

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

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2000

COMMISSION FILE NUMBER: 1-13011

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

DELAWARE
(State or other jurisdiction
of incorporation or organization)

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

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

Securities registered pursuant to Section 12(b) of the Act:

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

Securities registered pursuant to Section 12(g) of the Act: NONE

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

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

As of March 23, 2001, the aggregate market value of the 32,696,669 shares of the registrant's common stock held by non-affiliates of the registrant was \$80,106,839, based on the \$2.45 last sale price of the registrant's common stock on the New York Stock Exchange on that date.

As of March 23, 2001, 37,382,693 shares of the registrant's common stock

were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Part III (other than the required information regarding executive officers) is incorporated by reference from the registrant's definitive proxy statement, which will be filed with the Commission not later than 120 days following December 31, 2000.

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FORWARD-LOOKING STATEMENTS

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

PART I

ITEM 1. BUSINESS

Comfort Systems USA, Inc., a Delaware corporation ("Comfort Systems" and collectively with its subsidiaries, the "Company"), is a leading national provider of comprehensive heating, ventilation and air conditioning ("HVAC") installation, maintenance, repair and replacement services. The Company operates primarily in the commercial and industrial HVAC markets, and performs most of its services within manufacturing plants, office buildings, retail centers, apartment complexes, and healthcare, education and government facilities. In addition to standard HVAC services, the Company provides specialized applications such as process cooling, building automation control systems, electronic monitoring and process piping. Certain locations also perform related services such as electrical and plumbing. Approximately 97% of the Company's consolidated 2000 revenues were derived from commercial and industrial customers with approximately 58% of the revenues attributable to installation services and 42% attributable to maintenance, repair and replacement services.

On July 2, 1997, Comfort Systems completed the initial public offering (the "IPO") of its common stock (the "Common Stock") and simultaneously acquired 12 companies (collectively referred to as the "Founding Companies") engaged in providing HVAC services. The Founding Companies had 18 operating locations in 10 states. Subsequent to the IPO, and through December 31, 2000, the Company acquired 107 HVAC and complementary businesses (collectively with the Founding Companies, the "Acquired Companies"). These acquisitions included 26 "tuck-in" operations that have been integrated with existing Company operations. The Company currently serves its customers with 125 operating locations in 33 states.

INDUSTRY OVERVIEW

The HVAC industry as a whole is estimated to generate annual revenues in excess of \$75 billion, over \$40 billion of which is in the commercial and

industrial markets. HVAC systems are a necessity in virtually all commercial and industrial buildings as well as homes. Because most commercial buildings are sealed, HVAC systems provide the primary method of circulating fresh air in such buildings. Older commercial and industrial facilities often have poor air quality as well as inadequate air conditioning, and older HVAC systems result in significantly higher energy costs than do modern systems. In many instances, the replacement of an aging system with a modern, energy-efficient system will significantly reduce a building's operating costs while also improving air quality and the effectiveness of the HVAC system. These factors cause many facility owners to consider early replacement of older systems.

Growth in the HVAC industry is positively affected by a number of factors, particularly (i) the aging of the installed base, (ii) the increasing efficiency, sophistication and complexity of HVAC systems, (iii) the increasing opportunities associated with utility deregulation and (iv) the increasing standards relating to

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indoor air quality, and the reduction or elimination of the refrigerants commonly used in older HVAC systems. These factors are expected to increase demand for the reconfiguration or replacement of existing HVAC systems. The Company believes that these factors may also mitigate to some extent the effect on the HVAC industry of the cyclicity inherent in the traditional construction industry.

The HVAC industry can be broadly divided into installation services and maintenance, repair and replacement services.

Installation Services. Installation services consist of "design and build" and "plan and spec" projects. In "design and build" projects, the commercial HVAC firm is responsible for designing, engineering and installing a cost-effective, energy-efficient system customized to the specific needs of the building owner. Costs and other project terms are normally negotiated between the building owner or its representative and the HVAC firm. Firms which specialize in "design and build" projects generally have specially-trained HVAC engineers, CAD/CAM design systems and in-house sheet metal and prefabrication capabilities. These firms utilize a consultative approach with customers and tend to develop long-term relationships with building owners and developers, general contractors, architects and property managers. "Plan and spec" installation refers to projects where a third-party architect or consulting engineer designs the HVAC systems and the installation project is "put out for bid." The Company believes that "plan and spec" projects usually take longer to complete than "design and build" projects because the preparation of the system design by a third party and resulting bid process may often take months to complete. Furthermore, in "plan and spec" projects, the HVAC firm is not responsible for project design and any changes must be approved by other parties, thereby increasing overall project time and cost. Approximately 58% of the Company's consolidated 2000 revenues related to installation services and the majority of the revenues from installation projects was performed on a "design and build/negotiated" basis.

Maintenance, Repair and Replacement Services. These services include the maintenance, repair, replacement, reconfiguration and monitoring of previously installed HVAC systems and building automation controls. The growth and aging of the installed base of HVAC systems and the increasing demand for more efficient, sophisticated and complex systems and building automation controls have fueled growth in this service line. The increasing sophistication and complexity of these HVAC systems is leading many commercial and industrial building owners and property managers to increase attention to maintenance and to outsource maintenance and repair, often through service agreements with HVAC service providers. In addition, increasing restrictions are being placed on the use of certain types of refrigerants used in HVAC systems, which, along with indoor air quality concerns, may increase demand for the reconfiguration and replacement of existing HVAC systems. State-of-the-art control and monitoring systems feature electronic sensors and microprocessors. These systems require specialized training to install, maintain and repair, and the typical building engineer has

not received this training. Increasingly, HVAC systems in commercial and industrial buildings are being remotely monitored through PC-based communications systems to improve energy efficiency and expedite problem diagnosis and correction. Approximately 42% of the Company's consolidated 2000 revenues related to maintenance, repair and replacement services.

STRATEGY

The Company has implemented an operating strategy that emphasizes strengthening operating competencies and increasing operating income.

OPERATING STRATEGY. After the recent period of sustained growth through acquisitions, the Company is concentrating on the fundamental industry elements needed to increase operating income and cash flow. The key elements of the Company's operating strategy are:

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

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Achieve Operating Efficiencies. The Company believes there are opportunities to achieve operating efficiencies and cost savings through purchasing economies, the adoption of "best practices" operating programs and a focus on job management to deliver services in a cost-effective and efficient manner. The Company has begun and will continue to use its growing purchasing power to gain volume discounts on products and services such as HVAC components, raw materials, service vehicles, advertising, bonding, insurance and employee benefits.

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

Focus on Commercial and Industrial Markets. The Company primarily focuses on the commercial and industrial markets with particular emphasis on "design and build" installation services and maintenance, repair and replacement services. The Company believes that the commercial and industrial HVAC markets are attractive because of their growth opportunities, diverse customer base, reduced weather exposure as compared to residential markets, attractive margins and potential for long-term relationships with building owners, property managers, general contractors and architects. Approximately 97% of the Company's consolidated 2000 revenues were derived from commercial and industrial customers.

GROWTH IN OPERATING INCOME. A key component of the Company's strategy is to nurture growth in operating income and cash flow at the Company's subsidiaries. The key elements of the Company's internal growth strategy are:

Expand National Service Capabilities. The Company believes that significant demand exists from large regional and national companies to utilize the services of a single HVAC service company capable of providing commercial and industrial services on a regional or national basis. The Company has significantly increased its ability to handle multi-location service opportunities by internally developing a National Service Group to facilitate these activities including an Internet based technology platform and call center designed to manage HVAC and related service along with the information needs of multi-location customers. The Company believes its

growing ability to add value in these areas will lead to improved profitability.

Capitalize on Specialized Technical and Marketing Strengths. The Company believes it will be able to continue to expand the services it offers in its markets by leveraging the specialized technical and marketing strengths of individual companies. The Company also believes its size and geographical coverage will enable it to serve existing customers' needs in new regions that may have been beyond the service area of the Company's operations that originated the existing customer relationship.

Expand Alliances with Energy Providers. The Company believes that there is significant potential for mutually beneficial relationships with companies that market energy and energy services. The Company is currently working with several companies in the utility industry through cooperative marketing of the Company's services and is seeking to provide utilities the opportunity to profit and to benefit from the Company's own customer relationships. The Company believes it can expand these relationships as it gains experience with successful programs and as its geographic presence increases.

Leveraging Resources. The Company believes that there are significant operating efficiencies that can be achieved in the leveraging of resources between its operating locations. The Company has shifted certain prefabrication activities into centralized locations increasing asset utilization in these centralized locations and redirecting prefabrication employees into other operational areas that no longer perform these services. The Company has also transferred its engineering, field and supervisory labor from one operation to another in order to more fully utilize the employee base to meet the customers' needs and share expertise.

OPERATIONS SERVICES PROVIDED

The Company provides a wide range of installation, maintenance, repair and replacement services for HVAC and related systems in commercial and industrial properties. The Company manages its locations on a decentralized basis, with local management maintaining responsibility for day-to-day operating decisions. Local management is augmented by a regional team that focuses its efforts on cooperation and coordination between locations, implementation of best practices and focus on major corporate initiatives. In addition to senior management, local personnel generally include design engineers, sales personnel, customer service personnel, installation and service technicians, sheet metal and prefabrication technicians, estimators and administrative personnel. The Company has centralized certain administrative functions such as insurance, employee benefits, training, safety programs, marketing and cash management to enable the management of its locations to focus on pursuing new business opportunities and improving operating efficiencies. The Company is continuing to expand its national sales and purchasing programs.

Installation Services. The Company's installation business, which comprised approximately 58% of the Company's 2000 consolidated revenues, involves the design, engineering, integration, installation and start-up of HVAC and related systems. The commercial and industrial installation services performed by the Company consist of "design and build" and under some circumstances, "plan and spec" services for manufacturing plants, office buildings, retail centers, apartment complexes, health care, education and government facilities and other commercial and industrial facilities. In a "design and build" project, the customer typically has an overall design for the facility prepared by an architect or a consulting engineer who then enlists the Company's engineering personnel to prepare a specific design for the HVAC system. The Company determines the needed capacity, energy efficiency and type of building automation controls that best suit the proposed facility. The Company's engineer then estimates the amount of time, labor, materials and equipment needed to build the specified system. The final design, terms, price

and timing of the project are then negotiated with the customer or its representatives, after which any necessary modifications are made to the system. In "plan and spec" installation the Company participates in a bid process to provide labor, equipment, materials and installation based on plans and engineering provided by a customer or a general contractor.

