SPORTS AUTHORITY INC /DE/
Form 11-K
June 29, 2005

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THE SPORTS AUTHORITY 401(k) RETIREMENT PLAN FINANCIAL STATEMENTS AND SUPPLEMENTAL SCHEDULES As of December 31, 2004 and 2003 and for the Year ended December 31, 2004

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 11-K

(Mark One)

ý **ANNUAL REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [FEE REQUIRED]**

For the fiscal year ended December 31, 2004

OR

o **TRANSITION REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [NO FEE REQUIRED]**

Commission File No. 001-31746

A. Full title of the plan and address of the plan, if different from that of the issuer named below:

The Sports Authority 401(k) Retirement Plan

B. Name of issuer of the securities held pursuant to the plan and the address of its principal executive office:

The Sports Authority, Inc.

1050 West Hampden Avenue,
Englewood, Colorado 80110

(303) 200-5050
(Registrant's telephone number, including area code)

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, The Sports Authority, Inc., as plan administrator, has duly caused this Annual Report to be signed by the undersigned thereunto duly authorized.

	THE SPORTS AUTHORITY, INC.	
Date: June 29, 2005	By:	/s/ THOMAS T. HENDRICKSON
		Chief Financial Officer, Chief Administrative Officer and Treasurer

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THE SPORTS AUTHORITY 401(k) RETIREMENT PLAN
FINANCIAL STATEMENTS AND SUPPLEMENTAL SCHEDULES
As of December 31, 2004 and 2003 and for the Year ended December 31, 2004

Contents

REPORT OF REGISTERED PUBLIC ACCOUNTING FIRM

Participants and Administrator of
The Sports Authority 401(k) Retirement Plan

We have audited the accompanying statements of net assets available for benefits of The Sports Authority 401(k) Retirement Plan (the "Plan") as of December 31, 2004 and 2003, and the related statement of changes in net assets available for benefits for the year ended December 31, 2004. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Plan is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Plan's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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, such financial statements present fairly, in all material respects, the net assets available for benefits of the Plan as of December 31, 2004 and 2003, and the changes in net assets available for benefits for the year ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedules of (1) schedule of assets (held at end of year) as of December 31, 2004, and (2) Delinquent Participant Contributions for the year ended December 31, 2004 are presented for the purpose of additional analysis and are not a required part of the basic financial statements, but are supplementary information required by the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. These schedules are the responsibility of the Plan's management. Such schedules have been subjected to the auditing procedures applied in our audit of the basic 2004 financial statements and, in our opinion, are fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

DELOITTE & TOUCHE LLP

Denver, CO
June 28, 2005

THE SPORTS AUTHORITY 401(k) RETIREMENT PLAN

STATEMENTS OF NET ASSETS AVAILABLE FOR BENEFITS

	December 31,	
	2004	**2003**
Assets		
Investments, at fair value	$ 53,443,265	$ 37,878,976
Receivables:		
Contributions from plan participants	138,388	105,883
Contributions from employer	65,274	60,321
Total receivables	203,662	166,204
Total assets	53,646,927	38,045,180
Liabilities		
Excess contributions payable	459,530	
Net assets available for benefits	$ 53,187,397	$ 38,045,180

See accompanying notes to financial statements.

THE SPORTS AUTHORITY 401(k) RETIREMENT PLAN

STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

YEAR ENDED DECEMBER 31, 2004

Additions	
Investment income:	
Net appreciation in fair value of investments	$ 87,677
Interest income and other income	407,694
Net investment income	495,371
Contributions:	
From plan participants	4,477,795
From employer	2,015,152
From rollovers and other	204,062
Total contributions	6,697,009
Transfer of plan assets from Gart Sports Company Savings Plan	19,080,037
Total additions	26,272,417
Deductions	
Benefit payments	10,973,349
Administrative fees	156,851
Total deductions	11,130,200
Increase in net assets available for benefits	15,142,217
Net assets available for benefits at beginning of year	38,045,180
Net assets available for benefits at end of year	$ 53,187,397

See accompanying notes to financial statements.

THE SPORTS AUTHORITY 401(k) RETIREMENT PLAN

NOTES TO FINANCIAL STATEMENTS

December 31, 2004

NOTE 1 PLAN DESCRIPTION

On August 4, 2003, a wholly-owned subsidiary of Gart Sports Company completed a merger with The Sports Authority, Inc. (TSA), and Gart Sports Company was renamed The Sports Authority, Inc. The references made to the entities herein refer to The Sports Authority, Inc. (formerly Gart Sports Company, which is also referred to as "Sports Authority" or "Company"). TSA refers to the former The Sports Authority, Inc. In connection with the merger, the Company adopted TSA's 401(k) Savings and Profit Sharing Plan (the "Plan"). On January 1, 2004, the Gart Sports Company Savings Plan was merged into the Plan and renamed The Sports Authority, Inc. 401(k) Retirement Plan (the "Retirement Plan"), covering employees of the combined companies. The following provides a description of the Company's Retirement Plan, as well as significant changes resulting from the merger of the Plan into the Retirement Plan on January 1, 2004. This description provides only general information and participants should refer to the various plan documents for a more complete description of plan provisions.

General

The Plan is a voluntary, defined contribution plan available to TSA employees through December 31, 2003 and the Company's employees for the year ended December 31, 2004. Prior to the merger, employees were eligible to participate in the Plan upon attaining 21 years of age and completion of 1,000 hours of service within a 12-month period. Following the merger of the Plan into the Retirement Plan, full-time and part-time employees of the Company are eligible to participate in the Retirement Plan if they are 21 years of age or older and have completed three months of service with the Company.

The Plan and the Retirement Plan are subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

For the 2003 plan year, Cigna Retirement and Investment Services ("Cigna") acted as the trustee and recordkeeper, of the Plan. Cigna remained as recordkeeper and trustee of the Retirement Plan. Following its acquisition of Cigna in April 2004, Prudential Retirement, a business of Prudential Financial, Inc., became the recordkeeper and trustee of the Retirement Plan. The plans' administrator since the August 4, 2003 merger date is the Company's 401(k) Fiduciary Committee.

Contributions

In January 2003, the Plan was amended to provide for before-tax contributions only. Additionally, the amendment increased TSA's matching contribution to 100 percent of the first three percent of eligible compensation contributed by participants, and 50 percent of the next two percent of compensation. As a result of this amendment and the increase in TSA's matching contribution, the Plan became a Safe Harbor plan in 2003. In addition to matching contributions, the Plan and Retirement Plan provide for discretionary employer contributions to a participant's accounts. No discretionary contributions were made in 2004.

Following the merger of the plans, participants may contribute up to 15% of compensation on a before-tax basis. The Company matches 100% of participant contributions, up to a maximum of 3% of compensation. The Retirement Plan is not a Safe Harbor plan.

Under both the Plan and the Retirement Plan, participants may elect to change daily the amount of employee contributions made, as well as change the percentage allocated to each fund. Participants may also elect to discontinue contributions immediately with proper notification to the plan administrator, and may subsequently resume contributions without penalty. Prior to the August 4, 2003 merger date, participants could elect to invest some or all their account balance in TSA's common stock. This investment alternative was discontinued upon the merger.

Vesting

Under the Plan, participants vested 100% in employee contributions and related investment earnings, as well as 100% in TSA matching contributions. Under the Retirement Plan, participants vest 100% in employee contributions and related investment earnings, and generally vest in Company contributions at the rate of 20% per year of service with full vesting after five years; however, former TSA employees who remained employed with the Company following the merger vested 100% in Company matching contributions under a grandfather provision as of the date of the merger.

Investments

Participants direct the investment of their contributions into various investment options offered by the Retirement Plan. Company contributions made on behalf of the participant are invested in the Retirement Plan according to each participant's currently effective investment election. The Retirement Plan currently offers 17 mutual funds as investment options for participants.

Participant Accounts

Each participant's account is credited with the participant's contributions, matching and discretionary employer contributions, allocated investment earnings and administrative expenses. Allocations are based on the participant's account balances or earnings. The benefit to which a participant is entitled is equal to the vested balance in the participant's account.

Payment of Benefits

Following the merger of the plans, a participant is permitted to make cash withdrawals from his account while still employed by the Company in the following events: (i) the participant has attained the age of $59^1/_2$, (ii) the participant has met the hardship rules as defined in the Retirement Plan, or (iii) the withdrawal relates to contributions which were designated as after-tax contributions under the Plan or other previously-merged plans, or were rollover contributions from another plan.

Upon termination of employment, the participant may elect to receive partial or full distribution of his vested account balance. Such distribution may be subject to an early withdrawal payment of 10% under the provisions of the Internal Revenue Code. In the event the participant does not elect to receive a distribution of his account balance, the balance will be paid out on April 1 of the calendar year following the calendar year in which the participant attains the age of $70^1/_2$. Withdrawals and distributions are paid in cash, except where the participant elects to take the distribution in stock to the extent that the participant's account consists of shares of Company common stock. Participant account balances of less than $5,000 are distributed automatically on termination. Effective March 28, 2005, participant account balances of less than $1,000 are distributed automatically on termination.

Participant Loans

Participants may request a loan from their account balance subject to certain conditions, including a minimum loan of $1,000 and a maximum loan not to exceed the lesser of $50,000 or 50% of the participant's vested balance. No more than one loan may be outstanding to any participant at any time. The term of any loan shall range from one to five years, except loans for the purpose of purchasing a primary residence, which may be for a maximum of 15 years under the Retirement Plan. Participant loans originating under the Plan bear interest at the prime rate, while loans made under the

Retirement Plan bear interest at the prime rate plus one percent. Principal and interest is paid ratably through payroll deductions.

Profit Sharing Provisions

The Plan included a profit-sharing benefit whereby all eligible employees of TSA received employer contributions equal to at least one percent of their eligible compensation for each year. Profit-sharing contributions were invested in The Sports Authority Common Stock Fund until the employee fully vested, at which time the investment could be redirected by the participant. Vesting in TSA's profit sharing contribution was not accelerated upon change in control from the TSA merger, and accordingly the five-year service requirement under the Plan is still applicable. As a result of the increase in employer matching 401(k) contributions and the conversion to a Safe Harbor plan in 2003, profit sharing contributions were discontinued in 2003. Existing account balances invested in TSA common stock were converted at the merger date into common stock of the new Sports Authority consistent with the exchange ratio of 0.37 of new Sports Authority stock for each share of TSA common stock.

