change in Accounting Principle -- Effective January 1, 2002, we adopted SFAS No. 142, "Goodwill and Other Intangible Assets," which required a transitional assessment of our goodwill assets.

To perform the transitional impairment testing required by SFAS No. 142 under its new, more rigorous impairment criteria, we broke our operations into "reporting units," as prescribed by the new standard, and tested each of these

reporting units for impairment by comparing the unit's fair value to its carrying value. The fair value of each reporting unit was estimated using a discounted cash flow model combined with market valuation approaches. Significant estimates and assumptions were used in assessing the fair value of reporting units. These estimates and assumptions involved future cash flows, growth rates, discount rates, weighted average cost of capital and estimates of market valuations for each of the reporting units.

As provided by SFAS No. 142, the transitional impairment loss identified by applying the standard's new, more rigorous valuation methodology upon initial adoption of the standard was reflected as a cumulative effect of a change in accounting principle in our results of operations. The resulting non-cash charge was \$202.5 million, net of taxes.

2001 COMPARED TO 2000

Revenues -- Revenues decreased \$19.4 million, or 2.2%, to \$882.9 million in 2001 compared to 2000. The 2.2% decline in revenue for 2001 was comprised of a 4.1% decline in revenues related to operations that were sold or shut down during late 2000 or in 2001, which was partially offset by 1.9% of internal growth.

This low revenue growth resulted in part from a general slowing in the U.S. economy as well as management's decreased emphasis on revenue growth in favor of improvement in profit margins, operating efficiency, and cash flow.

Gross Profit -- Gross profit decreased \$0.5 million, or 0.3%, to \$165.6 million in 2001 compared to 2000. As a percentage of revenues, gross profit increased from 18.4% in 2000 to 18.8% in 2001. Excluding operations

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that were sold or shut down during late 2000 or in 2001, gross profit decreased \$3.5 million, or 2.1%, to \$166.2 million and gross profit as a percentage of revenues decreased from 19.9% in 2000 to 19.0% in 2001.

Our gross profit margin was hurt by sub par gross profit performance from certain ongoing operations that were undergoing operational and management changes. The results of these operations generally improved in the second half of 2001 as compared to the first half. The negative effect on gross profit percentages of these operations was offset by the divestiture of certain operations in 2001 that performed poorly in 2000 and by the improvement in two of our larger operations.

Selling, General and Administrative Expenses -- SG&A decreased \$9.9 million, or 6.4%, to \$143.7 million in 2001 as compared to 2000. As a percentage of revenues, SG&A decreased from 17.0% in 2000 to 16.3% in 2001. Excluding operations that were sold or shut down during late 2000 or in 2001, SG&A increased \$1.4 million, or 1.0%, to \$141.7 million in 2001 compared to 2000 and SG&A as a percentage of revenues decreased from 16.4% in 2000 to 16.2% in 2001. During the fourth quarter of 2001, we estimated and recorded bad debt expense of approximately \$3.5 million related to our receivables with Kmart, in light of that company's bankruptcy filing in January 2002. Substantially all of the Kmart charge related to our ongoing operations that were not divested. Excluding both the Kmart charge as well as operations sold or shut down in late 2000 or in 2001, SG&A declined \$2.1 million, or 1.5%, to \$138.2 million, and as a percentage of revenue, from 16.4% in 2000 to 15.8% in 2001.

SG&A as a percentage of revenues during these periods was higher than historical levels because the financial statements do not allocate any corporate overhead to the discontinued operations sold to Emcor, and therefore, SG&A does not reflect any potential reductions in corporate costs in response to this major change in our company. Excluding the Kmart charge, the decrease in SG&A is primarily related to operations that were sold or shut down as well as to a concerted effort to reduce SG&A throughout our company.

Restructuring Charges -- During the first quarter of 2001, we recorded restructuring charges of approximately \$0.2 million, primarily related to contractual severance obligations of two operating presidents in connection with our significant restructuring program undertaken in the second half of 2000. These restructuring charges are net of a gain of approximately \$0.1 million related to management's decision to sell a small operation during the first quarter of 2001.

As announced in the third quarter of 2000, management performed an extensive review of our operations during the second half of 2000. As part of this review, management decided to cease operating at three locations, sell five operations (including two smaller satellite operations), and merge two companies into other operations. As a result of these decisions, we estimated and recorded restructuring charges of approximately \$25.3 million, primarily associated with restructuring efforts at certain underperforming operations and our decision to cease our e-commerce activities at Outbound Services, a subsidiary of our company. The restructuring charges were primarily non-cash and included goodwill impairments of approximately \$11.5 million and the writedown of other long-lived assets of approximately \$8.5 million. The remaining restructuring items primarily include severance and lease termination costs. These restructuring actions were substantially completed in 2001.

During the third quarter of 2001, we decided to retain one of the operations that was previously held for sale and reversed approximately \$0.3 million of non-cash charges related to the anticipated loss on the sale of this operation. This amount was offset by an additional loss on the sale in late September 2001 of the final operation that was identified as part of this restructuring program. The losses associated with the other operations that were sold were consistent with the amounts recorded as restructuring charges in 2000.

Other Expense, Net -- Other expense, net, decreased \$3.0 million, or 28.1%, to \$7.6 million in 2001 compared to 2000. This decrease was primarily due to a reduction in interest expense as a result of the decline in our average debt levels throughout 2001 as compared to 2000. A portion of our actual interest expense in both years has been allocated to the discontinued operations caption based upon our net investment in these operations. Therefore, interest expense related to continuing operations does not reflect the pro forma reduction of interest expense from applying the proceeds from the sale of these operations to reduce debt in

any earlier periods. Interest expense allocated to the discontinued operations in 2000 and 2001 was \$15.5 million and \$13.8 million, respectively.

Reductions in Non-Operating Assets and Liabilities, Net -- During 2000, we recorded a non-cash charge of approximately \$1.1 million primarily related to the impairment of certain non-operating assets. This charge included an impairment of approximately \$1.4 million to our minority investment in two entities associated with the distribution and implementation of high-end engineering and design software. These entities have ceased operations. This charge also included an impairment of approximately \$0.3 million related to notes receivable from former owners of businesses acquired. Offsetting these items was a gain of approximately \$0.6 million on the reduction of a subordinated note payable to a former owner in connection with the settlement of claims with this former owner.

Income Tax Expense -- Our effective tax rates associated with results from continuing operations for 2000 and 2001 were 9.6% and 117.6%, respectively. Our provision for income taxes differs from the federal statutory rate primarily due to state income taxes (net of federal income tax benefit) and the non-deductibility of the amortization of goodwill attributable to certain acquisitions. The effective tax rate of 117.6% for 2001 is primarily due to the high level of permanent differences (primarily non-deductible goodwill amortization) as compared to the level of pre-tax income from continuing operations. In 2000, we reported income tax benefit of \$3.2 million on a pre-tax loss from continuing operations of \$33.1 million. This is primarily because of large restructuring-related writedowns of non-deductible goodwill that contributed to the 2000 book loss.

LIQUIDITY AND CAPITAL RESOURCES

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002

(IN THOUSANDS)

Cash provided by (used in):			
Operating activities.....	\$ 58,172	\$ 66,829	\$ 14,090

Investing activities.....	\$ (15,387)	\$ (4,003)	\$ 150,589
Financing activities.....	\$ (30,428)	\$ (68,222)	\$ (169,200)

Free cash flow:

Cash provided by operating activities.....	\$ 58,172	\$ 66,829	\$ 14,090
Purchases of property and equipment.....	(18,037)	(5,978)	(5,322)
Proceeds from sales of property and equipment.....	1,937	1,011	1,551
	-----	-----	-----
Free cash flow.....	\$ 42,072	\$ 61,862	\$ 10,319

Cash Flow -- Cash provided by operating activities less customary capital expenditures plus the proceeds from asset sales is generally called free cash flow. Positive free cash flow represents funds available to invest in significant operating initiatives, to acquire other companies or to reduce a company's outstanding debt or equity. If free cash flow is negative, additional debt or equity is generally required to fund the outflow of cash.

For the year ended December 31, 2002, we had positive free cash flow of \$10.3 million as compared to \$61.9 million for the same period in 2001. Free cash flow in 2000 was \$42.1 million. The 2001 and 2000 cash flow amounts include the 19 operations we sold to Emcor in 2002. This sale primarily accounts for the lower cash flow amounts in 2002.

The proceeds received at the closing of the Emcor transaction, the post-closing adjustment and related escrow received from Emcor, and free cash flow from our operations were all used to reduce our debt.

Credit Facility -- Our primary current debt financing capacity consists of a \$55 million senior credit facility, or the Facility, provided by a syndicate of three financial institutions led by General Electric Capital Corporation, or GE. The Facility includes a \$20 million sublimit for letters of credit. The Facility is secured by substantially all of our assets. The Facility was entered into on October 11, 2002 and replaces our previous revolving credit facility. The Facility consists of two parts: a term loan and a revolving credit facility.

The term loan under the Facility, or the Term Loan, is \$15 million, which we borrowed upon the closing of the Facility on October 11, 2002. The Term Loan must be repaid in quarterly installments over five years beginning December 31, 2002. The amount of each quarterly installment increases annually. These scheduled payments are recapped below under Amounts Outstanding, Capacity and Maturities.

The Facility requires certain prepayments of the Term Loan. Approximately half of any free cash flow (primarily cash from operations less capital expenditures) in excess of scheduled principal payments and voluntary prepayments must be used to pay down the Term Loan. This requirement is measured annually based on full-year results. We do not have any prepayments of the Term Loan due as of December 31, 2002 under this requirement primarily as a result of our significant amount of voluntary prepayments of debt during 2002. In addition, proceeds in excess of \$250,000 from any individual asset sales, or in excess of \$1 million for a full year's asset sales, must be used to pay down the Term Loan. Proceeds from asset sales that are less than these individual transaction or annual aggregate levels must also be used to pay down the Term Loan unless they are reinvested in long-term assets within six months of the receipt of such proceeds.

All prepayments under the Term Loan, whether required or voluntary, are applied to scheduled principal payments in inverse order, i.e. to the last scheduled principal payment first, followed by the second-to-last, etc. All principal payments under the Term Loan permanently reduce the original \$15 million capacity under this portion of the Facility.

The Facility also includes a three-year \$40 million revolving credit facility. Under this revolving credit facility, through July 31, 2003 we can borrow up to \$25 million, with the difference between actual borrowings and \$40 million available for letter of credit issuance up to a maximum of \$20 million in letters of credit. After July 31, 2003, we can borrow up to \$20 million under the revolving credit facility, with a maximum of \$20 million available for

letters of credit.

Interest Rates and Fees -- We have a choice of two interest rate options for borrowings under the Facility. Under one option, the interest rate is determined based on the higher of the Federal Funds Rate plus 0.5% or the prime rate of at least 75% of the U.S.'s 30 largest banks, as published each business day by the Wall Street Journal. An additional margin of 2.25% is then added to the higher of these two rates for borrowings under the Revolving Loan, while an additional margin of 2.75% is added to the higher of these two rates for borrowings under the Term Loan.

Under the other interest rate option, borrowings bear interest based on designated rates that are described in various general business media sources as the London Interbank Offered Rate or "LIBOR." Revolving Loan borrowings using this interest rate option then have 3.25% added to LIBOR, while Term Loan borrowings have 3.75% added to LIBOR.

The rates underlying these interest rate options are floating interest rates determined by the broad financial markets, meaning they can and do move up and down from time to time. The Facility required that we convert these floating interest rate terms on at least half of the Term Loan to fixed rates for at least a one-year term. In January 2003, we converted \$10 million of principal value to a fixed LIBOR-based interest rate of 5.62% for an eighteen-month term. This was done via a transaction known as a "swap" under which we agreed to pay fixed interest rate payments on \$10 million for eighteen months to a bank in exchange for receiving from the bank floating LIBOR interest rate payments on \$10 million for the same term. This transaction is a derivative and qualifies for hedge accounting treatment. As such, interest expense related to the hedged portion of this debt will be recorded at the fixed rate of 5.62% in our results of operations. Changes in market interest rates in any given period may increase or decrease the valuation of our obligations to the bank under this swap versus the bank's obligations to us. Such changes in market valuation will be reflected in stockholders' equity as other comprehensive income (loss) for that period, even though these obligations may not have been terminated and settled in cash during the period. Such adjustments are known as mark-to-market adjustments.

Commitment fees of 0.5% per annum are payable on the unused portion of the Revolving Loan.

We also incurred certain financing and professional costs in connection with the arrangement and the closing of the Facility. These costs will be amortized to interest expense over the term of the Facility in the

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amount of approximately \$0.4 million per quarter. To the extent prepayments of the Term Loan are made, we may have to accelerate amortization of these deferred financing and professional costs. Additionally, we expect to charge approximately \$0.5 million of deferred financing costs to interest expense in the first quarter of 2003 that were associated with higher levels of capacity under the Facility than the current total of \$55 million.

In connection with the Facility, we granted GE a warrant to purchase 409,051 shares of our common stock for nominal consideration. In addition, GE may "put," or require us to repurchase, these shares at the higher of market price, appraised price or book value per share, during the fifth and final year of the Facility -- October 11, 2006 to October 11, 2007. This put may be accelerated under certain circumstances including a change of control of our company, full repayments of amounts owing under the Facility, or a public offering of shares by us. This warrant and put are discussed in greater detail in Note 13, "Stockholders' Equity," to the Consolidated Financial Statements. The value of this warrant and put as of the start of the Facility of \$2.9 million is reflected as a discount of our obligation under the Facility and is being amortized over the term of the Facility, as described above. This warrant and put obligation is also recorded as a liability in the Company's balance sheet. The value of this warrant and put will change over time, principally in response to changes in the market price of our common stock. The warrant and the put qualify as a derivative for financial reporting purposes. Accordingly, such changes in the value of the warrant and put in any given period will be reflected in interest expense for that period, even though the warrant and put may not have been terminated and settled in cash during the period. Such adjustments are known as mark-to-market adjustments. The after-tax loss related to the warrant's mark-to-market obligation in 2002 was \$0.1 million.

The weighted average interest rate that we currently pay on borrowings

under the Facility is 5.6% per annum. This reflects a combination of borrowings under both interest rate options described above, as well as the swap of floating rates to a fixed rate described above. This rate does not include amortization of debt financing and arrangement costs, or mark-to-market adjustments for derivatives.

Restrictions and Covenants -- Borrowings under the Facility are specifically limited by our ratio of total debt to earnings before interest, taxes, depreciation, and amortization ("EBITDA") and by our ratio of EBITDA less taxes and capital expenditures to interest expense and scheduled principal payments, also known as the fixed charge coverage ratio. The Facility's definition of debt for purposes of the ratio of total debt to EBITDA includes aggregate letters of credit outstanding less \$10 million.

The definition of EBITDA under the Facility excludes certain items, generally non-cash amounts and transactions reported in Other Income and Expense, that are otherwise included in the determination of earnings under generally accepted accounting principles in our financial statements. As such, EBITDA as determined under the Facility's definition could be less than EBITDA as derived from our financial statements in the future.

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The financial covenants under the Facility are summarized below. Covenant compliance is measured on a monthly basis. Intra-quarter monthly covenants are at either the same or very similar levels to the quarter-end covenants shown below. EBITDA amounts are in thousands:

	FINANCIAL COVENANTS			
	MINIMUM TRAILING 12 MONTHS EBITDA	MAXIMUM DEBT TO EBITDA	MINIMUM FIXED CHARGE COVERAGE RATIO	MINIMUM INTEREST COVERAGE
FOR THE QUARTER ENDING				
ACTUAL				
December 31, 2002.....	\$23,639	0.64	4.04	7.17
COVENANT				
March 31, 2003.....	\$19,190	1.75	2.50	3.00
June 30, 2003.....	\$16,420	2.20	2.50	3.00
September 30, 2003.....	\$17,840	2.10	2.60	3.00
December 31, 2003.....	\$23,565	1.50	2.70	3.00
March 31, 2004.....	\$29,000	1.50	3.00	3.00
June 30, 2004.....	\$29,000	1.50	3.00	3.00
September 30, 2004.....	\$29,000	1.25	3.00	3.00
December 31, 2004.....	\$29,000	1.25	3.00	3.00
All quarters thereafter.....	\$31,000	1.25	3.00	3.00

Our trailing twelve months EBITDA as of December 31, 2002 as determined under the Facility did not comply with the covenant. Our lenders waived this violation. In addition, based on expectations of reduced operating results, at least through the first quarter of 2003 as described above under 2002 Compared to 2001 -- Gross Profit, our lenders agreed to reduce our minimum EBITDA, leverage and fixed charge covenants for 2003. Even at these reduced levels, these covenants leave only moderate room for variance based on our recent performance. If we again violate a covenant under the Facility, we may have to negotiate new borrowing terms under the Facility or obtain new financing. While we believe that our levels of debt in comparison to our EBITDA would enable us to negotiate new borrowing terms under the Facility or to obtain new financing from other sources if necessary, there can be no assurance that we would be successful in doing so.

The Facility prohibits us from paying dividends and repurchasing shares, limits annual lease expense and non-Facility debt, and restricts outlays of cash by us relating to certain investments, acquisitions and subordinate debt.

Notes to Affiliates and Former Owners -- Subordinated notes were issued to former owners of certain purchased companies as part of the consideration used to acquire their companies. As of December 31, 2002, these notes had been paid off. A gain of approximately \$0.7 million was recognized in 2002 related to

agreements with former owners for early repayment of certain of these notes, or other settlement of claims.

Other Commitments -- As is common in our industry, we have entered into certain off-balance sheet arrangements in the ordinary course of business that result in risks not directly reflected in our balance sheets. Our most significant off-balance sheet transactions include liabilities associated with noncancelable operating leases. We also have other off-balance sheet obligations involving letters of credit and surety guarantees.

We enter into noncancelable operating leases for many of our facility, vehicle and equipment needs. These leases allow us to conserve cash by paying a monthly lease rental fee for use of facilities, vehicles and equipment rather than purchasing them. At the end of the lease, we have no further obligation to the lessor. We may decide to cancel or terminate a lease before the end of its term. Typically we are liable to the lessor for the remaining lease payments under the term of the lease.

Some customers require us to post letters of credit to guarantee performance under our contracts and to ensure payment to our subcontractors and vendors under those contracts. Certain of our vendors also require

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letters of credit to ensure reimbursement for amounts they are disbursing on our behalf, such as to beneficiaries under our self-funded insurance programs. Such letters of credit are generally issued by a bank or similar financial institution. The letter of credit commits the issuer to pay specified amounts to the holder of the letter of credit if the holder demonstrates that we have failed to perform specified actions. If this were to occur, we would be required to reimburse the issuer of the letter of credit. Depending on the circumstances of such a reimbursement, we may also have to record a charge to earnings for the reimbursement. To date we have not had a claim made against a letter of credit that resulted in payments by the issuer of the letter of credit or by us. We believe that it is unlikely that we will have to fund claims under a letter of credit in the foreseeable future.

Many customers, particularly in connection with new construction, require us to post performance and payment bonds issued by a financial institution known as a surety. These bonds provide a guarantee to the customer that we will perform under the terms of a contract and that we will pay subcontractors and vendors. If we fail to perform under a contract or to pay subcontractors and vendors, the customer may demand that the surety make payments or provide services under the bond. We must reimburse the surety for any expenses or outlays it incurs. To date, we have not had any significant reimbursements to our surety for bond-related costs. We believe that it is unlikely that we will have to fund claims under our surety arrangements in the foreseeable future.

We have reached a preliminary agreement with our surety and GE to grant the surety a secured interest in assets such as receivables, costs incurred in excess of billings, and equipment related to projects for which bonds are outstanding as collateral for potential obligations under bonds. As of December 31, 2002, the amount of these assets is approximately \$41.9 million. We have also posted a \$5 million letter of credit as collateral for potential obligations under bonds.

Surety market conditions are currently difficult as a result of significant losses incurred by many sureties in recent periods, both in the construction industry as well as in certain larger corporate bankruptcies. As a result, less bonding capacity is available in the market and terms have become more restrictive. Further, under standard terms in the surety market, sureties issue bonds on a project by project basis, and can decline to issue bonds at any time. Historically, approximately 25% of our business has required bonds. While we have enjoyed a longstanding relationship with our surety, current market conditions as well as changes in our surety's assessment of our operating and financial risk could cause our surety to decline to issue bonds for our work. If that were to occur, our alternatives include doing more business that does not require bonds, posting other forms of collateral for project performance such as letters of credit or cash, and seeking bonding capacity from other sureties. There can be no assurance that we could easily achieve these alternatives. Accordingly, if we were to experience an interruption in the availability of bonding capacity, our revenues and profits could decline.

Amounts Outstanding, Capacity and Maturities -- The following recaps our debt amounts outstanding and capacity (in thousands):

	AS OF DEC. 31, 2002	AS OF MARCH 25, 2003	UNUSED CAPACITY AS OF MARCH 25, 2003
Revolving loan.....	\$ 107	\$12,975	\$8,055 (a)
Term loan.....	14,625	14,625	n/a
Other debt.....	502	495	n/a
	-----	-----	-----
Total debt.....	15,234	28,095	8,055
Less: discount on Facility.....	(2,850)	(2,750)	n/a
	-----	-----	-----
Total debt, net of discount.....	\$12,384	\$25,345	\$8,055
	=====	=====	=====
Letters of credit.....	\$ 9,800	\$12,844	\$7,156 (b)

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- (a) This amount reflects combined revolving loan capacity and letter of credit capacity and therefore includes letter of credit capacity shown above of \$7,156.
- (b) This amount is included in revolving loan capacity of \$8,055 shown above.

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The increase in our borrowings outstanding under the revolving loan during the first quarter of 2003 primarily results from the payment of a \$7.3 million tax liability relating to the Emcor transaction that was due in March 2003.

The following recaps the future maturities of this debt along with other contractual obligations. Debt maturities in this recap are based on amounts outstanding as of March 25, 2003 while operating lease maturities are based on amounts outstanding as of December 31, 2002 (in thousands):

	TWELVE MONTHS ENDED DECEMBER 31,						
	2003	2004	2005	2006	2007	THEREAFTER	TOTAL
Revolving loan.....	\$ --	\$ --	\$12,975	\$ --	\$ --	\$ --	\$12,975
Term loan.....	1,687	2,438	3,187	3,938	3,375	--	14,625
Other debt.....	86	112	57	58	58	124	495
	-----	-----	-----	-----	-----	-----	-----
Total debt.....	\$ 1,773	\$2,550	\$16,219	\$3,996	\$3,433	\$ 124	\$28,095
Less: discount on Facility.....							(2,750)

Total debt, net of discount.....							\$25,345
							=====
Operating lease obligations.....	\$10,265	\$8,260	\$ 6,041	\$4,789	\$4,202	\$15,425	\$48,982

As of December 31, 2002, we also have \$9.8 million of letter of credit commitments, all of which will expire in 2003.