Once an agreement has been reached, the Company orders the necessary materials and equipment for delivery to meet the project schedule. In most instances, the Company fabricates in its own facilities the ductwork and piping and assembles certain components for the system based on the mechanical drawing specifications, eliminating the need to subcontract ductwork or piping fabrication. The Company installs the system at the project site, working closely with the general contractor. Most commercial and industrial installation projects last from two weeks to one year and generate revenues from \$50,000 to \$3,000,000 per project. These projects are generally billed periodically as costs are incurred and, in most cases, with retainage of up to 10% held back until completion and successful start-up of the HVAC system.

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

Maintenance, Repair and Replacement Services. The Company's maintenance, repair and replacement services comprised approximately 42% of the Company's 2000 consolidated revenues, and include the maintenance, repair, replacement, reconfiguration and monitoring of HVAC systems and industrial process

piping. Over two-thirds of the Company's maintenance, repair and replacement revenues were derived from reconfiguring existing HVAC systems for commercial and industrial customers. Reconfiguration often utilizes consultative expertise similar to that provided in the "design and build" installation market. The Company believes that the reconfiguration of an existing system results in a more cost-effective, energy-efficient system that better meets the specific needs of the building owner. The reconfiguration also enables the Company to utilize its design and engineering personnel as well as its sheet metal and pre-fabrication facilities.

Maintenance and repair services are provided either in response to service calls or pursuant to a service agreement. Service calls are coordinated by customer service representatives or dispatchers that use computer and communication technology to process orders, arrange service calls, communicate with customers, dispatch technicians and invoice customers. Service technicians work from service vehicles equipped with commonly used parts, supplies and tools to complete a variety of jobs.

Commercial and industrial service agreements usually have terms of one to three years, with automatic annual renewals. The Company also provides 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 used by the Company include HVAC system components, ductwork, steel, sheet metal and copper tubing and piping. These raw materials and components are generally available from a variety of domestic or foreign suppliers at competitive prices. Delivery times are typically short for most raw materials and standard components, but during periods of peak demand, may extend to a month or more. Chillers for large units typically have the longest delivery time and generally have lead times of up to six months. The major components of commercial HVAC systems are compressors and chillers that are manufactured primarily by York Heating and Air Conditioning Corporation ("York"), Carrier Corporation and Trane Air Conditioning Company. The major suppliers of building automation control systems are Honeywell Inc., Johnson Controls Inc., York, Automated Logic, Novar and Andover Control Corporation. The Company does not have any significant contracts guaranteeing the Company a supply of raw materials or components.

SALES AND MARKETING

The Company has a diverse customer base, with no single customer accounting for more than 2% of consolidated 2000 revenues. Management and a dedicated sales force have been responsible for developing and maintaining successful long-term relationships with key customers. Customers generally include building owners and developers and property managers, as well as general contractors, architects and consulting engineers. The Company intends to continue its emphasis on developing and maintaining long-term relationships with its customers by providing superior, high-quality service in a professional manner. Moreover, the dedicated sales force receives technical and sales training to enhance the comprehensive selling skills necessary to serve the HVAC needs of their customers.

The Company has a national sales team to capitalize on cross-marketing and business development opportunities that management believes are available to the Company as a regional or national provider of comprehensive commercial and industrial HVAC and related services. Management believes that it can increasingly leverage the diverse technical and marketing strengths at individual locations to expand the services offered in other local markets.

EMPLOYEES

As of December 31, 2000, the Company had 10,959 employees, including 599 management personnel, 8,859 engineers, service and installation technicians, 358 sales personnel and 1,143 administrative personnel across its 125 operating locations. Certain of the Company's subsidiaries have collective bargaining agreements that cover, in the aggregate, approximately 2,795 employees. The Company has not experienced any

significant strikes or work stoppages and believes its relations with employees covered by collective bargaining agreements are good.

RECRUITING, TRAINING AND SAFETY

The Company's continued future success will depend, in part, on its ability to continue to attract, retain and motivate qualified service technicians, field supervisors and project managers. The Company believes that its success in retaining qualified employees will be based on the quality of its recruiting, training, compensation, employee benefits programs and opportunities for advancement. The Company has a national recruiting network and also recruits via the internet and at local technical schools and community colleges where students focus on learning basic industry skills. Additionally, Comfort Systems provides on-the-job training, technical training, apprenticeship programs, attractive benefit packages, steady employment and career advancement

opportunities within the Company.

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

RISK MANAGEMENT, INSURANCE AND LITIGATION

The primary risks in the Company's operations are bodily injury, property damage and injured workers' compensation. The Company maintains liability insurance for bodily injury, third party property damage and workers' compensation which it considers sufficient to insure against these risks, subject to self-insured amounts.

The Company is subject to certain claims and lawsuits arising in the normal course of business and maintains various insurance coverages to minimize financial risk associated with these claims. The Company has provided accruals for probable losses and legal fees associated with certain of these actions in its consolidated financial statements. In the opinion of management, uninsured losses, if any, resulting from the ultimate resolution of these matters will not have a material adverse effect on the Company's financial position or results of operations.

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

COMPETITION

The HVAC industry is highly competitive. The Company believes that purchasing decisions in the commercial and industrial markets are based on (i) long-term customer relationships, (ii) quality, timeliness and reliability of services provided, (iii) competitive price, (iv) range of services provided and (v) scale of operation. The Company's strategy of focusing on both the highly consultative "design and build" installation market and the maintenance, repair and replacement market promotes the development and strengthening of long-term customer relationships. In addition, the Company's ability to provide multi-location coverage, project financing and specialized technical skills for facilities owners gives it a strategic advantage over smaller competitors who may be unable to provide these services to customers at a competitive price.

Many of the Company's competitors are small, owner-operated companies that typically operate in a limited geographic area. There are also public companies, divisions of utility companies and equipment manufacturers that are focused on providing HVAC services in some of the same service lines provided by the

Company. Certain of the Company's competitors and potential competitors may have greater financial resources than the Company to finance development opportunities and support their operations.

FACILITIES AND VEHICLES

The Company leases the majority of its facilities. In most instances these leases are with the former owners of the Acquired Companies who are now employed

by the Company. Leased premises range in size from approximately 1,000 square feet to over 100,000 square feet. The Company believes that its facilities are sufficient for its current needs.

The Company operates a fleet of various owned or leased service trucks, vans and support vehicles. The Company believes that these vehicles generally are well maintained and adequate for its current operations.

GOVERNMENTAL REGULATION AND ENVIRONMENTAL MATTERS

The Company's operations are subject to various federal, state and local laws and regulations, including: (i) licensing requirements applicable to service technicians, (ii) building and HVAC codes and zoning ordinances, (iii) regulations relating to consumer protection, including those governing residential service agreements and (iv) regulations relating to worker safety and protection of the environment. The Company believes it has all required licenses to conduct its operations and is in substantial compliance with applicable regulatory requirements. Failure of the Company to comply with applicable regulations could result in substantial fines or revocation of the Company's operating licenses.

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

The Company's operations are subject to the federal Clean Air Act, as amended (the "Clean Air Act"), which governs air emissions and imposes specific requirements on the use and handling of chlorofluorocarbons ("CFCs") and certain other refrigerants. Clean Air Act regulations require the certification of service technicians involved in the service or repair of equipment containing these refrigerants and also regulate the containment and recycling of these refrigerants. These requirements have increased the Company's training expenses and expenditures for containment and recycling equipment. The Clean Air Act is intended ultimately to eliminate the use of CFCs in the United States and to require alternative refrigerants to be used in replacement HVAC systems.

EXECUTIVE OFFICERS

The Company has seven executive officers.

William F. Murdy, age 59, has served as Chairman of the Board and Chief Executive Officer of Comfort Systems since June 2000. Prior to this he was Interim President and Chief Executive Officer of Club Quarters, a privately-owned chain of membership hotels. From January 1998 through July 1999, Mr. Murdy served as President, Chief Executive Officer and Chairman of the Board of LandCare USA, a publicly-traded commercial landscape and tree services company. He was primarily responsible for the organization of LandCare USA and its listing as a publicly-traded company on the New York Stock Exchange in July 1998. LandCare USA was acquired in July 1999 by another publicly-traded company specializing in services to homeowners and commercial facilities. From 1989 through December 1997, Mr. Murdy was President and Chief Executive Officer of General Investment and Development Company, a privately-held real estate operating company. From 1981 to 1989, Mr. Murdy served as the Managing General Partner of the Morgan Stanley Venture Capital Fund. From 1974 to 1981, Mr. Murdy served as the Senior Vice President and Chief Operating Officer, among other positions, of Pacific Resources, Inc., a publicly-traded company involved primarily in petroleum refining and marketing.

Gary E. Hess, age 53, has served as President and Chief Operating Officer

since September 2000 and Executive Vice President and Chief Operating Officer of Comfort Systems since June 1999. Prior to this he was the Senior Vice President-Operations from February 1999 to May 1999. In March 2000, the Board of Directors unanimously elected Mr. Hess as a director of Comfort Systems. He served Comfort Systems as regional director of its Northeast region from August 1998 to January 1999. Prior to that, he was employed by Hess Mechanical Corporation, a wholly-owned subsidiary of the Company, since 1980, serving as Chairman and Chief Executive Officer. Mr. Hess was President of Associated Builders and Contractors during 1996 and was selected as their 1997 Contractor of the Year.

J. Gordon Beittenmiller, age 42, has served as Executive Vice President, Chief Financial Officer and a director of Comfort Systems since May 1998, and was Senior Vice President, Chief Financial Officer and a director of Comfort Systems from February 1997 to April 1998. From 1994 to February 1997, Mr. Beittenmiller was Corporate Controller of Keystone International, Inc. ("Keystone"), a publicly-traded manufacturer of industrial valves and actuators, and served Keystone in other financial positions from 1991 to 1994. From 1987 to 1991, he was Vice President-Finance of Critical Industries, Inc., a publicly-traded manufacturer and distributor of specialized safety equipment. From 1982 to 1987, he held various positions with Arthur Andersen LLP. Mr. Beittenmiller is a Certified Public Accountant.

Reagan S. Busbee, age 37, has served as Senior Vice President of Comfort Systems since January 1997. From 1992 through 1996, Mr. Busbee served as Vice President of Chas. P. Young Co., a financial printer and a wholly-owned subsidiary of Consolidated Graphics Inc., a publicly-traded consolidator of the printing industry. From August 1986 to May 1992, he held various positions and was a Certified Public Accountant with Arthur Andersen LLP.