The Retirement Plan does not contain a profit-sharing provision.

Forfeitures

Forfeitures are used to reduce the Company's 401(k) or profit sharing contributions and, if so elected by the Company, to reduce administrative expenses. Forfeitures of $285,515 were used to reduce Company contributions for the year ended December 31, 2004. The amount of forfeitures available to reduce future contributions or administrative expenses were $6,989 and zero as of December 31, 2004 and December 31, 2003, respectively.

Plan Expenses

Expenses of administering the Retirement Plan may be paid by either the employer or by the Retirement Plan. For the year ended December 31, 2004, the Company paid approximately $4,000 in fees. Other administrative fees, processing fees for loans, in-service withdrawals and other services, commissions and transaction charges are charged to the participants' accounts.

Plan Termination

Although it has not expressed any intent to do so, the Company has the right under the Retirement Plan to discontinue its contributions and to terminate the plan subject to the provisions of ERISA. In the event of plan termination, participants will become 100% vested in both 401(k) and profit sharing contributions made by the Company.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements are prepared on the accrual basis of accounting.

Use of Estimates The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Investment Valuation and Income Recognition Investments are stated at fair value. Common stock is valued at the quoted market price. Mutual funds are valued at quoted market prices, which represent the net asset values of shares held at year-end. Participant loans are valued at their outstanding balances, which approximates fair value.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

Excess Contributions Payable The Retirement Plan is required to return contributions received during the year in excess of the Internal Revenue Code limits. Contribution refunds payable to participants because of non-discrimination testing results as of December 31, 2004 are $459,530 and are included on the statement of assets available for benefits.

Risks Investments are exposed to various risks, such as interest rate, market and credit. These risks could result in a material effect on participant account balances and the amounts reported in the statements of net assets available for benefits and the statements of changes in net assets available for benefits.

NOTE 3 INVESTMENTS

The fair value of individual investments that represent 5% or more of net assets available for benefits as of December 31, 2004 and 2003, are as follows:

	December 31,	
	2004	**2003**
Prudential Retirement Insurance & Annuity Co.:		
Guaranteed Income Fund	$ 9,498,652	$ 5,777,336
Oakmark Equity & Income CL 1	7,348,641	4,645,271
Large Cap Value Fund/Wellington Management	11,011,270	8,425,010
Mid Cap Value Fund/Wellington Management	3,347,150	2,885,025
Dryden S&P Index Fund	3,578,985	
Core Plus Bond/PIMCO Fund	3,105,367	
The Sports Authority, Inc.		
Common Stock *	6,580,744	12,786,773

* Includes non participant-directed amounts.

Information about net assets that include non participant-directed amounts as of December 31, 2004 and 2003, and the significant changes in those assets during the year ended December 31, 2004, are as follows:

The Sports Authority, Inc. Common Stock:

Balance as of December 31, 2003	$ 12,786,773
Changes in asset balance:	
Net depreciation in fair value of investments	(3,765,816)
Loan activity	(136,282)
Administrative fees and expenses	(111,074)
Fund transfers	(214,618)
Benefit payments	(1,978,239)
Total changes	(6,206,029)
Balance as of December 31, 2004	$ 6,580,744

The Retirement Plan's investments (including investments bought, sold and held during the year) appreciated in fair value for the year ended December 31, 2004 as follows:

Mutual funds	$	3,853,493
Common stock		(3,765,816)
Net appreciation in fair value of investments	$	87,677

NOTE 4 RECONCILIATION OF FINANCIAL STATEMENTS TO FORM 5500

The following is a reconciliation of the participant loans per the financial statements to the Form 5500 as of December 31, 2004. The reconciliation is necessary, as delinquent loans are deemed distributions on the Form 5500 but not in the financial statements.

Participant loans per the financial statements	$	1,448,717
Delinquent loans deemed distributions		(2,890)
Participant loans per the Form 5500 (unaudited)	$	1,445,827

The following is a reconciliation of distributions to plan participants per the financial statements to the Form 5500 for the year ended December 31, 2004.

	Year Ended December 31, 2004	
Distributions to plan participants per the financial statements	$	10,973,349
Delinquent loans deemed distributions		2,890
Distributions to plan participants per the Form 5500 (unaudited)	$	10,976,239

NOTE 5 INCOME TAX STATUS

The Plan has received a determination letter from the Internal Revenue Service dated July 17, 2002, stating that the Plan is qualified under Section 401(a) of the Internal Revenue Code (the "Code") and, therefore, the related trust is exempt from taxation. The Plan has been amended since receiving the determination letter, and was merged into the new Retirement Plan on January 1, 2004; however, the plan administrator believes the Retirement Plan is being operated in compliance with the applicable requirements of the Code, and is therefore qualified and the related trust tax exempt. Therefore, no provision for income taxes has been included in the financial statements. The Company is currently in the process of filing with the Internal Revenue Service an application for determination of the qualified status of the Retirement Plan.

NOTE 6 EXEMPT PARTY-IN-INTEREST TRANSACTIONS

Certain Retirement Plan investments are in funds that are managed or maintained by Prudential or its subsidiaries and affiliates. Prudential is also the trustee of the fund and, therefore, these transactions qualify as party-in-interest transactions. Fees paid by the Retirement Plan for investment management services were included as a reduction of the return earned on each fund.

As of December 31, 2004 and 2003, the Retirement Plan and the Plan held 255,563 and 332,989 shares of Sports Authority common stock valued at $6,580,744 and $12,786,773, respectively. During the year ended December 31, 2004 there were no dividends from the TSA common stock.

NOTE 7 NONEXEMPT PARTY-IN-INTEREST TRANSACTION

The Company remitted certain January 2004 participant contributions of $352,855 to the trustee later than required by the D.O.L. Regulation 2510.3-102. Participant accounts were credited with the amount of investment income which would have been earned had the participant contribution been remitted on a timely basis.

THE SPORTS AUTHORITY 401(k) RETIREMENT PLAN
FORM 5500, SCHEDULE H, PART IV, LINE 4i
SCHEDULE OF ASSETS (HELD AT END OF YEAR)
December 31, 2004

(a)	(b) Identity of Issue, Borrower, Lessor or Similar Party	(c) Description of Investment Including Maturity Date, Rate of Interest, Collateral, Par or Maturity Value	(d) Cost	(e) Current Value
*	Prudential Retirement Insurance & Annuity Co.	Guaranteed Income Fund	**	$ 9,498,652
		Oppenheimer Cap Apprec CL A	**	1,081,548
		Dryden S&P Index Fund	**	3,578,985
		Mid Cap Growth/Artisan Partners	**	1,254,726
		Mid Cap Value/Wellington Management	**	3,347,150
		Small Cap Value/Perkins Wolf McDonnell	**	1,095,257
		Nations International Val CL A	**	1,403,976
		Core Plus Bond/PIMCO Fund	**	3,105,367
		Oakmark Equity & Income CL 1	**	7,348,641
		Retirement Goal Fund	**	17,831
		Retirement Goal 2010 Fund	**	36,825
		Retirement Goal 2020 Fund	**	87,993
		Retirement Goal 2030 Fund	**	59,772
		Retirement Goal 2040 Fund	**	57,785
		Large Cap Value/Wellington Management	**	11,011,270
*	Manager's Fund	Managers Special Equity	**	792,713
*	American Funds	American Funds Euro Pacific Growth	**	1,635,313
*	The Sports Authority, Inc.	Common Stock	$ 4,822,295	6,580,744
	Participant loans	Interest rates ranging from 4.75% to 10.25%, maturing from 2005 to 2018		1,448,717
	Total investments (held at end of year)			$ 53,443,265

* Denotes a party-in-interest to the Retirement Plan (Note 6).

** Cost information is not presented as investment is participant-directed.

THE SPORTS AUTHORITY 401(k) RETIREMENT PLAN
FORM 5500, SCHEDULE H, PART IV, LINE 4a
DELINQUENT PARTICIPATION CONTRIBTIONS
For The Year Ended December 31, 2004

Line 4a "Did the employer fail to transmit to the plan any participant contributions within the time period described in 29 CFR 2510.3-102", was answered "yes".

Identity of Party Involved	Relationship to Plan, Employer, or Other Party-in-Interest	Description of Transactions	Amount
The Sports Authority, Inc.	Employer/Plan Sponsor	Participant contributions for employees were not funded within the time period prescribed by D.O.L. Regulation 2510.3-102. The January 2004 participant contribution was deposited later than required.	$ 352,855

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INDEX TO EXHIBITS

Exhibits	
23.1	Consent of Deloitte & Touche LLP

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Strategic Service Initiative. Over the last two years we have made substantial incremental investments to expand our service and maintenance revenue by increasing the value we can offer to service and maintenance customers. We are actively concentrating existing and new managerial and sales resources on training and hiring experienced employees to sell and profitably perform service work. In many locations we have added or upgraded our capability, and we believe our investments and efforts are providing a compelling customer value offering that will ultimately stimulate growth in all aspects of our construction, renovation, service, and maintenance and repair businesses.

Seek Growth through Expansion and Acquisitions We believe that we can increase our cash flow and operating income by opportunistically entering new markets or service lines through expansion and acquisition. We have dedicated a significant portion of our cash flow to seeking opportunities to acquire businesses that have attractive capabilities and meet other criteria involving valuation, financial, operational, management, growth and geographic considerations.

Operations and Services Provided

We provide a wide range of construction, renovation, expansion, maintenance, repair and replacement services for mechanical and related systems in commercial, industrial and institutional properties. Our local management teams maintain responsibility for day-to-day operating decisions. Local management is augmented by regional leadership that focuses on core business competencies, regional financial performance, cooperation and coordination between locations, implementing best practices and 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 combine certain back office and administrative functions at various locations.

Construction and Installation Services for New Buildings Our installation business related to newly constructed facilities, which comprised approximately 44% of our consolidated 2015 revenue, involves the design, engineering, integration, installation and start-up of mechanical and related systems. We provide "design and build" and "plan and spec" installation services for office buildings, retail centers, apartment complexes, manufacturing plants, healthcare, education and government facilities and other commercial, industrial and institutional facilities. In a "design and build" installation, working with the customer, we determine the needed capacity and energy efficiency of the HVAC system that best suits the proposed facility. We estimate 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 plan. In "plan and spec" installation, we participate in a bid process to provide labor, equipment, materials and installation based on the end user's plans and engineering specifications.