Outlook -- As noted above, we have generated positive free cash flow in most recent periods, and we currently have a moderate level of debt. We anticipate that free cash flow from operations and borrowing capacity under the Facility will provide us with sufficient liquidity to fund our operations for the foreseeable future. However, we do not have a significant amount of excess borrowing capacity in comparison to expected working capital requirements over the balance of 2003. We believe that our levels of debt in comparison to our EBITDA and our cash flows would enable us to obtain new financing if necessary, but there can be no assurance that we would be successful in doing so.

We currently have \$12.8 million in letters of credit outstanding. We self-insure a significant portion of our workers compensation, auto liability

and general liability risks. We use third parties to manage this self-insurance and to retain some of these risks. As is customary under such arrangements, these third parties can require letters of credit as security for amounts they fund or risks they might potentially absorb on our behalf. Under our current self-insurance arrangements, we expect that we will be required to post approximately \$3.0 million per quarter during the first three quarters of 2003. In addition, we may receive other letter of credit requests in the ordinary course of business, and we may have a net increase in the amount of insurance-related letters of credit we must post when we renew our insurance arrangements in the fourth quarter of next year. Accordingly, our letter of credit requirements over the next year may exceed the current letter of credit sublimit of \$20 million under our credit facility. If so, we may have to seek additional letter of credit capacity or post different forms of security such as bonds or cash in lieu of letters of credit. We believe that our levels of debt in comparison to our EBITDA and free cash flows would enable us to obtain additional letter of credit capacity or to otherwise meet financial security requirements of third parties if necessary, but there can be no assurance that we would be successful in doing so.

As described above, we must comply with a number of financial covenants in connection with the Facility. Our trailing twelve months EBITDA as of December 31, 2002 as determined under the Facility did not comply with covenant. Our lenders waived this violation. In addition, based on expectations of lower operating results at least through the first quarter of 2003 as described above under 2002 Compared to 2001 -- Gross Profit, our lenders agreed to modify our minimum EBITDA, leverage and fixed charge covenants for 2003. Even at these modified levels, these covenants leave only moderate room for variance based on our recent performance. If we again violate a covenant under the Facility, we may have to negotiate new borrowing terms under the Facility or obtain new financing. While we believe that our levels of debt in comparison to our EBITDA and our cash flows would enable us to negotiate new borrowing terms under the

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Facility or to obtain new financing from other sources if necessary, there can be no assurance that we would be successful in doing so.

SEASONALITY AND CYCLICALITY

The HVAC industry is subject to seasonal variations. Specifically, the demand for new installation and replacement is generally lower during the winter months (the first quarter of the year) due to reduced construction activity during inclement weather and less use of air conditioning during the colder months. Demand for HVAC services is generally higher in the second and third calendar quarters due to increased construction activity and increased use of air conditioning during the warmer months. Accordingly, we expect our revenues and operating results generally will be lower in the first and fourth calendar quarters.

Historically, the construction industry has been highly cyclical. As a result, our volume of business may be adversely affected by declines in new installation projects in various geographic regions of the United States.

NEW ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 establishes new accounting and reporting requirements for goodwill and other intangible assets. We adopted this new standard effective January 1, 2002. See Note 4 of the Consolidated Financial Statements for further discussion.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." We adopted SFAS No. 144 effective January 1, 2002. Under SFAS No. 144, the operating results of companies sold or held for sale meeting certain criteria, as well as any gain or loss on the sale of these operations, are presented as discontinued operations in our statements of operations. See Note 3 of the Consolidated Financial Statements for a discussion of our discontinued operations. The operating results for companies which were sold or shut down during 2001 are presented as continuing operations through the date of disposition. The adoption of SFAS No. 144 did affect the presentation of discontinued operations in the consolidated financial statements; however, it did not have any overall financial impact on our results of operations, financial position or cash flows.

In April 2002, the FASB issued SFAS No. 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections ("SFAS No. 145"). SFAS No. 145 requires that gains and losses from extinguishment of debt be classified as extraordinary items only if they meet the criteria in Accounting Principles Board Opinion No. 30 ("Opinion No. 30"). Applying the provisions of Opinion No. 30 will distinguish transactions that are part of an entity's recurring operations from those that are unusual and infrequent and meet the criteria for classification as an extraordinary item. In connection with our new credit facility, we fully amortized \$0.4 million of deferred debt costs and recognized a \$0.7 million gain on the extinguishment of subordinated debt in 2002. These amounts are recorded in "Other Expense, net" in our results of operations.

In July 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities ("SFAS No. 146"). SFAS No. 146 addresses financial accounting and reporting for costs associated with exit or disposal activities, such as restructurings, involuntarily terminating employees, and consolidating facilities initiated after December 31, 2002. The implementation of SFAS No. 146 will not require the restatement of previously issued financial statements. Implementation of the pronouncement will therefore have no impact on our current year financial statements.

In November 2002, the FASB issued Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others ("FIN 45"). It clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee, including its ongoing obligation to stand ready to perform over the term of the guarantee in the event that the specified triggering events or conditions occur. The objective of the initial measurement of the liability is the fair value of the guarantee at its inception. The initial

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recognition and initial measurement provisions of FIN 45 are effective for us on a prospective basis for guarantees issued after December 31, 2002. Although we from time to time guarantee the performance of systems or designs we provide, we currently have no material guarantees.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation -- Transition and Disclosure." SFAS 148 amends FASB Statement No. 123, "Accounting for Transition for Stock-Based Compensation" to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS 148 amends the disclosure requirements of SFAS 123 to require prominent disclosures in both annual and interim financial statements of the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS 148 is effective for fiscal years ending after December 15, 2002 and was adopted by us for all periods presented.

FACTORS WHICH MAY AFFECT FUTURE RESULTS

Our future operating results are difficult to predict and may be affected by a number of factors, including the lack of a combined operating history and the difficulty of integrating formerly separate businesses, retention of key management, national or regional declines in non-residential construction activity, difficulty in obtaining or increased costs associated with debt financing or bonding, shortages of labor and specialty building materials, seasonal fluctuations in the demand for HVAC systems and the use of incorrect estimates for bidding a fixed price contract. As a result of these and other factors, there can be no assurance that we will not experience material fluctuations in future operating results or cash flows on a quarterly or annual basis.

Our success depends in part on our ability to integrate and further consolidate the companies we have acquired. These businesses operated as separate, independent entities prior to their affiliation with us, and there can be no assurance that we will be able to integrate the operations of these businesses successfully or institute the necessary systems and procedures, including accounting and financial reporting systems, to effectively manage the combined enterprise on a profitable basis. The historical results are not necessarily indicative of our future results because, among other reasons, our subsidiary operations were not under common control or management prior to their acquisition. There are also risks associated with unanticipated events or

liabilities resulting from the acquired businesses' operations prior to the acquisition.

Many customers, particularly in connection with new construction, require us to post performance and payment bonds issued by a financial institution known as a surety. These bonds provide a guarantee to the customer that we will perform under the terms of a contract and that we will pay subcontractors and vendors. If we fail to perform under a contract or to pay subcontractors and vendors, the customer may demand that the surety make payments or provide services under the bond. We must reimburse the surety for any expenses or outlays it incurs. To date, we have not had any significant reimbursements to our surety for bond-related costs. We believe that it is unlikely that we will have to fund claims under our surety arrangements in the foreseeable future.

Surety market conditions are currently difficult as a result of significant losses incurred by many sureties in recent periods, both in the construction industry as well as in certain larger corporate bankruptcies. As a result, less bonding capacity is available in the market and terms have become more restrictive. Further, under standard terms in the surety market, sureties issue bonds on a project by project basis, and can decline to issue bonds at any time. Historically, approximately 25% of our business has required bonds. While we have enjoyed a longstanding relationship with our surety, current market conditions as well as changes in our surety's assessment of our operating and financial risk could cause our surety to decline to issue bonds for our work. If that were to occur, our alternatives include doing more business that does not require bonds, posting other forms of collateral for project performance such as letters of credit or cash, and seeking bonding capacity from other sureties. There can be no assurance that we could easily achieve these alternatives. Accordingly, if we were to experience an interruption in the availability of bonding capacity, our revenues and profits could decline.

The existing senior management at many of our subsidiary operations is generally comprised of former owners who committed to stay with their operations after acquisition. Certain of these individuals have

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suffered losses in the value of our common stock or have lower incomes than they averaged when they owned their former businesses. Further, former owners generally have noncompetition obligations that expire on the fifth anniversary of their date of acquisition, and thus these obligations expire from July 2002 through 2004. There is no assurance that we will be able to retain these individuals or find suitable replacements if such individuals leave the Company. The failure to retain or replace such management on a timely basis could negatively impact results from operations at such locations.

Key elements of our strategy are to both maintain and improve the profitability and cash flow of the individual businesses. Our level of success in this strategy, if any, will be affected by demand for new or replacement HVAC systems. In part, such demand will be contingent upon factors outside our control, such as the level of new construction or the potential for slower replacement based upon the overall level of activity in the economy. The HVAC industry is subject to both seasonal and cyclical variations, meaning that temperate weather and downturns in the domestic or regional economies will negatively affect overall demand for our services.

The timely provision of high-quality installation service and maintenance, repair and replacement of HVAC systems requires an adequate supply of skilled HVAC technicians. In addition, we depend on the senior management of the businesses we acquire and regional and corporate management to remain committed to our success. Accordingly, our ability to maintain and increase our productivity and profitability is also affected by our ability to employ, train and retain the skilled technicians necessary to meet our service requirements, and to retain senior management at the corporate, regional and local level.

Our ability to generate positive cash flow at our historical levels in the future could be adversely impacted by a reduction in our billings and collections as a result of a decline in new projects. The risk associated with a decline in new projects could be further perpetuated by our accelerated billing for our project work because we will continue to incur costs on older projects where payment may have already been received from the customer. Such indebtedness, together with the financial and other restrictive covenants in our debt instruments, could limit our ability to borrow additional funds. Additionally, failing to comply with those covenants could result in an event of default, which, if not cured or waived, could have a material adverse effect on

the Company.

HVAC systems are subject to various environmental statutes and regulations, including the Clean Air Act and those regulating the production, servicing and disposal of certain ozone depleting refrigerants used in HVAC systems. There can be no assurance that the regulatory environment in which we operate will not change significantly in the future. Our failure to comply, or the costs of compliance, with such laws and regulations could adversely affect our future results.

Because of these and other factors, past financial performance should not necessarily be considered an indicator of future performance. Investors should not rely solely on historical trends to anticipate future results and should be aware that the trading price of our Common Stock may be subject to wide fluctuations in response to quarter-to-quarter variations in operating results, general conditions in the HVAC industry, the increasing supply of tradable stock, changes in analysts' earnings estimates, recommendations by analysts, or other events.

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

We are exposed to market risk primarily related to potential adverse changes in interest rates as discussed below. Management is actively involved in monitoring exposure to market risk and continues to develop and utilize appropriate risk management techniques. In January 2003, we converted \$10 million of our Term Loan to a fixed rate of 5.62% for an eighteen-month term. This was done via a transaction known as a "swap" under which we agree to pay fixed LIBOR-based interest rate payments on \$10 million for eighteen months to a bank in exchange for receiving from the bank floating LIBOR-based interest rate payments on \$10 million for the same term. This transaction is a derivative and qualifies for hedge accounting treatment. We are not exposed to any other significant financial market risks including commodity price risk, foreign currency exchange risk or interest rate risks from the use of derivative financial instruments. Management does not use derivative financial instruments for trading or to speculate on changes in interest rates or commodity prices.

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Our exposure to changes in interest rates primarily results from our short-term and long-term debt with both fixed and floating interest rates. Our debt with fixed interest rates consists of capital leases and various notes payable. This differs from the exposure for the fiscal year ended December 31, 2001 due to the elimination of convertible subordinated notes and subordinated notes as exposures. Our debt with variable interest rates consists entirely of our Facility. The following table presents principal amounts (stated in thousands) and related weighted average interest rates by year of maturity for our debt obligations and their indicated fair market value at December 31, 2002:

	2003	2004	2005	2006	2007	THEREAFTER	TOTAL	FAIR VALUE
	-----	-----	-----	-----	-----	-----	-----	-----
LIABILITIES -- LONG-TERM								
DEBT:								
Fixed Rate Debt.....	\$ 93	\$ 112	\$ 57	\$ 58	\$ 58	\$124	\$ 502	\$ 502
Average Interest Rate.....	9.0%	8.1%	7.3%	7.2%	7.2%	6.2%	7.0%	7.0%
Variable Rate Debt.....	\$1,687	\$2,438	\$3,294	\$3,938	\$3,375	\$ --	\$14,732	\$14,732
Average Interest Rate.....	5.2%	5.2%	5.2%	5.2%	5.2%	5.2%	5.2%	5.2%

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTAL DATA

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REPORT OF INDEPENDENT AUDITORS

Board of Directors and Stockholders
Comfort Systems USA, Inc.

We have audited the accompanying consolidated balance sheets of Comfort Systems USA, Inc. (the "Company") as of December 31, 2001 and 2002, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2002. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Comfort Systems USA, Inc. as of December 31, 2001 and 2002, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States.

As discussed in Note 4 to the consolidated financial statements, on January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," which changed the method of accounting for goodwill and other intangible assets.

ERNST & YOUNG LLP

Houston, Texas
March 28, 2003

COMFORT SYSTEMS USA, INC.

CONSOLIDATED BALANCE SHEETS

	DECEMBER 31,	
	2001	2002
	(IN THOUSANDS, EXCEPT SHARE AMOUNTS)	
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents.....	\$ 4,156	\$ 6,104
Accounts receivable, less allowance for doubtful accounts of \$9,645 and \$6,048.....	175,735	168,392
Other receivables.....	5,684	7,892
Inventories.....	14,855	12,415
Prepaid expenses and other.....	13,174	10,626
Costs and estimated earnings in excess of billings.....	19,413	17,964
Assets related to discontinued operations.....	326,076	--

Total current assets.....	559,093	223,393
PROPERTY AND EQUIPMENT, net.....	18,956	16,111
GOODWILL, net.....	297,251	113,427
OTHER NONCURRENT ASSETS.....	1,325	13,604
	-----	-----
Total assets.....	\$876,625	\$ 366,535
	=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:

Current maturities of long-term debt.....	\$ 73	\$ 1,780
Current maturities of notes to affiliates and former owners.....	2,374	--
Accounts payable.....	57,719	56,773
Accrued compensation and benefits.....	23,626	22,830
Billings in excess of costs and estimated earnings.....	26,663	26,672
Income taxes payable.....	5,606	9,797
Other current liabilities.....	23,495	29,801
Liabilities related to discontinued operations.....	140,474	--
	-----	-----

Total current liabilities.....	280,030	147,653
LONG-TERM DEBT, NET OF CURRENT MATURITIES AND DISCOUNT OF \$2,850 in 2002.....	164,012	10,604
NOTES TO AFFILIATES AND FORMER OWNERS, NET OF CURRENT		

MATURITIES.....	15,569	--
OTHER LONG-TERM LIABILITIES.....	3,193	3,192
	-----	-----

Total liabilities.....	462,804	161,449
------------------------	---------	---------

COMMITMENTS AND CONTINGENCIES

STOCKHOLDERS' EQUITY:

Preferred stock, \$.01 par, 5,000,000 shares authorized, none issued and outstanding.....	--	--
Common stock, \$.01 par, 102,969,912 shares authorized, 39,258,913 shares issued.....	393	393
Treasury stock, at cost, 1,749,334 and 1,341,419 shares, respectively.....	(10,924)	(8,214)
Additional paid-in capital.....	340,186	338,606
Deferred compensation.....	--	(785)
Retained earnings (deficit).....	84,166	(124,914)
	-----	-----
Total stockholders' equity.....	413,821	205,086
	-----	-----
Total liabilities and stockholders' equity.....	\$876,625	\$ 366,535
	=====	=====

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

COMFORT SYSTEMS USA, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002
	-----	-----	-----
	(IN THOUSANDS, EXCEPT PER SHARE DATA)		
REVENUES.....	\$902,289	\$882,861	\$ 819,282
COST OF SERVICES.....	736,191	717,284	676,268
	-----	-----	-----
Gross profit.....	166,098	165,577	143,014
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	153,563	143,675	127,051
GOODWILL AMORTIZATION AND IMPAIRMENT.....	8,678	8,238	218
RESTRUCTURING CHARGES.....	25,344	238	1,878
	-----	-----	-----
Operating income (loss).....	(21,487)	13,426	13,867
OTHER INCOME (EXPENSE):			
Interest income.....	261	112	71

Interest expense.....	(11,349)	(8,112)	(4,951)
Other.....	580	446	1,395
	-----	-----	-----
Other income (expense).....	(10,508)	(7,554)	(3,485)
	-----	-----	-----
REDUCTIONS IN NON-OPERATING ASSETS AND LIABILITIES, NET.....	(1,095)	--	--
	-----	-----	-----
INCOME (LOSS) BEFORE INCOME TAXES.....	(33,090)	5,872	10,382
INCOME TAX EXPENSE (BENEFIT).....	(3,192)	6,905	4,903
	-----	-----	-----
INCOME (LOSS) FROM CONTINUING OPERATIONS.....	(29,898)	(1,033)	5,479
DISCONTINUED OPERATIONS:			
Operating income (loss), net of applicable income tax benefit (expense) of \$(8,977), \$(9,627), and \$1,880....	13,045	14,157	(36)
Estimated loss on disposition, including income tax expense of \$23,324.....	--	--	(12,002)
	-----	-----	-----
INCOME (LOSS) BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE.....	(16,853)	13,124	(6,559)
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET OF INCOME TAX BENEFIT OF \$26,317.....	--	--	(202,521)
	-----	-----	-----
NET INCOME (LOSS).....	\$ (16,853)	\$ 13,124	\$ (209,080)
	=====	=====	=====
INCOME (LOSS) PER SHARE:			
Basic --			
Income (loss) from continuing operations.....	\$ (0.80)	\$ (0.03)	\$ 0.15
Discontinued operations --			
Income (loss) from operations.....	0.35	0.38	--
Estimated loss on disposition.....	--	--	(0.32)
Cumulative effect of change in accounting principle....	--	--	(5.39)
	-----	-----	-----
Net income (loss).....	\$ (0.45)	\$ 0.35	\$ (5.56)
	=====	=====	=====
Diluted --			
Income (loss) from continuing operations.....	\$ (0.80)	\$ (0.03)	\$ 0.14
Discontinued operations --			
Income (loss) from operations.....	0.35	0.38	--
Estimated loss on disposition.....	--	--	(0.31)
Cumulative effect of change in accounting principle....	--	--	(5.28)
	-----	-----	-----
Net income (loss).....	\$ (0.45)	\$ 0.35	\$ (5.45)
	=====	=====	=====
SHARES USED IN COMPUTING INCOME (LOSS) PER SHARE:			
Basic.....	37,397	37,436	37,605
	=====	=====	=====
Diluted.....	37,397	37,436	38,367
	=====	=====	=====

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

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COMFORT SYSTEMS USA, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	COMMON STOCK		TREASURY STOCK		ADDITIONAL PAID-IN CAPITAL	DEFERRED COMPENSATION	RETAINED EARNINGS (DEFICIT)	TOTAL STOCKHOLDERS' EQUITY
	SHARES	AMOUNT	SHARES	AMOUNT				
	(IN THOUSANDS, EXCEPT SHARE AMOUNTS)							
BALANCE AT DECEMBER 31, 1999....	39,258,913	\$393	(1,695,524)	\$(11,978)	\$342,655	\$ --	\$ 87,895	\$ 418,965
Issuance of Treasury Stock:								
Issuance of Employee Stock Purchase Plan shares.....	--	--	329,212	2,254	(732)	--	--	1,522
Common Stock repurchases.....	--	--	(175,513)	(1,224)	--	--	--	(1,224)
Shares exchanged in repayment of notes receivable.....	--	--	(385,996)	(1,975)	--	--	--	(1,975)
Shares received from sale of businesses.....	--	--	(74,808)	(196)	--	--	--	(196)
Net loss.....	--	--	--	--	--	--	(16,853)	(16,853)
	-----	-----	-----	-----	-----	-----	-----	-----
BALANCE AT DECEMBER 31, 2000....	39,258,913	393	(2,002,629)	(13,119)	341,923	--	71,042	400,239
Issuance of Treasury Stock:								
Issuance of Employee Stock Purchase Plan shares.....	--	--	398,287	2,570	(1,737)	--	--	833
Shares received from sale of businesses.....	--	--	(144,992)	(375)	--	--	--	(375)
Net income.....	--	--	--	--	--	--	13,124	13,124
	-----	-----	-----	-----	-----	-----	-----	-----
BALANCE AT DECEMBER 31, 2001....	39,258,913	393	(1,749,334)	(10,924)	340,186	--	84,166	413,821

Issuance of Treasury Stock:								
Issuance of shares for options exercised.....	--	--	242,146	1,499	(803)	--	--	696
Issuance of restricted stock.....	--	--	275,000	1,698	(618)	(1,080)	--	--
Shares exchanged in repayment of notes receivable.....	--	--	(49,051)	(204)	--	--	--	(204)
Shares received from sale of business.....	--	--	(55,882)	(263)	--	--	--	(263)
Shares received from settlement with former owner.....	--	--	(4,298)	(20)	--	--	--	(20)
Amortization of deferred compensation.....	--	--	--	--	(159)	295	--	136
Net loss.....	--	--	--	--	--	--	(209,080)	(209,080)
BALANCE AT DECEMBER 31, 2002....	39,258,913	\$393	(1,341,419)	\$ (8,214)	\$338,606	\$ (785)	\$(124,914)	\$ 205,086