William George, III, age 36, has served as Senior Vice President, General Counsel and Secretary of Comfort Systems since May 1998, and was Vice President, General Counsel and Secretary of Comfort Systems 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 consolidator of the healthcare transportation industry. From September 1992 to September 1995, Mr. George practiced corporate and antitrust law at Ropes & Gray, a Boston, Massachusetts law firm.

Milburn Honeycutt, age 37, has served as Vice President and Corporate Controller of Comfort Systems since February 1997. He was promoted to Senior Vice President in September 2000. From 1994 to January 1997, Mr. Honeycutt was Financial Accounting Manager -- Corporate Controllers Group for Browning-Ferris Industries, Inc., a publicly-traded waste services company. From 1986 to 1994, he held various positions with Arthur Andersen LLP and was a Certified Public Accountant.

D. F. "Rick" Miller, age 56, has served as Senior Vice President-Organizational Development of Comfort Systems since January 2001. In September 1999, Mr. Miller founded Innovative Leadership Partners LLP, a leadership development consulting partnership serving both individuals and organizations and was a consultant with that entity through December 2000. From January 1999 to August 1999, Mr. Miller was Vice President of Administration with Integrated Electrical Services, a publicly-traded provider of specialty contractor services in the electrical and communications industry. Mr. Miller served as a senior consultant involved with organizational improvement and people development at Mercuri Urval USA from March 1998 to December 1998. Prior to that, Mr. Miller served as a career naval officer and carrier aviator from June 1968 to February 1998, where he held numerous leadership positions in carrier-based squadrons and served in the Pentagon, on the Joint Staff and in the office of the Secretary of the Navy.

Most of the Company's subsidiaries lease the real property and buildings from which they operate. The Company's facilities consist of offices, shops, maintenance and warehouse facilities. Generally, leases range from five to ten years and are on terms the Company believes to be commercially reasonable. Certain of these facilities are leased from related parties. In order to maximize available capital, the Company generally intends to continue to lease the majority of its properties. The Company believes that its facilities are adequate for its current needs.

The Company leases its executive and administrative offices in Houston, Texas.

ITEM 3. LEGAL PROCEEDINGS

The Company is subject to certain claims and lawsuits arising in the normal course of business and maintains various insurance coverages to minimize financial risk associated with these claims. The Company has provided accruals for probable losses and legal fees associated with certain of these actions in its consolidated financial statements. In the opinion of management, uninsured losses, if any, resulting from the ultimate resolution of these matters will not have a material adverse effect on the Company's financial position or results of operations.

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

None.

PART II

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

The following table sets forth the reported high and low sales prices of the Common Stock for the quarters indicated as traded at the New York Stock Exchange. The Common Stock is traded under the symbol FIX.

	HIGH -----	LOW -----
First Quarter, 1999.....	\$ 18.50	\$11.375
Second Quarter, 1999.....	\$18.5625	\$13.125
Third Quarter, 1999.....	\$ 18.625	\$ 11.25
Fourth Quarter, 1999.....	\$ 12.00	\$6.4375
First Quarter, 2000.....	\$ 9.375	\$ 6.375
Second Quarter, 2000.....	\$ 7.50	\$ 3.875
Third Quarter, 2000.....	\$ 5.625	\$ 3.375
Fourth Quarter, 2000.....	\$ 5.1875	\$ 2.00
January 1 -- March 23, 2001.....	\$ 2.80	\$2.0625

As of March 23, 2001, there were approximately 657 stockholders of record of the Company's Common Stock, and the last reported sale price on that date was \$2.45 per share.

The Company has never declared or paid a dividend on its Common Stock. The Company currently expects to retain future earnings in order to repay debt and finance growth and, consequently, does not intend to declare any dividend on the Common Stock for the foreseeable future. In addition, the Company's revolving credit agreement restricts the ability of the Company to pay dividends without the lenders' consent. The Company's Restricted Voting Common Stock converts to Common Stock upon sale and under certain other conditions.

RECENT SALES OF UNREGISTERED SECURITIES

During 2000, the Company did not issue any unregistered shares of its Common Stock.

ITEM 6. SELECTED FINANCIAL DATA

Comfort Systems acquired the 12 Founding Companies in connection with the IPO on July 2, 1997. Subsequent to the IPO and through December 31, 2000, the Company completed 107 acquisitions, 17 of which were accounted for as poolings-of-interests (the "Pooled Companies") and 90 of which were accounted for as purchases (the "Purchased Companies"). The following selected historical financial data has been derived from the audited financial statements of the Company. The historical financial statement data reflects the acquisitions of the Founding Companies and Purchased Companies as of their respective acquisition dates and reflects 15 of the Pooled Companies (the "Restated Companies") for all periods presented. Two of the Pooled Companies are considered immaterial poolings based upon criteria set forth by the Securities and Exchange Commission and have not been restated for all periods presented. The selected historical financial data below should be read in conjunction with the historical Consolidated Financial Statements and related notes.

	YEAR ENDED DECEMBER 31,				
	1996	1997	1998	1999	2000
	(IN THOUSANDS)				
STATEMENT OF OPERATIONS DATA:					
Revenues.....	\$161,419	\$297,646	\$853,961	\$1,370,035	\$1,591,066
Operating income.....	\$ 6,575	\$ 5,699	\$ 68,497	\$ 93,204	\$ 20,427
Net income (loss).....	\$ 4,589	\$ (2,064)	\$ 35,013	\$ 42,322	\$ (16,853)
BALANCE SHEET DATA:					
Working capital.....	\$ 13,971	\$ 63,137	\$133,390	\$ 168,341	\$ 173,219
Total assets.....	\$ 50,366	\$308,779	\$789,293	\$ 934,530	\$ 926,410
Total debt, including					
current portion.....	\$ 8,376	\$ 24,726	\$236,446	\$ 305,833	\$ 274,601
Stockholders' equity.....	\$ 15,429	\$217,635	\$379,932	\$ 418,965	\$ 400,239

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

INTRODUCTION

The following discussion should be read in conjunction with the historical Consolidated Financial Statements of Comfort Systems USA, Inc. ("Comfort Systems" and collectively with its subsidiaries, the "Company") and related notes thereto included elsewhere in this Form 10-K. This discussion contains forward-looking statements regarding the business and industry of Comfort Systems within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based on the current plans and expectations of the Company and involve risks and uncertainties that could cause actual future activities and results of operations to be materially different from those set forth in the forward-looking statements. Important factors that could cause actual results to differ are discussed under "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Factors Which May Affect Future Results."

The Company is a leading national provider of comprehensive HVAC installation, maintenance, repair and replacement services. The Company operates primarily in the commercial and industrial HVAC markets and performs most of its services within manufacturing plants, office buildings, retail centers, apartment complexes, and healthcare, education and government facilities. In

addition to standard HVAC services, the Company provides specialized applications such as process cooling, building automation control systems, electronic monitoring and process piping. Certain locations also perform related services such as electrical and plumbing.

RESULTS OF OPERATIONS

	YEAR ENDED DECEMBER 31,					
	1998		1999		2000	
	(IN THOUSANDS)					
Revenues.....	\$853,961	100.0%	\$1,370,035	100.0%	\$1,591,066	100.0%
Cost of services.....	647,512	75.8%	1,077,329	78.6%	1,306,816	82.1%
Gross profit.....	206,449	24.2%	292,706	21.4%	284,250	17.9%
Selling, general and administrative expenses.....	130,820	15.3%	187,771	13.7%	225,894	14.2%
Goodwill amortization.....	7,132	0.8%	11,731	0.9%	12,585	0.8%
Restructuring charges.....	--	--	--	--	25,344	1.6%
Operating income.....	68,497	8.1%	93,204	6.8%	20,427	1.3%
Other expense, net.....	(6,435)	(0.8)%	(19,144)	(1.4)%	(25,628)	(1.6)%
Reductions in non-operating assets and liabilities, net.....	--	--	--	--	(5,867)	(0.4)%
Income (loss) before income taxes.....	62,062	7.3%	74,060	5.4%	(11,068)	(0.7)%
Income tax expense.....	27,049		31,738		5,785	
Net income (loss).....	\$ 35,013	4.1%	\$ 42,322	3.1%	\$ (16,853)	(1.1)%

2000 Compared to 1999

Revenues -- Revenues increased \$221.0 million or 16.1% to \$1.6 billion in 2000 compared to 1999. The 16.1% revenue growth was comprised of approximately 12.0% internal growth and 4.1% for 1999 acquisitions that are included in the Company's results for the full year of 2000. Approximately 3% of the revenue growth resulted from the Company's ability to increase volume by subcontracting portions of projects to other contractors.

Of the 12.0% internal growth rate compared to last year, approximately one-half of this internal growth was attributable to the Company's largest single operation. This growth represented substantial increases in volume at this operation which did not result in commensurate increases in profitability due to scarce technical and skilled labor and customer scheduling and site restrictions related to strong business conditions. The Company has experienced these kinds of challenges at numerous other operations as well, and believes they reflect high levels of activity and capacity constraints for the construction industry in general. As a result, management is placing less emphasis on revenue growth and more on operations, cash flow, efficiency and profit margin improvements for 2001 across all operations. It is likely, therefore, that the Company will experience flat to slower revenue growth in future periods. There can be no assurance, however, that this strategy will lead to improved profit margins in the near term.

Gross Profit -- Gross profit decreased \$8.5 million, or 2.9%, to \$284.3 million in 2000 compared to 1999. As a percentage of revenues, gross profit decreased from 21.4% in 1999 to 17.9% in 2000.

During 2000, the Company experienced disappointing results from certain locations due to execution shortfalls on projects and weak performance at several locations relating to ongoing turnaround efforts.

During 2000, the Company experienced significant execution shortfalls on certain projects at its largest operation, and at an operating location on the West Coast, and at a location in the Southeast. These execution shortfalls resulted from difficulty in obtaining quality skilled and technical labor in certain markets, scheduling changes imposed by the customers and poor pricing and estimating by two previous operating managers. The Company also experienced weak operating performance at several locations relating to ongoing turnaround efforts and execution difficulties. The Company has decided to cease operating at or sell eight of these locations which reported a combined negative gross profit of \$2.7 million during 2000.