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 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. Finally, we install the system at the project site, working closely with the owner or general contractor. Our average project takes six to nine months to complete, with an average contract price of approximately $512,000. We also perform larger project work, with 383 contracts in progress at December 31, 2015 with contract prices in excess of $1 million. Our largest project in progress at December 31, 2015 had a contract price of $24.7 million. Project contracts typically provide for periodic billings to the customer as we meet progress milestones or incur cost on the project. Project contracts in our industry also frequently allow for a small portion of progress billings or contract price to be withheld by the customer until after we have completed the work, typically for six months. Amounts withheld under this practice are known as retention or retainage.

Renovation, Expansion, Maintenance, Repair and Replacement Services for Existing Buildings Our renovation, expansion, maintenance, repair and replacement services in existing buildings comprised approximately 56% of our consolidated 2015 revenue and include the maintenance, repair, replacement, renovation, expansion, reconfiguration and monitoring of mechanical systems including HVAC systems and industrial process piping. Approximately 68% of our maintenance, repair and replacement revenue were derived from renovation, expansion, replacement and reconfiguration of existing systems for commercial, industrial and institutional customers. Renovation, expansion, replacement and reconfiguration services are typically performed on a project basis and frequently use consultative expertise similar to that provided in the "design and build" installation market.

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, industrial and institutional service agreements usually have terms of one to three years, with automatic annual renewals, and typically include thirty- to sixty-day cancellation notice periods. 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 one month or more. We estimate that direct purchase of commodities and finished products comprises between 10% and 15% of our average project cost. We have procedures to reduce commodity cost exposure; early buying of commodities for particular projects, or for general inventory, as well as including escalation and escape provisions in project bids and contracts wherever possible.

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 Carrier, Lennox, McQuay, Trane and York. 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.

Cyclicality and Seasonality

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

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 revenue and operating results generally will be lower in the first calendar quarter.

Sales and Marketing

We have a diverse customer base, with no single customer accounting for more than 3% of consolidated 2015 revenue. Management and a dedicated sales force are 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 believe we can continue to leverage the diverse technical and marketing strengths at individual locations to expand the services offered in other local markets. With respect to multi-location service opportunities, we maintain a national sales force in our national accounts group.

Employees

As of December 31, 2015, we had 7,301 employees. We have collective bargaining agreements covering eleven 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 provide numerous training programs for management, sales and leadership, as well as on-the-job training, technical training, apprenticeship programs, attractive benefit packages and career advancement opportunities within our company.

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. Safety leadership establishes safety programs and benchmarking to improve safety across the Company. Finally, our employment screening process seeks to determine that prospective employees have requisite skills, sufficient background references and acceptable driving records, if applicable. Our rate of incidents recordable under the standards of the Occupational Safety and Health Administration ("OSHA") per one hundred employees per year, also known as the OSHA recordable rate, was 1.99 during 2015. This level was 26% better than the most recently published OSHA rate for our industry.

Insurance and Litigation

The primary insured risks in our operations are bodily injury, property damage and workers' compensation injuries. We retain the risk for workers' compensation, employer's liability, auto liability, general liability and employee group health claims resulting from uninsured deductibles per incident or occurrence. Because we have very large deductibles, the vast majority of our claims are paid by us, so as a practical matter we self-insure the great majority of these risks. Losses up to such per-incident deductible amounts are estimated and accrued based upon known facts, historical trends and industry averages using the assistance of an actuary to project the extent of these obligations.

We are subject to certain claims and lawsuits arising in the normal course of business. We maintain various insurance coverages to minimize financial risk associated with these claims. We have estimated and provided accruals for probable losses and related legal fees associated with certain litigation in our consolidated financial statements. While we cannot predict the outcome of these proceedings, in our opinion and based on reports of counsel, any liability arising from these matters individually and in the aggregate will not have a material effect on our operating results, cash flows or financial condition, after giving effect to provisions already recorded.

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 thirty days after servicing existing HVAC systems. We do not expect warranty claims to have a material adverse effect on our financial position or results of operations.

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Competition

The HVAC industry is highly competitive and consists of thousands of local and regional companies. We believe that purchasing decisions in the commercial, industrial and institutional markets are based on (i) competitive price, (ii) long-term customer relationships, (iii) quality, timeliness and reliability of services provided, (iv) an organization's perceived stability based on years in business, financial strength and access to bonding, (v) range of services provided, and (vi) scale of operation. To improve our competitive position we focus on both the 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.

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 divisions of larger contracting companies, utilities and HVAC equipment manufacturers that provide HVAC services in some of the same service lines and geographic areas 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, (iv) special bidding and procurement requirements on government projects, (v) wage and hour regulations, and (vi) regulations relating to worker safety and protection of the environment. For example, our operations are subject to the requirements of the Occupational Safety and Health Act, or OSHA, and comparable state laws directed towards protection of employees. 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 seek 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 ozone-depleting refrigerants generally classified as chlorofluorocarbons (CFCs) or hydrochlorofluorocarbons (HCFCs). Clean Air Act regulations promulgated by the United States Environmental Protection Agency (USEPA) 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 ozone-depleting substances such as CFCs and HCFCs in the United States and to require alternative refrigerants to be used in replacement HVAC systems. Some replacement refrigerants, already in use, and classified as hydrofluorocarbons (HFCs) are not ozone-depleting substances. HFCs are considered by USEPA to have high global warming potential. USEPA may at some point require the phase-out of HFCs and expand existing technician certification requirements to cover the handling of HFCs. We do not believe the existing regulations governing technician certification requirements for the handling of ozone-depleting substances or possible future regulations applicable to HFCs will materially affect our business on the whole because, although they require us to incur modest ongoing training costs, our competitors also incur such costs, and such regulations may encourage or require our customers to update their HVAC systems.

ITEM 1A. *Risk Factors*

Our business is subject to a variety of risks. You should carefully consider the risks described below, together with all the information included in this report. Our business, financial condition and results of operations could be adversely affected by the occurrence of any of these events, which could cause actual results to differ materially from expected and historical results, and the trading price of our common stock could decline.

Many of the markets we do work in are currently experiencing or have recently experienced an economic downturn that may materially and adversely affect our business because our business is dependent on levels of construction activity.

The demand for our services is dependent upon the existence of construction projects and service requirements within the markets in which we operate. Any period of economic recession affecting a market or industry in which we transact business is likely to adversely impact our business. Many of the projects we work on have long lifecycles from conception to completion, and the bulk of our performance generally occurs late in a construction project's lifecycle. We experience the results of economic trends well after an economic cycle begins, and therefore will continue to experience the results of an economic recession well after conditions in the general economy have improved. Further, some of the local or regional markets we do work in have yet to enter a period of sustained recovery.

The industries and markets we operate in have always been and will continue to be vulnerable to macroeconomic downturns because they are cyclical in nature. When there is a reduction in demand, it often leads to greater price competition as well as decreased revenue and profit. The lasting effects of a recession can also increase economic instability with our vendors, subcontractors, developers, and general contractors, which can cause us greater liability exposure and can result in us not being paid on some projects, as well as decreasing our revenue and profit. Further, to the extent some of our vendors, subcontractors, developers, or general contractors seek bankruptcy protection, the bankruptcy will likely force us to incur additional costs in attorneys' fees, as well as other professional consultants, and will result in decreased revenue and profit. Additionally, a reduction in federal, state, or local government spending in our industries and markets could result in decreased revenue and profit for us.

Because we bear the risk of cost overruns in most of our contracts, we may experience reduced profits or, in some cases, losses under these contracts if costs increase above our estimates.

Our contract prices are established largely upon estimates and assumptions of our projected costs, including assumptions about: future economic conditions; prices, including commodities prices; availability of labor, including the costs of providing labor, equipment, and materials; and other factors outside our control. If our estimates or assumptions prove to be inaccurate, if circumstances change in

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a way that renders our assumptions and estimates inaccurate or we fail to successfully execute the work, cost overruns may occur and we could experience reduced profits or a loss for affected projects. For instance, unanticipated technical problems may arise, we could have difficulty obtaining permits or approvals, local laws, labor costs or labor conditions could change, bad weather could delay construction, raw materials prices could increase, our suppliers or subcontractors may fail to perform as expected or site conditions may be different than we expected. We are also exposed to increases in energy prices, particularly as they relate to gasoline prices. Additionally, in certain circumstances, we guarantee project completion or the achievement of certain acceptance and performance testing levels by a scheduled date. Failure to meet schedule or performance requirements typically results in additional costs to us, and in some cases we may also create liability for consequential and liquidated damages. Performance problems for existing and future projects could cause our actual results of operations to differ materially from those we anticipate and could damage our reputation within our industry and our customer base.

Our backlog is subject to unexpected adjustments and cancellations, which means that amounts included in our backlog may not result in actual revenue or translate into profits.

The revenue projected from our backlog may not be realized, or, if realized, may not result in profits. Projects may remain in our backlog for an extended period of time, or project cancellations or scope adjustments may occur with respect to contracts reflected in our backlog.

Intense competition in our industry could reduce our market share and our profit.

The markets we serve are highly fragmented and competitive. Our industry is characterized by many small companies whose activities are geographically concentrated. We compete on the basis of our technical expertise and experience, financial and operational resources, nationwide presence, industry reputation and dependability. While we believe our customers consider a number of these factors in awarding available contracts, a large portion of our work is awarded through a bid process. Consequently, price is often the principal factor in determining which contractor is selected, especially on smaller, less complex projects. Smaller competitors are sometimes able to win bids for these projects based on price alone due to their lower cost and financial return requirements. We expect competition to intensify in our industry, presenting us with significant challenges in our ability to maintain strong growth rates and acceptable profit margins. We also expect increased competition from in-house service providers, because some of our customers have employees who perform service work similar to the services we provide. Vertical consolidation is also expected to intensify competition in our industry. If we are unable to meet these competitive challenges, we will lose market share to our competitors and experience an overall reduction in our profits. In addition, our profitability would be impaired if we have to reduce our prices to remain competitive.

Our recent and future acquisitions may not be successful.

We expect to continue pursuing selective acquisitions of businesses. We cannot assure that we will be able to locate acquisitions or that we will be able to consummate transactions on terms and conditions acceptable to us, or that acquired businesses will be profitable. Acquisitions may expose us to additional business risks different than those we have traditionally experienced. We also may encounter difficulties integrating acquired businesses and successfully managing the growth we expect to experience from these acquisitions.