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

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COMFORT SYSTEMS USA, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002
	(IN THOUSANDS)		
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income (loss).....	\$ (16,853)	\$ 13,124	\$(209,080)
Adjustments to reconcile net income (loss) to net cash provided by operating activities --			
Cumulative effect of change in accounting principle.....	--	--	202,521
Estimated loss on disposition of discontinued operations.....	--	--	12,002
Restructuring charges.....	25,344	238	1,878
Reductions in non-operating assets and liabilities, net...	5,867	--	--
Depreciation and amortization expense.....	24,902	24,466	7,008
Bad debt expense.....	5,883	10,329	3,701
Deferred tax expense (benefit).....	(2,590)	(1,408)	3,715
Extinguishment of subordinated notes.....	--	--	(658)
Amortization of debt financing costs.....	1,272	1,444	2,088
Gain on sale of assets.....	(697)	(199)	(893)
Goodwill impairment.....	--	--	218
Deferred compensation expense.....	--	--	136
Mark-to-market warrant obligation.....	--	--	180
Amortization of debt discount.....	--	--	147
Changes in operating assets and liabilities, net of effects of acquisitions and divestitures --			
(Increase) decrease in --			
Receivables, net.....	(36,791)	12,095	13,292
Inventories.....	1,103	940	2,427
Prepaid expenses and other current assets.....	1,496	(3,516)	2,598
Costs and estimated earnings in excess of billings...	9,373	11,007	(822)
Other noncurrent assets.....	2,002	(412)	565
Increase (decrease) in --			
Accounts payable and accrued liabilities.....	21,946	(3,178)	(27,744)
Billings in excess of costs and estimated earnings...	17,105	2,513	1,052
Other, net.....	(1,190)	(614)	(241)
Net cash provided by operating activities.....	58,172	66,829	14,090
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchases of property and equipment.....	(18,037)	(5,978)	(5,322)
Proceeds from sales of property and equipment.....	1,937	1,011	1,551
Proceeds from businesses sold, net of cash sold and transaction costs.....	713	964	154,360
Net cash provided by (used in) investing activities.....	(15,387)	(4,003)	150,589
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from issuance of common stock.....	1,522	833	--
Net borrowings payments on revolving line of credit.....	(1,515)	(60,000)	(163,593)
Payments on other long-term debt.....	(29,795)	(9,113)	(18,338)

Borrowings of other long-term debt.....	584	58	15,202
Repurchases of common stock.....	(1,224)	--	--
Debt financing costs.....			(3,167)
Proceeds from exercise of options.....	--	--	696
	-----	-----	-----
Net cash used in financing activities.....	(30,428)	(68,222)	(169,200)
	-----	-----	-----
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	12,357	(5,396)	(4,521)
CASH AND CASH EQUIVALENTS, beginning of year -- continuing operations and discontinued operations.....	3,664	16,021	10,625
	-----	-----	-----
CASH AND CASH EQUIVALENTS, end of year -- continuing operations and discontinued operations.....	\$ 16,021	\$ 10,625	\$ 6,104
	=====	=====	=====

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

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2002

1. BUSINESS AND ORGANIZATION

Comfort Systems USA, Inc., a Delaware corporation ("Comfort Systems" and collectively with its subsidiaries, the "Company"), is a national provider of comprehensive heating, ventilation and air conditioning ("HVAC") installation, maintenance, repair and replacement services within the mechanical services industry. The Company operates primarily in the commercial and industrial HVAC markets, and performs most of its services within office buildings, retail centers, apartment complexes, manufacturing plants, and healthcare, education and government facilities. In addition to standard HVAC services, the Company provides specialized applications such as building automation control systems, fire protection, process cooling, electronic monitoring and process piping. Certain locations also perform related activities such as electrical service and plumbing. Approximately 52% of the Company's consolidated 2002 revenues were attributable to installation of systems in newly constructed facilities, with the remaining 48% attributable to maintenance, repair and replacement services. The Company's consolidated 2002 revenues related to the following service activities: HVAC -- 73%, plumbing -- 10%, building automation control systems -- 5%, electrical -- 3%, fire protection -- 2% and other -- 7%. These service activities are within the mechanical services industry which is the single industry segment served by Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets," which is discussed in Note 4 and SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which is discussed in Note 3 during the first quarter of 2002. There were no other significant changes in the accounting policies of the Company during the period.

PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of Comfort Systems and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

CASH FLOW INFORMATION

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Cash paid for interest for continuing and discontinued operations in 2000, 2001 and 2002 was approximately \$25.8 million, \$20.7 million and \$5.3 million, respectively. Cash paid for income taxes for continuing and discontinued operations in 2000, 2001 and 2002 was approximately \$13.1 million, \$10.1 million and \$10.7 million, respectively.

INVENTORIES

Inventories consist of parts and supplies held for use in the ordinary course of business and are stated at the lower of cost or market using the first-in, first-out method.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost, and depreciation is computed using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are capitalized and amortized over the lesser of the expected life of the lease or the estimated useful life of the asset.

Expenditures for repairs and maintenance are charged to expense when incurred. Expenditures for major renewals and betterments, which extend the useful lives of existing equipment, are capitalized and depreciated

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

over the remaining useful life of the equipment. Upon retirement or disposition of property and equipment, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized in "Other income (expense)" in the statement of operations.

GOODWILL

Goodwill represents the excess of the aggregate purchase price paid by the Company in acquisitions accounted for as purchases over the fair value of the net tangible assets acquired. Prior to 2002, goodwill was amortized on a straight-line basis over 40 years. As further discussed in Note 4, effective January 1, 2002, goodwill is no longer subject to scheduled amortization, but is subjected to an annual impairment test.

LONG-LIVED ASSETS

Long-lived assets are comprised principally of goodwill, property and equipment, and deferred income tax assets. The Company periodically evaluates whether events and circumstances have occurred that indicate that the remaining balances of these assets may not be recoverable. The Company uses an estimate of future income from operations and cash flows, as well as other economic and business factors as a measure of recoverability of these assets.

REVENUE RECOGNITION

Under the percentage of completion method of accounting as provided by American Institute of Certified Public Accountants Statement of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts," contract revenue recognizable at any time during the life of a contract is determined by multiplying expected total contract revenue by the percentage of contract costs incurred at any time to total estimated contract costs. More specifically, as part of the negotiation and bidding process in which the Company engages in connection with obtaining installation contracts, the Company estimates contract costs, which include all direct materials (net of estimated rebates), labor and subcontract costs and indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and depreciation costs. Then, as the Company performs under those contracts, such costs are measured as incurred, compared to total estimated costs to complete the contract, and a corresponding proportion of contract revenue is recognized. As a result, contract revenues recognized in the statement of operations can and usually do differ from amounts that can be billed or invoiced to the customer at any point during the contract.

Changes in job performance, job conditions, estimated profitability and final contract settlements may result in revisions to estimated costs and, therefore, revenues. Such revisions are frequently based on further estimates and subjective assessments. The effects of these revisions are recognized in the period in which the revisions are determined. When such revisions lead to a conclusion that a loss will be recognized on a contract, the full amount of the estimated ultimate loss is recognized in the period such a conclusion is reached, regardless of the percentage of completion of the contract. Depending on the size of a project, variations from estimated project costs could have a significant impact on the Company's operating results.

Revenues associated with maintenance, repair and monitoring services and related contracts are recognized as services are performed.

ACCOUNTS RECEIVABLE

Accounts receivable include amounts billed to but not paid by customers pursuant to retainage provisions in construction contracts. These amounts are due upon completion of the contracts and acceptance by the customer. Based on the Company's experience with similar contracts in recent years, billings for such retention balances at each balance sheet date are finalized and collected within the subsequent year. The retainage balances at December 31, 2001 and 2002 are \$33.1 million, and are included in accounts receivable.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

The carrying value of the Company's receivables, net of the allowance for doubtful accounts, represents their estimated net realizable value. The Company estimates its allowance for doubtful accounts based upon the creditworthiness of its customer, prior collection history, the ongoing relationship with its customers, the aging of past due balances, the Company's lien rights, if any, in the property where the Company performed the work, and the availability, if any, of payment bonds applicable to the contract. The estimate of the allowance is based upon the best facts available and is re-evaluated and adjusted as additional information is received.

COSTS AND ESTIMATED EARNINGS IN EXCESS OF BILLINGS

The current asset "Costs and estimated earnings in excess of billings" represents revenues recognized in excess of amounts billed under the terms of the contract. These amounts are billable upon completion of contract performance milestones or other specified conditions of the contract.

Claims or unapproved change orders represent amounts to be recovered from the customer or other third parties for errors, changes in specifications or design or other unanticipated customer-related changes resulting in additional contract costs. These amounts are recorded as "Costs and estimated earnings in excess of billings" at their estimated net realizable amounts when realization is probable and such amounts can be reasonably estimated. These claims and unapproved change orders involve estimates which will be revised as additional information becomes known. The amounts for such claims and unapproved change orders that are currently included in costs and estimated earnings in excess of billings are not material.

SELF-INSURANCE LIABILITIES

The Company retains the risk of worker's compensation, employer's liability, auto liability, general liability and employee group health claims resulting from uninsured deductibles per accident or occurrence. Losses up to the deductible amounts are estimated and accrued based upon known facts, historical trends and industry averages utilizing the assistance of an actuary to determine the best estimate of these obligations.

WARRANTY COSTS

The Company typically warrants labor for the first year after installation on new HVAC systems. The Company generally warrants labor for 30 days after servicing of existing HVAC systems. A reserve for warranty costs is estimated and recorded based upon the historical level of warranty claims and management's estimate of future costs.

INCOME TAXES

The Company files a consolidated return for federal income tax purposes. Income taxes are provided for under the liability method in accordance with SFAS No. 109, "Accounting for Income Taxes," which takes into account differences between financial statement treatment and tax treatment of certain transactions. Deferred tax assets represent the tax effect of activity that has been reflected in the financial statements but which will not be deductible for tax purposes until future periods. Deferred tax liabilities represent the tax effect of activity that has been reflected in the financial statements but which will not be taxable until future periods.

NEW ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards board ("FASB") issued SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 establishes new accounting and reporting requirements for goodwill and other intangible assets. The Company adopted this new standard effective January 1, 2002. See Note 4 for further discussion.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

In August 2001, the FASB issued SFAS No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets." The Company adopted SFAS No. 144 effective January 1, 2002. Under SFAS No. 144, the operating results of companies sold or held for sale meeting certain criteria, as well as any gain or loss on the sale of these operations, are presented as discontinued operations in the Company's statements of operations. See Note 3 for a discussion of the Company's discontinued operations. The operating results for companies which were sold or shut down during 2001 are presented as continuing operations through the date of disposition. The adoption of SFAS No. 144 did affect the presentation of discontinued operations in the consolidated financial statements; however, it did not have any overall financial impact on the Company's results of operations, financial position or cash flows.

In April 2002, the FASB issued SFAS No. 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections ("SFAS No. 145"). SFAS No. 145 requires that gains and losses from extinguishment of debt be classified as extraordinary items only if they meet the criteria in Accounting Principles Board Opinion No. 30 ("Opinion No. 30"). Applying the provisions of Opinion No. 30 will distinguish transactions that are part of an entity's recurring operations from those that are unusual and infrequent and meet the criteria for classification as an extraordinary item. In connection with the Company's new credit facility, the Company fully amortized \$0.4 million of deferred debt costs and recognized a \$0.7 million gain on the extinguishment of subordinated debt in 2002. These amounts are recorded in "Other Expense, net" in the Company's statement of operations.

In July 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities ("SFAS No. 146"). SFAS No. 146 addresses financial accounting and reporting for costs associated with exit or disposal activities, such as restructurings, involuntarily terminating employees, and consolidating facilities initiated after December 31, 2002. The implementation of SFAS No. 146 will not require the restatement of previously issued financial statements. Implementation of the pronouncement will therefore have no impact on the Company's current year financial statements.

In November 2002, the FASB issued Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others ("FIN 45"). It clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee, including its ongoing obligation to stand ready to perform over the term of the guarantee in the event that the specified triggering events or conditions occur. The objective of the initial measurement of the liability is the fair value of the guarantee at its inception. The initial recognition and initial measurement provisions of FIN 45 are effective for the Company on a prospective basis for guarantees issued after December 31, 2002. Although the Company from time to time guarantees the performance of systems or designs it provides, the Company does not currently have any material guarantees.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation -- Transition and Disclosure." SFAS 148 amends FASB Statement No. 123, "Accounting for Transition for Stock-Based Compensation" to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS 148 amends the disclosure requirements of SFAS 123 to require prominent disclosures in both annual and interim financial statements of the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS 148 is effective for fiscal years ending after December 15, 2002 and was adopted by the Company for all periods presented.

SEGMENT DISCLOSURE

Comfort Systems' activities are within the mechanical services industry which is the single industry segment served by the Company. Under SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information," each operating subsidiary represents an operating segment and these segments have

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

been aggregated, as no individual operating unit is material and the operating units meet a majority of the aggregation criteria.

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions by management in determining the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The most significant estimates used in the Company's financial statements include revenue and cost recognition for construction contracts, allowance for doubtful accounts and self-insurance accruals.

CONCENTRATIONS OF CREDIT RISK

The Company provides services to a broad range of geographical regions. The Company's credit risk primarily consists of receivables from a variety of customers including general contractors, property owners and developers, and commercial and industrial companies. The Company reviews its accounts receivable and provides estimates of allowances regularly.

FINANCIAL INSTRUMENTS

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, receivables from related parties, other receivables, accounts payable, a line of credit, notes payable, notes payable to related parties and long-term debt. The Company believes that the carrying values of these instruments on the accompanying balance sheets approximate their fair values.

STOCK-BASED COMPENSATION

The Company accounts for its stock-based compensation using the intrinsic value method under Accounting Principles Board Statement No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). Under this accounting method, no expense in connection with the stock option plan or the stock purchase plan is recognized in the consolidated statements of operations when the exercise price of the stock options is greater than or equal to the value of the Common Stock on the date of grant. In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation," which requires that if a company accounts for stock-based compensation in accordance with APB 25, the company must also disclose the effects on its results of operations as if an estimate of the value of stock-based compensation at the date of

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

grant was recorded as an expense in the company's statement of operations. These effects for the Company are as follows (in thousands, except per share data):

	2000	2001	2002
	-----	-----	-----
Net Income (Loss) as reported.....	\$(16,853)	\$13,124	\$(209,080)
Less: Compensation expense per SFAS No. 123, net of			

tax.....	(3,212)	(3,569)	(3,290)
Pro forma Net Income (Loss).....	\$ (20,065)	\$ 9,555	\$ (212,370)
Net Income (Loss) Per Share -- Basic			
Net Income (Loss) as reported.....	\$ (0.45)	\$ 0.35	\$ (5.56)
Less: Compensation expense per SFAS No. 123, net of tax.....	(0.09)	(0.10)	(0.09)
Pro forma Net Income (Loss) per share.....	\$ (0.54)	\$ 0.25	\$ (5.65)
Net Income (Loss) Per Share -- Diluted			
Net Income (Loss) as reported.....	\$ (0.45)	\$ 0.35	\$ (5.45)
Less: Compensation expense per SFAS No. 123, net of tax.....	(0.09)	(0.10)	(0.08)
Pro forma Net Income (Loss) per share.....	\$ (0.54)	\$ 0.25	\$ (5.53)

Stock Option Plans -- The effects of applying SFAS No. 123 in the pro forma disclosure may not be indicative of future amounts as additional option awards in future years are anticipated. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2000	2001	2002
Expected dividend yield.....	0.00%	0.00%	0.00%
Expected stock price volatility.....	52.42%	75.46%	64.87%
Risk free interest rate.....	5.58%-6.94%	4.92%-5.61%	4.07%-5.51%
Expected life of options.....	7-10 years	10 years	10 years

Employee Stock Purchase Plan -- Compensation cost associated with the stock purchase plan is recognized for the fair value of the employees' purchase rights, which is estimated using the Black-Scholes model with the following assumptions:

	2000	2001
Expected dividend yield.....	0.00%	0.00%
Expected volatility.....	76.24%	105.90%
Risk free interest rate.....	6.00%-6.30%	4.85%
Expected life of purchase rights.....	0.5 years	0.5 years

The weighted average fair values of the purchase rights granted in 2000 and 2001 were \$1.65 per share and \$0.88 per share, respectively. No purchase rights were granted in 2002.

RECLASSIFICATIONS

Certain reclassifications have been made in prior period financial statements to conform to current period presentation. These reclassifications have not resulted in any changes to previously reported net income for any periods.

3. DISCONTINUED OPERATIONS

On March 1, 2002, the Company sold 19 operations to Emcor Group, Inc. ("Emcor"). The total purchase price was \$186.25 million, including the assumption by Emcor of approximately \$22.1 million of subordinated notes to former owners of certain of the divested companies.

The transaction with Emcor provided for a post-closing adjustment based on a final accounting, done after the closing of the transaction, of the net assets of the operations that were sold to Emcor. That accounting indicated that the net assets transferred to Emcor were approximately \$7 million greater than a target amount that had been agreed to with Emcor. In the second quarter of 2002, Emcor paid the Company that amount, and released \$2.5 million that had been escrowed in connection with this element of the transaction.

Of Emcor's purchase price, \$5 million was deposited into an escrow account to secure potential obligations on the Company's part to indemnify Emcor for future claims and contingencies arising from events and circumstances prior to closing, all as specified in the transaction documents. Of this escrow, \$4 million has been applied in determining the Company's liability to Emcor in connection with the settlement of certain claims as described subsequently in this section. The remaining \$1 million of escrow is available for book purposes to apply to any future claims and contingencies in connection with this transaction, and has not been recognized as part of the Emcor transaction purchase price.

The net cash proceeds of approximately \$164 million received to date from the Emcor transaction have been used to reduce the Company's debt. The Company paid \$7.3 million of federal taxes related to this transaction in March 2003.

In the fourth quarter of 2002, the Company recognized a charge of \$1.2 million, net of tax benefits of \$2.7 million, in "Estimated loss on disposition, including income tax" in the Company's statement of operations in connection with the Emcor transaction. This charge primarily relates to a preliminary agreement to settle claims from Emcor for reimbursement of impaired assets and additional liabilities associated with the operations acquired from the Company. Under this settlement, the Company also agreed to partially reimburse Emcor for any loss on the eventual resolution of certain claims involving a project at one of the operations Emcor acquired from the Company, and the Company was released from liability on all other outstanding receivables and issues relating to the profitability of projects that were in process at the time Emcor acquired these operations. The settlement agreement also includes the use of \$2.5 million of the \$5 million escrow described above to fund settled claims. The Company further estimated that an additional \$1.5 million of the remaining escrow would be applied against elements of the settlement that will not be fully resolved until a later date, principally the one open project referred to above. Accordingly, for book purposes, \$1.0 million of escrow remains available to apply against future claims that may arise from Emcor in connection with this transaction. The Company recorded a tax benefit of \$1.4 million related to this additional charge. In addition, the \$1.2 million charge recognized during the fourth quarter is also net of a tax credit of \$1.3 million as a result of lower final tax liabilities in connection with the overall Emcor transaction than we originally estimated in the first quarter.

Under SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which took effect for the Company on January 1, 2002, the operating results of the companies sold to Emcor for all periods presented through the sale, as well as the loss on the sale of these operations, have been presented as discontinued operations in the Company's statements of operations. The Company realized a total loss of \$11.8 million, including related tax expense, in connection with the sale of these operations. As a result of the adoption of SFAS No. 142, "Goodwill and Other Intangible Assets," the Company also recognized a goodwill impairment charge related to these operations of \$32.4 million, net of taxes, as of January 1, 2002. The reporting of the Company's aggregate initial goodwill impairment charge in connection with adopting SFAS No. 142 is discussed further in Note 4.

In March 2002, the Company also decided to divest of an additional operating company. In the first quarter of 2002, the Company recorded an estimated loss of \$0.6 million from this planned disposition in "Estimated loss on disposition, including income tax" in the Company's statement of operations. In the fourth quarter of 2002, the Company reversed this estimated loss because the Company decided not to sell this unit.

During the second quarter of 2002, the Company sold a division of one of

its operations. The operating loss for this division for the first two quarters of 2002 of \$0.3 million, net of taxes, has been reported in discontinued operations under "Operating income (loss), net of applicable income taxes" in the Company's statement of operations. The Company realized a loss of \$0.3 million on the sale of this division. This loss is included in "Estimated loss on disposition, including income tax" during the second quarter of 2002 in the Company's statement of operations.

Assets and liabilities related to discontinued operations were as follows (in thousands):

	DECEMBER 31, 2001 -----
Accounts receivable, net.....	\$140,061
Other current assets.....	29,802
Property and equipment, net.....	13,824
Goodwill, net.....	141,197
Other noncurrent assets.....	1,192

Total assets.....	\$326,076
	=====
Current maturities of debt and notes.....	\$ 1,262
Accounts payable.....	43,847
Other current liabilities.....	68,634
Long-term debt and notes.....	21,842
Other long-term liabilities.....	4,889

Total liabilities.....	\$140,474
	=====

Revenues and pre-tax income (loss) related to discontinued operations were as follows (in thousands):

	YEAR ENDED DECEMBER 31, -----		
	2000	2001	2002
	-----	-----	-----
Revenues.....	\$688,777	\$663,421	\$96,039
Pre-tax income (loss).....	\$ 22,022	\$ 23,784	\$(1,916)

Interest expense allocated to the discontinued operations in 2000, 2001 and 2002 was \$15.5 million, \$13.8 million and \$1.5 million, respectively. These amounts have been allocated based upon the Company's net investment in these operations.

4. GOODWILL

Effective January 1, 2002, the Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 requires companies to assess goodwill asset amounts for impairment each year, and more frequently if circumstances suggest an impairment may have occurred. In addition to discontinuing the regular charge, or amortization, of goodwill against income, the new standard also introduces more rigorous criteria for determining how much goodwill should be reflected as an asset in a company's balance sheet.

To perform the transitional impairment testing required by SFAS No. 142 under its new, more rigorous impairment criteria, the Company broke its operations into "reporting units," as prescribed by the new

standard, and tested each of these reporting units for impairment by comparing the unit's fair value to its carrying value. The fair value of each reporting unit was estimated using a discounted cash flow model combined with market valuation approaches. Significant estimates and assumptions were used in assessing the fair value of reporting units. These estimates and assumptions involved future cash flows, growth rates, discount rates, weighted average cost of capital and estimates of market valuations for each of the reporting units.

As provided by SFAS No. 142, the transitional impairment loss identified by applying the standard's new, more rigorous valuation methodology upon initial adoption of the standard was reflected as a cumulative effect of a change in accounting principle in the Company's statement of operations. The resulting non-cash charge was \$202.5 million, net of taxes. Impairment charges recognized after the initial adoption, if any, generally are to be reported as a component of operating income. An additional impairment charge of \$0.2 million was recorded during the fourth quarter of 2002.

The changes in the carrying amount of goodwill for the year ended December 31, 2002 are as follows (in thousands):

Goodwill balance as of January 1, 2002(a).....	\$ 438,448
Impairment adjustments.....	(229,056)
Goodwill related to sale of operations.....	(95,965)

Goodwill balance as of December 31, 2002.....	\$ 113,427
	=====

(a) A portion of this goodwill balance is included in assets related to discontinued operations in the Company's consolidated balance sheet.