Gross profit in 2000 was also reduced, to a lesser extent, by the Company's e-commerce activities which were abandoned in the fourth quarter of 2000. The costs associated with these decisions are included in the

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restructuring charges discussed below. The remaining decrease in gross profit as a percentage of revenues resulted from increased labor costs, pricing pressures in certain markets and scheduling and efficiency challenges associated with labor availability and productivity at the high levels of activity at most of our operations. The Company has also increased the amount of activity it subcontracts to third parties. Pricing to the Company's customers of such subcontracted work generally carries lower margins than the Company's self-performed work.

Selling, General and Administrative Expenses ("SG&A") -- SG&A increased \$38.1 million, or 20.3%, to \$225.9 million in 2000 compared to 1999. As a percentage of revenues, SG&A increased from 13.7% in 1999 to 14.2% in 2000. This increase in SG&A as a percentage of revenues resulted primarily from the inclusion in 2000 of results of companies acquired in 1999 that have higher SG&A as a percentage of revenues than the rest of the Company's operations. These acquisitions included Outbound Services where the Company incurred significantly higher SG&A to support expansion of its e-commerce activities. During the 4th quarter of 2000, the Company decided to cease its e-commerce activities at Outbound, and costs associated with this decision are included in restructuring charges as discussed below.

The Company has also increased corporate and regional office spending to support the requirements of a larger organization, and to increase its efforts to obtain more national account and energy project business. In addition, as discussed above, the Company has experienced weak performance at several locations related to turnaround efforts and execution difficulties, and these companies have realized a disproportionate amount of SG&A as compared to their revenues. During the latter part of 2000, the Company identified certain accounts receivable that were deemed uncollectible and written off. This necessitated increased provisions for bad debt in SG&A, which also contributed to the Company's higher SG&A as a percentage of revenues.

Restructuring Charges -- During 2000, the Company recorded restructuring charges of approximately \$25.3 million primarily associated with restructuring efforts at certain underperforming operations and its decision to cease its e-commerce activities at Outbound Services, a subsidiary of the Company. As announced by the Company in the third quarter of 2000, management performed an extensive review of its operations during the second half of 2000. As part of this review, management decided to cease operating at three locations, sell five operations (including two smaller satellite operations), and merge two companies into other operations. These actions are substantially complete except that the Company is seeking buyers for two operations it is holding for sale. The Company anticipates that these operations will be sold during the first half of 2001. The aggregate results for 2000 related to the operations and activities included in the restructuring charges were revenues of \$46.1 million and operating losses of \$17.1 million. The restructuring charges are primarily non-cash and include goodwill impairments of approximately \$11.5 million and the writedown of other long-lived assets of approximately \$8.5 million. The remaining restructuring items primarily include severance and lease termination costs. Severance costs

relate to the termination of approximately 145 employees including certain corporate personnel and the management and employees of certain underperforming locations, and to the departure of the Company's former chief executive officer.

Other Expense, Net -- Other expense, net, increased \$6.5 million, or 33.9%, to \$25.6 million in 2000 compared to 1999. This increase was primarily due to the increase in interest expense related to additional borrowings and consideration paid for companies acquired in 1999.

Reductions in Non-Operating Assets and Liabilities, Net -- During 2000, the Company recorded a non-cash charge of approximately \$5.9 million primarily related to the impairment of certain non-operating assets. These assets primarily related to notes receivable from former business owners that were collateralized by shares of the Company's stock. This charge also included an impairment of approximately \$1.4 million to the Company's minority investment in two entities associated with the distribution and implementation of high-end engineering and design software. These entities have ceased operations. Also included in this charge was a gain of approximately \$0.6 million on the reduction of the Company's subordinated note payable to a former owner in connection with the settlement of claims with this former owner.

Income Tax Expense -- The Company's effective tax rate for 2000 was (52.3%) as compared to 42.9% for 1999. The Company reported income tax expense of \$5.8 million for 2000 related to its pre-tax loss of \$11.1 million primarily due to the writedown of non-deductible goodwill associated with the Company's

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restructuring activities. The Company's provision for income taxes also differs from the federal statutory rate due to state income taxes (net of federal income tax benefit) and the non-deductibility of the amortization of goodwill attributable to certain acquisitions.

1999 Compared to 1998

Revenues -- Revenues increased \$516.1 million, or 60.4%, to \$1.4 billion in 1999 compared to 1998. The increase in revenues over the prior year is primarily due to the acquisition of Purchased Companies in 1998 and 1999; however, the Company experienced lower internal revenue growth in the latter part of fiscal 1999 as compared to previous periods. The Company believes that this is primarily attributable to a slowing in the growth of the construction industry due to shortages in both labor and specialty building materials, which in turn impacted HVAC installations.

Gross Profit -- Gross profit increased \$86.3 million, or 41.8%, to \$292.7 million in 1999 compared to 1998. The increase in gross profit is primarily due to the acquisitions described above. As a percentage of revenues, gross profit decreased from 24.2% in 1998 to 21.4% in 1999. This decrease primarily resulted from the change in classification of certain costs from SG&A to cost of services. These costs relate to activities that directly support project or service work. Management believes this revised presentation better aligns the presentation of cost of services and SG&A across all of our acquired operations. Excluding the effect of this change in classification for 1999 of approximately \$37.2 million, gross profit as a percentage of revenues remained relatively unchanged at 24.1% in 1999 versus 24.2% in 1998.

During 1999, the Company experienced increased gross profit margins from strong performances in commercial and industrial markets in the Northeast, Phoenix and Orlando as well as operating synergies achieved between its western Michigan companies. However, in the latter part of fiscal 1999 the Company has experienced lower internal revenue growth as a result of construction industry capacity issues as discussed above. In addition, there has been a shift in the mix of installation projects to higher labor-intensive projects with lower gross profit percentages, pricing competition in certain markets and execution shortfalls and inefficiencies as the Company sought stronger revenue growth levels.

Selling, General and Administrative Expenses -- SG&A increased \$57.0 million, or 43.5%, to \$187.8 million in 1999 compared to 1998. Most of this increase was related to Purchased Companies along with an increase in corporate personnel and corporate office expenses commensurate with the increase in the number of Acquired Companies. As a percentage of revenues, SG&A decreased from 15.3% in 1998 to 13.7% in 1999. This decrease is primarily attributable to the change in classification of certain costs as described above. Excluding the effect of this change in classification for 1999 of approximately \$37.2 million, SG&A expenses as a percentage of revenues increased from 15.3% for 1998 to 16.4% for 1999. This increase in SG&A as a percentage of revenues resulted primarily from lower internal revenue growth as discussed above and increased healthcare costs under the Company's self-insured medical plan. SG&A for 1998 includes \$1.8 million of salaries and benefits paid to the former owners of the Pooled Companies which the former owners contractually agreed would not continue following their acquisition by Comfort Systems.

Operating Income -- Operating income increased \$24.7 million, or 36.1%, to \$93.2 million in 1999 compared to 1998 primarily due to the addition of Purchased Companies. As a percentage of revenues, operating income decreased from 8.1% in 1998 to 6.8% in 1999. The decrease in operating income as a percentage of revenues resulted from issues discussed above.

Other Expense, Net -- Other expense, net, increased \$12.7 million, or 197.5%, to \$19.1 million in 1999 compared to 1998 primarily due to the increase in interest expense related to the acquisition of the Purchased Companies.

Income Tax Expense -- The Company's effective tax rate for 1999 was 42.9% as compared to 43.6% for 1998. The Company's provision for income taxes differs from the federal statutory rate primarily due to state income taxes (net of federal income tax benefit) and the non-deductibility of the amortization of goodwill attributable to certain acquisitions.

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LIQUIDITY AND CAPITAL RESOURCES

Cash Flow -- For the year ended December 31, 2000, net cash provided by operating activities was \$58.2 million, or an increase of \$39.8 million over the prior year. This improvement primarily results from lengthier payment cycles on accounts payable and accrued liabilities, and from faster billing by the Company for its project work while maintaining the same average days to collect receivables once billed. Cash provided by operations for 1999 was \$18.4 million and cash used in operations in 1998 was \$5.5 million.

Cash used in investing activities was \$15.4 million for the year ended December 31, 2000, primarily in connection with purchases of property and equipment for \$18.0 million. Cash flows used in investing activities for 1999 and 1998 were \$46.5 million and \$143.1 million, respectively. The uses of cash in 1999 and 1998 were primarily for the acquisition of purchased companies.

Cash used in financing activities for the year ended December 31, 2000 was \$30.4 million and was primarily attributable to net payments on long-term debt of \$30.7 million. Net cash provided by financing activities in 1999 was \$24.7 million and was due primarily to net borrowings of long-term debt which were used to fund acquisitions. Net cash provided by financing activities in 1998 was \$137.5 million and was primarily attributable to the \$16.7 million received from the second public offering and net borrowings of long-term debt of \$124.2 million, which were primarily used to fund acquisitions.

Revolving Credit Facility -- The Company amended its revolving credit facility (the "Credit Facility" or the "Facility") provided by Bank One, Texas, N.A. ("Bank One") and other banks (the "Bank Group") in March 2001. As amended, the Credit Facility provides the Company with a revolving line of credit of up to the lesser of \$270 million or 80% of net accounts receivable. The Facility decreases to the lesser of \$250 million or 80% of net accounts receivable as of December 31, 2001, and to the lesser of \$240 million or 80% of net accounts

receivable as of June 30, 2002. Borrowings under the Facility are secured by accounts receivable, inventory, fixed assets other than real estate, and the shares of capital stock of the Company's subsidiaries. The Credit Facility expires on January 1, 2003, at which time all amounts outstanding are due.

The Company has a choice of two interest rate options under the Facility. Under one option, the interest rate is determined based on the higher of the Federal Funds Rate plus 0.5% or Bank One's prime rate. An additional margin of 1% to 2% is then added to the higher of these two rates. Under the other interest rate option, borrowings bear interest based on designated short-term Eurodollar rates (which generally approximate London Interbank Offered Rates or "LIBOR") plus 2.5% to 3.5%. The additional margin for both options depends on the ratio of the Company's debt to earnings before interest, taxes, depreciation and amortization ("EBITDA"), as defined. Commitment fees of 0.375% to 0.5% per annum, also depending on the ratio of debt to EBITDA, are payable on the unused portion of the Facility.

The Credit Facility prohibits payment of dividends by the Company, limits certain non-Bank Group debt, and restricts outlays of cash by the Company relating to certain investments, capital expenditures, vehicle leases, acquisitions and subordinate debt. The Credit Facility also provides for the maintenance of certain levels of shareholder equity and EBITDA, and for the maintenance of certain ratios of the Company's EBITDA to interest expense and debt to EBITDA.