We may choose to finance future acquisitions with debt, equity, cash or a combination of the three. Future acquisitions could dilute earnings or disrupt the payment of a stockholder dividend. To the extent we succeed in making acquisitions, a number of risks will result, including:

- the assumption of material liabilities (including for environmental-related costs);

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- failure of due diligence to uncover situations that could result in legal exposure or to quantify the true liability exposure from known risks;

- the diversion of management's attention from the management of daily operations to the integration of operations;

- difficulties in the assimilation and retention of employees, in the assimilation of different cultures and practices, in the assimilation of broad and geographically dispersed personnel and operations, and the retention of employees generally;

- the risk of additional financial and accounting challenges and complexities in areas such as tax planning, treasury management, financial reporting and internal controls; and

- we may not be able to realize the cost savings or other financial benefits we anticipated prior to the acquisition.

The failure to successfully integrate acquisitions could have an adverse effect on our business, financial condition and results of operations.

Information technology system failures, network disruptions or cyber security breaches could adversely affect our business.

We use sophisticated information technology systems, networks, and infrastructure in conducting some of our day-to-day operations and providing services to certain customers. Information technology system failures, including suppliers' or vendors' system failures, could disrupt our operations by causing transaction errors, processing inefficiencies, the loss of customers, other business disruptions or the loss of employee personal information. In addition, these systems, networks, and infrastructure may be vulnerable to deliberate cyber-attacks that interfere with their functionality or the confidentiality of our information or our customers' data. These events could impact our customers, employees and reputation and lead to financial losses from remediation actions, loss of business or potential liability or an increase in expense, all of which may have a material adverse effect on our business.

Third parties contribute significantly to our completion of many projects.

We hire third-party subcontractors to perform work and depend on third-party suppliers to provide equipment and materials necessary to complete our projects. If we are unable to retain qualified subcontractors or suppliers, or if our subcontractors or suppliers do not perform as anticipated for any reason, our execution and profitability could be harmed.

Earnings for future periods may be impacted by impairment charges for goodwill and intangible assets.

We carry a significant amount of goodwill and identifiable intangible assets on our consolidated balance sheets. Goodwill is the excess of purchase price over the fair value of the net assets of acquired businesses. We assess goodwill for impairment each year, and more frequently if circumstances suggest an impairment may have occurred. We have determined in the past and may again determine in the future that a significant impairment has occurred in the value of our unamortized intangible assets or fixed assets, which could require us to write off a portion of our assets and could adversely affect our financial condition or our reported results of operations.

Actual and potential claims, lawsuits and proceedings could ultimately reduce our profitability and liquidity and weaken our financial condition.

We are likely to continue to be named as a defendant in legal proceedings claiming damages from us in connection with the operation of our business. These actions and proceedings may involve claims for, among other things, compensation for alleged personal injury, workers' compensation, employment

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discrimination, breach of contract or property damage. In addition, we may be subject to class action lawsuits involving allegations of violations of the Fair Labor Standards Act and state wage and hour laws. Due to the inherent uncertainties of litigation, we cannot accurately predict the ultimate outcome of any such actions or proceedings. We also are, and are likely to continue to be, from time to time a plaintiff in legal proceedings against customers, in which we seek to recover payment of contractual amounts we are owed as well as claims for increased costs we incur. When appropriate, we establish provisions against possible exposures, and we adjust these provisions from time to time according to ongoing exposure. If our assumptions and estimates related to these exposures prove to be inadequate or inaccurate, we could experience a reduction in our profitability and liquidity and a weakening of our financial condition. In addition, claims, lawsuits and proceedings may harm our reputation or divert management resources away from operating our business.

We typically warrant the services we provide, guaranteeing the work performed against defects in workmanship and the material we supply. Historically, warranty claims have not been material as our customers evaluate much of the work we perform for defects shortly after work is completed. However, if warranty claims occur, we could be required to repair or replace warrantied items at our cost. In addition, our customers may elect to repair or replace the warrantied item by using the services of another provider and require us to pay for the cost of the repair or replacement. Costs incurred as a result of warranty claims could adversely affect our operating results and financial condition.

Our use of the percentage-of-completion method of accounting could result in a reduction or reversal of previously recorded revenue or profits.

A material portion of our revenue is recognized using the percentage-of-completion method of accounting, which results in our recognizing contract revenue and earnings ratably over the contract term in the proportion that our actual costs bear to our estimated contract costs. The earnings or losses recognized on individual contracts are based on estimates of contract revenue, costs and profitability. We review our estimates of contract revenue, costs and profitability on an ongoing basis. Prior to contract completion, we may adjust our estimates on one or more occasions as a result of change orders to the original contract, collection disputes with the customer on amounts invoiced or claims against the customer for increased costs incurred by us due to customer-induced delays and other factors. Contract losses are recognized in the fiscal period when the loss is determined. Contract profit estimates are also adjusted in the fiscal period in which it is determined that an adjustment is required. As a result of the requirements of the percentage-of-completion method of accounting, the possibility exists, for example, that we could have estimated and reported a profit on a contract over several periods and later determined, usually near contract completion, that all or a portion of such previously estimated and reported profits were overstated. If this occurs, the full aggregate amount of the overstatement will be reported for the period in which such determination is made, thereby eliminating all or a portion of any profits from other contracts that would have otherwise been reported in such period or even resulting in a loss being reported for such period. On a historical basis, we believe that we have made reasonably reliable estimates of the progress towards completion on our long-term contracts. However, given the uncertainties associated with these types of contracts, it is possible for actual costs to vary from estimates previously made, which may result in reductions or reversals of previously recorded revenue and profits.

A significant portion of our business depends on our ability to provide surety bonds. Any difficulties in the financial and surety markets may adversely affect our bonding capacity and availability.

In the past we have expanded, and it is possible we will continue to expand, the number and percentage of total contract dollars that require an underlying bond. Historically surety market conditions have experienced times of difficulty as a result of significant losses incurred by many surety companies and the results of macroeconomic trends outside of our control. Consequently, during times when less overall bonding capacity is available in the market, surety terms have become more expensive and more restrictive. As such, we cannot guarantee our ability to maintain a sufficient level of bonding capacity in the future, which could preclude our ability to bid for certain contracts or successfully contract with some customers. Additionally, even if we continue to be able to access bonding capacity to sufficiently bond future work, we may be required to post collateral to secure bonds, which would decrease the liquidity we would have available for other purposes. Our surety providers are under no commitment to guarantee our access to new bonds in the future; thus, our ability to access or increase bonding capacity is at the sole discretion of our surety providers. If our surety companies were to limit or eliminate our access to bonds, our alternatives would include seeking bonding capacity from other surety companies, increasing business with clients that do not require bonds and posting other forms of collateral for project performance, such as letters of credit or cash. We may be unable to secure these alternatives in a timely manner, on acceptable terms, or at all. As such, if we were to experience an interruption or reduction in the availability of bonding capacity, it is likely we would be unable to compete for or work on certain projects.

We are a decentralized company and place significant decision making powers with our subsidiaries' management, which presents certain risks.

We believe that our practice of placing significant decision making powers with local management is important to our successful growth and allows us to be responsive to opportunities and to our customers' needs. However, this practice presents certain risks, including the risk that we may be slower or less effective in our attempts to identify or react to problems affecting an important business than we would under a more centralized structure or that we would be slower to identify a misalignment between a subsidiary's and the Company's overall business strategy. Further, if a subsidiary location fails to follow the Company's compliance policies, we could be made party to a contract, arrangement or situation that requires the assumption of large liabilities or has less advantageous terms than is typically found in the market.

Our insurance policies against many potential liabilities require high deductibles, and our risk management policies and procedures may leave us exposed to unidentified or unanticipated risks. Additionally, difficulties in the insurance markets may adversely affect our ability to obtain necessary insurance.

Although we maintain insurance policies with respect to our related exposures, these policies are subject to high deductibles; as such, we are, in effect, self-insured for substantially all of our typical claims. We hire an actuary to determine any liabilities for unpaid claims and associated expenses for the three major lines of coverage (workers' compensation, general liability and auto liability). The determination of these claims and expenses and the appropriateness of the estimated liability are reviewed and updated quarterly. However, insurance liabilities are difficult to assess and estimate due to the many relevant factors, the effects of which are often unknown, including the severity of an injury, the determination of our liability in proportion to other parties, the number of incidents that have occurred but are not reported and the effectiveness of our safety program. Our accruals are based on known facts, historical trends (both internal trends and industry averages) and our reasonable estimate of our future expenses. We believe our accruals are adequate. However, our risk management strategies and techniques may not be fully effective in mitigating our risk exposure in all market environments or against all types of risk. If any of the variety of instruments, processes or strategies we use to manage our exposure to various types of risk are not effective, we may incur losses that are not covered by our insurance policies or that exceed our accruals or coverage limits.

Additionally, we typically are contractually required to provide proof of insurance on projects we work on. Historically insurance market conditions become more difficult for insurance consumers during periods when insurance companies suffer significant investment losses as well as casualty losses. Consequently, it is possible that insurance markets will become more expensive and restrictive. Also, our prior casualty loss history might adversely affect our ability to procure insurance within commercially reasonable ranges. As such, we may not be able to maintain commercially reasonable levels of insurance coverage in the future, which could preclude our ability to work on many projects. Our insurance providers are under no commitment to renew our existing insurance policies in the future; therefore, our ability to obtain necessary levels or kinds of insurance coverage is subject to market forces outside our control. If we were unable to obtain necessary levels of insurance, it is likely we would be unable to compete for or work on most projects.

Failure to remain in compliance with covenants under our credit agreement, service our indebtedness, or fund our other liquidity needs could adversely impact our business.

Our credit agreement and related restrictive and financial covenants are more fully described in Note 9 of "Notes to the Consolidated Financial Statements." Our failure to comply with any of these covenants, or to pay principal, interest or other amounts when due thereunder, would constitute an event of default under the credit agreement. Default under our credit agreement could result in (1) us no longer being entitled to borrow under the agreement; (2) termination of the agreement; (3) acceleration of the maturity of outstanding indebtedness under the agreement; and/or (4) foreclosure on any collateral securing the obligations under the agreement. If we are unable to service our debt obligations or fund our other liquidity needs, we could be forced to curtail our operations, reorganize our capital structure (including through bankruptcy proceedings) or liquidate some or all of our assets in a manner that could cause holders of our securities to experience a partial or total loss of their investment in us.