The unaudited results of operations presented below (in thousands) for the years ended December 31, 2000, 2001 and 2002 reflect the adoption of the non-amortization provisions of SFAS No. 142 effective January 1, 2000 and exclude the impact of the cumulative effect of change in accounting principle recorded in the first quarter of 2002. Therefore, the component of the cumulative effect of change in accounting principle related to the operations sold to Emcor is included in the estimated loss on disposition for purposes of this table.

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002
	-----	-----	-----
Income (loss) from continuing operations.....	\$ (29,898)	\$ (1,033)	\$ 5,479
Add: Goodwill amortization, net of tax.....	8,069	7,622	--
	-----	-----	-----
Adjusted income (loss) from continuing operations.....	(21,829)	6,589	5,479
Discontinued operations --			
Operating income (loss), net of tax.....	13,045	14,157	(36)
Add: Goodwill amortization, net of tax.....	3,026	2,987	--
	-----	-----	-----
Adjusted operating income (loss), net of tax.....	16,071	17,144	(36)
Estimated loss on disposition, including tax.....	--	--	(45,776)
	-----	-----	-----
Adjusted net income (loss).....	\$ (5,758)	\$23,733	\$ (40,333)
	=====	=====	=====

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002
Adjusted income (loss) per share:			
Basic --			
Income (loss) from continuing operations.....	\$ (0.58)	\$ 0.18	\$ 0.15
Discontinued operations --			
Income (loss) from operations.....	0.43	0.45	--
Estimated loss on disposition.....	--	--	(1.22)
Net income (loss).....	\$ (0.15)	\$ 0.63	\$ (1.07)
Diluted --			
Income (loss) from continuing operations.....	\$ (0.58)	\$ 0.18	\$ 0.14
Discontinued operations --			
Income (loss) from operations.....	0.43	0.45	--
Estimated loss on disposition.....	--	--	(1.19)
Net income (loss).....	\$ (0.15)	\$ 0.63	\$ (1.05)

5. RESTRUCTURING CHARGES

During the first quarter of 2002, the Company recorded restructuring charges of approximately \$1.9 million. These charges included approximately \$0.8 million for severance costs primarily associated with the reduction in corporate overhead in light of the Company's smaller size following the Emcor transaction. The severance costs related to the termination of 33 employees, all of whom were terminated as of March 31, 2002. In addition, these charges include approximately \$0.7 million for costs associated with decisions to merge or close three smaller divisions and realign regional operating management. These restructuring charges are primarily cash obligations but did include approximately \$0.3 million of non-cash writedowns associated with long-lived assets.

During the first quarter of 2001, the Company recorded restructuring charges of approximately \$0.2 million, primarily related to contractual severance obligations of two operating presidents in connection with the Company's significant restructuring program in the second half of 2000. These restructuring charges are net of a gain of approximately \$0.1 million related to management's decision to sell a small operation during the first quarter of 2001.

During the second half of 2000, the Company recorded restructuring charges of approximately \$25.3 million primarily associated with restructuring efforts at certain underperforming operations and its decision to cease its e-commerce activities at Outbound Services, a subsidiary of the Company. Management performed an extensive review of its operations during the second half of 2000 and as part of this review management decided to cease operating at three locations, sell five operations (including two smaller satellite operations), and merge two companies into other operations. The restructuring charges were primarily non-cash and included goodwill impairments of approximately \$11.5 million and the writedown of other long-lived assets of approximately \$8.5 million. The remaining items in these restructuring charges primarily included severance and lease termination costs.

During the third quarter of 2001, the Company decided to retain one of the operations that was previously held for sale and reversed approximately \$0.3 million of non-cash charges related to the anticipated loss on the sale of this operation. This amount was offset by an additional loss on the sale in late September 2001 of the final operation that was identified as part of this restructuring program. The losses associated with the other operations that were sold were consistent with the amounts recorded as restructuring charges in 2000.

Severance costs recorded in 2000 and 2001 relate to the termination of 147 employees (all of whom had been terminated by June 30, 2001) including certain corporate personnel and the management and employees of certain underperforming locations, and to the departure of the Company's former chief executive officer.

Aggregated financial information for 2000 and 2001 related to the operations addressed by the 2000 and 2001 restructuring charges is as follows (in thousands):

	YEAR ENDED DECEMBER 31,	
	2000	2001
Revenues.....	\$ 48,010	\$ 6,337
Operating loss.....	\$ (17,173)	\$ (2,666)

The following table shows the remaining liabilities associated with the cash portion of the restructuring charges as of December 31, 2000, 2001 and 2002 (in thousands):

	BALANCE AT BEGINNING OF PERIOD	ADDITIONS	PAYMENTS	BALANCE AT END OF PERIOD
Year Ended December 31, 2000:				
Severance.....	\$ --	\$2,487	\$ (1,269)	\$1,218
Lease termination costs and other.....	--	2,920	(608)	2,312
Total.....	\$ --	\$5,407	\$ (1,877)	\$3,530
Year Ended December 31, 2001:				
Severance.....	\$1,218	\$ 350	\$ (1,358)	\$ 210
Lease termination costs and other.....	2,312	--	(1,164)	1,148
Total.....	\$3,530	\$ 350	\$ (2,522)	\$1,358
Year Ended December 31, 2002:				
Severance.....	\$ 210	\$ 846	\$ (1,056)	\$ --
Lease termination costs and other.....	1,148	704	(852)	1,000
Total.....	\$1,358	\$1,550	\$ (1,908)	\$1,000

6. REDUCTIONS IN NON-OPERATING ASSETS AND LIABILITIES, NET

During 2000, the Company recorded a non-cash charge of approximately \$1.1 million primarily related to the impairment of certain non-operating assets. This charge principally included an impairment of approximately \$1.4 million to the Company's minority investment in two entities associated with the distribution and implementation of high-end engineering and design software. These entities have ceased operations. This charge also included an impairment of approximately \$0.3 million related to notes receivable from former owners of businesses acquired by the Company. Offsetting these items was a gain of approximately \$0.6 million on the reduction of the Company's subordinated note payable to a former owner in connection with the settlement of claims with this former owner.

7. PROPERTY AND EQUIPMENT

Property and equipment consist of the following (dollars in thousands):

	USEFUL LIVES IN YEARS	-----	
		2001	2002
	-----	-----	-----
Land.....	N/A	\$ 60	\$ --
Transportation equipment.....	3-7	17,790	15,094
Machinery and equipment.....	3-10	16,391	16,443
Computer and telephone equipment.....	3-7	14,292	14,989
Buildings and leasehold improvements.....	3-40	7,884	8,050
Furniture and fixtures.....	3-10	5,672	5,971
		-----	-----
		62,089	60,547
Less -- Accumulated depreciation.....		(43,133)	(44,436)
		-----	-----
Property and equipment, net.....		\$ 18,956	\$ 16,111
		=====	=====

Depreciation expense for the years ended December 31, 2000, 2001 and 2002 was \$8.1 million, \$8.0 million and \$6.4 million, respectively.

8. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS

Activity in the Company's allowance for doubtful accounts consists of the following (in thousands):

	DECEMBER 31,		
	2000	2001	2002
	-----	-----	-----
Balance at beginning of year.....	\$ 3,735	\$ 4,262	\$ 9,645
Additions for bad debt expense.....	3,612	7,632	2,088
Deductions for uncollectible receivables written off, net of recoveries.....	(2,875)	(2,249)	(5,685)
Allowance for doubtful accounts of businesses sold or held for sale.....	(210)	--	--
	-----	-----	-----
Balance at end of year.....	\$ 4,262	\$ 9,645	\$ 6,048
	=====	=====	=====

Other current liabilities consist of the following (in thousands):

	DECEMBER 31,	
	2001	2002
	-----	-----
Accrued warranty costs.....	\$ 2,697	\$ 2,274
Accrued insurance expense.....	11,615	11,838
Accrued interest.....	1,446	213
Liabilities associated with discontinued operations.....	--	8,600
Other current liabilities.....	7,737	6,876
	-----	-----
	\$23,495	\$29,801
	=====	=====

Contracts in progress are as follows (in thousands):

	2001	2002
	-----	-----
Costs incurred on contracts in progress.....	\$ 472,849	\$ 463,684
Estimated earnings, net of losses.....	116,134	113,952
Less -- Billings to date.....	(596,233)	(586,344)
	-----	-----
	\$ (7,250)	\$ (8,708)
	=====	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 19,413	\$ 17,964
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(26,663)	(26,672)
	-----	-----
	\$ (7,250)	\$ (8,708)
	=====	=====

Other long-term liabilities consist of the following (in thousands):

	2001	2002
	-----	-----
Warrant and put obligation.....	\$ --	\$3,177
Deferred income taxes.....	2,925	--
Other long-term liabilities.....	268	15
	-----	-----
	\$3,193	\$3,192
	=====	=====

9. LONG-TERM DEBT OBLIGATIONS

Long-term debt obligations consist of the following (in thousands):

	DECEMBER 31,	
	2001	2002
	-----	-----
Revolving credit facility.....	\$163,700	\$ 107
Term loan.....	--	14,625
Notes to affiliates and former owners.....	17,943	--
Other.....	385	502
	-----	-----
Total debt.....	182,028	15,234
Less -- current maturities.....	(2,447)	(1,780)
	-----	-----
Total long-term portion of debt.....	179,581	13,454
Less -- discount on Facility.....	--	(2,850)
	-----	-----
Long-term portion of debt, net of discount.....	\$179,581	\$10,604
	=====	=====

At December 31, 2002, future principal payments of long-term debt are as follows (in thousands):

Year Ending December 31 --	
2003.....	\$ 1,780
2004.....	2,550

2005.....	3,351
2006.....	3,996
2007.....	3,433
Thereafter.....	124

	\$15,234
	=====

CREDIT FACILITY

The Company's primary current debt financing capacity consists of a \$55 million senior credit facility (the "Facility") provided by a syndicate of three financial institutions led by General Electric Capital Corporation ("GE"). The Facility includes a \$20 million sublimit for letters of credit. The Facility is secured by substantially all the assets of the Company. The Facility was entered into on October 11, 2002 and replaces the Company's previous revolving credit facility. The Facility consists of two parts: a term loan and a revolving credit facility.

The term loan under the Facility (the "Term Loan") is \$15 million, which the Company borrowed upon the closing of Facility on October 11, 2002. The Term Loan must be repaid in quarterly installments over five years beginning December 31, 2002. The amount of each quarterly installment increases annually.

The Facility requires certain prepayments of the Term Loan. Approximately half of any free cash flow (primarily cash from operations less capital expenditures) in excess of scheduled principal payments and voluntary prepayments must be used to pay down the Term Loan. This requirement is measured annually based on full-year results. We do not have any prepayments of the Term Loan due as of December 31, 2002 under this requirement primarily as a result of the significant amount of voluntary prepayments of debt made by the Company during 2002. In addition, proceeds in excess of \$250,000 from any individual asset sales, or in excess of \$1 million for a full year's asset sales, must be used to pay down the Term Loan. Proceeds from asset sales that are less than these individual transaction or annual aggregate levels must also be used to pay down the Term Loan unless they are reinvested in long-term assets within six months of the receipt of such proceeds.

All prepayments under the Term Loan, whether required or voluntary, are applied to scheduled principal payments in inverse order, i.e. to the last scheduled principal payment first, followed by the second-to-last, etc. All principal payments under the Term Loan permanently reduce the original \$15 million capacity under this portion of the Facility.

The Facility also includes a three-year \$40 million revolving credit facility (the "Revolving Loan"). Under this revolving credit facility, through July 31, 2003, the Company can borrow up to \$25 million, with the difference between actual borrowings and \$40 million available for letter of credit issuance up to a maximum of \$20 million in letters of credit. After July 31, 2003, the Company can borrow up to \$20 million under the revolving credit facility, with a maximum of \$20 million available for letters of credit.

The Company has reached a preliminary agreement with its surety and GE to grant the surety a secured interest in assets such as receivables, costs incurred in excess of billings, and equipment related to projects for which bonds are outstanding as collateral for potential obligations under bonds. As of December 31, 2002 the amount of these assets is approximately \$41.9 million. The Company has also posted a \$5 million letter of credit as collateral for potential obligations under bonds.

INTEREST RATES AND FEES

The Company has a choice of two interest rate options for borrowings under the Facility. Under one option, the interest rate is determined based on the higher of the Federal Funds Rate plus 0.5% or the prime rate of at least 75% of the US's 30 largest banks, as published each business day by the Wall Street Journal. An additional margin of 2.25% is then added to the higher of these two rates for borrowings under the Revolving Loan, while an additional margin of

2.75% is added to the higher of these two rates for borrowings under the Term Loan.

Under the other interest rate option, borrowings bear interest based on designated rates that are described in various general business media sources as the London Interbank Offered Rate or "LIBOR." Revolving Loan borrowings using this interest rate option then have 3.25% added to LIBOR, while Term Loan borrowings have 3.75% added to LIBOR.

The rates underlying these interest rate options are floating interest rates determined by the broad financial markets, meaning they can and do move up and down from time to time. The Facility required that the Company convert these floating interest rate terms on at least half of the Term Loan to fixed rates for at least a one-year term. In January 2003, the Company converted \$10 million of principal value to a fixed LIBOR-based interest rate of 5.62% for an eighteen-month term. This was done via a swap transaction under which the Company agreed to pay fixed interest rate payments on \$10 million for eighteen months to a bank in exchange for receiving from the bank floating LIBOR interest rate payments on \$10 million for the same term. This transaction is a derivative and qualifies for hedge accounting treatment. As such, interest expense related to the hedged portion of this debt will be recorded at the fixed rate of 5.62% in the Company's statement of operations. Changes in market interest rates in any given period may increase or decrease the market valuation of the Company's obligations to the bank under this swap versus the bank's obligations to the Company. Such changes in market valuation will be reflected in stockholders' equity as other comprehensive income (loss) for that period, even though these obligations may not have been terminated and settled in cash during the period. Such adjustments are known as mark-to-market adjustments.

Commitment fees of 0.5% per annum are payable on the unused portion of the Revolving Loan.

The Company also incurred certain financing and professional costs in connection with the arrangement and the closing of the Facility. These costs will be amortized to interest expense over the term of the Facility in the amount of approximately \$0.4 million per quarter. To the extent prepayments of the Term Loan are made, the Company may have to accelerate amortization of these deferred financing and professional costs. Additionally, the Company expects to charge approximately \$0.5 million of deferred financing costs to interest expense in the first quarter of 2003 that were associated with higher levels of capacity under the Facility than the current total of \$55 million.

In connection with the Facility, the Company granted GE a warrant to purchase 409,051 shares of Company common stock for nominal consideration. In addition, GE may "put," or require the Company to repurchase, these shares at the higher of market price, appraised price or book value per share, during the fifth and final year of the Facility -- October 11, 2006 to October 11, 2007. This put may be accelerated under certain circumstances including a change of control of the Company, full repayment of amounts owing under the Facility, or a public offering of shares by the Company. This warrant and put are discussed in greater detail in Note 13, "Stockholders' Equity." The value of this warrant and put as of the start of the Facility of \$2.9 million is reflected as a discount of the Company's obligation under the Facility and is being amortized over the term of the Facility, as described above. This warrant and put obligation is also recorded as a liability in the Company's balance sheet. The value of this warrant and put will change over time, principally in response to changes in the market price of the Company's common stock. The warrant and the put qualify as a derivative for financial reporting purposes. Accordingly, such changes in the value of the warrant and put in any given period will be reflected in interest expense for that period, even though the warrant and put may not

have been terminated and settled in cash during the period. Such adjustments are known as mark-to-market adjustments. The after-tax loss related to the warrant's mark-to-market obligation in 2002 was \$0.1 million.

The weighted average interest rate that the Company currently pays on borrowings under the Facility is 5.6% per annum. This reflects a combination of borrowings under both interest rate options described above, as well as the swap of floating rates to a fixed rate described above. This rate does not include

amortization of debt financing and arrangement costs, or mark-to-market adjustments for derivatives.

RESTRICTIONS AND COVENANTS

Borrowings under the Facility are specifically limited by the Company's ratio of total debt to earnings before interest, taxes, depreciation, and amortization ("EBITDA") and by the Company's ratio of EBITDA less taxes and capital expenditures to interest expense and scheduled principal payments, also known as the fixed charge coverage ratio. The Facility's definition of debt for purposes of the ratio of total debt to EBITDA includes aggregate letters of credit outstanding less \$10 million.

The definition of EBITDA under the Facility excludes certain items, generally non-cash amounts and transactions reported in Other Income and Expense, that are otherwise included in the determination of earnings under generally accepted accounting principles in the Company's financial statements. As such, EBITDA as determined under the Facility's definition could be less than EBITDA as derived from the Company's financial statements in the future.

The financial covenants under the Facility are summarized below. Covenant compliance is measured on a monthly basis. Intra-quarter monthly covenants are at either the same or very similar levels to the quarter-end covenants shown below. EBITDA amounts are in thousands.

FOR THE QUARTER ENDING	FINANCIAL COVENANTS			
	MINIMUM TRAILING 12 MONTHS EBITDA	MAXIMUM DEBT TO EBITDA	MINIMUM FIXED CHARGE COVERAGE RATIO	MINIMUM INTEREST COVERAGE
ACTUAL				
December 31, 2002.....	\$23,639	0.64	4.04	7.17
COVENANT				
March 31, 2003.....	\$19,190	1.75	2.50	3.00
June 30, 2003.....	\$16,420	2.20	2.50	3.00
September 30, 2003.....	\$17,840	2.10	2.60	3.00
December 31, 2003.....	\$23,565	1.50	2.70	3.00
March 31, 2004.....	\$29,000	1.50	3.00	3.00
June 30, 2004.....	\$29,000	1.50	3.00	3.00
September 30, 2004.....	\$29,000	1.25	3.00	3.00
December 31, 2004.....	\$29,000	1.25	3.00	3.00
All quarters thereafter.....	\$31,000	1.25	3.00	3.00

The Company's trailing twelve months EBITDA as of December 31, 2002 as determined under the Facility did not comply with the covenant. Our lenders waived this violation. In addition, based on expectations of lower operating results at least through the first quarter of 2003, the Company's lenders agreed to modify the minimum EBITDA, leverage and fixed charge covenants for 2003. Even at these modified levels, these covenants leave only moderate room for variance based on the Company's recent performance. If the Company again violates a covenant under the Facility, the Company may have to negotiate new borrowing terms under the Facility or obtain new financing. While the Company believes that its levels of debt in

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

comparison to its EBITDA and its cash flows would enable the Company to negotiate new borrowing terms under the Facility or to obtain new financing from other sources if necessary, there can be no assurance that the Company would be successful in doing so.

The Facility prohibits payment of dividends and the repurchase of shares by the Company, limits annual lease expense and non-Facility debt, and restricts outlays of cash by the Company relating to certain investments, acquisitions and subordinate debt.

NOTES TO AFFILIATES AND FORMER OWNERS

Subordinated notes were issued to former owners of certain purchased companies as part of the consideration used to acquire their companies. As of December 31, 2002, these notes had been paid off. A gain of approximately \$0.7 million was recognized in 2002 related to agreements with former owners for early repayment of certain of these notes, or other settlement of claims.

AMOUNTS OUTSTANDING AND CAPACITY

The following recaps the Company's debt amounts outstanding and capacity (in thousands):

	AS OF DEC. 31, 2002	AS OF MARCH 25, 2003	UNUSED CAPACITY AS OF MARCH 25, 2003
	-----	-----	-----
Revolving loan.....	\$ 107	\$12,975	\$8,055 (a)
Term loan.....	14,625	14,625	n/a
Other debt.....	502	495	n/a
	-----	-----	-----
Total debt.....	15,234	28,095	8,055
Less: discount on Facility.....	(2,850)	(2,750)	n/a
	-----	-----	-----
Total debt, net of discount.....	\$12,384	\$25,345	\$8,055
	=====	=====	=====
Letters of credit.....	\$ 9,800	\$12,844	\$7,156 (b)

(a) This amount reflects combined revolving loan capacity and letter of credit capacity and therefore includes letter of credit capacity shown above of \$7,156.

(b) This amount is included in revolving loan capacity of \$8,055 shown above.

The increase in the Company's borrowings outstanding under the revolving loan during the first quarter of 2003 primarily results from the payment of a \$7.3 million tax liability relating to the Emcor transaction that was due in March 2003.

OTHER LONG-TERM OBLIGATIONS DISCLOSURES

The Company estimates the fair value of long-term debt as of December 31, 2001 and 2002 to be approximately the same as the recorded value.

The Company has generated positive operating cash flow in most recent periods, and it currently has a moderate level of debt. The Company anticipates that cash flow from operations and borrowing capacity under the Facility will provide the Company with sufficient liquidity to fund its operations for the foreseeable future. However, the Company does not have a significant amount of excess borrowing capacity in comparison to expected working capital requirements over the balance of 2003. The Company believes that its levels of debt in comparison to its EBITDA and its cash flows would enable it to obtain new financing if necessary, but there can be no assurance that it would be successful in doing so.

Some customers require the Company to post letters of credit to guarantee performance under its contracts and to ensure payment to its subcontractors and vendors under those contracts. Certain of the Company's vendors also require letters of credit to ensure reimbursement for amounts they are disbursing on the Company's behalf, such as to beneficiaries under its self-funded insurance program. Such letters of credit are generally issued by a bank or similar financial institution. The letter of credit commits the issuer to pay specified amounts to the holder of the letter of credit if the holder demonstrates that the Company has failed to perform specified actions. If this were to occur, the Company would be required to reimburse the issuer of the letter of credit.

Depending on the circumstances of such a reimbursement, the Company may also have to record a charge to earnings for the reimbursement. To date the Company has not had a claim made against a letter of credit that resulted in payments by the issuer of the letter of credit or by the Company. The Company believes that it is unlikely that it will have to fund claims under a letter of credit in the foreseeable future.

The Company currently has \$12.8 million in letters of credit outstanding. The Company self-insures a significant portion of its worker's compensation, auto liability and general liability risks. The Company uses third parties to manage this self-insurance and to retain some of these risks. As is customary under such arrangements, these third parties can require letters of credit as security for amounts they fund or risks they might potentially absorb on the Company's behalf. Under its current self-insurance arrangements, the Company expects that it will be required to post approximately \$3.0 million per quarter during the first three quarters of 2003. In addition, the Company may receive other letter of credit requests in the ordinary course of business, and it may have a net increase in the amount of insurance-related letters of credit it must post when it renews its insurance arrangements in the fourth quarter of next year. Accordingly, the Company's letter of credit requirements over the next year may exceed the current letter of credit sublimit of \$20 million under the Company's credit facility. If so, the Company may have to seek additional letter of credit capacity or post different forms of security such as bonds or cash in lieu of letters of credit. The Company believes that its levels of debt in comparison to its EBITDA and its cash flows would enable it to obtain additional letter of credit capacity or to otherwise meet financial security requirements of third parties if necessary, but there can be no assurance that the Company would be successful in doing so.