Under the terms of the Credit Facility that were in effect as of June 30 and September 30, 2000, the Company was in violation of certain of the Facility's financial balance and ratio requirements. The Bank Group waived these violations. The restrictions and financial balance and ratio requirements currently effective under the Facility allow for performance during the first and second quarters of 2001 consistent with the Company's results in recent quarters, excluding restructuring and other nonrecurring charges. The Facility's restrictions and requirements then call for improvement from recent performance levels in the third and fourth quarters of 2001 and on a quarterly basis in 2002. The Facility also prohibits repurchase of the Company's stock and has relatively tight approval requirements on acquisitions. The Facility's requirements reflect tighter restrictions, greater specificity and smaller allowable variances on most financial balances and ratios than is typical for such agreements due to the Company's weaker results in 2000. While management believes its restructuring efforts and operating strategies along with general market conditions in the commercial/industrial HVAC and building automation controls industry will enable the Company to meet the

Facility's requirements, there can be no assurance that the Company will be successful in doing so. Management intends to seek more flexible terms under its borrowing relationships as its results and credit market conditions allow.

As of December 31, 2000, the Company had \$223.7 million in borrowings outstanding under the Credit Facility and had incurred interest expense at an average rate of approximately 8.9% for the year ended December 31, 2000. The Credit Facility's interest rate terms as summarized above are effective as of March 22, 2001 and currently result in an all-in floating interest rate under the Facility's LIBOR option of approximately 8.9%. As of December 31, 2000, the Company also had \$2.0 million in letters of credit outstanding under the Facility, and unused borrowing capacity under the Facility of \$41.6 million. As of March 23, 2001, \$226.9 million in borrowings and \$1.9 million in letters of credit were outstanding under the Facility, and \$36.6 million in unused capacity was available.

Notes to Affiliates and Former Owners -- Subordinated notes were issued to former owners of certain purchased companies as part of the consideration used to acquire their companies. These notes had an outstanding balance of \$50.3 million as of December 31, 2000. Of these notes, \$49.9 million bear interest, payable quarterly, at a weighted average interest rate of 5.8% and \$0.4 million

are non-interest bearing. In addition, \$1.2 million of these notes are convertible by the holders into shares of the Company's Common Stock at a weighted average price of \$25.27 per share. The originally scheduled maturities of the subordinated notes are \$3.4 million in 2000, \$24.0 million in 2001, \$22.0 million in 2002, and \$0.9 million in 2003.

As a result of the Company's covenant violations in 2000 under the Credit Facility, the Bank Group required that originally scheduled principal payments to subordinate debt holders be suspended. This requirement took effect in October 2000. In March 2001, the Company entered into amended agreements with subordinate debt holders representing \$44.4 million in principal, including all the principal originally scheduled to be paid through 2001. These amended agreements allow for partial payments against certain originally scheduled payment amounts, defer remaining principal balances to April 2003, and increase the interest rate on this debt to 10% per annum, payable quarterly. As a result of these amended agreements, the Company's annual maturities of subordinate debt are now \$8.9 million in 2001, \$6.6 million in 2002, and \$34.8 million in 2003.

Stock Repurchases -- On October 5, 1999, the Company announced that its Board of Directors had approved a share repurchase program authorizing the Company to buy up to 4.0 million shares of its Common Stock. During 1999, the Company purchased approximately 1.8 million shares at a cost of approximately \$12.9 million. During 2000, the Company purchased approximately 0.2 million shares at a cost of approximately \$1.2 million. The Company does not expect further share repurchases under this program for the foreseeable future.

Outlook -- The Company anticipates that available borrowings under its Credit Facility and cash flow from operations will be sufficient to meet the Company's normal working capital and capital expenditure needs. As noted above, the Company has agreed to relatively tight restrictions under the Credit Facility. If the Company violates any of these restrictions, it will be required to negotiate new terms with its banks. There can be no assurance that in that event, the Company will receive satisfactory new terms from its banks, or that if the Company needs additional financing, that such financing can be secured when needed or on terms the Company deems acceptable.

SEASONALITY AND CYCLICALITY

The HVAC industry is subject to seasonal variations. Specifically, the demand for new installation and replacement is generally lower during the winter months 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, the Company expects its revenues and operating results generally will be lower in the first and fourth calendar quarters.

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

FACTORS WHICH MAY AFFECT FUTURE RESULTS

The Company's future operating results are difficult to predict and may be affected by a number of factors, including the lack of a combined operating history and the difficulty of integrating acquired businesses, retention of key management, a national downturn or one or more regional downturns in construction, shortages of labor and specialty building materials, difficulty in obtaining or increased costs associated with debt financing, seasonal fluctuations in the demand for HVAC systems and the use of incorrect estimates for bidding a fixed price contract. As a result of these and other factors, there can be no assurance that the Company will not experience material fluctuations in future operating results on a quarterly or annual basis.

The Company's success depends in part on its ability to integrate the companies it has acquired. These businesses operated as separate, independent entities prior to their affiliation with the Company, and there can be no assurance that the Company will be able to integrate the operations of these businesses successfully or institute the necessary systems and procedures, including accounting and financial reporting systems, to effectively manage the combined enterprise on a profitable basis. The historical results are not necessarily indicative of future results of the Company because, among other reasons, the Company's subsidiary operations were not under common control or management prior to their acquisition.

The existing senior management at many of the Company's subsidiary operations is generally comprised of former owners who committed to stay with their operations after acquisition. Certain of these individuals have suffered losses in the Company stock or have lower incomes than they averaged when they owned their former businesses. Further, former owners generally have noncompetition obligations that expire on the fifth anniversary of their date of acquisition. There is no assurance that the Company will be able to retain these individuals or find suitable replacements if such individuals leave the Company. The failure to retain or replace such management on a timely basis could negatively impact results from operations at such locations.

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

Recently acquired businesses also involve a number of special risks, including failure of the acquired business to achieve expected results, diversion of management's attention and failure to retain various personnel of the acquired business. There are also risks associated with unanticipated events or liabilities resulting from the acquired businesses' operations prior to their acquisition. Any of these risks, or a combination of them, could have a material adverse effect on the Company's business, financial condition and results of operations.

The timely provision of high-quality installation service and maintenance, repair and replacement of HVAC systems by the Company requires an adequate supply of skilled HVAC technicians. In addition, the Company depends on the senior management of the businesses it acquires and regional and corporate management to remain committed to the success of the Company. Accordingly, the Company's ability to maintain and increase its productivity and profitability is also affected by its ability to employ, train and retain the skilled technicians necessary to meet the Company's service requirements, and to retain senior management in acquired businesses and at the corporate and regional level.

The Company has a substantial amount of debt that could limit its ability to fund future working capital needs and increase its exposure during adverse economic conditions.

Such indebtedness could increase vulnerability to adverse operational performance and economic and industry conditions; limit the ability to fund future working capital, capital expenditures and other general corporate requirements; limit flexibility in planning for, or reacting to, changes in our business or industry; place the Company at a disadvantage compared to a competitor that has less debt. Such indebtedness, together with the financial and other restrictive covenants in our debt instruments, could limit our ability to borrow additional funds. Additionally, failing to comply with those covenants

could result in an event of default, which, if not cured or waived, could have a material adverse effect on the Company.

HVAC systems are also 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 the Company operates will not change significantly in the future. The Company's failure to comply, or the costs of compliance, with such laws and regulations could adversely affect the Company's future results.

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

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

The Company is exposed to market risk primarily related to potential adverse changes in interest rates as discussed below. Management is actively involved in monitoring exposure to market risk and continues to develop and utilize appropriate risk management techniques. The Company is not exposed to any other significant financial market risks including commodity price risk, foreign currency exchange risk or interest rate risks from the use of derivative financial instruments. Management does not use derivative financial instruments for trading or to speculate on changes in interest rates or commodity prices.

The Company's exposure to changes in interest rates primarily results from its short-term and long-term debt with both fixed and floating interest rates. The Company's debt with fixed interest rates consists of capital leases, convertible subordinated notes, subordinated notes and various other notes payable. The Company's debt with variable interest rates consists entirely of its revolving Credit Facility. The following table presents principal amounts (stated in thousands) and related average interest rates by year of maturity for the Company's debt obligations and their indicated fair market value at December 31, 2000:

	2001	2002	2003	2004	2005	THEREAFTER	FAIR VALUE
	-----	-----	-----	----	----	-----	-----
Liabilities -- Long-Term Debt:							
Variable Rate Debt.....	\$ --	\$ --	\$223,700	\$ --	\$ --	\$ --	\$223,700
Average Interest Rate.....	--%	--%	8.9%	--%	--%	--%	8.9%
Fixed Rate Debt.....	\$9,066	\$6,710	\$ 34,912	\$ 71	\$ 43	\$ 99	\$ 50,901
Average Interest Rate.....	9.9%	6.2%	10.0%	6.6%	5.6%	5.0%	9.5%

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTAL DATA

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REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Comfort Systems USA, Inc.:

We have audited the accompanying consolidated balance sheets of Comfort Systems USA, Inc. (a Delaware corporation) and subsidiaries as of December 31, 1999 and 2000, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2000. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Comfort Systems USA, Inc., and subsidiaries as of December 31, 1999 and 2000, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States.