If we experience delays and/or defaults in customer payments, we could be unable to recover all expenditures.

Because of the nature of our contracts, at times we commit resources to projects prior to receiving payments from the customer in amounts sufficient to cover expenditures on projects as they are incurred. Delays in customer payments may require us to make a working capital investment. If a customer defaults in making their payments on a project to which we have devoted resources, it could have a material negative effect on our results of operations.

If we are unable to attract and retain qualified managers and employees, we will be unable to operate efficiently, which could reduce our profitability.

Our business is labor intensive, and many of our operations experience a high rate of employment turnover. At times of low unemployment rates in the United States, it will be more difficult for us to find qualified personnel at low cost in some geographic areas where we operate. Additionally, our business is managed by a small number of key executive and operational officers. We may be unable to hire and retain the sufficient skilled labor force necessary to operate efficiently and to support our growth strategy. Our labor expenses may increase as a result of a shortage in the supply of skilled personnel. Labor shortages, increased labor costs or the loss of key personnel could reduce our profitability and negatively impact our business. Further, our relationship with some customers could suffer if we are unable to retain the employees with whom those customers primarily work and have established relationships.

Our inability to properly utilize our workforce could have a negative impact on our profitability

The extent to which we utilize our workforce affects our profitability. Underutilizing our workforce could result in lower gross margins and, consequently, a decrease in short-term profitability. On the other hand, overutilization of our workforce could negatively impact safety, employee satisfactions and

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project execution, leading to a potential decline in future project awards. The utilization of our workforce is impacted by numerous factors, including:

- our estimate of headcount requirements and our ability to manage attrition;
- efficiency in scheduling projects and our ability to minimize downtime between project assignments; and
- productivity.

Misconduct by our employees, subcontractors or partners or our overall failure to comply with laws or regulations could harm our reputation, damage our relationships with customers, reduce our revenue and profits, and subject us to criminal and civil enforcement actions.

Misconduct, fraud, non-compliance with applicable laws and regulations, or other improper activities by one or more of our employees, subcontractors or partners could have a significant negative impact on our business and reputation. Examples of such misconduct include employee or subcontractor theft, the failure to comply with safety standards, laws and regulations, customer requirements, environmental laws and any other applicable laws or regulations. While we take precautions to prevent and detect these activities, such precautions may not be effective and are subject to inherent limitations, including human error and fraud. Our failure to comply with applicable laws or regulations or acts of misconduct could subject us to fines and penalties, harm our reputation, damage our relationships with customers, reduce our revenue and profits and subject us to criminal and civil enforcement actions.

Failure or circumvention of our disclosure controls and procedures or internal controls over financial reporting could seriously harm our financial condition, results of operations, and our business.

We plan to continue to maintain and strengthen internal controls and procedures to enhance the effectiveness of our disclosure controls and internal controls over financial reporting. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, and not absolute, assurances that the objectives of the system are met. Any failure of our disclosure controls and procedures or internal controls over financial reporting could harm our financial condition and results of operations.

We have subsidiary operations through the United States and are exposed to multiple state and local regulations, as well as federal laws and requirements applicable to government contractors. Changes in law, regulations or requirements, or a material failure of any of our subsidiaries or us to comply with any of them, could increase our costs and have other negative impacts on our business.

Our 89 locations are located in 27 states, which exposes us to a variety of different state and local laws and regulations, particularly those pertaining to contractor licensing requirements. These laws and regulations govern many aspects of our business, and there are often different standards and requirements in different locations. In addition, our subsidiaries that perform work for federal government entities are subject to additional federal laws and regulatory and contractual requirements. Changes in any of these laws, or any of our subsidiaries' material failure to comply with them, can adversely impact our operations by, among other things, increasing costs, distracting management's time and attention from other items, and harming our reputation.

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As government contractors, our subsidiaries are subject to a number of rules and regulations, and their contracts with government entities are subject to audit. Violations of the applicable rules and regulations could result in a subsidiary being barred from future government contracts.

Government contractors must comply with many regulations and other requirements that relate to the award, administration and performance of government contracts. A violation of these laws and regulations could result in imposition of fines and penalties, the termination of a government contract or debarment from bidding on government contracts in the future. Further, despite our decentralized nature, a violation at one of our locations could impact other locations' ability to bid on and perform government contracts; additionally, because of our decentralized nature, we face risks in maintaining compliance with all local, state and federal government contracting requirements. Prohibition against bidding on future government contracts could have an adverse effect on our financial condition and results of operations.

Past and future environmental, safety and health regulations could impose significant additional costs on us that reduce our profits.

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. Various local, state and federal laws and regulations impose licensing standards on technicians who install and service HVAC systems. And additional laws, regulations and standards apply to contractors who perform work that is being funded by public money, particularly federal public funding. Our failure to comply with these laws and regulations could subject us to substantial fines, the loss of our licenses or potentially debarment from future publicly funded work. It is impossible to predict the full nature and effect of judicial, legislative or regulatory developments relating to health and safety regulations and environmental protection regulations applicable to our operations.

Unsatisfactory safety performance may subject us to penalties, affect customer relationships, result in higher operating costs, negatively impact employee morale and result in higher employee turnover.

Our projects are conducted at a variety of sites including construction sites and industrial facilities. Each location is subject to numerous safety risks, including electrocutions, fires, explosions, mechanical failures, weather-related incidents, transportation accidents and damage to equipment. These hazards can cause personal injury and loss of life, severe damage to or destruction of property and equipment and other consequential damages and could lead to suspension of operations, large damage claims and, in extreme cases, criminal liability. While we have taken what we believe are appropriate precautions to minimize safety risks, we have experienced serious accidents, including fatalities, in the past and may experience additional accidents in the future. Serious accidents may subject us to penalties, civil litigation or criminal prosecution. Claims for damages to persons, including claims for bodily injury or loss of life, could result in significant costs and liabilities, which could adversely affect our financial condition and results of operations. Poor safety performance could also jeopardize our relationships with our customers and harm our reputation.

If we do not effectively manage the size and cost of our operations, our existing infrastructure may become either strained or over-burdensome, and we may be unable to increase revenue growth.

The growth that we have experienced in the past, and that we may experience in the future, may provide challenges to our organization, requiring us to expand our personnel and our operations. Future growth may strain our infrastructure, operations and other managerial and operating resources. We have also experienced in the past severe constriction in the markets in which we operate and, as a result, in our operating requirements. Failing to maintain the appropriate cost structure for a particular

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economic cycle may result in our incurring costs that affect our profitability. If our business resources become strained or over-burdensome, our earnings may be adversely affected and we may be unable to increase revenue growth. Further, we may undertake contractual commitments that exceed our labor resources, which could also adversely affect our earnings and our ability to increase revenue growth.

We are susceptible to adverse weather conditions, which may harm our business and financial results.

Our business may be adversely affected by severe weather in areas where we have significant operations. Repercussions of severe weather conditions may include:

- curtailment of services;
- suspension of operations;
- inability to meet performance schedules in accordance with contracts and potential liability for liquidated damages;
- injuries or fatalities;
- weather related damage to our facilities;
- disruption of information systems;
- inability to receive machinery, equipment and materials at jobsites; and
- loss of productivity.

Future climate change could adversely affect us.

Climate change may create physical and financial risk. Physical risks from climate change could, among other things, include an increase in extreme weather events (such as floods or hurricanes), rising sea levels and limitations on water availability and quality. Such extreme weather conditions may limit the availability of resources, increasing the costs of our projects, or may cause projects to be delayed or cancelled.

Legislation, nationwide protocols, regulation or other restrictions related to climate change could negatively impact our operations or our customers' operations. Such legislation or restrictions could increase the costs of projects for our customers or, in some cases, prevent a project from going forward, which could in turn have an adverse effect on our financial condition and results of operations.

Force majeure events, including natural disasters and terrorists' actions, could negatively impact our business, which may affect our financial condition, results of operations or cash flows.

Force majeure or extraordinary events beyond the control of the contracting parties, such as natural and man-made disasters, as well as terrorist actions, could negatively impact us. We typically negotiate contract language where we are allowed certain relief from force majeure events in private client contracts and review and attempt to mitigate force majeure events in both public and private client contracts. We remain obligated to perform our services after most extraordinary events subject to relief that may be available pursuant to a force majeure clause. If we are not able to react quickly to force majeure events, our operations may be affected significantly, which would have a negative impact on our financial position, results of operations, cash flows and liquidity.

Deliberate, malicious acts, including terrorism and sabotage, could damage our facilities, disrupt our operations or injure employees, contractors, customers or the public and result in liability to us.

Intentional acts of destruction could damage or destroy our facilities, reducing our operational production capacity and requiring us to repair or replace our facilities at substantial cost. Additionally, employees, contractors and the public could suffer substantial physical injury from acts of terrorism for which we could be liable. Governmental authorities may also impose security or other requirements that could make our operations more difficult or costly. The consequences of any such actions could adversely affect our financial condition and results of operations.

Our common stock, which is listed on the New York Stock Exchange, has from time to time experienced significant price and volume fluctuations. These fluctuations are likely to continue in the future, and our stockholders may suffer losses.

The market price of our common stock may change significantly in response to various factors and events beyond our control. A variety of events may cause the market price of our common stock to fluctuate significantly, including the following: (i) the risk factors described in this Report on Form 10-K; (ii) a shortfall in operating revenue or net income from that expected by securities analysts and investors; (iii) quarterly fluctuations in our operating results; (iv) changes in securities analysts' estimates of our financial performance or that of our competitors or companies in our industry generally; (v) general conditions in our customers' industries; (vi) general conditions in the securities markets; (vii) our announcements of significant contracts, milestones, acquisitions; (viii) our relationship with other companies; (ix) our investors' view of the sectors and markets in which we operate; and (x) additions or departures of key personnel. Some companies that have volatile market prices for their securities have been subject to security class action suits filed against them. If a suit were to be filed against us, regardless of the outcome, it could result in substantial costs and a diversion of our management's attention and resources. This could have a material adverse effect on our business, results of operations and financial condition.

We are required to assess and report on our internal controls each year. Findings of inadequate internal controls could reduce investor confidence in the reliability of our financial information.