As described above, the Company must comply with a number of financial covenants in connection with the Facility. The Company's trailing twelve months EBITDA as of December 31, 2002 as determined under the Facility did not comply with covenant. The Company's lenders waived this violation. In addition, based on expectations of lower operating results at least through the first quarter of 2003, the Company's lenders agreed to modify the minimum EBITDA, leverage and fixed charge covenants for 2003. Even at these modified levels, these covenants leave only moderate room for variance based on the Company's recent performance. If the Company again violates a covenant under the Facility, the Company may have to negotiate new borrowing terms under the Facility or obtain new financing. While the Company believes that its levels of debt in comparison to its EBITDA and its cash flows would enable the Company to negotiate new borrowing terms under the Facility or to obtain new financing from other sources if necessary, there can be no assurance that the Company would be successful in doing so.

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

10. INCOME TAXES

The provision for income taxes consists of the following (in thousands):

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002
	-----	-----	-----
Current --			
Federal.....	\$(2,173)	\$ 6,826	\$ 290
State and Puerto Rico.....	2,246	2,299	948
	-----	-----	-----
	73	9,125	1,238
	-----	-----	-----
Deferred --			
Federal.....	(3,588)	(2,000)	2,884
State and Puerto Rico.....	323	(220)	781
	-----	-----	-----
	(3,265)	(2,220)	3,665
	-----	-----	-----
	\$(3,192)	\$ 6,905	\$4,903
	=====	=====	=====

The difference in income taxes provided for and the amounts determined by applying the federal statutory tax rate to income before income taxes results from the following (in thousands):

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002
Income tax expense (benefit) at the statutory rate.....	\$ (11,582)	\$2,055	\$3,634
Increase resulting from --			
State income taxes, net of federal tax effect.....	1,119	1,605	1,123
Non-deductible goodwill amortization.....	2,267	2,238	--
Non-deductible goodwill writeoffs related to			
restructuring.....	4,300	--	--
Non-deductible expenses.....	701	987	146
Other.....	3	20	--
	=====	=====	=====
	\$ (3,192)	\$6,905	\$4,903

Deferred income tax provisions result from current period activity that has been reflected in the financial statements but which is not includable in determining the Company's tax liabilities until future periods. Deferred tax assets and liabilities reflect the tax effect in future periods of all such activity to date that has

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

been reflected in the financial statements but which is not includable in determining the Company's tax liabilities until future periods.

	DECEMBER 31,	
	2001	2002
	-----	-----
	(IN THOUSANDS)	
Deferred income tax assets --		
Accounts receivable and allowance for doubtful accounts...	\$ 3,884	\$ 2,226
Goodwill.....	--	9,632
Accrued liabilities and expenses.....	6,092	7,230
Net operating loss.....	2,933	4,055
Other.....	1,663	445
	-----	-----
Total deferred income tax assets.....	14,572	23,588
Deferred income tax liabilities --		
Property and equipment.....	(1,102)	(1,026)
Long-term contracts.....	(1,562)	(1,262)
Goodwill.....	(4,205)	--
Other.....	--	(46)
	-----	-----
Total deferred income tax liabilities.....	(6,869)	(2,334)
Less -- Valuation allowance.....	(1,046)	(2,545)
	-----	-----
Net deferred income tax assets.....	\$ 6,657	\$18,709
	=====	=====

The deferred income tax assets and liabilities reflected above are included in the consolidated balance sheets as follows (in thousands):

	DECEMBER 31,	
	2001	2002
Deferred income tax assets --		
Prepaid expenses and other.....	\$ 9,582	\$ 9,285
Other non-current assets.....	--	9,424
	-----	-----
Total deferred income tax assets.....	9,582	18,709
	-----	-----
Deferred income tax liabilities --		
Other long-term liabilities.....	(2,925)	--
	-----	-----
Net deferred income tax assets.....	\$ 6,657	\$18,709
	=====	=====

At December 31, 2002 the Company had \$4.1 million of available state net operating loss carry forwards for income tax purposes which expire 2013-2022.

At December 31, 2002, the Company's net deferred tax assets are partially offset by a valuation allowance. The Company will continue to assess the valuation allowance and to the extent it is determined that such allowance is no longer required, the tax benefit of the remaining net deferred tax assets will be recognized in the future.

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

11. EMPLOYEE BENEFIT PLANS

The Company and certain of the Company's subsidiaries sponsor various retirement plans for most full-time and some part-time employees. These plans consist of defined contribution plans and multi-employer pension plans and cover employees at substantially all of the Company's operating locations. The defined contribution plans generally provide for contributions up to 2.5% of covered employees' salaries or wages in 2002 and up to 6% of covered employees' salaries or wages in previous periods and totaled \$4.5 million for 2000, \$4.5 million for 2001 and \$3.3 million for 2002. Of these amounts, approximately \$1.8 million and \$0.8 million was payable to the plans at December 31, 2001 and 2002, respectively.

Certain of the Company's subsidiaries also participate in various multi-employer pension plans for the benefit of their employees who are union members. Company contributions to these plans were approximately \$0.3 million for 2000, \$0.2 million for 2001 and \$0.3 million for 2002. The data available from administrators of the multi-employer pension plans is not sufficient to determine the accumulated benefit obligations, nor the net assets attributable to the multi-employer plans in which Company employees participate.

12. COMMITMENTS AND CONTINGENCIES

LEASES

The Company leases certain facilities and equipment under noncancelable operating leases. Rent expense for the years ended December 31, 2000, 2001 and 2002 was \$15.5 million, \$16.2 million and \$16.6 million, respectively. Concurrent with the acquisitions of certain acquired companies, the Company entered into various agreements with previous owners to lease land and buildings used in the Company's operations. The terms of these leases range from three to ten years and provide for certain escalations in the rental expenses each year. Included in the 2000, 2001 and 2002 rent expense above is approximately \$4.5 million, \$5.8 million and \$4.7 million of rent paid to these related parties, respectively. The following represents future minimum rental payments under noncancelable operating leases (in thousands):

2003.....	\$10,265
2004.....	8,260
2005.....	6,041
2006.....	4,789
2007.....	4,202
Thereafter.....	15,425

	\$48,982
	=====

CLAIMS AND LAWSUITS

The Company is party to litigation in the ordinary course of business. The Company has estimated and provided accruals for probable losses and related legal fees associated with certain of these actions in the accompanying consolidated financial statements. There are currently no pending legal proceedings that, in management's opinion, would have a material adverse effect on the Company's operating results or financial condition.

SELF-INSURANCE

The Company retains the risk of worker's compensation, employer's liability, auto liability, general liability and employee group health claims resulting from uninsured deductibles per accident or occurrence. Losses up to the deductible amounts are estimated and accrued based upon known facts, historical trends and

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

industry averages utilizing the assistance of an actuary to determine the best estimate of these obligations. A wholly owned insurance company subsidiary reinsures a portion of the risk associated with surety bonds issued by a third party insurance company. Because no claims have been made against these financial instruments in the past, management does not expect that these instruments will have a material effect on the Company's consolidated financial statements.

SURETY

Many customers, particularly in connection with new construction, require the Company to post performance and payment bonds issued by a financial institution known as a surety. These bonds provide a guarantee to the customer that the Company will perform under the terms of a contract and that the Company will pay subcontractors and vendors. If the Company fails to perform under a contract or to pay subcontractors and vendors, the customer may demand that the surety make payments or provide services under the bond. The Company must reimburse the surety for any expenses or outlays it incurs. To date, the Company has not had any significant reimbursements to its surety for bond-related costs. The Company believes that it is unlikely that it will have to fund claims under its surety arrangements in the foreseeable future.

Surety market conditions are currently difficult as a result of significant losses incurred by many sureties in recent periods, both in the construction industry as well as in certain larger corporate bankruptcies. As a result, less bonding capacity is available in the market and terms have become more restrictive. Further, under standard terms in the surety market, sureties issue bonds on a project by project basis, and can decline to issue bonds at any time. Historically, approximately 25% of the Company's business has required bonds. While the Company has enjoyed a longstanding relationship with its surety, current market conditions as well as changes in the surety's assessment of the Company's operating and financial risk could cause the surety to decline to issue bonds for the Company's work. If that were to occur, the alternatives include doing more business that does not require bonds, posting other forms of collateral for project performance such as letters of credit or cash, and seeking bonding capacity from other sureties. There can be no assurance that the Company could easily achieve these alternatives. Accordingly, if the Company were to experience an interruption in the availability of bonding capacity, the Company's revenues and profits could decline.

13. STOCKHOLDERS' EQUITY

RESTRICTED STOCK GRANT

The Company awarded 200,000 shares of restricted stock to its Chief Executive Officer on March 22, 2002 under its 2000 Equity Incentive Plan. The shares are subject to forfeiture if the Company does not meet certain performance measures for the twelve-month period ending March 31, 2003 or if the executive leaves voluntarily or is terminated for cause. Such forfeiture provisions lapse upon achievement of the performance measures and pro rata over a four-year period.

The Company awarded 75,000 shares of restricted stock to its President on November 1, 2002 under its 2000 Equity Incentive Plan. The shares are subject to forfeiture if the Company does not meet certain performance measures for the twelve-month period ending December 31, 2003 or if the executive leaves voluntarily or is terminated for cause. Such forfeiture provisions lapse upon achievement of the performance measures and pro rata over a four-year period.

Compensation expense relating to the grants will be charged to earnings over the four-year period. The initial value of the award was established based on the market price on the date of grant. The unearned compensation is shown as a reduction of stockholders' equity in the accompanying consolidated balance sheet and is being amortized against earnings based upon the market value of the stock until the achievement of performance measures. The value of the stock grant remaining after this determination will be amortized ratably over the remaining three years of the restricted period.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

TREASURY STOCK

On October 5, 1999, the Company announced that its Board of Directors had approved a share repurchase program authorizing the Company to buy up to 4.0 million shares of its Common Stock. During 1999, the Company purchased approximately 1.8 million shares at a cost of approximately \$12.9 million. During 2000, the Company purchased approximately 0.2 million shares at a cost of approximately \$1.2 million. Under the current terms of the Company's credit facility, the Company is prohibited from purchasing additional shares of its Common Stock.

RESTRICTED COMMON STOCK

In March 1997, Notre Capital Ventures II, L.L.C. ("Notre") exchanged 2,742,912 shares of Common Stock for an equal number of shares of restricted voting common stock ("Restricted Voting Common Stock"). The holders of Restricted Voting Common Stock are entitled to elect one member of the Company's Board of Directors and to 0.55 of one vote for each share on all other matters on which they are entitled to vote. Holders of Restricted Voting Common Stock are not entitled to vote on the election of any other directors.

Each share of Restricted Voting Common Stock will automatically convert to Common Stock on a share-for-share basis (i) in the event of a disposition of such share of Restricted Voting Common Stock by the holder thereof (other than a distribution which is a distribution by a holder to its partners or beneficial owners, or a transfer to a related party of such holders (as defined in Sections 267, 707, 318 and/or 4946 of the Internal Revenue Code of 1986, as amended)), (ii) in the event any person acquires beneficial ownership of 15% or more of the total number of outstanding shares of Common Stock of the Company, or (iii) in the event any person offers to acquire 15% or more of the total number of outstanding shares of Common Stock of the Company. After July 1, 1998, the Board of Directors may elect to convert any remaining shares of Restricted Voting Common Stock into shares of Common Stock in the event 80% or more of the originally outstanding shares of Restricted Voting Common Stock have been previously converted into shares of Common Stock. As of December 31, 2002, there were 1,128,112 shares of Restricted Voting Common Stock remaining.

EARNINGS PER SHARE

Basic earnings per share ("EPS") is computed by dividing net income by the weighted average number of shares of common stock outstanding during the year. Diluted EPS is computed considering the dilutive effect of stock options,

convertible subordinated notes, warrants and contingently issuable restricted stock. Options to purchase 3.2 million shares of Common Stock at prices ranging from \$3.81 to \$21.44 per share were outstanding as of December 31, 2002, but were not included in the computation of diluted EPS because the options' exercise prices were greater than the respective average market price of the Common Stock. Options had an anti-dilutive effect for the years ended December 31, 2000 and 2001 because the Company reported a loss from continuing operations during these periods, and therefore, were not included in the diluted EPS calculation. The Company would have included 175,767 shares related to the dilutive impact of stock options for the year ended December 31, 2000 and 62,688 shares related to the dilutive impact of stock options for the year ended December 31, 2001 if it were not for the loss from continuing operations during each of these periods.

Diluted EPS is also computed by adjusting both net earnings and shares outstanding as if the conversion of the convertible subordinated notes occurred on the first day of the year. The convertible subordinated notes had an anti-dilutive effect during the years ended December 31, 2000 and 2001, and therefore, are not included in the diluted EPS calculation. The convertibility provisions of the remaining convertible subordinated notes expired during the first quarter of 2002. The dilutive impact of the warrants is computed assuming the issuance of shares required to fulfill the warrant obligation at the end of the reporting period. The after-tax

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

loss related to the warrant's mark-to-market adjustment was \$0.1 million in 2002 and this amount is added to net income for purposes of calculating diluted earnings per share. The shares associated with contingently issuable restricted stock are included in diluted earnings per share because it is probable that the performance requirement for the issuance of these shares will be met.

The following table reconciles the number of shares outstanding with the number of shares used in computing basic and diluted earnings per share for each of the periods presented (in thousands):

	YEAR ENDED DECEMBER 31,		
	2000	2001	2002
Common shares outstanding, end of period(a).....	37,256	37,510	37,642
Effect of using weighted average common shares outstanding.....	141	(74)	(37)
Shares used in computing earnings per share -- basic.....	37,397	37,436	37,605
Effect of shares issuable under stock option plans based on the treasury stock method.....	--	--	381
Effect of shares issuable related to warrants.....	--	--	213
Effect of contingently issuable restricted shares.....	--	--	168
Shares used in computing earnings per share -- diluted.....	37,397	37,436	38,367

(a) Excludes 275,000 shares of contingently issuable restricted stock outstanding as of December 31, 2002 (see "Restricted Stock Grant" paragraphs above).

WARRANT

In connection with the arrangement of the Company's new debt facility as described above in Note 9, "Long-Term Debt Obligations," the Company granted GE, its lender, a warrant to purchase 409,051 shares of Company common stock for nominal consideration. The warrant agreement also provides for the following:

- In most situations where the Company issues shares, options or warrants, GE may acquire additional shares or warrants on equivalent terms to maintain the proportionate interest its warrant shares represent in

comparison to the Company's total shares outstanding.

- GE may require the Company to register its warrant shares.
- GE may include its warrant shares in any public offering of stock by the Company.
- GE may "put," or require the Company to repurchase, some or all of its warrant shares at the higher of market price, appraised price or book value per share, during the fifth and final year of the debt facility -- October 11, 2006 to October 11, 2007. This put may be accelerated under certain circumstances including a change of control of the Company, full repayment of amounts owing under the Facility, or a public offering of shares by the Company.

The initial value of this warrant and put of \$2.9 million is reflected as a discount of the Company's obligations under its debt facility with GE, net of amortization of \$0.1 million, and as an obligation in long-term liabilities. The value of this warrant and put will change over time, principally in response to changes in the market price of the Company's common stock. The warrant and the put qualify as a derivative for financial reporting purposes. Accordingly, such changes in the value of the warrant and put in any given period will be reflected in interest expense for that period and in the Company's long-term warrant obligation, even though the warrant and put may not have been terminated and settled in cash during the period. Such adjustments are known as mark-to-market adjustments. The after-tax loss related to the warrant's mark-to-market obligation in 2002 was \$0.1 million.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

14. STOCK OPTION PLANS

LONG-TERM INCENTIVE PLANS

In March 1997, the Company's stockholders approved the Company's 1997 Long-Term Incentive Plan which provides for the granting or awarding of incentive or non-qualified stock options, stock appreciation rights, restricted or deferred stock, dividend equivalents or other incentive awards to directors, officers, key employees and consultants to the Company.

The Company's 1997 Long-Term Incentive Plan provides for the granting of options to key employees to purchase an aggregate of not more than 13% of the total number of shares of the Company's Common Stock outstanding at the time of grant. Such options have been issued by the Company at fair market value on the date of grant and become exercisable in five equal annual installments beginning on the first anniversary of the date of grant. The options expire after seven years from the date of grant if unexercised. Outstanding options may be canceled and reissued under terms specified in the plan.

In May 2000, the Company's stockholders approved the Company's 2000 Incentive Plan which provides for the granting or awarding of incentive or non-qualified stock options, restricted stock or performance awards to directors, officers, key employees and other persons or entities as approved by the Board of Directors. Options granted under this plan have been issued by the Company at fair market value on the date of grant and become exercisable in four equal annual installments beginning on the first anniversary of the date of grant. The options expire after ten years from the date of grant if unexercised.

NON-EMPLOYEE DIRECTORS' STOCK PLAN

In March 1997, the Company's stockholders approved the 1997 Non-Employee Directors' Stock Plan (the "Directors' Plan"), which provides for the granting or awarding of stock options and stock appreciation rights to non-employees. The number of shares authorized and reserved for issuance under the Directors' Plan is 500,000 shares. The Directors' Plan provided for the automatic grant of options to purchase 10,000 shares to each non-employee director serving at the commencement of the initial public offering of the Company.

Each non-employee director will be granted options to purchase 10,000 shares at the time of the initial election. In addition, each non-employee director is automatically granted options to purchase an additional 10,000

shares at each annual meeting of the stockholders that is more than two months after the date of the director's initial election. All options are granted with an exercise price equal to the fair market value at the date of grant and are immediately vested upon grant.

Either at the time of the initial public offering or upon election as a director, options were granted to six members of the board of directors to purchase in each case 10,000 shares of Common Stock at the initial public offering price or at the price in effect at the time of their election. Each of these directors received options for shares on the dates of the annual meetings which they have attended. In addition, directors who cease to be employees become eligible for the annual grant. One former employee received an annual grant in 2000. These options will expire at the earlier of 10 years from the date of grant or one year after termination of service as a director. As of December 31, 2002, 130,000 options were outstanding related to this plan.

The Directors' Plan allows non-employee directors to receive shares ("Deferred Shares") at future settlement dates in lieu of cash. The number of Deferred Shares will have an aggregate fair market value equal to the fees payable to the directors. No Deferred Shares have been issued as of December 31, 2002.

The Company has never altered the price of any option after its grant.

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

The following table summarizes activity under the Company's stock option plans:

FIXED OPTIONS	2000		2001		2002	
	SHARES	WEIGHTED-AVERAGE EXERCISE PRICE	SHARES	WEIGHTED-AVERAGE EXERCISE PRICE	SHARES	WEIGHTED-AVERAGE EXERCISE PRICE
Outstanding at beginning of year.....	4,557,133	\$15.18	7,356,159	\$ 9.35	7,158,722	\$8.59
Granted.....	3,692,000	\$ 3.29	585,000	\$ 2.34	229,000	\$3.79
Exercised.....	--	\$ --	--	\$ --	(242,146)	\$2.88
Forfeited.....	(892,974)	\$13.95	(782,437)	\$10.94	(1,627,275)	\$9.90
Expired.....	--	\$ --	--	\$ --	--	\$ --
Outstanding at end of year.....	<u>7,356,159</u>	<u>\$ 9.35</u>	<u>7,158,722</u>	<u>\$ 8.59</u>	<u>5,518,301</u>	<u>\$8.26</u>
Options exercisable at year-end.....	1,838,099		3,044,485		3,579,155	
Weighted-average fair value of options granted during the year.....	\$ 2.46		\$ 1.93		\$ 2.90	

The following table summarizes information about fixed stock options outstanding at December 31, 2002:

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	NUMBER OUTSTANDING AT 12/31/02	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED-AVERAGE EXERCISE PRICE	NUMBER AT 12/31/02	WEIGHTED-AVERAGE EXERCISE PRICE
\$2.14 - 7.625.....	3,184,958	7.76 years	\$ 3.27	1,501,271	\$ 3.36
\$11.75 - 16.875.....	1,764,018	1.92 years	\$13.64	1,603,074	\$13.53
\$17.875 - 21.438.....	569,325	2.39 years	\$19.50	474,810	\$19.44
\$2.14 - 21.438.....	<u>5,518,301</u>	5.34 years	\$ 8.26	<u>3,579,155</u>	\$10.05

In September 1997, the Company's stockholders approved the Company's 1998 Employee Stock Purchase Plan which allows employees to purchase shares from the Company's authorized but unissued shares of Common Stock or from shares of Common Stock reacquired by the Company, including shares repurchased on the open market.

The Company's 1998 Employee Stock Purchase Plan originally provided for the purchase of up to 300,000 shares, which was increased by an additional 600,000 shares in May 2000, at semi-annual intervals. In March 2001, after all of the shares were distributed, the Board of Directors of the Company voted to suspend the Employee Stock Purchase Plan indefinitely. Through the suspension date, full-time employees were eligible to purchase shares with payroll deductions ranging from 2% to 8% of compensation with a maximum deduction of \$2,000 for any purchase period for each participant. The purchase price per share is 85% of the lower of the market price on the first business day of the purchase period or the purchase date.