ARTHUR ANDERSEN LLP

Houston, Texas
March 27, 2001

COMFORT SYSTEMS USA, INC.
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AMOUNTS)

	DECEMBER 31,	
	----- 1999	2000 -----
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents.....	\$ 3,664	\$ 16,021
Accounts receivable, less allowance of \$5,568 and \$6,789.....	309,031	334,152
Other receivables.....	4,575	5,879
Inventories.....	20,907	19,399

Prepaid expenses and other.....	11,471	10,568
Costs and estimated earnings in excess of billings.....	54,575	44,078
Net assets held for sale.....	--	3,197
	-----	-----
Total current assets.....	404,223	433,294
PROPERTY AND EQUIPMENT, net.....	41,964	40,085
GOODWILL, net.....	474,529	450,493
OTHER NONCURRENT ASSETS.....	13,814	2,538
	-----	-----
Total assets.....	\$934,530	\$926,410
	=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:

Current maturities of long-term debt.....	\$ 3,353	\$ 216
Current maturities of notes to affiliates and former owners.....	24,536	8,850
Accounts payable.....	96,032	114,613
Accrued compensation and benefits.....	36,187	40,880
Billings in excess of costs and estimated earnings.....	52,170	68,574
Other current liabilities.....	23,604	26,942
	-----	-----
Total current liabilities.....	235,882	260,075

LONG-TERM DEBT, NET OF CURRENT MATURITIES..... 225,471 224,111

NOTES TO AFFILIATES AND FORMER OWNERS, NET OF CURRENT

MATURITIES.....	52,473	41,424
OTHER LONG-TERM LIABILITIES.....	1,739	561
	-----	-----

Total liabilities..... 515,565 526,171

COMMITMENTS AND CONTINGENCIES

STOCKHOLDERS' EQUITY:

Preferred stock, \$.01 par, 5,000,000 shares authorized, none issued and outstanding.....	--	--
Common stock, \$.01 par, 102,969,912 shares authorized, 39,258,913 shares issued.....	393	393
Treasury stock, at cost, 1,695,524 and 2,002,629 shares, respectively.....	(11,978)	(13,119)
Additional paid-in capital.....	342,655	341,923
Retained earnings.....	87,895	71,042
	-----	-----
Total stockholders' equity.....	418,965	400,239
	-----	-----
Total liabilities and stockholders' equity.....	\$934,530	\$926,410
	=====	=====

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

COMFORT SYSTEMS USA, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	YEAR ENDED DECEMBER 31,		
	1998	1999	2000
	-----	-----	-----
REVENUES.....	\$853,961	\$1,370,035	\$1,591,066

COST OF SERVICES.....	647,512	1,077,329	1,306,816
Gross profit.....	206,449	292,706	284,250
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	130,370	187,771	225,894
GOODWILL AMORTIZATION.....	7,132	11,731	12,585
ACQUISITION RELATED EXPENSES.....	450	--	--
RESTRUCTURING CHARGES.....	--	--	25,344
Operating income.....	68,497	93,204	20,427
OTHER INCOME (EXPENSE):			
Interest income.....	957	841	514
Interest expense.....	(7,633)	(20,033)	(26,886)
Other.....	241	48	744
Other expense, net.....	(6,435)	(19,144)	(25,628)
REDUCTIONS IN NON-OPERATING ASSETS AND LIABILITIES, NET...	--	--	(5,867)
INCOME (LOSS) BEFORE INCOME TAXES.....	62,062	74,060	(11,068)
INCOME TAX EXPENSE.....	27,049	31,738	5,785
NET INCOME (LOSS).....	\$ 35,013	\$ 42,322	\$ (16,853)
NET INCOME (LOSS) PER SHARE:			
Basic.....	\$ 1.06	\$ 1.10	\$ (0.45)
Diluted.....	\$ 1.04	\$ 1.09	\$ (0.45)
SHARES USED IN COMPUTING NET INCOME (LOSS) PER SHARE:			
Basic.....	32,962	38,561	37,397
Diluted.....	34,329	39,699	37,397

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

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COMFORT SYSTEMS USA, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(IN THOUSANDS, EXCEPT SHARE AMOUNTS)

	COMMON STOCK		TREASURY STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	TOTAL STOCKHOLDERS' EQUITY
	SHARES	AMOUNT	SHARES	AMOUNT			
BALANCE AT DECEMBER 31, 1997.....	28,013,436	\$280	--	\$ --	\$205,829	\$ 11,526	\$217,635
Issuance of Common Stock:							
Second Public Offering.....	861,479	9	--	--	15,892	--	15,901
Acquisition of Purchased Companies...	9,212,573	92	--	--	111,456	--	111,548
Issuance of Employee Stock Purchase Plan shares.....	29,362	--	--	--	482	--	482
Issuance of shares for options exercised.....	24,330	--	--	--	319	--	319
S Corporation distributions made by certain Pooled Companies.....	--	--	--	--	--	(966)	(966)
Net income.....	--	--	--	--	--	35,013	35,013
BALANCE AT DECEMBER 31, 1998.....	38,141,180	381	--	--	333,978	45,573	379,932
Issuance of Common Stock:							
Acquisition of Purchased Companies...	958,533	10	125,197	885	6,164	--	7,059
Issuance of Employee Stock Purchase Plan shares.....	142,276	2	--	--	2,036	--	2,038
Issuance of shares for options exercised.....	16,924	--	--	--	477	--	477
Common Stock repurchases.....	--	--	(1,820,721)	(12,863)	--	--	(12,863)
Net income.....	--	--	--	--	--	42,322	42,322
BALANCE AT DECEMBER 31, 1999.....	39,258,913	393	(1,695,524)	(11,978)	342,655	87,895	418,965
Issuance of Common Stock:							
Issuance of Employee Stock Purchase Plan shares.....	--	--	329,212	2,254	(732)	--	1,522
Common Stock repurchases.....	--	--	(175,513)	(1,224)	--	--	(1,224)
Shares exchanged in repayment of notes receivable.....	--	--	(385,996)	(1,975)	--	--	(1,975)
Shares received from sale of businesses.....	--	--	(74,808)	(196)	--	--	(196)
Net loss.....	--	--	--	--	--	(16,853)	(16,853)
BALANCE AT DECEMBER 31, 2000.....	39,258,913	\$393	(2,002,629)	\$ (13,119)	\$341,923	\$ 71,042	\$400,239

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

COMFORT SYSTEMS USA, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,		
	1998	1999	2000
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income (loss).....	\$ 35,013	\$ 42,322	\$ (16,853)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities --			
Restructuring charges.....	--	--	25,344
Reductions in non-operating assets and liabilities, net...	--	--	5,867
Depreciation and amortization expense.....	14,001	23,055	24,902
Bad debt expense.....	1,253	1,650	5,883
Deferred tax expense (benefit).....	960	1,339	(2,590)
Gain on sale of property and equipment.....	(274)	(260)	(697)
Changes in operating assets and liabilities, net of effects of acquisitions of purchased companies --			
(Increase) decrease in --			
Receivables, net.....	(34,915)	(58,096)	(36,791)
Inventories.....	(788)	(4,822)	1,103
Prepaid expenses and other current assets.....	2,437	3,213	2,734
Costs and estimated earnings in excess of billings...	(7,926)	(15,433)	9,373
Other noncurrent assets.....	113	(293)	2,002
Increase (decrease) in --			
Accounts payable and accrued liabilities.....	(14,991)	20,166	21,980
Billings in excess of costs and estimated earnings...	208	6,080	17,105
Other, net.....	(616)	(507)	(1,190)
Net cash provided by (used in) operating activities.....	(5,525)	18,414	58,172
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchases of property and equipment.....	(11,137)	(16,054)	(18,037)
Proceeds from sales of property and equipment.....	1,369	1,507	1,937
Cash paid for purchased companies, net of cash acquired...	(133,338)	(31,417)	--
Proceeds from businesses sold.....	--	--	713
Other.....	--	(500)	--
Net cash used in investing activities.....	(143,106)	(46,464)	(15,387)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Payments on long-term debt.....	(109,508)	(236,372)	(314,360)
Borrowings of long-term debt.....	233,684	271,706	283,634
S Corporation distributions paid by certain pooled companies.....	(966)	--	--
Proceeds from issuance of common stock, net of offering costs.....	16,702	2,258	1,522
Repurchases of common stock.....	--	(12,863)	(1,224)
Other.....	(2,393)	--	--
Net cash provided by (used in) financing activities.....	137,519	24,729	(30,428)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	(11,112)	(3,321)	12,357
CASH AND CASH EQUIVALENTS, beginning of year.....	18,097	6,985	3,664
CASH AND CASH EQUIVALENTS, end of year.....	\$ 6,985	\$ 3,664	\$ 16,021

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2000

1. BUSINESS AND ORGANIZATION:

Comfort Systems USA, Inc., a Delaware corporation ("Comfort Systems" and collectively with its subsidiaries, the "Company"), is a leading national provider of comprehensive heating, ventilation and air conditioning ("HVAC") installation, maintenance, repair and replacement services. The Company operates primarily in the commercial and industrial HVAC markets, and performs most of its services within manufacturing plants, office buildings, retail centers, apartment complexes, and healthcare, education and government facilities. In addition to standard HVAC services, the Company provides specialized applications such as process cooling, building automation control systems, electronic monitoring and process piping. Certain locations also perform related services such as electrical and plumbing. Approximately 58% of the Company's consolidated 2000 revenues were attributable to installation services, with the remaining 42% attributable to maintenance, repair and replacement services.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

PRINCIPLES OF CONSOLIDATION

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

CASH FLOW INFORMATION

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

Cash paid for interest in 1998, 1999 and 2000 was approximately \$6.6 million, \$17.8 million and \$25.8 million, respectively. Cash paid for income taxes in 1998, 1999 and 2000 was approximately \$33.3 million, \$33.6 million and \$13.1 million, respectively.

INVENTORIES

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

PROPERTY AND EQUIPMENT

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

Expenditures for repairs and maintenance are charged to expense when incurred. Expenditures for major renewals and betterments, which extend the useful lives of existing equipment, are capitalized and depreciated over the remaining useful life of the equipment. Upon retirement or disposition of property and equipment, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized in the statement of operations.

GOODWILL

Goodwill represents the excess of the aggregate purchase price paid by the Company in acquisitions accounted for as purchases over the fair value of the net tangible assets acquired. Goodwill is amortized on a straight-line basis over periods not exceeding 40 years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

As of December 31, 1999 and 2000, accumulated amortization of goodwill was approximately \$20.7 million and \$32.9 million, respectively.

LONG-LIVED ASSETS

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

REVENUE RECOGNITION

The Company recognizes revenue when services are performed except when work is being performed under a construction contract. Revenues from construction contracts are recognized on the percentage-of-completion method measured by the percentage of costs incurred to total estimated costs for each contract. Contract costs include all direct material (net of estimated rebates), labor and subcontract costs and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and depreciation costs. Provisions for the total estimated losses on uncompleted contracts are made in the period in which such losses are determined. Changes in job performance, job conditions, estimated profitability and final contract settlements may result in revisions to costs and revenues, and their effects are recognized in the period in which the revisions are determined.

Receivable balances billed but not paid by customers pursuant to retainage provisions in construction contracts are due upon completion of the contracts and acceptance by the customer. Based on the Company's experience with similar contracts in recent years, the retention balance at each balance sheet date is billed and collected within the subsequent fiscal year. The retainage balances at December 31, 1999 and 2000 are \$58.2 million and \$67.7 million, respectively, and are included in accounts receivable.