As directed by the Sarbanes-Oxley Act, the SEC adopted rules generally requiring public companies, including us, to include in their annual reports on Form 10-K a report of management that contains an assessment by management of the effectiveness of our internal control over financial reporting. In addition, the independent registered public accounting firm auditing our financial statements must report on the effectiveness of our internal control over financial reporting. A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the company are being made only in accordance with authorizations of management and records of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

We may discover in the future that we have deficiencies in the design and operation of our internal controls. If any of the deficiencies in our internal control, either by itself or in combination with other deficiencies, becomes a "material weakness", such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis, we may be unable to conclude that we have effective internal control over financial reporting. In such event, investors could lose confidence in the reliability of our financial statements,

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which may significantly harm our business and cause our stock price to decline. In addition, the failure to maintain effective internal controls could also result in unauthorized transactions.

Future sales of our common stock may depress our stock price.

Sales of a substantial number of shares of our common stock in the public market or otherwise, either by us, a member of management or a major stockholder, or the perception that these sales could occur, could depress the market price of our common stock and impair our ability to raise capital through the sale of additional equity securities.

Increases in our health insurance costs could adversely impact our results of operations and cash flows.

The costs of employee health care insurance have been increasing in recent years due to rising health care costs, legislative changes, and general economic conditions. Additionally, we may incur additional costs as a result of the Patient Protection and Affordable Care Act (the "Affordable Care Act") that was signed into law in March 2010. A continued increase in health care costs or additional costs incurred as a result of the Affordable Care Act could have a negative impact on our financial position and results of operations.

Rising inflation and/or interest rates could have an adverse effect on our business, financial condition and results of operations.

Economic factors, including inflation and fluctuations in interest rates, could have a negative impact on our business. If our costs were to become subject to significant inflationary pressures or interest rate increases, we may not be able to fully offset such higher costs through price increases. Our inability or failure to do so could harm our financial position and results of operations.

Our effective tax rate may increase.

We conduct business across the United States and file income taxes in various tax jurisdictions. Our effective tax rates could be affected by many factors, some of which are outside of our control, including changes in tax laws and regulations in the various tax jurisdictions in which we file income taxes, issues relating to tax audits or examinations and any related interest or penalties, and uncertainty in obtaining deductions or credits claimed in various jurisdictions. Our results of operations is reported based on our determination of the amount of taxes we owe in various tax jurisdictions. Significant judgment is required in determining our provision for income taxes and our determination of tax liability is always subject to review or examination by tax authorities in applicable tax jurisdictions. An adverse outcome of such a review of examination could adversely affect our operating results and financial condition. Further, the results of tax examinations and audits could have a negative impact on our financial results and cash flows where the results differ from the liabilities recorded in our financial statements.

Our charter contains certain anti-takeover provisions that may inhibit or delay a change in control.

Our certificate of incorporation authorizes our board of directors to issue, without stockholder approval, one or more series of preferred stock having such preferences, powers and relative, participating, optional and other rights (including preferences over the common stock respecting dividends and distributions and voting rights) as the board of directors may determine. The issuance of this "blank-check" preferred stock could render more difficult or discourage an attempt to obtain control by means of a tender offer, merger, proxy contest or otherwise. Additionally, certain provisions of the Delaware General Corporation Law may also discourage takeover attempts that have not been approved by the Board of Directors.

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ITEM 1B. ***Unresolved Staff Comments***

None.

ITEM 2. ***Properties***

As of December 31, 2015, we owned five properties. Other than these five owned properties, we lease the real property and buildings from which we operate. Our facilities are located in 27 states and consist of offices, shops and fabrication, maintenance and warehouse facilities. Generally, leases range from three to ten years and are on terms we believe to be commercially reasonable. A majority of these premises are leased from individuals or entities with whom we have no other business relationship. In certain instances these leases are with current or former employees. To the extent we renew, enter into leases or otherwise change leases with current or former employees, we enter into such agreements on terms that reflect a fair market valuation for the properties. Leased premises range in size from approximately 1,000 square feet to 110,000 square feet. To maximize available capital, we generally intend to continue to lease our properties, but may consider further purchases of property where we believe ownership would be more economical. 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 normal course of business. We maintain various insurance coverages to minimize financial risk associated with these claims. We have estimated and provided accruals for probable losses and related legal fees associated with certain litigation in our consolidated financial statements. While we cannot predict the outcome of these proceedings, in our opinion and based on reports of counsel, any liability arising from these matters individually and in the aggregate will not have a material effect on our operating results, cash flows or financial condition, after giving effect to provisions already recorded.

ITEM 4. ***Mine Safety Disclosures***

Not applicable.

ITEM 4A. ***Executive Officers of the Registrant***

Executive officers are appointed by our Board of Directors and hold office until their successors are elected and duly qualified. The following persons serve as executive officers of the Company.

Brian Lane, age 58, has served as our Chief Executive Officer and President since December 2011 and as a director since November 2010. Mr. Lane served as our President and Chief Operating Officer from March 2010 until December 2011. Mr. Lane joined the Company in October 2003 and served as Vice President and then Senior Vice President for Region One of the Company until he was named Executive Vice President and Chief Operating Officer in January 2009. Prior to joining the Company, Mr. Lane spent fifteen years at Halliburton, the global service and equipment company devoted to energy, industrial, and government customers. During his tenure at Halliburton, he held various positions in business development, strategy, and project initiatives. He departed as the Regional Director of Europe and Africa. Mr. Lane's additional experience included serving as a Regional Director of Capstone Turbine Corporation, a distributed power manufacturer. He also was a Vice President of Kvaerner, an international engineering and construction company where he focused on the chemical industry.

William George, age 51, has served as our Executive Vice President and Chief Financial Officer since May 2005, was our Senior Vice President, General Counsel and Secretary from May 1998 to

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May 2005, 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.

Julie S. Shaeff, age 50, has served as our Senior Vice President and Chief Accounting Officer since May 2005, was our Vice President and Corporate Controller from March 2002 to May 2005, and was our Assistant Corporate Controller from September 1999 to February 2002. From 1996 to August 1999, Ms. Shaeff was Financial Accounting Manager Corporate Controllers Group for Browning-Ferris Industries, Inc., a publicly-traded waste services company. From 1987 to 1995, she held various positions with Arthur Andersen LLP. Ms. Shaeff is a Certified Public Accountant.

Trent T. McKenna, age 43, has served as our Senior Vice President, General Counsel and Secretary since August 2013, was our Vice President, General Counsel and Secretary from May 2005 to August 2013, and was our Associate General Counsel from August 2004 to May 2005. From February 1999 to August 2004, Mr. McKenna was a practicing attorney in the area of complex commercial litigation in the Houston, Texas office of Akin Gump Strauss Hauer & Feld LLP, an international law firm.

James Mylett, age 52, has served as our Senior Vice President of Service since October 2013. Prior to joining the Company, Mr. Mylett spent fourteen years at Johnson Controls, which manufactures, installs, and services automatic temperature regulation systems for buildings. During his time at Johnson Controls, Mr. Mylett held various positions, including that of Vice President and General Manager North America Service Operations from August 2011 to October 2013. From October 2010 to August 2011, he served as Vice President and General Manager West Region, and from December 2005 to September 2010, he served as Vice President of Service and Solutions South Region. Previously, Mr. Mylett worked for Carrier Corporation, where he established and developed the Company's national accounts service business.

PART II

ITEM 5. *Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*

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	Cash Dividends Declared
Fourth Quarter, 2015	$ 33.71	$ 27.47	$ 0.065
Third Quarter, 2015	$ 30.12	$ 22.98	$ 0.065
Second Quarter, 2015	$ 23.90	$ 20.11	$ 0.060
First Quarter, 2015	$ 21.18	$ 15.87	$ 0.060
Fourth Quarter, 2014	$ 17.42	$ 12.81	$ 0.060
Third Quarter, 2014	$ 16.38	$ 13.55	$ 0.055
Second Quarter, 2014	$ 17.14	$ 14.61	$ 0.055
First Quarter, 2014	$ 19.62	$ 15.24	$ 0.055

As of February 17, 2016 there were approximately 273 stockholders of record of our Common Stock, and the last reported sale price on that date was $26.20 per share.

We expect to continue paying cash dividends quarterly, although there is no assurance as to future dividends because they depend on future earnings, capital requirements, and financial condition. In

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addition, our revolving credit agreement may limit the amount of dividends we can pay at any time that our Net Leverage Ratio exceeds 1.0.

The following Corporate Performance Graph and related information shall not be deemed "soliciting material" or to be "filed" with the SEC, nor shall such information be incorporated by reference into any future filing under the Securities Act or the Exchange Act, except to the extent that we specifically incorporate it by reference into such filing.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*

Among Comfort Systems USA, Inc., the S&P 500 Index, and the Russell 2000 Index

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*

$100 invested on 12/31/10 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

Recent Sales of Unregistered Securities

None.

Issuer Purchases of Equity Securities

On March 29, 2007, our Board of Directors (the "Board") approved a stock repurchase program to acquire up to 1.0 million shares of our outstanding common stock. Subsequently, the Board has from time to time approved extensions of the program to acquire additional shares. Since the inception of the repurchase program, the Board has approved 7.6 million shares to be repurchased. As of December 31, 2015, we have repurchased a cumulative total of 6.9 million shares at an average price of $11.99 per share under the repurchase program.

The share repurchases will be made from time to time at our discretion in the open market or privately negotiated transactions as permitted by securities laws and other legal requirements, and subject to market conditions and other factors. The Board may modify, suspend, extend or terminate the program at any time. During the twelve months ended December 31, 2015, we repurchased 0.3 million shares for approximately $8.3 million at an average price of $26.36 per share.