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

15. QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

Quarterly financial information for the years ended December 31, 2001 and 2002 is summarized as follows (in thousands, except per share data):

	2001			
	Q1	Q2	Q3	Q4
Revenues.....	\$203,581	\$228,547	\$235,156	\$215,577
Gross profit.....	\$ 36,428	\$ 43,220	\$ 44,563	\$ 41,366
Operating income (loss).....	\$ (1,353)	\$ 5,504	\$ 6,949	\$ 2,326
Income (loss) from continuing operations.....	\$ (2,352)	\$ 1,177	\$ 1,277	\$ (1,135)
Discontinued operations --				
Operating results, net of tax.....	\$ 3,452	\$ 2,114	\$ 4,365	\$ 4,226
Net income.....	\$ 1,100	\$ 3,291	\$ 5,642	\$ 3,091
INCOME (LOSS) PER SHARE:				
Basic --				
Income (loss) from continuing operations.....	\$ (0.06)	\$ 0.03	\$ 0.03	\$ (0.03)
Discontinued operations --				
Income from operations.....	0.09	0.06	0.12	0.11
Net income.....	\$ 0.03	\$ 0.09	\$ 0.15	\$ 0.08
Diluted --				
Income (loss) from continuing operations.....	\$ (0.06)	\$ 0.03	\$ 0.03	\$ (0.03)
Discontinued operations --				
Income from operations.....	0.09	0.06	0.12	0.11
Net income.....	\$ 0.03	\$ 0.09	\$ 0.15	\$ 0.08
Cash flow from operations.....	\$ 6,836	\$ 25,170	\$ 9,772	\$ 25,051

	2002			
	Q1	Q2	Q3	Q4
Revenues.....	\$ 190,550	\$212,557	\$215,331	\$200,844
Gross profit.....	\$ 30,453	\$ 38,759	\$ 40,060	\$ 33,742
Operating income (loss).....	\$ (3,932)	\$ 8,137	\$ 7,922	\$ 1,740
Income (loss) from continuing operations.....	\$ (3,943)	\$ 5,170	\$ 3,740	\$ 512
Discontinued operations --				
Operating results, net of tax.....	\$ 197	\$ (233)	\$ --	\$ --
Estimated loss on disposition, including tax....	\$ (10,987)	\$ (169)	\$ --	\$ (846)
Income (loss) before cumulative effect of change in accounting principle.....	\$ (14,733)	\$ 4,768	\$ 3,740	\$ (334)

Cumulative effect of change in accounting principle.....	\$ (202,521)	\$ --	\$ --	\$ --
Net income (loss).....	\$ (217,254)	\$ 4,768	\$ 3,740	\$ (334)

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

	2002			
	Q1	Q2	Q3	Q4
INCOME (LOSS) PER SHARE:				
Basic --				
Income (loss) from continuing operations.....	\$ (0.11)	\$ 0.14	\$ 0.10	\$ 0.01
Discontinued operations --				
Income (loss) from operations.....	0.01	(0.01)	--	--
Estimated loss on disposition.....	(0.29)	--	--	(0.02)
Cumulative effect of change in accounting principle.....	(5.40)	--	--	--
Net income (loss).....	\$ (5.79)	\$ 0.13	\$ 0.10	\$ (0.01)
Diluted --				
Income (loss) from continuing operations.....	\$ (0.11)	\$ 0.13	\$ 0.10	\$ 0.01
Discontinued operations --				
Income (loss) from operations.....	0.01	(0.01)	--	--
Estimated loss on disposition.....	(0.29)	--	--	(0.02)
Cumulative effect of change in accounting principle.....	(5.40)	--	--	--
Net income (loss).....	\$ (5.79)	\$ 0.12	\$ 0.10	\$ (0.01)
Cash flow from operations.....	\$ (9,262)	\$ 10,955	\$ 12,114	\$ 283

The sum of the individual quarterly earnings per share amounts do not agree with year-to-date earnings per share as each quarter's computation is based on the weighted average number of shares outstanding during the quarter, the weighted average stock price during the quarter and the dilutive effects of the convertible subordinated notes, warrants, and contingently issuable restricted stock in each quarter.

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

For a discussion of a change in the Company's accountants, please see our Current Report on Form 8-K dated May 24, 2002.

PART III

ITEMS 10 TO 15 INCLUSIVE

These items have been omitted in accordance with the instructions to Form 10-K. The Company will file with the Commission a definitive proxy statement including the information to be disclosed under the items in the 120 days following December 31, 2002.

ITEM 14. CONTROLS AND PROCEDURES

Within 90 days before the date of this report on Form 10-K, under the supervision and with the participation of our management, including our Chairman of the Board and Chief Executive Officer (our principal executive officer) and our Chief Financial Officer (our principal financial officer), we evaluated the effectiveness of our disclosure controls and procedures (as defined under Rule 13a-14(c) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")). Based on this evaluation, our Chairman of the Board and Chief Executive Officer and our Chief Financial Officer believe that our disclosure controls and

procedures are effective to ensure that information we are required to disclose in the reports that we file or submit under the Exchange Act fairly represents, in all material respects, our financial condition, results of operations and cash flows.

There were no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of such evaluation.

PART IV

ITEM 16. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a) The following documents are filed as part of this report:

(1) Consolidated Financial Statements (Included Under Item 8): The Index to the Consolidated Financial Statements is included on page 27 of this report and is incorporated herein by reference.

(2) Financial Statement Schedules:

None.

(b) Reports on Form 8-K

None.

(c) Exhibits

Reference is made to the Index of Exhibits beginning on page 66 which index is incorporated herein by reference.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

COMFORT SYSTEMS USA, INC.

By: /s/ WILLIAM F. MURDY

William F. Murdy
Chairman of the Board and
Chief Executive Officer

By: /s/ J. GORDON BEITTENMILLER

J. Gordon Beittenmiller
Executive Vice President and
Chief Financial Officer

Date: March 31, 2003

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that the persons whose signatures appear below, constitute and appoint J. Gordon Beittenmiller and William George, and each of them as their true and lawful attorneys-in-fact and agents, with full power and substitution and resubstitution, for them and in their names, places and steads, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto, and the other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as they might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their or his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this

report has been signed by the following persons in the capacities and on the date indicated.

SIGNATURE -----	TITLE -----	DATE -----
/s/ WILLIAM F. MURDY ----- William F. Murdy	Chairman of the Board and Chief Executive Officer	March 31, 2003
/s/ NORMAN C. CHAMBERS ----- Norman C. Chambers	President and Director	March 31, 2003
/s/ J. GORDON BEITTENMILLER ----- J. Gordon Beittenmiller	Executive Vice President, Chief Financial Officer and Director (Principal Accounting Officer)	March 31, 2003
/s/ HERMAN E. BULLS ----- Herman E. Bulls	Director	March 31, 2003
/s/ VINCENT J. COSTANTINI ----- Vincent J. Costantini	Director	March 31, 2003

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SIGNATURE -----	TITLE -----	DATE -----
/s/ ALFRED J. GIARDINELLI, JR. ----- Alfred J. Giardinelli, Jr.	Director	March 31, 2003
/s/ STEVEN S. HARTER ----- Steven S. Harter	Director	March 31, 2003
/s/ JAMES H. SCHULTZ ----- James H. Schultz	Director	March 31, 2003
/s/ ROBERT D. WAGNER, JR. ----- Robert D. Wagner, Jr.	Director	March 31, 2003

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CERTIFICATION

I, William F. Murdy, Chairman of the Board and Chief Executive Officer, certify that:

1. I have reviewed this annual report on Form 10-K of Comfort Systems USA, Inc.;

2. Based on my knowledge, this annual 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 annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

(a) Designed such disclosure controls and procedures 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 annual report is being prepared;

(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

(c) Presented in this annual report

Our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ WILLIAM F. MURDY

William F. Murdy
Chairman of the Board and
Chief Executive Officer

Dated: March 31, 2003

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CERTIFICATION

I, J. Gordon Beittenmiller, Executive Vice President and Chief Financial Officer, certify that:

1. I have reviewed this annual report on Form 10-K of Comfort Systems USA, Inc.;

2. Based on my knowledge, this annual 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 annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

(a) Designed such disclosure controls and procedures 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 annual report is being prepared;

(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

(c) Presented in this annual report

Our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ J. GORDON BEITTENMILLER

J. Gordon Beittenmiller
Executive Vice President and
Chief Financial Officer

Dated: March 31, 2003

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INDEX OF EXHIBITS

		INCORPORATED BY REFERENCE TO THE EXHIBIT INDICATED BELOW AND TO THE FILING WITH THE COMMISSION INDICATED BELOW	
EXHIBIT NUMBER	DESCRIPTION OF EXHIBITS	EXHIBIT NUMBER	FILING OR FILE NUMBER
-----	-----	-----	-----
3.1	-- Second Amended and Restated Certificate of Incorporation of the Registrant.	3.1	333-24021
3.2	-- Certificate of Amendment dated May 21, 1998.	3.2	1998 Form 10-K
3.3	-- Bylaws of the Registrant, as amended.	3.3	1999 Form 10-K
4.1	-- Form of certificate evidencing ownership of Common Stock of the Registrant.	4.1	333-24021
*10.1	-- Comfort Systems USA, Inc. 1997 Long-Term Incentive Plan.	10.1	333-24021
*10.2	-- Comfort Systems USA, Inc. 1997 Non-Employee Directors' Stock Plan.	10.2	333-24021
*10.3	-- Form of Employment Agreement between the Registrant and J. Gordon Beittenmiller.	10.4	333-24021
*10.4	-- Form of Employment Agreement between the Registrant and William George III.	10.5	333-24021

*10.5	--	Form of Employment Agreement between the Registrant, Eastern Heating & Cooling, Inc. and Alfred J. Giardinelli, Jr.	10.10	333-24021
*10.6	--	Employment Agreement between the Registrant, Shambaugh & Son, Inc. and Mark P. Shambaugh.	10.17	1998 Form 10-K
10.7	--	Form of Agreement among certain stockholders.	10.16	333-24021
10.8	--	Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (Opportunity Drive).	10.28	1998 Form 10-K
10.9	--	Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Son, Inc. (Di Salle Boulevard).	10.29	1998 Form 10-K
10.10	--	Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (Speedway Drive).	10.30	1998 Form 10-K
10.11	--	Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (South Bend).	10.31	1998 Form 10-K
10.12	--	Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (Lafayette).	10.32	1998 Form 10-K
*10.13	--	Employment Agreement between William F. Murdy and the Registrant dated June 27, 2000.	10.2	Second Quarter 2000 Form 10-Q
*10.14	--	Comfort Systems USA, Inc. 2000 Incentive Plan.	10.7	Second Quarter 2000 Form 10-Q
*10.15	--	Employment Agreement between the Registrant and Milburn Honeycutt dated January 2, 2001.	10.35	2000 Form 10-K
10.16	--	Purchase Agreement between the Registrant and EMCOR-CSI Holding Co. dated February 11, 2002.	2.1	February 2002 Form 8-K
*10.17	--	Form of Restricted Stock Award Agreement between William F. Murdy and the Company dated March 22, 2002.	10.2	First Quarter 2002 Form 10-Q
*10.18	--	Employment Agreement between David Lanphar and the Company dated September 1, 2001.	10.1	Second Quarter 2002 Form 10-Q/A
*10.19	--	Amendment to the 1997 Non-Employee Directors' Stock Plan dated May 23, 2002.	10.3	Second Quarter 2002 Form 10-Q/A

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INCORPORATED BY REFERENCE
TO THE EXHIBIT INDICATED BELOW AND
TO THE FILING WITH THE
COMMISSION INDICATED BELOW

EXHIBIT NUMBER		DESCRIPTION OF EXHIBITS	EXHIBIT NUMBER	FILING OR FILE NUMBER
10.20	--	Credit Agreement dated as of October 11, 2002 by and among the Company, as Borrower, and the other persons party thereto that are designated as credit parties, and General Electric Capital Corporation, as Agent, L/C Issuer and a Lender, and the other financial institutions party thereto, as Lenders.	10.1	Third Quarter 2002 Form 10-Q
10.21	--	Stock Purchase Warrant and Repurchase Agreement dated October 11, 2002 granted by the Company to General Electric Capital Corporation.	10.2	Third Quarter 2002 Form 10-Q
10.22	--	Registration Rights Agreement dated October 11, 2002 by and among the Company and General Electric Capital Corporation.	10.3	Third Quarter 2002 Form 10-Q
*10.23	--	Employment Agreement dated November 4, 2002 by and among Comfort Systems USA (Texas), L.P. and Norman C. Chambers.	10.4	Third Quarter 2002 Form 10-Q
*10.24	--	Restricted Stock Award Agreement dated November 1, 2002 from the Company to Norman C. Chambers.	10.5	Third Quarter 2002 Form 10-Q
10.25	--	Amendment No. 1 to Credit Agreement dated as of December 9, 2002 by and between the Company and General Electric Capital Corporation, as Agent for the Lenders.		Filed Herewith
10.26	--	Amendment No. 2 to Credit Agreement dated as of December 20, 2002 by and between the Company, the other credit parties, and General Electric Capital Corporation, as Agent for the Lenders.		Filed Herewith
10.27	--	Waiver and Amendment No. 3 to Credit Agreement dated as of March 28, 2003.		Filed Herewith
16.1	--	Letter from Arthur Andersen LLP to the Securities and Exchange Commission dated May 24, 2002.	Exhibit 16	May 24, 2002 Form 8-K
21.1	--	List of subsidiaries of Comfort Systems USA, Inc.		Filed Herewith
23.1	--	Consent of Ernst & Young LLP.		Filed Herewith
24.1	--	Power of Attorney (included in the signature page hereto).		Filed Herewith
99.1	--	Certification Of William F. Murdy pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.		Filed Herewith
99.2	--	Certification Of J. Gordon Beittenmiller pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.		Filed Herewith

* Management contract or compensatory plan or arrangement required to be filed as an exhibit to this report.

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AMENDMENT NO. 1 TO CREDIT AGREEMENT

This Amendment No. 1 to Credit Agreement, dated as of December 9, 2002 (this "Amendment"), is entered into by and between Comfort Systems USA, Inc., a Delaware corporation ("Borrower"), and General Electric Capital Corporation, as Agent ("Agent") for the Lenders (as defined in the Credit Agreement referred to below).

RECITALS

WHEREAS, Borrower and Agent are parties to that certain Credit Agreement, dated as of October 11, 2002 (the "Credit Agreement"), by and among Borrower, the other Credit Parties signatory thereto, Agent and the Lenders from time to time signatory thereto;

WHEREAS, Borrower desires to extend the time period within which Borrower is required to enter into the Interest Rate Agreements as required pursuant to Section 2.8 of the Credit Agreement;

WHEREAS, Borrower, Agent and Lenders are each desirous of entering into an amendment to the Credit Agreement as and to the extent set forth in this Amendment and subject to the terms and conditions set forth herein; and

WHEREAS, this document shall constitute a Loan Document and these Recitals shall be construed as part of this Amendment;

NOW THEREFORE, in consideration of the premises and the mutual covenants hereinafter contained, and for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged by the parties, Borrower and Agent hereby agree as follows:

1. Definitions. Except to the extent otherwise specified herein, capitalized terms used in this Amendment shall have the same meanings ascribed to them in the Credit Agreement and Annex A thereto.

2. Amendment. Section 2.8 of the Credit Agreement is amended by deleting the words "within sixty (60) days after the Closing Date" in their entirety and replacing them with the following:

"On or prior to January 15, 2003,"

3. Conditions Precedent to Effectiveness. The effectiveness of the amendment set forth in Section 2 hereof is subject to Agent's receipt of counterparts of this Amendment, duly executed by the Borrower and Agent.

4. Counterparts. This Amendment may be executed in any number of counterparts, each of which when so executed shall be deemed an original but all such counterparts shall constitute one and the same instrument. Delivery of an executed counterpart

of a signature page to this Amendment by telecopier shall be as effective as delivery of a manually executed counterpart signature page to this Amendment.

5. Costs and Expenses. As provided in Section 11.3 of the Credit Agreement, Borrower shall pay the fees, costs and expenses incurred by Agent in connection with the preparation, execution and delivery of this Amendment (including, without limitation, reasonable attorneys' fees).

6. GOVERNING LAW. THIS AMENDMENT SHALL BE GOVERNED BY AND CONSTRUED AND ENFORCED IN ACCORDANCE WITH THE INTERNAL LAWS (AS OPPOSED TO CONFLICTS OF LAW PROVISIONS) OF THE STATE OF NEW YORK.

7. Headings. Section headings in this Amendment are included herein for convenience of reference only and shall not constitute a part of this Amendment for any other purpose.

[Signature Pages Follow]

IN WITNESS WHEREOF, this Amendment has been duly executed as of the date first written above.

BORROWER:

COMFORT SYSTEMS USA, INC.

By: /s/ J. Gordon Beittenmiller

Name: J. Gordon Beittenmiller
Title: Executive Vice President

AGENT:

GENERAL ELECTRIC CAPITAL CORPORATION,
as Agent for Lenders

By: /s/ Justin Staadecker

Its Duly Authorized Signatory

AMENDMENT NO. 2 TO CREDIT AGREEMENT

This Amendment No. 2 to Credit Agreement, dated as of December 20, 2002 (this "Amendment"), is entered into by and between Comfort Systems USA, Inc., a Delaware corporation ("Borrower"), the other Credit Parties, and General Electric Capital Corporation ("GE Capital"), as Agent ("Agent") for the Lenders (as defined in the Credit Agreement referred to below) and as a Lender, and the other Lenders party to the Credit Agreement.

RECITALS

WHEREAS, Borrower, Agent and GE Capital, as a Lender, are parties to that certain Credit Agreement, dated as of October 11, 2002 (as amended by Amendment No. 1 to Credit Agreement, dated as of December 10, 2002, and as the same may be further amended, restated, supplemented or otherwise amended from time to time hereafter, the "Credit Agreement"), by and among Borrower, the other Credit Parties signatory thereto, Agent and Lenders;

WHEREAS, Borrower is desirous of obtaining a \$20,000,000 increase in the Revolving Loan Commitment from \$40,000,000 to \$60,000,000 and has requested a corresponding increase in the Commitments from \$55,000,000 to \$75,000,000. Agent and GE Capital, as a Lender, are agreeable to the foregoing; provided, that, the \$20,000,000 increase in the Revolving Loan Commitment is provided through the provision of an \$8,000,000 portion of the Revolving Loan by each of BANK OF TEXAS, NA ("Bank of Texas") and REGIONS BANK ("Regions Bank" and; together with Bank of Texas, the "New Lenders") and a \$4,000,000 increase in portion of the Revolving Loan by GE Capital;

WHEREAS, GE Capital, as a Lender, is agreeable to reducing its Term Loan Commitment to \$11,000,000 and its outstanding Term Loan to \$11,000,000, with each of the New Lenders having a Term Loan Commitment of \$2,000,000 and having an outstanding Term Loan of \$2,000,000, and to increasing its Revolving Loan Commitment to \$44,000,000;

WHEREAS, each of the New Lenders is agreeable to becoming a Lender with a Revolving Loan Commitment of \$8,000,000, and a Term Loan Commitment of \$2,000,000, and an outstanding Term Loan of \$2,000,000 (and in connection therewith paying to GE Capital, as a Lender, \$2,000,000 in order to correspondingly reduce GE Capital's outstanding Term Loan) and is otherwise agreeable to the foregoing;

WHEREAS, Borrower, Credit Parties, Agent and Lenders are each desirous of entering into an amendment to the Credit Agreement, as and to the extent set forth in this Amendment and subject to the terms and conditions set forth herein; and

WHEREAS, this document shall constitute a Loan Document and these Recitals shall be construed as part of this Amendment;

NOW THEREFORE, in consideration of the premises and the mutual covenants hereinafter contained, and for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged by the parties, Borrower, Credit Parties, Agent and Lenders each hereby agree as follows:

1. Definitions. Except to the extent otherwise specified herein, capitalized terms used in this Amendment shall have the same meanings ascribed to them in the Credit Agreement and Annex A thereto.

2. Amendments. The Credit Agreement is amended as follows:

2.1 Annex A to the Credit Agreement is amended by deleting the following definitions in their entirety and replacing them with the following:

"Commitments" means (a) as to any Lender, the aggregate of such Lender's Revolving Loan Commitment and Term Loan Commitment as set forth on Annex B to the Agreement or in the most recent Assignment Agreement executed by such Lender and (b) as to all Lenders, the aggregate of all Lenders' Revolving Loan Commitments and Term Loan Commitments, which aggregate commitment shall be Seventy-Five Million Dollars (\$75,000,000) (comprised of aggregate Revolving Loan Commitments of \$60,000,000 and Term Loan Commitments of \$15,000,000), as such Commitments may be reduced, amortized or

adjusted from time to time in accordance with the Agreement.

'L/C Issuer' means any Lender or a Subsidiary thereof or a bank or other legally authorized Person selected by or acceptable to Agent, in its sole discretion, in such Person's capacity as an issuer of Letters of Credit hereunder.

'Requisite Lenders' means Lenders having (a) more than 70% of the Commitments of all Lenders, or (b) if the Commitments have been terminated, more than 70% of the aggregate outstanding amount of the Loans; provided, further, that in addition to the foregoing 70% requirement, if there shall be more than one Lender, "Requisite Lenders" shall at all times require at least two Lenders.

'Revolving Loan Commitment' means (a) as to any Lender, the commitment of such Lender to make its Pro Rata Share of Revolving Credit Advances or incur its Pro Rata Share of Letter of Credit Obligations (including, in the case of the Swing Line Lender, its commitment to make Swing Line Advances as a portion of its Revolving Loan Commitment) as set forth on Annex B or in the most recent Assignment Agreement, if any, executed by such Lender and (b) as to all Lenders, the aggregate commitment of all Lenders to make the Revolving Credit Advances (including, in the case of the Swing Line Lender, Swing Line Advances) or incur Letter of Credit Obligations, which aggregate commitment shall be Sixty Million Dollars (\$60,000,000), as such amount may be adjusted, if at all, from time to time in accordance with the Agreement."

2.2 Annex B to the Credit Agreement is hereby amended by deleting existing Annex B in its entirety and replacing it with the new Annex B which is attached hereto as Exhibit A.

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3. New Lenders. (a) Upon this Amendment becoming effective, Bank of Texas and Regions Bank shall each automatically become a Lender under the Credit Agreement, each with a Revolving Loan Commitment of \$8,000,000, and a Term Loan Commitment of \$2,000,000, and each shall thereupon have all of the rights and obligations of a Lender under the Credit Agreement and each of the other Loan Documents.

(b) Concurrently with this Amendment becoming effective, Bank of Texas and Regions Bank shall each pay to GE Capital, as a Lender, \$2,000,000 in cash by wire transfer of same day funds to the account designated by GE Capital.

4. Representations and Warranties of Borrower and Credit Parties. Borrower and each Credit Party hereby represents and warrants that:

4.1 The execution, delivery and performance by it of this Amendment has been duly authorized by all necessary corporate action, including, without limitation, all necessary action by its Board of Directors and stockholders, and that this Amendment is a legal, valid and binding obligation of it, enforceable against it in accordance with its terms, except as the enforcement hereof may be subject to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar law affecting creditors' rights generally or to general principles of equity.

4.2 The execution, delivery and performance of this Amendment by and of the New Notes (as such term is defined below) by Borrower does not, and will not, contravene or conflict with any provision of (i) law, (ii) any judgment, decree or order, or (iii) the certificate or articles of incorporation or by-laws of such Credit Party, and does not, and will not, contravene or conflict with, or cause any Lien to arise under, any provision of any agreement, mortgage, lease, instrument or other document binding upon or otherwise affecting Borrower, any other Credit Party or any of their respective Subsidiaries or any property of Borrower, any other Credit Party or any of their respective Subsidiaries.