The current asset "Costs and estimated earnings in excess of billings" represents revenues recognized in excess of amounts billed. The current liability "Billings in excess of costs and estimated earnings" represents billings in excess of revenues recognized.

WARRANTY COSTS

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

INCOME TAXES

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

Certain pooled companies were S Corporations for income tax purposes and, accordingly, any income tax liabilities for the periods prior to the acquisition

date are the responsibility of the respective stockholders. All acquired entities are subject to corporate income taxes subsequent to their acquisition.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions by management in determining the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

CONCENTRATIONS OF CREDIT RISK

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

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

ACCOUNTING PRONOUNCEMENT

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133"). This standard requires entities to recognize all derivative instruments (including certain derivative instruments embedded in other contracts) as assets or liabilities in its balance sheet and measure them at fair value. The statement requires that changes in the derivatives' fair value be recognized currently in earnings unless specific hedge accounting criteria are met. SFAS No. 133, as amended, is effective for the Company beginning January 1, 2001. The Company adopted these standards effective January 1, 2001 and there was no impact as the Company does not currently hold or trade derivative instruments.

RECLASSIFICATIONS

Certain reclassifications have been made in prior period financial statements to conform to current period presentation. During 1999, the Company began presenting certain costs in cost of services that relate to activities that directly support project or service work. These costs were previously presented in selling, general and administrative expenses ("SG&A"). Management believes this revised presentation better aligns cost of services and SG&A across all acquired operations. The change in classification in 1999 resulted in approximately \$37.2 million of costs included in cost of services which would have been included in SG&A under the prior presentation. Exclusive of this change in classification, gross profit in 1999 would have been approximately \$329.9 million. Prior periods were not restated.

3. RESTRUCTURING CHARGES:

During 2000, the Company recorded restructuring charges of approximately \$25.3 million primarily associated with restructuring efforts at certain underperforming operations and its decision to cease its e-commerce activities at Outbound Services, a subsidiary of the Company. As announced by the Company in the third quarter of 2000, management performed an extensive review of its

operations during the second half of 2000. As part of this review, management decided to cease operating at three locations, sell five operations (including two smaller satellite operations), and merge two companies into other operations. These actions are substantially complete except that the Company is seeking buyers for two operations it is holding for sale. The Company anticipates that these operations will be sold during the first half of 2001. The restructuring charges

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

are primarily non-cash and include goodwill impairments of approximately \$11.5 million and the writedown of other long-lived assets of approximately \$8.5 million. The remaining restructuring items primarily include severance and lease termination costs. Severance costs relate to the termination of approximately 145 employees (approximately 90 of these employees were terminated as of December 31, 2000) including certain corporate personnel and the management and employees of certain underperforming locations, and to the departure of the Company's former chief executive officer. The following table shows the portions of the restructuring charges that are expected to result in cash disbursements, and how much of those amounts had been paid by December 31, 2000 (in thousands):

	TOTAL ACCRUAL	PAYMENTS	BALANCE AT DECEMBER 31, 2000
	-----	-----	-----
Severance.....	\$2,487	\$(1,269)	\$1,218
Lease termination costs and other.....	2,920	(608)	2,312
	-----	-----	-----
Total.....	\$5,407	\$(1,877)	\$3,530
	=====	=====	=====

Aggregated financial information related to the operations and activities included in the restructuring charges is as follows (in thousands):

	TWELVE MONTHS ENDED DECEMBER 31,		
	-----	-----	-----
	1998	1999	2000
	-----	-----	-----
Revenues.....	\$14,086	\$50,235	\$ 46,062
Operating income (loss).....	\$ 838	\$ 1,427	\$(17,053)

As of December 31, 2000, net assets held for sale are comprised of the following (in thousands):

Current Assets (primarily accounts receivable).....	\$ 5,789
Long-Term Assets.....	6
Current Liabilities (primarily accounts payable).....	(2,577)
Long-Term Liabilities.....	(21)

Total.....	\$ 3,197
	=====

The restructuring charges associated with the operations that were held for sale at December 31, 2000 were \$3.7 million and primarily related to impairments of goodwill and other long-lived assets based upon the estimated proceeds from the anticipated sale of these operations.

4. REDUCTIONS IN NON-OPERATING ASSETS AND LIABILITIES, NET:

During 2000, the Company recorded a non-cash charge of approximately \$5.9 million primarily related to the impairment of certain non-operating assets. These assets primarily related to notes receivable from former business owners that were collateralized by shares of the Company's stock. This charge also included an impairment of approximately \$1.4 million to the Company's minority investment in two entities associated with the distribution and implementation of high-end engineering and design software. These entities have ceased operations. Also included in this charge was a gain of approximately \$0.6 million on the reduction of the Company's subordinated note payable to a former owner in connection with the settlement of claims with this former owner.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

5. BUSINESS COMBINATIONS:

POOLINGS

During 1998, the Company acquired all of the outstanding stock of three businesses which were accounted for as poolings-of-interests in exchange for 1,437,767 shares of the Company's common stock ("Common Stock"). These companies provide HVAC and related services. The historical financial statements for 1998 include the operations of these poolings prior to their acquisition by the Company.

PURCHASES

During 1998, the Company acquired 52 businesses which were accounted for as purchases. These companies provide HVAC and related services. The aggregate consideration paid in these transactions was \$161.2 million in cash, 9,212,573 shares of Common Stock with a fair value at the date of acquisition totaling \$111.5 million, \$57.4 million in the form of convertible subordinated notes and \$3.1 million in the form of subordinated notes. Subsequent to the issuance of certain of the convertible subordinated notes, the Company entered into agreements with certain of the convertible noteholders to modify the terms of \$49.3 million of these notes to eliminate the provisions relating to convertibility into Common Stock. The remaining convertible subordinated notes are convertible into 42,608 shares of Common Stock.

During 1999, the Company acquired 25 businesses which were accounted for as purchases. These companies provide HVAC and related services. The aggregate consideration paid in these transactions was \$38.0 million in cash, 1,151,907 shares of Common Stock with a fair value at the date of acquisition totaling \$8.5 million, \$2.2 million in the form of convertible subordinated notes and \$21.3 million in the form of subordinated notes. In addition, the Company received 68,177 shares from a former owner related to a prior year acquisition. Subsequent to the issuance of certain of the convertible subordinated notes, the Company entered into agreements with certain of the convertible noteholders to modify the terms of \$2.1 million of these notes to eliminate the provisions relating to convertibility into Common Stock. The remaining convertible subordinated notes are convertible into 5,133 shares of Common Stock.

The accompanying consolidated balance sheets include allocations of the respective purchase prices to the assets acquired and liabilities assumed based on fair value. The allocations in 1999 resulted in \$55.7 million in goodwill which represents the excess of the purchase price over the estimated fair value of the net assets acquired for the purchased companies. In conjunction with the

acquisitions, goodwill was determined as follows (in thousands):

	1999

Fair value of assets acquired, net of cash acquired.....	\$(27,806)
Liabilities assumed.....	20,138
Cash paid, net of cash acquired.....	31,417
Estimated fair value of stock consideration.....	8,463
Issuance of notes.....	23,473

Goodwill.....	\$ 55,685
	=====

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

The unaudited pro forma data presented below consists of the income statement data presented in these consolidated financial statements plus income statement data for the purchased companies as if the acquisitions had occurred on January 1, 1999 (in thousands, except per share data):

	YEAR ENDED DECEMBER 31,	

	1998	1999

	(UNAUDITED)	
Revenues.....	\$1,355,733	\$1,425,182
Net income.....	\$ 40,657	\$ 41,966
Net income per share -- diluted.....	\$ 1.03	\$ 1.06
Shares used in computing net income per share -- diluted....	40,113	40,156

Pro forma adjustments included in the preceding table relate to (a) certain reductions in salaries and benefits to the former owners of the purchased companies which the former owners agreed would take effect as of the acquisition date, (b) amortization of goodwill related to the purchased companies, (c) interest expense on borrowings used in the acquisition of the purchased companies and (d) interest expense related to subordinated notes issued in the acquisition of certain of the purchased companies. In addition, an incremental tax provision has been recorded as if all applicable purchased companies had been subject to federal and state income taxes.

The pro forma results presented above are not necessarily indicative of actual results which might have occurred had the operations and management teams of the Company and the purchased companies been combined at the beginning of the period presented.

6. PROPERTY AND EQUIPMENT:

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

ESTIMATED USEFUL LIVES IN YEARS	DECEMBER 31,	
-----	-----	
	1999	2000
	-----	-----

Land.....	N/A	\$ 178	\$ 155
Transportation equipment.....	3-10	32,781	30,118
Machinery and equipment.....	3-10	27,542	25,978
Computer and telephone equipment.....	3-7	15,942	20,612
Buildings and leasehold improvements.....	3-39	12,079	13,935
Furniture and fixtures.....	3-10	8,815	9,146
		-----	-----
		97,337	99,944
Less -- Accumulated depreciation.....		55,373	59,859
		-----	-----
Property and equipment, net.....		\$41,964	\$40,085
		=====	=====

Depreciation expense for the years ended December 31, 1998, 1999 and 2000 was \$6.9 million, \$11.3 million and \$12.3 million, respectively.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

7. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

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

	DECEMBER 31,		
	1998	1999	2000
	-----	-----	-----
Balance at beginning of year.....	\$1,698	\$ 4,758	\$ 5,568
Additions for bad debt expense.....	1,253	1,650	5,883
Deductions for uncollectible receivables written off, net of recoveries.....	(909)	(1,940)	(4,452)
Allowance for doubtful accounts of purchased companies at date of acquisition.....	2,716	1,100	--
Allowance for doubtful accounts of businesses sold or held for sale.....	--	--	(210)
	-----	-----	-----
Balance at end of year.....	\$4,758	\$ 5,568	\$ 6,789
	=====	=====	=====

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

	DECEMBER 31,	
	1999	2000
	-----	-----
Accrued warranty costs.....	\$ 4,587	\$ 4,715
Accrued insurance expense.....	6,835	6,710
Deferred revenue.....	2,210	2,397
Other current liabilities.....	9,972	13,120
	-----	-----
	\$23,604	\$26,942
	=====	=====

Installation contracts in progress are as follows (in thousands):