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During the year ended December 31, 2015, we purchased our common shares in the following amounts at the following weighted-average prices:

Period	Total Number of Shares Purchased		Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
January 1 - January 31		$		6,566,368	994,815
February 1 - February 28		$		6,566,368	994,815
March 1 - March 31		$		6,566,368	994,815
April 1 - April 30	43,750	$	20.61	6,610,118	951,065
May 1 - May 31	29,283	$	21.28	6,639,401	921,782
June 1 - June 30		$		6,639,401	921,782
July 1 - July 31		$		6,639,401	921,782
August 1 - August 31	40,439	$	27.74	6,679,840	881,343
September 1 - September 30	82,361	$	27.71	6,762,201	798,982
October 1 - October 31	37,002	$	26.51	6,799,203	761,980
November 1 - November 30	4,058	$	31.38	6,803,261	757,922
December 1 - December 31	79,060	$	28.99	6,882,321	678,862
	315,953	$	26.36	6,882,321	678,862

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ITEM 6. ***Selected Financial Data***

The following selected historical financial data has been derived from our audited financial statements and should be read in conjunction with the historical Consolidated Financial Statements and related notes:

	Year Ended December 31,				
	2015	2014	2013	2012	2011
	(in thousands, except per share amounts)				
STATEMENT OF OPERATIONS DATA:					
Revenue	$ 1,580,519	$ 1,410,795	$ 1,357,272	$ 1,331,185	$ 1,216,654
Operating income (loss)(a)	$ 90,044	$ 42,222	$ 46,258	$ 22,303	$ (42,641)
Income (loss) from continuing operations	$ 57,440	$ 28,614	$ 28,632	$ 11,494	$ (32,474)
Discontinued operations					
Operating income (loss), net of tax	$	$ (15)	$ (76)	$ 355	$ (4,018)
Net income (loss) including noncontrolling interests	$ 57,440	$ 28,599	$ 28,556	$ 11,849	$ (36,492)
Net income (loss) attributable to Comfort Systems USA, Inc.	$ 49,364	$ 23,063	$ 27,269	$ 13,463	$ (36,830)
Income (loss) per share attributable to Comfort Systems USA, Inc.:					
Basic					
Income (loss) from continuing operations	$ 1.32	$ 0.61	$ 0.73	$ 0.35	$ (0.88)
Discontinued operations					
Income (loss) from operations				0.01	(0.11)
Net income (loss)	$ 1.32	$ 0.61	$ 0.73	$ 0.36	$ (0.99)
Diluted					
Income (loss) from continuing operations	$ 1.30	$ 0.61	$ 0.73	$ 0.35	$ (0.88)
Discontinued operations					
Income (loss) from operations				0.01	(0.11)
Net income (loss)	$ 1.30	$ 0.61	$ 0.73	$ 0.36	$ (0.99)
Cash dividends per share	$ 0.250	$ 0.225	$ 0.210	$ 0.200	$ 0.200
BALANCE SHEET DATA:					
Working capital	$ 118,882	$ 111,433	$ 109,618	$ 84,349	$ 90,800
Total assets	$ 691,594	$ 655,942	$ 592,789	$ 573,461	$ 589,947
Total debt	$ 11,507	$ 40,346	$ 2,000	$ 7,400	$ 15,381
Total stockholders' equity	$ 365,005	$ 321,393	$ 314,022	$ 287,306	$ 283,106
Total Comfort Systems USA, Inc. stockholders' equity	$ 346,721	$ 306,281	$ 295,834	$ 270,405	$ 264,591

(a) Included in operating income are goodwill impairment charges of \$0.7 million and \$57.3 million for 2014 and 2011, respectively. There were no goodwill impairment charges for 2015, 2013 or 2012.

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 annual report on Form 10-K. Also see "Forward-Looking Statements" discussion.

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Introduction and Overview

We are a national provider of comprehensive mechanical installation, renovation, maintenance, repair and replacement services within the mechanical services industry. We operate primarily in the commercial, industrial and institutional HVAC markets and perform most of our services within office buildings, retail centers, apartment complexes, manufacturing plants, and healthcare, education and government facilities.

Nature and Economics of Our Business

Approximately 82% of our revenue is earned on a project basis for installation of mechanical systems in newly constructed facilities or for replacement of systems in existing facilities. Customers hire us to ensure such systems deliver specified or generally expected heating, cooling, conditioning and circulation of air in a facility. This entails installing core system equipment such as packaged heating and air conditioning units, or in the case of larger facilities, separate core components such as chillers, boilers, air handlers, and cooling towers. We also typically install connecting and distribution elements such as piping and ducting. Our responsibilities usually require conforming the systems to pre-established engineering drawings and equipment and performance specifications, which we frequently participate in establishing. Our project management responsibilities include staging equipment and materials to project sites, deploying labor to perform the work, and coordinating with other service providers on the project, including any subcontractors we might use to deliver our portion of the work.

When competing for project business, we usually estimate the costs we will incur on a project, and then propose a bid to the customer that includes a contract price and other performance and payment terms. Our bid price and terms are intended to cover our estimated costs on the project and provide a profit margin to us commensurate with the value of the installed system to the customer, the risk that project costs or duration will vary from estimate, the schedule on which we will be paid, the opportunities for other work that we might forego by committing capacity to this project, and other costs that we incur more broadly to support our operations but which are not specific to the project. Typically customers will seek bids from competitors for a given project. While the criteria on which customers select the winning bid vary widely and include factors such as quality, technical expertise, on-time performance, post-project support and service, and company history and financial strength, we believe that price is the most influential factor for most customers in choosing a mechanical installation and service provider.

After a customer accepts our bid, we generally enter into a contract with the customer that specifies what we will deliver on the project, what our related responsibilities are, and how much and when we will be paid. Our overall price for the project is typically set at a fixed amount in the contract, although changes in project specifications or work conditions that result in unexpected additional work are usually subject to additional payment from the customer via what are commonly known as change orders. Project contracts typically provide for periodic billings to the customer as we meet progress milestones or incur cost on the project. Project contracts in our industry also frequently allow for a small portion of progress billings or contract price to be withheld by the customer until after we have completed the work, typically for six months. Amounts withheld under this practice are known as retention or retainage.

Labor and overhead costs account for the majority of our cost of service. Accordingly, labor management and utilization have the most impact on our project performance. Given the fixed price nature of much of our project work, if our initial estimate of project costs is wrong or we incur cost overruns that cannot be recovered in change orders, we can experience reduced profits or even significant losses on fixed price project work. We also perform some project work on a cost-plus or a time and materials basis, under which we are paid our costs incurred plus an agreed-upon profit margin, although such projects are sometimes subject to a guaranteed maximum cost. These margins are frequently less than fixed-price contract margins because there is less risk of unrecoverable cost overruns in cost-plus or time and materials work.

As of December 31, 2015, we had 3,843 projects in process. Our average project takes six to nine months to complete, with an average contract price of approximately $512,000. Our projects generally require working capital funding of equipment and labor costs. Customer payments on periodic billings generally do not recover these costs until late in the job. Our average project duration together with typical retention terms as discussed above generally allow us to complete the realization of revenue and earnings in cash within one year. We have what we believe is a well-diversified distribution of revenue across end-use sectors that we believe reduces our exposure to negative developments in any given sector. Because of the integral nature of HVAC and related controls systems to most buildings, we have the legal right in almost all cases to attach liens to buildings or related funding sources when we have not been fully paid for installing systems, except with respect to some government buildings. The service work that we do, which is discussed further below, usually does not give rise to lien rights.

We also perform larger projects. As of December 31, 2015, we had 12 projects in process with a contract price greater than $15 million, 21 projects between $10 million and $15 million, 64 projects between $5 million and $10 million, and 286 projects between $1 million and $5 million. Taken together, projects with contract prices of $1 million or more totaled $1,565.0 million of aggregate contract value as of December 31, 2015, or approximately 80%, out of a total contract value for all projects in progress of $1,966.4 million. Generally, projects closer in size to $1 million will be completed in one year or less. It is unusual for us to work on a project that exceeds two years in length.

In addition to project work, approximately 18% of our revenue represents maintenance and repair service on already installed HVAC and controls systems. This kind of work usually takes from a few hours to a few days to perform. Prices to the customer are usually based on the equipment and materials used in the service as well as technician labor time. We usually bill the customer for service work when it is complete, typically with payment terms of up to thirty days. We also provide maintenance and repair service under ongoing contracts. Under these contracts, we are paid regular monthly or quarterly amounts and provide specified service based on customer requirements. These agreements typically cover periods ranging from one to three years with thirty- to sixty-day cancellation notice periods.

A relatively small portion of our revenue comes from national and regional account customers. These customers typically have multiple sites, and contract with us to perform maintenance and repair service. These contracts may also provide for us to perform new or replacement systems installation. We operate a national call center to dispatch technicians to sites requiring service. We perform the majority of this work with our own employees, with the balance being subcontracted to third parties that meet our performance qualifications. We will also typically use proprietary information systems to maintain information on the customer's sites and equipment, including performance and service records, and related cost data. These systems track the status of ongoing service and installation work, and may also monitor system performance data. Under these contractual relationships, we usually provide consolidated billing and credit payment terms to the customer.

Profile and Management of Our Operations

We manage our 35 operating units based on a variety of factors. Financial measures we emphasize include profitability, and use of capital as indicated by cash flow and by other measures of working capital principally involving project cost, billings and receivables. We also monitor selling, general, administrative and indirect project support expense, backlog, workforce size and mix, growth in revenue and profits, variation of actual project cost from original estimate, and overall financial performance in comparison to budget and updated forecasts. Operational factors we emphasize include project selection, estimating, pricing, management and execution practices, labor utilization, safety, training, and the make-up of both existing backlog as well as new business being pursued, in terms of project size, technical application and facility type, end-use customers and industries, and location of the work.

Most of our operations compete on a local or regional basis. Attracting and retaining effective operating unit managers is an important factor in our business, particularly in view of the relative uniqueness of each market and operation, the importance of relationships with customers and other market participants such as architects and consulting engineers, and the high degree of competition and low barriers to entry in most of our markets. Accordingly, we devote considerable attention to operating unit management quality, stability, and contingency planning, including related considerations of compensation, and non-competition protection where applicable.

Economic and Industry Factors

As a mechanical and building controls services provider, we operate in the broader nonresidential construction services industry and are affected by trends in this sector. While we do not have operations in all major cities of the United States, we believe our national presence is sufficiently large that we experience trends in demand for and pricing of our services that are consistent with trends in the national nonresidential construction sector. As a result, we monitor the views of major construction sector forecasters along with macroeconomic factors they believe drive the sector, including trends in gross domestic product, interest rates, business investment, employment, demographics, and the general fiscal condition of federal, state and local governments.

Spending decisions for building construction, renovation and system replacement are generally made on a project basis, usually with some degree of discretion as to when and if projects proceed. With larger amounts of capital, time, and discretion involved, spending decisions are affected to a significant degree by uncertainty, particularly concerns about economic and financial conditions and trends. We have experienced periods of time when economic weakness caused a significant slowdown in decisions to proceed with installation and replacement project work.