4.3 All of the representations and warranties contained in the Credit Agreement and each other Loan Document are true and correct in all material respects on and as of the date hereof as if made on the date hereof. No Default or Event of Default exists under the Credit Agreement or any other Loan Document or will exist after or be triggered by the execution and delivery of this Amendment or the New Notes or the consummation of the transactions contemplated hereby. In addition, each Credit Party represents and warrants that

the Credit Agreement and each of the other Loan Documents remains in full force and effect and each is hereby ratified and confirmed in all respects.

5. Conditions Precedent to Effectiveness. The effectiveness of each of amendments set forth in Section 2 hereof is subject to the satisfaction of each of the following conditions precedent in a manner acceptable to Agent:

5.1. Documentation. Borrower shall have delivered to Agent all of the following, each duly executed and dated the date hereof, in form and substance satisfactory to the Agent:

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- (a) New Notes. (i) A replacement Revolving Note of Borrower in favor of GE Capital (the "GE Capital Replacement Revolving Note"), substantially in the form set forth as Exhibit B hereto, delivered to the Agent for the Account of GE Capital, as a Lender, in an amount equal to its Revolving Loan Commitment of \$44,000,000, (ii) a replacement Term Note of Borrower in favor of GE Capital (the "GE Capital Replacement Term Note"), substantially in the form set forth as Exhibit C hereto, delivered to the Agent for the Account of GE Capital, as a Lender, in an amount equal to its Term Loan Commitment of \$11,000,000, (iii) a Revolving Note of Borrower in favor of Bank of Texas (the "Bank of Texas Revolving Note"), substantially in the form set forth as Exhibit B hereto, delivered to the Agent for the account of Bank of Texas, as a Lender, in an amount equal to its Revolving Loan Commitment of \$8,000,000, (iv) a Term Note of Borrower in favor of Bank of Texas (the "Bank of Texas Term Note"), substantially in the form set forth as Exhibit C hereto, delivered to the Agent for the account of Bank of Texas, as a Lender, in an amount equal to its Term Loan Commitment of \$2,000,000, (v) a Revolving Note of Borrower in favor of Regions Bank (the "Regions Bank Revolving Note"), substantially in the form set forth as Exhibit B hereto, delivered to the Agent for the account of Regions Bank, as a Lender, in an amount equal to its Revolving Loan Commitment of \$8,000,000 and (vi) a Term Note of Borrower in favor of Regions Bank (the "Regions Bank Term Note" and together with the GE Capital Replacement Revolving Note, the GE Capital Replacement Term Note, the Bank of Texas Revolving Note, the Bank of Texas Term Note and the Regions Bank Revolving Note, the "New Notes"), substantially in the form set forth as Exhibit C hereto, delivered to the Agent for the account of Regions Bank, as a Lender, in an amount equal to its Term Loan Commitment of \$2,000,000. Upon receipt of the GE Capital Replacement Term Note and the GE Capital Replacement Revolving Note, GE Capital shall promptly thereafter return to Borrower for cancellation the original Term Note payable to GE Capital in the principal amount of \$15,000,000 and the original Revolving Note payable to GE Capital in the maximum principal amount of \$40,000,000;
- (b) Amendment. Counterparts of this Amendment, duly executed by the Borrower, each of the other Credit Parties, Agent and all of the Lenders;
- (c) Certificates. Certificates of the secretary or an assistant secretary of Borrower and each of the other Credit Parties, as appropriate, (i) certifying that the existing resolutions adopted in connection with the Credit Agreement were validly adopted, have not since their adoption been in any way modified or rescinded and are in full force and effect on the date hereof, (ii) certifying that the certificates of incorporation, partnership, or limited liability company, as appropriate, are in force as filed with the appropriate governmental office in the appropriate jurisdiction of incorporation, (iii) attaching a true and correct copy of the bylaws as in force on the date hereof;
- (d) Opinion. An opinion of Bracewell & Patterson, LLP, counsel to Borrower and the other Credit Parties, addressed to Agent and Lenders, in substantially the form of Exhibit D hereto; and

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- (e) Opinion. An opinion of general counsel to Borrower and the other Credit Parties, addressed to Agent and Lenders, in substantially the form of Exhibit E hereto.

5.2. No Default or Event of Default. No Default or Event of Default shall have occurred and be continuing or would result from the effectiveness of this Amendment or the consummation of any of the transactions contemplated thereby.

5.3. Outstanding Term Loan. Bank of Texas and Regions Bank shall have each paid to GE Capital, as a Lender, \$2,000,000 in cash by wire transfer of same day funds to the account designated by GE Capital to fund their respective Term Loan Commitments and to, in the aggregate, reduce GE Capital's outstanding Term Loan to \$11,000,000, which is GE Capital's new Term Loan Commitment.

6. Reference to and Effect Upon the Credit Agreement and other Loan Agreements.

6.1. Except as specifically amended in Section 2 above, the Credit Agreement and each other Loan Document shall remain in full force and effect and is hereby ratified and confirmed.

6.2. The execution, delivery and effect of this Amendment shall be limited precisely as written and shall not be deemed to (i) be a consent to any waiver of any term or condition, or to any amendment or modification of any term or condition (except as specifically amended in Section 2 above), of the Credit Agreement or any other Loan Document or (ii) prejudice any right, power or remedy which the Agent or any Lender now has or may have in the future under or in connection with the Credit Agreement or any other Loan Document. Each reference in the Credit Agreement to "this Agreement", "hereunder", "hereof", "herein" or any other word or words of similar import shall mean and be a reference to the Credit Agreement as amended hereby, and each reference in any other Loan Document to the Credit Agreement or any word or words of similar import shall be and mean a reference to the Credit Agreement as amended hereby.

7. Acknowledgment and Consent of Credit Parties. Each Credit Party hereby consents to this Amendment and hereby confirms and agrees that (a) the Guaranty and each other Loan Document to which it is a party is, and shall continue to be, in full force and effect and is hereby ratified and confirmed in all respects, and (b) the Collateral Documents to which such Credit Party is a party and all of the Collateral described therein do, and shall continue to, secure the payment of all of the Obligations.

8. Counterparts. This Amendment may be executed in any number of counterparts, each of which when so executed shall be deemed an original but all such counterparts shall constitute one and the same instrument. Delivery of an executed counterpart

5

of a signature page to this Amendment by telecopier shall be as effective as delivery of a manually executed counterpart signature page to this Amendment.

9. Costs and Expenses. As provided in Section 1.3 of the Credit Agreement, Borrower shall pay the fees, costs and expenses incurred by Agent in connection with the preparation, execution and delivery of this Amendment (including, without limitation, reasonable attorneys' fees).

10. GOVERNING LAW. THIS AMENDMENT SHALL BE GOVERNED BY AND CONSTRUED AND ENFORCED IN ACCORDANCE WITH THE INTERNAL LAWS (AS OPPOSED TO CONFLICTS OF LAW PROVISIONS) OF THE STATE OF NEW YORK.

11. Headings. Section headings in this Amendment are included herein for convenience of reference only and shall not constitute a part of this Amendment for any other purpose.

[Signature Pages Follow]

6

IN WITNESS WHEREOF, this Amendment has been duly executed as of the date first written above.

BORROWER:

COMFORT SYSTEMS USA, INC.

By: /s/ J. Gordon Beittenmiller

Name: J. Gordon Beittenmiller
Title: Executive Vice President

CREDIT PARTIES:

ACI MECHANICAL, INC.

ARC COMFORT SYSTEMS USA, INC.

ACCURATE AIR SYSTEMS, L.P., by
Atlas-Accurate Holdings, L.L.C.,
as General Partner

ACCU-TEMP GP, INC.

ACCU-TEMP LP, INC.

ACCU-TEMP LLC,
by Accu-Temp GP, Inc., as acting member

AIR SOLUTIONS USA, INC.

AIR TEMP, INC.

ATLAS-ACCURATE HOLDINGS, L.L.C.,
by CS53 Acquisition Corp.,
as acting member

ATLAS AIR CONDITIONING COMPANY, L.P.,
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BATCHELOR'S MECHANICAL CONTRACTORS, INC.

BCM CONTROLS CORPORATION

CARSON BROTHERS, INC.

CEL, INC.

CENTRAL MECHANICAL, INC.

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COMFORT SYSTEMS USA (BALTIMORE), INC.

COMFORT SYSTEMS USA (BOWLING GREEN), INC.

COMFORT SYSTEMS USA (BRISTOL), INC.

COMFORT SYSTEMS USA (CLEVELAND), INC.

COMFORT SYSTEMS USA (FLORIDA), INC.

COMFORT SYSTEMS USA G.P., INC.

COMFORT SYSTEMS US (HARTFORD), INC.

COMFORT SYSTEMS USA (INTERMOUNTAIN), INC.

COMFORT SYSTEMS USA NATIONAL SERVICE
ORGANIZATION, INC.

COMFORT SYSTEMS USA (OREGON), INC.

COMFORT SYSTEMS USA (SOUTH BOSTON), INC.

COMFORT SYSTEMS USA (SYRACUSE), INC.

COMFORT SYSTEMS USA (TEXAS), L.P.,
by Comfort Systems USA G.P., Inc.,
as general partner

COMFORT SYSTEMS USA (TWIN CITIES), INC.

COMFORT SYSTEMS USA (WESTERN
MICHIGAN), INC.

CS44 ACQUISITION CORP.

CS53 ACQUISITION CORP.

DESIGN MECHANICAL INCORPORATED
EASTERN HEATING & COOLING, INC.

ESS ENGINEERING, INC.

GULFSIDE MECHANICAL, INC.

H & M MECHANICAL, INC.

HELM CORPORATION

HELM CORPORATION SAN DIEGO

HESS MECHANICAL CORPORATION

INDUSTRIAL COOLING INC.

J & J MECHANICAL, INC.

JAMES AIR CONDITIONING ENTERPRISE INC.

MARTIN HEATING, INC.

MECHANICAL SERVICE GROUP, INC.

MECHANICAL TECHNICAL SERVICES, L.P.,
by Atlas-Accurate Holdings, L.L.C.,
as general partner

MJ MECHANICAL SERVICES, INC.

NEEL MECHANICAL CONTRACTORS, INC.

NORTH AMERICAN MECHANICAL, INC.

OK SHEET METAL AND AIR CONDITIONING, INC.

QUALITY AIR HEATING & COOLING, INC.

S&K AIR CONDITIONING CO., INC.

S. I. GOLDMAN COMPANY, INC.

S.M. LAWRENCE COMPANY, INC.

SA ASSOCIATES, INC.

SALMON & ALDER, LLC,
by SA Associates, Inc.,
as acting member

SEASONAIR, INC.

SHEREN PLUMBING & HEATING, INC.

STANDARD HEATING & AIR CONDITIONING
COMPANY

SUPERIOR MECHANICAL SYSTEMS, INC.

TARGET CONSTRUCTION, INC.

TEMP-RIGHT SERVICE, INC.

THE CAPITAL REFRIGERATION COMPANY

TRI-CITY MECHANICAL, INC.

UNITED ENVIRONMENTAL SERVICES, L.P.,
by Atlas-Accurate Holdings, L.L.C.,
as general partner

WEATHER ENGINEERING, INC.

WESTERN BUILDING SERVICES, INC.

By: /s/ J. Gordon Beittenmiller

Name: J. Gordon Beittenmiller
Title: Vice President

GENERAL ELECTRIC CAPITAL CORPORATION,
as Agent and a Lender

By: /s/ Justin Staadecker

Its Duly Authorized Signatory

BANK OF TEXAS, NA, as a Lender

By: /s/ H. Gale Smith, Jr.

Name: H. Gale Smith, Jr.
Title: Senior Vice President

REGIONS BANK, as a Lender

By: /s/ Mark Burr

Name: Mark Burr
Title: Vice President Corporate Banking

WAIVER AND AMENDMENT NO. 3 TO CREDIT AGREEMENT

This Waiver and Amendment No. 3 to Credit Agreement, dated as of March __, 2003 (this "Amendment"), is entered into by and between Comfort Systems USA, Inc., a Delaware corporation ("Borrower"), the other Credit Parties, General Electric Capital Corporation ("GE Capital"), as Agent (in such capacity, "Agent") for the Lenders (as defined in the Credit Agreement referred to below) and as a Lender, and the other Lenders party to the Credit Agreement.

RECITALS

WHEREAS, Borrower, the other Credit Parties, Agent and Lenders are parties to that certain Credit Agreement, dated as of October 11, 2002 (as amended by Amendment No. 1 to Credit Agreement, dated as of December 10, 2002, and Amendment No. 2 to Credit Agreement, dated as of December 20, 2002, and as the same may be further amended, restated, supplemented or otherwise amended from time to time hereafter, the "Credit Agreement");

WHEREAS, Borrower has notified Agent and Lenders that an Event of Default is currently in existence under the Credit Agreement based upon Borrower's breach of the "Minimum EBITDA" financial covenant set forth in Section 4.2 of the Credit Agreement for the period ended December 31, 2002 (the "Existing Event of Default");

WHEREAS, Borrower has requested that Agent and Lenders waive the Existing Event of Default and reset certain financial covenants set forth in Section 4 of the Credit Agreement, and Agent and Lenders are willing to do so pursuant to the terms and conditions set forth in this Amendment;

WHEREAS, Borrower, Credit Parties, Agent and Lenders are each desirous of entering into an amendment to certain other provisions the Credit Agreement, as and to the limited extent set forth in this Amendment and subject to the terms and conditions set forth herein; and

WHEREAS, this document shall constitute a Loan Document and these Recitals shall be construed as part of this Amendment;

NOW THEREFORE, in consideration of the premises and the mutual covenants herein contained, and for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged by the parties, Borrower, Credit Parties, Agent and Lenders each hereby agree as follows:

1. Definitions. Except to the extent otherwise specified herein, capitalized terms used in this Amendment shall have the same meanings ascribed to them in the Credit Agreement and Annex A thereto.

2. Waiver.

2.1. Existing Event of Default. Agent and Lenders hereby waive the Existing Event of Default; provided, that, Borrower shall be in compliance with all of the terms and conditions of the Credit Agreement as hereby amended. The foregoing waiver is only applicable and shall only be effective in the specific instance and for the specific purpose for which made. Such waiver is expressly limited to the facts and circumstances referred to herein and shall not operate (a) as a waiver of or consent to non-compliance with any other provision of the Credit Agreement or any other Loan Document, (b) as a waiver of any other right, power or remedy of Agent or Lenders under the Credit Agreement or any other Loan Document or (c) as a waiver of or consent to any other Default or Event of Default under the Credit Agreement or any other Loan Document.

3. Amendments. The Credit Agreement is amended as follows:

3.1. Annex A to the Credit Agreement is amended by deleting the existing definitions of "Commitments" and "Revolving Loan Commitment" in their entirety and replacing them with the following:

"Commitments" means (a) as to any Lender, the aggregate of such Lender's Revolving Loan Commitment and Term Loan Commitments set forth on Annex B to the Agreement or in the most recent

Assignment Agreement executed by such Lender and (b) as to all Lenders, the aggregate of all Lenders' Revolving Loan Commitments and Term Loan Commitments, which aggregate commitment shall be Fifty-Five Million Dollars (\$55,000,000) (comprised of aggregate Revolving Loan Commitments of \$40,000,000 and Term Loan Commitments of \$15,000,000), as such Commitments may be reduced, amortized or adjusted from time to time in accordance with the Agreement.

"Revolving Loan Commitment" means (a) as to any Lender, the commitment of such Lender to make its Pro Rata Share of Revolving Credit Advances or incur its Pro Rata Share of Letter of Credit Obligations (including, in the case of the Swing Line Lender, its commitment to make Swing Line Advances as a portion of its Revolving Loan Commitment) as set forth on Annex B or in the most recent Assignment Agreement, if any, executed by such Lender and (b) as to all Lenders, the aggregate commitment of all Lenders to make the Revolving Credit Advances (including, in the case of the Swing Line Lender, Swing Line Advances) or incur Letter of Credit Obligations, which aggregate commitment shall be Forty Million Dollars (\$40,000,000), as such amount may be adjusted, if at all, from time to time in accordance with the Agreement."

3.2. Annex A to the Credit Agreement is amended by inserting the following definitions in alphabetical order therein:

"Emcor Sale" means that sale of certain assets of the Borrower to Emcor prior to the Closing Date during Fiscal Year 2002.

3.3. Section 1.1(b) (Revolving Loans) is amended by inserting the following proviso at the end of the second sentence thereof:

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"and provided, further, that, notwithstanding anything contained in this Agreement or any other Loan Document to the contrary, a portion of the Revolving Loan Commitment in the principal amount of (i) at all times from the Closing Date through July 31, 2003, \$15,000,000 and (ii) at all times from August 1, 2003 through the Commitment Termination Date, \$20,000,000 shall be available only to be utilized, subject to the satisfaction of the conditions set forth in this Agreement, upon the request of Borrower for the issuance of Letters of Credit pursuant to Section 1.1(d) hereof."

3.4. Section 3.6 (Restrictions on Fundamental Changes) to the Credit Agreement is hereby amended by deleting the text immediately following the first sentence thereof in its entirety, beginning with the words "Notwithstanding the foregoing" through and including clause (xii) thereof (such that such Section 3.6 shall consist only of the first sentence thereof).

3.5. Section 4.2 (Minimum EBITDA) to the Credit Agreement is hereby amended and restated in its entirety as follows:

"4.2 Minimum EBITDA. Borrower and its Subsidiaries on a consolidated basis shall have, at the end of each month set forth below, EBITDA for the 12-month period then ended of not less than the following:

Period -----	EBITDA -----
December 31, 2002	\$ 23,639,000
January 31, 2003	\$ 21,983,000
February 28, 2003	\$ 22,745,000
March 31, 2003	\$ 19,190,000
April 30, 2003	\$ 18,010,000
May 31, 2003	\$ 16,985,000
June 30, 2003	\$ 16,420,000
July 31, 2003	\$ 16,420,000

August 30, 2003	\$ 16,420,000
September 30, 2003	\$ 17,840,000
October 31, 2003	\$ 17,840,000
November 30, 2003	\$ 17,840,000
December 31, 2003	\$ 23,565,000
January 31, 2004	\$ 25,640,000
February 29, 2004	\$ 26,820,000
March 31, 2004	\$ 29,000,000
April 30, 2004	\$ 29,000,000

3

May 31, 2004	\$ 29,000,000
June 30, 2004	\$ 29,000,000
July 31, 2004	\$ 29,000,000
August 30, 2004	\$ 29,000,000
September 30, 2004	\$ 29,000,000
October 31, 2004	\$ 29,000,000
November 30, 2004	\$ 29,000,000
December 31, 2004	\$ 29,000,000
January 31, 2005	\$ 29,000,000
February 28, 2005	\$ 29,000,000
March 31, 2005 and each month thereafter	\$ 31,000,000"

3.6. Section 4.3 (Minimum Fixed Charge Coverage Ratio) to the Credit Agreement is hereby amended and restated in its entirety as follows:

"4.3 Minimum Fixed Charge Coverage Ratio. Borrower and its Subsidiaries shall have on a consolidated basis at the end of each month set forth below, a Fixed Charge Coverage Ratio for the 12-month period then ended of not less than the following:

2.3 to 1.0 for the month ending December 31, 2002;
2.3 to 1.0 for the month ending January 31, 2003;
2.3 to 1.0 for the month ending February 28, 2003;
2.5 to 1.0 for the month ending March 31, 2003;
2.5 to 1.0 for the month ending April 30, 2003;
2.5 to 1.0 for the month ending May 31, 2003;
2.5 to 1.0 for the month ending June 30, 2003;
2.5 to 1.0 for the month ending July 31, 2003;
2.5 to 1.0 for the month ending August 31, 2003;
2.6 to 1.0 for the month ending September 30, 2003;
2.6 to 1.0 for the month ending October 31, 2003;
2.6 to 1.0 for the month ending November 30, 2003;
2.7 to 1.0 for the month ending December 31, 2003; and
3.0 to 1.0 for each month ending thereafter."

3.7. Section 4.4 (Minimum Interest Coverage Ratio) to the Credit Agreement is hereby amended and restated in its entirety as follows:

"4.4 Minimum Interest Coverage Ratio. Borrower and its Subsidiaries on a consolidated basis shall have at the end of each and every month, an Interest Coverage Ratio for the 12-month period then ended of not less than 3.00 to 1.0."

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3.8. Section 4.5 (Maximum Leverage Ratio) to the Credit Agreement is hereby amended and restated in its entirety as follows:

"4.5 Maximum Leverage Ratio. Borrower and its Subsidiaries on a consolidated basis shall have, at the end of each month set forth below, a Leverage Ratio as of the last day of such month and for the 12-month period then ended of not more than the following:

1.75 to 1.0 for the month ending December 31, 2002;
1.75 to 1.0 for the month ending January 31, 2003;
1.75 to 1.0 for the month ending February 28, 2003;

1.75 to 1.0 for the month ending March 31, 2003;
2.20 to 1.0 for the month ending April 30, 2003;
2.20 to 1.0 for the month ending May 31, 2003;
2.20 to 1.0 for the month ending June 30, 2003;
2.20 to 1.0 for the month ending July 31, 2003;
2.20 to 1.0 for the month ending August 31, 2003;
2.10 to 1.0 for the month ending September 30, 2003;
2.10 to 1.0 for the month ending October 31, 2003;
2.10 to 1.0 for the month ending November 30, 2003;
1.50 to 1.0 for the month ending December 31, 2003;
1.50 to 1.0 for the month ending January 31, 2004;
1.50 to 1.0 for the month ending February 28, 2004;
1.50 to 1.0 for the month ending March 31, 2004;
1.50 to 1.0 for the month ending April 30, 2004;
1.50 to 1.0 for the month ending May 31, 2004;
1.50 to 1.0 for the month ending June 30, 2004;
1.50 to 1.0 for the month ending July 31, 2004;
1.50 to 1.0 for the month ending August 31, 2004;
1.25 to 1.0 for the month ending September 30, 2004; and
1.25 to 1.0 for each month ending thereafter."

3.9. Section 4.6(1) (Compliance and Excess Cash Flow Certificate) to the Credit Agreement is hereby amended by deleting the parenthetical "(but only to the extent delivered at the end of a month that is also the end of a Fiscal Quarter or Fiscal Year)" in its entirety.

3.10. Schedule 2 to Exhibit 4.6(1) (Excess Cash Flow) to the Credit Agreement is hereby amended by: (a) adding the following to "decreases in Working Capital during the Fiscal Year*" (an item under the heading "Plus:"):

", excluding decreases in Working Capital related solely to the treatment of the Emcor Sale and discontinued operations";

and

(b) adding the following parenthetical following the words "Funded Debt" in the third item under the heading "Less:"

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"(excluding payments paid in 2002 prior to the Closing Date in respect of Funded Debt in connection with the Emcor Sale)"

3.11. Annex B to the Credit Agreement (Pro Rata Shares and Commitment Amounts) is hereby amended by deleting existing Annex B in its entirety and replacing it with new Annex B which is attached hereto as Exhibit A.

4. Representations and Warranties of Borrower and Credit Parties. Borrower and each Credit Party hereby represents and warrants that:

4.1 The execution, delivery and performance by it of this Amendment has been duly authorized by all necessary corporate action, including, without limitation, all necessary action by its Board of Directors and stockholders, and that this Amendment is a legal, valid and binding obligation of it, enforceable against it in accordance with its terms, except as the enforcement hereof may be subject to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar law affecting creditors' rights generally or to general principles of equity.

4.2 The execution, delivery and performance of this Amendment by Borrower does not, and will not, contravene or conflict with any provision of (i) law, (ii) any judgment, decree or order, or (iii) the certificate or articles of incorporation or by-laws of such Credit Party, and does not, and will not, contravene or conflict with, or cause any Lien to arise under, any provision of any agreement, mortgage, lease, instrument or other document binding upon or otherwise affecting Borrower, any other Credit Party or any of their respective Subsidiaries or any property of Borrower, any other Credit Party or any of their respective Subsidiaries.

4.3 All of the representations and warranties contained in the Credit Agreement and each other Loan Document are true and correct in all material respects on and as of the date hereof as if made on the date hereof. No Default or Event of Default exists under the Credit Agreement or any other Loan

Document or will exist after or be triggered by the execution and delivery of this Amendment or the consummation of the transactions contemplated hereby. In addition, each Credit Party represents and warrants that the Credit Agreement and each of the other Loan Documents remains in full force and effect and each is hereby ratified and confirmed in all respects.

5. Conditions Precedent to Effectiveness. The effectiveness of each of the waiver set forth in Section 2 and the amendments set forth in Section 3 hereof is subject to the satisfaction of each of the following conditions precedent in a manner acceptable to Agent:

5.1. Documentation. Borrower shall have delivered to Agent all of the following, each duly executed and dated the date hereof, in form and substance satisfactory to the Agent:

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- (a) Amendment. Counterparts of this Amendment, duly executed by the Borrower, each of the other Credit Parties, Agent and all of the Lenders;
- (b) New Notes. (i) A replacement Revolving Note of Borrower in favor of GE Capital (the "GE Capital Replacement Revolving Note"), substantially in the form set forth as Exhibit B hereto, delivered to the Agent for the Account of GE Capital, as a Lender, in an amount equal to its Revolving Loan Commitment of \$29,333,333, (ii) a replacement Revolving Note of Borrower in favor of Bank of Texas (the "Bank of Texas Replacement Revolving Note"), substantially in the form set forth as Exhibit B hereto, delivered to the Agent for the account of Bank of Texas, as a Lender, in an amount equal to its Revolving Loan Commitment of \$5,333,333, (iii) a replacement Revolving Note of Borrower in favor of Regions Bank (the "Regions Bank Replacement Revolving Note" and together with the GE Capital Replacement Revolving Note and the Bank of Texas Replacement Revolving Note, the "New Notes"), substantially in the form set forth as Exhibit B hereto, delivered to the Agent for the account of Regions Bank, as a Lender, in an amount equal to its Revolving Loan Commitment of \$5,333,333. Upon receipt of the GE Capital Replacement Revolving Note, GE Capital shall promptly thereafter return to Borrower for cancellation the original Revolving Note payable to GE Capital in the maximum principal amount of \$44,000,000. Upon receipt of the Bank of Texas Replacement Revolving Note, the Bank of Texas shall promptly thereafter return to Borrower for cancellation the original Revolving Note payable to Bank of Texas in the principal amount of \$8,000,000. Upon receipt of the Regions Bank Replacement Revolving Note, Regions Bank shall promptly thereafter return to Borrower for cancellation the original Revolving Note payable to Regions Bank in the principal amount of \$8,000,000; and
- (c) Board Resolutions. Agent shall have received resolutions of the board of directors of Borrower and each Credit Party authorizing and approving the execution, delivery and performance of this Amendment and the transactions contemplated hereby and each other agreement, document or instrument executed in connection herewith, certified as of the date of this Amendment by the secretary or assistant secretary of such Person as being in full force and effect without modification.

5.2. No Default or Event of Default. No Default or Event of Default shall have occurred and be continuing or would result from the effectiveness of this Amendment or the consummation of any of the transactions contemplated thereby.

5.3. Amendment Fee. Borrower shall pay to Agent, for the account of the Lenders, an amendment fee in an amount equal to \$562,500, to be distributed pro rata to all Lenders based on each Lender's Commitments immediately prior to the effectiveness of this Amendment.

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6. Reference to and Effect Upon the Credit Agreement and other Loan Agreements.

6.1. Except as specifically amended in Section 3 above, the Credit Agreement and each other Loan Document shall remain in full force and effect and is hereby ratified and confirmed.

6.2. The execution, delivery and effect of this Amendment shall be limited precisely as written and shall not be deemed to (i) be a consent to any waiver of any term or condition, or to any amendment or modification of any term or condition (except as specifically waived in Section 2 above or amended in Section 3 above), of the Credit Agreement or any other Loan Document or (ii) prejudice any right, power or remedy which the Agent or any Lender now has or may have in the future under or in connection with the Credit Agreement or any other Loan Document. Each reference in the Credit Agreement to "this Agreement", "hereunder", "hereof", "herein" or any other word or words of similar import shall mean and be a reference to the Credit Agreement as amended hereby, and each reference in any other Loan Document to the Credit Agreement or any word or words of similar import shall be and mean a reference to the Credit Agreement as amended hereby.

7. Acknowledgment and Consent of Credit Parties. Each Credit Party hereby consents to this Amendment and hereby confirms and agrees that (a) the Guaranty and each other Loan Document to which it is a party is, and shall continue to be, in full force and effect and is hereby ratified and confirmed in all respects, and (b) the Collateral Documents to which such Credit Party is a party and all of the Collateral described therein do, and shall continue to, secure the payment of all of the Obligations.

8. Counterparts. This Amendment may be executed in any number of counterparts, each of which when so executed shall be deemed an original but all such counterparts shall constitute one and the same instrument. Delivery of an executed counterpart of a signature page to this Amendment by telecopier shall be as effective as delivery of a manually executed counterpart signature page to this Amendment.

9. Costs and Expenses. As provided in Section 1.3 of the Credit Agreement, Borrower shall pay the fees, costs and expenses incurred by Agent in connection with the preparation, execution and delivery of this Amendment (including, without limitation, reasonable attorneys' fees).

10. GOVERNING LAW. THIS AMENDMENT SHALL BE GOVERNED BY AND CONSTRUED AND ENFORCED IN ACCORDANCE WITH THE INTERNAL LAWS (AS OPPOSED TO CONFLICTS OF LAW PROVISIONS) OF THE STATE OF NEW YORK.

11. Headings. Section headings in this Amendment are included herein for convenience of reference only and shall not constitute a part of this Amendment for any other purpose.

[Signature Pages Follow]

IN WITNESS WHEREOF, this Amendment has been duly executed as of the date first written above.

BORROWER:

COMFORT SYSTEMS USA, INC.

By: _____
Name: _____
Title: _____

CREDIT PARTIES:

ACI MECHANICAL, INC.

ARC COMFORT SYSTEMS USA, INC.

ACCURATE AIR SYSTEMS, L.P., by
Atlas-Accurate Holdings, L.L.C.,
as General Partner

ACCU-TEMP GP, INC.

ACCU-TEMP LP, INC.

ACCU-TEMP LLC,
by Accu-Temp GP, Inc., as acting member

AIR SOLUTIONS USA, INC.

AIR TEMP, INC.

ATLAS-ACCURATE HOLDINGS, L.L.C.,
by CS53 Acquisition Corp.,
as acting member

ATLAS AIR CONDITIONING
COMPANY, L.P., by Atlas-Accurate
Holdings, L.L.C., as general partner

BATCHELOR'S MECHANICAL CONTRACTORS, INC.

BCM CONTROLS CORPORATION

CARSON BROTHERS, INC.

CEL, INC.

CENTRAL MECHANICAL, INC.

COMFORT SYSTEMS USA (ARKANSAS), INC.

COMFORT SYSTEMS USA (BALTIMORE), INC.

10

COMFORT SYSTEMS USA (BOWLING GREEN), INC.

COMFORT SYSTEMS USA (BRISTOL), INC.

COMFORT SYSTEMS USA (CLEVELAND), INC.

COMFORT SYSTEMS USA (FLORIDA), INC.

COMFORT SYSTEMS USA G.P., INC.

COMFORT SYSTEMS US (HARTFORD), INC.

COMFORT SYSTEMS USA (INTERMOUNTAIN), INC.

COMFORT SYSTEMS USA NATIONAL SERVICE ORGANIZATION, INC.

COMFORT SYSTEMS USA (OREGON), INC.

COMFORT SYSTEMS USA (SOUTH BOSTON), INC.

COMFORT SYSTEMS USA (SYRACUSE), INC.

COMFORT SYSTEMS USA (TEXAS), L.P.,
by Comfort Systems USA G.P., Inc.,
as general partner

COMFORT SYSTEMS USA (TWIN CITIES), INC.
COMFORT SYSTEMS USA (WESTERN MICHIGAN), INC.
CS44 ACQUISITION CORP.
CS53 ACQUISITION CORP.
DESIGN MECHANICAL INCORPORATED

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EASTERN HEATING & COOLING, INC.
ESS ENGINEERING, INC.
GULFSIDE MECHANICAL, INC.
H & M MECHANICAL, INC.
HELM CORPORATION
HELM CORPORATION SAN DIEGO
HESS MECHANICAL CORPORATION
INDUSTRIAL COOLING INC.
J & J MECHANICAL, INC.
JAMES AIR CONDITIONING ENTERPRISE INC.
MARTIN HEATING, INC.
MECHANICAL SERVICE GROUP, INC.
MECHANICAL TECHNICAL
SERVICES, L.P., by Atlas-Accurate
Holdings, L.L.C., as general partner
MJ MECHANICAL SERVICES, INC.
NEEL MECHANICAL CONTRACTORS, INC.
NORTH AMERICAN MECHANICAL, INC.
OK SHEET METAL AND AIR CONDITIONING, INC.
QUALITY AIR HEATING & COOLING, INC.
S&K AIR CONDITIONING CO., INC.
S. I. GOLDMAN COMPANY, INC.

12

S.M. LAWRENCE COMPANY, INC.
SA ASSOCIATES, INC.
SALMON & ALDER, LLC,
by SA Associates, Inc., as acting member
SEASONAIR, INC.
SHEREN PLUMBING & HEATING, INC.
STANDARD HEATING & AIR CONDITIONING COMPANY
SUPERIOR MECHANICAL SYSTEMS, INC.
TARGET CONSTRUCTION, INC.

TEMP-RIGHT SERVICE, INC.

THE CAPITAL REFRIGERATION COMPANY

TRI-CITY MECHANICAL, INC.

UNITED ENVIRONMENTAL
SERVICES, L.P., by Atlas-Accurate Holdings,
L.L.C., as general partner

WEATHER ENGINEERING, INC.

WESTERN BUILDING SERVICES, INC.

By: _____
Name: _____
Title: _____

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GENERAL ELECTRIC CAPITAL CORPORATION,
as Agent and a Lender

By: _____
Its Duly Authorized Signatory

14

BANK OF TEXAS, NA, as a Lender

By: _____
Name: _____
Title: _____

15

REGIONS BANK, as a Lender

By: _____
Name: _____
Title: _____

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ANNEX B (FROM ANNEX A - COMMITMENTS DEFINITION)
to
CREDIT AGREEMENT

PRO RATA SHARES AND COMMITMENT AMOUNTS

Commitment -----	Lender -----
Revolving Loan Commitment (including a Swing Line Commitment of \$5,000,000) \$29,333,333	GENERAL ELECTRIC CAPITAL CORPORATION
Revolving Loan Commitment \$5,333,333	BANK OF TEXAS, NA
Revolving Loan Commitment \$5,333,333	REGIONS BANK
Term Loan Commitment: \$11,000,000	GENERAL ELECTRIC CAPITAL CORPORATION
Term Loan Commitment: \$2,000,000	BANK OF TEXAS, NA
Term Loan Commitment: \$2,000,000	REGIONS BANK

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EXHIBIT B
TO AMENDMENT NO. 3

REVOLVING NOTE

\$ _____,000,000

New York, New York
March _____, 2003
--

FOR VALUE RECEIVED, the undersigned, COMFORT SYSTEMS USA, INC. ("Borrower"), HEREBY PROMISES TO PAY to the order of _____ ("Lender"), at the offices of GENERAL ELECTRIC CAPITAL CORPORATION, a Delaware corporation, as Agent for Lenders ("Agent"), at its address at 335 Madison Avenue, New York, New York 10017 or at such other place as Agent may designate from time to time in writing, in lawful money of the United States of America and in immediately available funds, the amount of _____ Million Dollars (\$____,000,000) or, if less, the aggregate unpaid amount of all Revolving Credit Advances made to the undersigned under the "Credit Agreement" (as hereinafter defined). All capitalized terms used but not otherwise defined herein have the meanings given to them in the Credit Agreement or in Annex A thereto.

This Revolving Note is one of the Revolving Notes issued pursuant to that certain Credit Agreement dated as of October 11, 2002 by and among the Borrower, the other Persons named therein as Credit Parties, Agent, Lender and the other Persons signatory thereto from time to time as Lenders (including all annexes, exhibits and schedules thereto, and as amended by Amendment No. 1 to Credit Agreement, dated as of December 10, 2002, Amendment No. 2 to Credit Agreement, dated as of December 20, 2002, and Waiver and Amendment No. 3 to Credit Agreement dated as of the date hereof, and as the same may be further amended, restated, supplemented or otherwise amended from time to time, the "Credit Agreement"), and is entitled to the benefit and security of the Credit Agreement, the Security Agreement and all of the other Loan Documents referred to therein. Reference is hereby made to the Credit Agreement for a statement of all of the terms and conditions under which the Loans evidenced hereby are made and are to be repaid. The date and amount of each Revolving Credit Advance made by Lenders to Borrower, the rates of interest applicable thereto and each

payment made on account of the principal thereof, shall be recorded by Agent on its books; provided that the failure of Agent to make any such recordation shall not affect the obligations of Borrower to make a payment when due of any amount owing under the Credit Agreement or this Note in respect of the Revolving Credit Advances made by Lender to Borrower.

The principal amount of the indebtedness evidenced hereby shall be payable in the amounts and on the dates specified in the Credit Agreement, the terms of which are hereby incorporated herein by reference. Interest thereon shall be paid until such principal amount is paid in full at such interest rates and at such times, and pursuant to such calculations, as are specified in the Credit Agreement.

If any payment on this Revolving Note becomes due and payable on a day other than a Business Day, the maturity thereof shall be extended to the next succeeding Business Day and, with respect to payments of principal, interest thereon shall be payable at the then applicable rate during such extension.

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Upon and after the occurrence of any Event of Default, this Revolving Note may, as provided in the Credit Agreement, be declared, and immediately shall become, due and payable.

Time is of the essence of this Revolving Note. Demand, presentment, protest and notice of nonpayment and protest are hereby waived by Borrower.

Except as provided in the Credit Agreement, this Revolving Note may not be assigned by Lender to any Person.

[signature page follows]

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THIS REVOLVING NOTE SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK APPLICABLE TO CONTRACTS MADE AND PERFORMED IN THAT STATE.

COMFORT SYSTEMS USA, INC.

By: _____
Name: _____
Title: _____

COMFORT SYSTEMS USA, INC.
LIST OF SUBSIDIARIES

ENTITY NUMBER -----	NAME OF ENTITY -----	STATE OF ORGANIZATION -----
1.	ACI Mechanical, Inc.	Delaware
2.	ACI Mechanical USA, Inc. (formerly Comfort Systems USA (Oregon), Inc.)	
3.	ARC Comfort Systems USA, Inc. (formerly American Refrigeration Contractors, Inc.)	Delaware
4.	Accurate Air Systems, L.P.	Texas
5.	Accu-Temp GP, Inc.	Delaware
6.	Accu-Temp LP, Inc.	Delaware
7.	Accu-Temp, LLC	Indiana
8.	Air Solutions USA, Inc.	Delaware
9.	Air Temp, Inc.	Delaware
10.	American Refrigeration Contractors, Inc. (Name Hold)	California
11.	Atlas-Accurate Holdings, L.L.C.	Delaware
12.	Atlas Air Conditioning Company, L.P.	Texas
13.	Batchelor's Mechanical Contractors, Inc.	Alabama
14.	BCM Controls Corporation	Massachusetts
15.	CEL, Inc. (Casey Electric)	Delaware
16.	Central Mechanical, Inc.	Delaware
17.	Climate Control, Inc. (formerly Comfort Systems USA (South Boston), Inc.)	Delaware
18.	Comfort Systems USA (Arkansas), Inc. (formerly River City Mechanical, Incorporated)	Delaware
19.	Comfort Systems USA (Baltimore), Inc.	Delaware
20.	Comfort Systems USA (Bowling Green), Inc. (formerly Southern Bluegrass Mechanical, Inc.)	Delaware
21.	Comfort Systems USA (Bristol), Inc. (formerly Fred Hayes Mechanical Contractors, Inc.-Delaware)	Delaware
22.	Comfort Systems USA (Cleveland), Inc. (formerly Tech Heating and Air Conditioning, Inc..)	Ohio
23.	Comfort Systems USA (Florida), Inc. (formerly The Drake Corporation--All Temp Services, Inc. merged into it)	Florida
24.	Comfort Systems USA G.P., Inc.	Delaware
25.	Comfort Systems USA (Hartford), Inc. (formerly The Harvey Robbin Company)	
26.	Comfort Systems USA (Intermountain), Inc. (formerly Contract Service, Inc merged with Freeway Heating & Air Conditioning, Inc.)	Utah
27.	Comfort Systems USA National Service Organization, Inc.	Delaware
28.	Comfort Systems USA (Syracuse), Inc. (formerly Armani Plumbing & Mechanical, Inc.)	New York
29.	Comfort Systems USA (Western Michigan), Inc. (reorganization of River City Mechanical, Inc. and H&H Plumbing & Heating, Inc.)	Michigan
30.	Comfort Systems USA (Texas), L.P.	Texas
31.	Comfort Systems USA (Twin Cities), Inc. (formerly EDS, Inc./Energy Development Services)	Minnesota

COMFORT SYSTEMS USA, INC.
LIST OF SUBSIDIARIES

ENTITY NUMBER -----	NAME OF ENTITY -----	STATE OF ORGANIZATION -----
32.	CS44 Acquisition Corp. [Edmonds/Service Refrigeration]	Delaware
33.	CS53 Acquisition Corp. (Mgm Member Atlas-Accurate)	Delaware
34.	Design Mechanical Incorporated	Delaware
35.	Eastern Heating & Cooling, Inc.	New York
36.	Eastern Refrigeration Co., Inc.	New York
37.	ESS Engineering, Inc.	Delaware
38.	FIX Reinsurance Corporation	Vermont
39.	Fred Hayes Mechanical Contractors, Inc. (Name Hold)	Virginia
40.	Gulfside Mechanical, Inc.	Delaware
41.	H & M Mechanical, Inc.	Delaware
42.	Helm Corporation	Colorado
43.	Helm Corporation San Diego	California
44.	Hess Mechanical Corporation	Delaware
45.	Industrial Cooling Inc.	Delaware
46.	J & J Mechanical, Inc.	Kentucky
47.	James Air Conditioning Enterprise Inc.	Puerto Rico
48.	Martin Heating, Inc.	Wyoming
49.	MDC Service Corporation (Name Hold)	California
50.	Mechanical Service Group, Inc. [Page]	Delaware
51.	Mechanical Technical Services, L.P.	Texas
52.	MJ Mechanical Services, Inc.	Delaware
53.	Neel Mechanical Contractors, Inc.	Delaware
54.	North American Mechanical, Inc.	Delaware
55.	OK Sheet Metal and Air Conditioning, Inc.	Delaware
56.	Plant Services Incorporated	Iowa
57.	Quality Air Heating & Cooling, Inc.	Michigan
58.	S&K Air Conditioning Co., Inc.	Georgia
59.	S. I. Goldman Company, Inc.	Delaware
60.	S.M. Lawrence Company, Inc.	Tennessee
61.	SA Associates, Inc. (fka Salmon & Alder, Inc.)	Utah
62.	Salmon & Alder, LLC	Utah
63.	Seasonair, Inc.	Maryland
64.	Sheren Plumbing & Heating, Inc.	Delaware
65.	Standard Heating & Air Conditioning Company	Alabama
66.	Superior Mechanical Systems, Inc. (formerly Superior Heating and Sheet Metal Company)	Delaware
67.	Target Construction, Inc.	Delaware
68.	Temp-Right Service, Inc.	Delaware
69.	The Capital Refrigeration Company	Delaware
70.	Tri-City Mechanical, Inc.	Arizona

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COMFORT SYSTEMS USA, INC.
LIST OF SUBSIDIARIES

ENTITY NUMBER -----	NAME OF ENTITY -----	STATE OF ORGANIZATION -----
71.	United Environmental Services, L.P.	Texas
72.	Weather Engineering, Inc.	Delaware
73.	Western Building Services, Inc.	Colorado

CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in each of the following Registration Statements of Comfort Systems USA, Inc. and in each related Prospectus of our report dated March 28, 2003 with respect to the consolidated financial statements of Comfort Systems USA, Inc. included in the Annual Report (Form 10-K) for the three years ended December 31, 2002.

Registration Statement No. -----	Purpose -----
No. 333-38011	Registration Statement on Form S-8
No. 333-75595	Registration Statement on Form S-4
No. 333-44352	Registration Statement on Form S-8
No. 333-44354	Registration Statement on Form S-8
No. 333-44356	Registration Statement on Form S-8

Houston, Texas
March 31, 2003

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K for the period ending December 31, 2002 of Comfort Systems USA, Inc. (the "Company") as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, William F. Murdy, Chairman of the Board and Chief Executive Officer of the Company, certify that, to my knowledge, (i) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ William F. Murdy

William F. Murdy
Chairman of the Board and
Chief Executive Officer
(Principal Executive Officer)

March 31, 2003

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K for the period ending December 31, 2002 of Comfort Systems USA, Inc. (the "Company") as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, J. Gordon Beittenmiller, Vice President and Chief Financial Officer of the Company, certify that, to my knowledge, (i) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ J. Gordon Beittenmiller

J. Gordon Beittenmiller
Vice President and
Chief Financial Officer
(Principal Financial Officer)

March 31, 2003