Operating Environment and Management Emphasis

Nonresidential building construction and renovation activity, as reported by the federal government, declined over the four year period from 2009 to 2012, and 2013 and 2014 activity levels were relatively stable at the low levels of the preceding years. While we expect that activity levels and the underlying environment for nonresidential construction activity will remain below prior peaks, we have seen industry conditions improve during 2015.

As a result of our continued strong emphasis on cash flow, at December 31, 2015 we had modest indebtedness under our revolving credit facility and substantial uncommitted cash balances, as discussed further in "Liquidity and Capital Resources" below. We have a credit facility in place with considerably less restrictive terms than those of our previous facilities; this facility does not expire until October 2019. We have strong surety relationships to support our bonding needs, and we believe our relationships with the surety markets are strong and benefit from our solid current results and financial position. We have generated positive free cash flow in each of the last seventeen calendar years and will continue our emphasis in this area. We believe that the relative size and strength of our balance sheet and surety support as compared to most companies in our industry represent competitive advantages for us.

As discussed at greater length in "Results of Operations" below, we expect price competition to continue as our customers and local and regional competitors respond cautiously to changing conditions. We will continue our efforts to expand and improve our service business, to find the more active sectors in our markets, and to increase our regional and national account business. Our primary

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emphasis for 2016 will be on execution and cost control, but we are seeking growth based on our belief that industry conditions are beginning to improve, and we believe that activity levels will permit us to earn improved profits while preserving and developing our workforce. We continue to focus on project qualification, estimating, pricing and management; and we are investing in service growth and improved performance.

Critical Accounting Policies

Our critical accounting policies are 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. Our most critical accounting policy is revenue recognition. As discussed elsewhere in this annual report on Form 10-K, 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 of 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, valuation of deferred tax assets, accounting for acquisitions and the recoverability of goodwill and identifiable intangible assets. These accounting policies, as well as others, are described in Note 2 to the Consolidated Financial Statements included elsewhere in this annual report on Form 10-K.

Percentage of Completion Method of Accounting

Approximately 82% of our revenue was earned on a project basis and recognized through the percentage of completion method of accounting during 2015. Under this method, 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 connection with obtaining installation contracts, we estimate our contract costs, which include all direct materials (exclusive of rebates), labor and subcontract costs and indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and depreciation costs. These contract costs are included in our results of operations under the caption "Cost of Services." Then, as we perform under those contracts, we measure costs incurred, compare them to total estimated costs to complete the contract, and recognize a corresponding proportion of contract revenue. Labor costs are considered to be incurred as the work is performed. Subcontractor labor is recognized as the work is performed, but is generally subjected to approval as to milestones or other evidence of completion. Non-labor project costs consist of purchased equipment, prefabricated materials and other materials. Purchased equipment on our projects is substantially produced to job specifications and is a value added element to our work. The costs are considered to be incurred when title is transferred to us, which typically is upon delivery to the worksite. Prefabricated materials, such as ductwork and piping, are generally performed at our shops and recognized as contract costs when fabricated for the unique specifications of the job. Other materials costs are not significant and are generally recorded when delivered to the worksite. This measurement and comparison process requires updates to the estimate of total costs to complete the contract, and these updates may include subjective assessments.

We generally do not incur significant costs prior to receiving a contract, and therefore, these costs are expensed as incurred. In limited circumstances, when significant pre-contract costs are incurred, they are deferred if the costs can be directly associated with a specific contract and if their recoverability from the contract is probable. Upon receiving the contract, these costs are included in contract costs. Deferred costs associated with unsuccessful contract bids are written off in the period that we are informed that we will not be awarded the contract.

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Project contracts typically provide for a schedule of billings or invoices to the customer based on reaching agreed upon milestones or as we incur costs. The schedules for such billings usually do not precisely match the schedule on which costs are incurred. As a result, contract revenue recognized in the statement of operations can and usually does differ from amounts that can be billed or invoiced to the customer at any point during the contract. Amounts by which cumulative contract revenue recognized on a contract as of a given date exceed cumulative billings to the customer under the contract are reflected as a current asset in our balance sheet under the caption "Costs and estimated earnings in excess of billings." Amounts by which cumulative billings to the customer under a contract as of a given date exceed cumulative contract revenue recognized on the contract are reflected as a current liability in our balance sheet under the caption "Billings in excess of costs and estimated earnings."

The percentage of completion method of accounting is also affected by changes in job performance, job conditions, and final contract settlements. These factors may result in revisions to estimated costs and, therefore, revenue. Such revisions are frequently based on further estimates and subjective assessments. The effects of these revisions are recognized in the period in which 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 conclusion is reached, regardless of the percentage of completion of the contract.

Revisions to project costs and conditions can give rise to change orders under which the customer agrees to pay additional contract price. Revisions can also result in claims we might make against the customer to recover project variances that have not been satisfactorily addressed through change orders with the customer. Except in certain circumstances, we do not recognize revenue or margin based on change orders or claims until they have been agreed upon with the customer. The amount of revenue associated with unapproved change orders and claims was immaterial for the year ended December 31, 2015.

Variations from estimated project costs could have a significant impact on our operating results, depending on project size, and the recoverability of the variation via additional customer payments.

Accounting for Allowance for Doubtful Accounts

We are required to estimate the collectability of accounts receivable and provide an allowance for doubtful accounts for receivable amounts we believe we will not ultimately collect. This requires us to make certain judgments and estimates involving, among others, the creditworthiness of our customers, prior collection history with our customers, 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 the contract. These estimates are evaluated and adjusted as needed when additional information is received.

Accounting for Self-Insurance Liabilities

We are substantially self-insured for workers' compensation, employer's liability, auto liability, general liability and employee group health claims in view of the relatively high per-incident deductibles we absorb under our insurance arrangements for these risks. Losses up to deductible amounts are estimated and accrued based upon known facts, historical trends and industry averages. Loss estimates associated with the larger and longer-developing risks workers' compensation, auto liability and general liability are reviewed by a third party actuary quarterly.

We believe these accruals are adequate. However, insurance liabilities are difficult to 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, ongoing treatment or loss mitigation, general trends in litigation recovery outcomes and the effectiveness of safety and risk management programs. Therefore,

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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 such experience becomes known.

Accounting for Deferred Tax Assets

We regularly evaluate valuation allowances established for deferred tax assets for which future realization is uncertain. We perform this evaluation quarterly. In assessing the realizability of deferred tax assets, we must consider whether it is more likely than not that some portion, or all, of the deferred tax assets will not be realized. We consider all available evidence, both positive and negative, in determining whether a valuation allowance is required. Such evidence includes the scheduled reversal of deferred tax liabilities, projected future taxable income, taxable income in prior carryback years and tax planning strategies in making this assessment, and judgment is required in considering the relative weight of negative and positive evidence.

Acquisitions

We recognize assets acquired and liabilities assumed in business combinations, including contingent assets and liabilities, based on fair value estimates as of the date of acquisition.

Contingent Consideration In certain acquisitions, we agree to pay additional amounts to sellers contingent upon achievement by the acquired businesses of certain predetermined profitability targets. We have recognized liabilities for these contingent obligations based on their estimated fair value at the date of acquisition with any differences between the acquisition-date fair value and the ultimate settlement of the obligations being recognized in income from operations.

Contingent Assets and Liabilities Assets and liabilities arising from contingencies are recognized at their acquisition date fair value when their respective fair values can be determined. If the fair values of such contingencies cannot be determined, they are recognized at the acquisition date if the contingencies are probable and an amount can be reasonably estimated. Acquisition date fair value estimates are revised as necessary if, and when, additional information regarding these contingencies becomes available to further define and quantify assets acquired and liabilities assumed.

Recoverability of Goodwill and Identifiable Intangible Assets

Goodwill is the excess of purchase price over the fair value of the net assets of acquired businesses. We assess goodwill for impairment each year, and more frequently if circumstances suggest an impairment may have occurred.

When the carrying value of a given reporting unit exceeds its fair value, an impairment loss is recorded to the extent that the implied fair value of the goodwill of the reporting unit is less than its carrying value. If other reporting units have had increases in fair value, such increases may not be recorded. Accordingly, such increases may not be netted against impairments at other reporting units. The requirements for assessing whether goodwill has been impaired involve market-based information. This information, and its use in assessing goodwill, entails some degree of subjective assessment.

We perform our annual impairment testing as of October 1 and any impairment charges resulting from this process are reported in the fourth quarter. We segregate our operations into reporting units based on the degree of operating and financial independence of each unit and our related management of them. We perform our annual goodwill impairment testing at the reporting unit level. Each of our operating units represents an operating segment, and our operating segments are our reporting units.

In the evaluation of goodwill for impairment, we have the option to first assess qualitative factors to determine whether the existence of events or circumstances lead to a determination that it is more likely than not that the fair value of one of our reporting units is greater than its carrying value. If, after completing such assessment, we determine it is more likely than not that the fair value of a reporting unit is greater than its carrying amount, then there is no need to perform any further testing. If we conclude otherwise, then we perform the first step of a two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying value of the reporting unit.

We estimate the fair value of the reporting unit based on two market approaches and an income approach, which utilizes discounted future cash flows. Assumptions critical to the fair value estimates under the discounted cash flow model include discount rates, cash flow projections, projected long-term growth rates and the determination of terminal values. The market approaches utilized market multiples of invested capital from comparable publicly traded companies ("public company approach") and comparable transactions ("transaction approach"). The market multiples from invested capital include revenue, book equity plus debt and earnings before interest, taxes, depreciation and amortization ("EBITDA").

There are significant inherent uncertainties and management judgment involved in estimating the fair value of each reporting unit. While we believe we have made reasonable estimates and assumptions to estimate the fair value of our reporting units, it is possible that a material change could occur. If actual results are not consistent with our current estimates and assumptions, or the current economic outlook worsens, goodwill impairment charges may be recorded in future periods.

We amortize identifiable intangible assets with finite lives over their useful lives. Changes in strategy and/or market condition, may result in adjustments to recorded intangible asset balances or their useful lives.

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Results of Operations (in thousands):

	Year Ended December 31,					
	2015		2014		2013	
Revenue	$ 1,580,519	100.0%	$ 1,410,795	100.0%	$ 1,357,272	100.0%
Cost of services	1,262,390	79.9%	1,161,024	82.3%	1,117,389	82.3%

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