	DECEMBER 31,	
	1999	2000
Costs incurred on contracts in progress.....	\$ 895,662	\$ 1,252,685
Estimated earnings, net of losses.....	209,887	252,205
Less -- Billings to date.....	(1,103,144)	(1,529,223)
Less -- Amounts related to businesses held for sale.....	--	(163)
	=====	=====
	\$ 2,405	\$ (24,496)
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 54,575	\$ 44,078
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(52,170)	(68,574)
	=====	=====
	\$ 2,405	\$ (24,496)

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

8. LONG-TERM DEBT OBLIGATIONS:

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

	DECEMBER 31,	
	1999	2000
Revolving credit facility.....	\$225,215	\$223,700
Notes to affiliates and former owners.....	77,009	50,274
Other.....	3,609	627
	=====	=====
Total debt.....	305,833	274,601
Less: current maturities.....	27,889	9,066
	=====	=====
	\$277,944	\$265,535

At December 31, 2000, future principal payments of long-term debt are as follows (in thousands):

Year Ending December 31 --	
2001.....	\$ 9,066
2002.....	6,710
2003.....	258,612
2004.....	71
2005.....	43
Thereafter.....	99
	=====
	\$274,601
	=====

REVOLVING CREDIT FACILITY

The Company amended its revolving credit facility (the "Credit Facility" or the "Facility") provided by Bank One, Texas, N.A. ("Bank One") and other banks (the "Bank Group") in March 2001. As amended, the Credit Facility provides the Company with a revolving line of credit of up to the lesser of \$270 million or 80% of net accounts receivable. The Facility decreases to the lesser of \$250 million or 80% of net accounts receivable as of December 31, 2001, and to the lesser of \$240 million or 80% of net accounts receivable as of June 30, 2002. Borrowings under the Facility are secured by accounts receivable, inventory, fixed assets other than real estate, and the shares of capital stock of the Company's subsidiaries. The Credit Facility expires on January 1, 2003, at which time all amounts outstanding are due.

The Company has a choice of two interest rate options under the Facility. Under one option, the interest rate is determined based on the higher of the Federal Funds Rate plus 0.5% or Bank One's prime rate. An additional margin of 1% to 2% is then added to the higher of these two rates. Under the other interest rate option, borrowings bear interest based on designated short-term Eurodollar rates (which generally approximate London Interbank Offered Rates or "LIBOR") plus 2.5% to 3.5%. The additional margin for both options depends on the ratio of the Company's debt to earnings before interest, taxes, depreciation and amortization ("EBITDA"), as defined. Commitment fees of 0.375% to 0.5% per annum, also depending on the ratio of debt to EBITDA, are payable on the unused portion of the Facility.

The Credit Facility prohibits payment of dividends by the Company, limits certain non-Bank Group debt, and restricts outlays of cash by the Company relating to certain investments, capital expenditures, vehicle leases, acquisitions and subordinate debt. The Credit Facility also provides for the maintenance of certain levels of shareholder equity and EBITDA, and for the maintenance of certain ratios of the Company's EBITDA to interest expense and debt to EBITDA.

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COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Under the terms of the Credit Facility that were in effect as of June 30 and September 30, 2000, the Company was in violation of certain of the Facility's financial balance and ratio requirements. The Bank Group waived these violations. The restrictions and financial balance and ratio requirements currently effective under the Facility allow for performance during the first and second quarters of 2001 consistent with the Company's results in recent quarters, excluding restructuring and other nonrecurring charges. The Facility's restrictions and requirements then call for improvement from recent performance levels in the third and fourth quarters of 2001 and on a quarterly basis in 2002. The Facility also prohibits repurchase of the Company's stock and has relatively tight approval requirements on acquisitions. The Facility's requirements reflect tighter restrictions, greater specificity and smaller allowable variances on most financial balances and ratios than is typical for such agreements due to the Company's weaker results in 2000. While management believes its restructuring efforts and operating strategies along with general market conditions in the commercial/industrial HVAC and building automation controls industry will enable the Company to meet the Facility's requirements, there can be no assurance that the Company will be successful in doing so. Management intends to seek more flexible terms under its borrowing relationships as its results and credit market conditions allow.

As of December 31, 2000, the Company had \$223.7 million in borrowings outstanding under the Credit Facility and had incurred interest expense at an average rate of approximately 8.9% for the year ended December 31, 2000. The Credit Facility's interest rate terms as summarized above are effective as of March 22, 2001 and currently result in an all-in floating interest rate under the Facility's LIBOR option of approximately 8.9%. As of December 31, 2000, the Company also had \$2.0 million in letters of credit outstanding under the

Facility, and unused borrowing capacity under the Facility of \$41.6 million. As of March 23, 2001, \$226.9 million in borrowings and \$1.9 million in letters of credit were outstanding under the Facility, and \$36.6 million in unused capacity was available.

NOTES TO AFFILIATES AND FORMER OWNERS

Subordinated notes were issued to former owners of certain purchased companies as part of the consideration used to acquire their companies. These notes had an outstanding balance of \$50.3 million as of December 31, 2000. Of these notes, \$49.9 million bear interest, payable quarterly, at a weighted average interest rate of 5.8% and \$0.4 million are non-interest bearing. In addition, \$1.2 million of these notes are convertible by the holders into shares of the Company's Common Stock at a weighted average price of \$25.27 per share. The originally scheduled maturities of the subordinated notes are \$3.4 million in 2000, \$24.0 million in 2001, \$22.0 million in 2002, and \$0.9 million in 2003.

As a result of the Company's covenant violations in 2000 under the Credit Facility, the Bank Group required that originally scheduled principal payments to subordinate debt holders be suspended. This requirement took effect in October 2000. In March 2001, the Company entered into amended agreements with subordinate debt holders representing \$44.4 million in principal, including all the principal originally scheduled to be paid through 2001. These amended agreements allow for partial payments against certain originally scheduled payment amounts, defer remaining principal balances to April 2003, and increase the interest rate on this debt to 10% per annum, payable quarterly. As a result of these amended agreements, the Company's annual maturities of subordinate debt are now \$8.9 million in 2001, \$6.6 million in 2002, and \$34.8 million in 2003.

OTHER LONG-TERM OBLIGATION DISCLOSURES

The Company estimates the fair value of long-term debt as of December 31, 1999 and 2000 to be approximately the same as the recorded value.

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

The Company anticipates that available borrowings under its Credit Facility and cash flow from operations will be sufficient to meet the Company's normal working capital and capital expenditure needs. As noted above, the Company has agreed to relatively tight restrictions under the Credit Facility. If the Company violates any of these restrictions, it will be required to negotiate new terms with its banks. There can be no assurance that in that event, the Company will receive satisfactory new terms from its banks, or that if the Company needs additional financing, that such financing can be secured when needed or on terms the Company deems acceptable.

9. INCOME TAXES:

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

	YEAR ENDED DECEMBER 31,		
	1998	1999	2000
	-----	-----	-----
Current --			
Federal.....	\$21,650	\$25,622	\$ 4,841
State and Puerto Rico.....	4,439	4,777	3,534
	-----	-----	-----
	26,089	30,399	8,375
	-----	-----	-----
Deferred --			

Federal.....	907	2,067	(2,679)
State and Puerto Rico.....	53	(728)	89
	-----	-----	-----
	960	1,339	(2,590)
	-----	-----	-----
	\$27,049	\$31,738	\$ 5,785
	=====	=====	=====

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

	YEAR ENDED DECEMBER 31,		
	1998	1999	2000
	-----	-----	-----
Income tax expense (benefit) at the statutory rate.....	\$21,713	\$25,921	\$ (3,838)
Increase (decrease) resulting from --			
State income taxes, net of federal tax effect.....	3,148	2,567	1,652
Non-deductible goodwill amortization.....	2,047	2,730	2,817
Non-deductible goodwill writeoffs related to restructuring.....	--	--	4,300
Non-deductible expenses.....	364	492	778
Effect of S Corporation income previously taxed to the former owners.....	(308)	--	--
Non-deductible acquisition costs related to pooled companies.....	157	--	--
Provision (benefit) recognized upon termination of Subchapter S election.....	(101)	--	--
Other.....	29	28	76
	-----	-----	-----
	\$27,049	\$31,738	\$ 5,785
	=====	=====	=====

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

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

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

	DECEMBER 31,	
	1999	2000
	-----	-----
	(IN THOUSANDS)	
Deferred income tax assets --		
Accounts receivable and allowance for doubtful accounts...	\$ 1,854	\$ 2,652
Accrued liabilities and expenses.....	7,206	8,210
Net operating loss.....	1,343	4,355
Other.....	630	541
	-----	-----
Total deferred income tax assets.....	11,033	15,758
	-----	-----

Deferred income tax liabilities --		
Property and equipment.....	(1,113)	(1,729)
Long-term installation contracts.....	(3,821)	(995)
Goodwill.....	(3,180)	(5,833)
Other.....	(628)	(369)
	-----	-----
Total deferred income tax liabilities.....	(8,742)	(8,926)
	-----	-----
Less -- Valuation allowance.....	--	(1,951)
	-----	-----
Net deferred income tax assets.....	\$ 2,291	\$ 4,881
	=====	=====

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

	DECEMBER 31,	

	1999	2000
	-----	-----
Deferred income tax assets --		
Prepaid expenses and other.....	\$ 983	\$4,478
Other non-current assets.....	1,308	403

Total deferred income tax assets.....	\$2,291	\$4,881
	=====	=====

At December 31, 2000, the Company has \$56.3 million of available state net operating loss carryforwards for income tax purposes which expire 2012 through 2020.

At December 31, 2000, the Company's net deferred tax assets are partially offset by a valuation allowance. The Company will continue to assess the valuation allowance and to the extent it is determined that such allowance is no longer required, the tax benefit of the remaining net deferred tax assets will be recognized in the future.

10. EMPLOYEE BENEFIT PLANS:

The Company and certain of the Company's subsidiaries sponsor various retirement plans for most full-time and some part-time employees. These plans consist of defined contribution plans and multi-employer pension plans and cover employees at substantially all of the Company's operating locations. The defined contribution plans generally provide for contributions ranging from 1% to 6% of covered employees' salaries or wages and totaled \$3.6 million for 1998, \$5.4 million for 1999, and \$5.9 million for 2000. Of these amounts, approximately \$2.5 million and \$2.9 million was payable to the plans at December 31, 1999 and 2000, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Certain of the Company's subsidiaries also participate in various multi-employer pension plans for the benefit of their employees who are union members. Company contributions to these plans were approximately \$8.1 million for 1998, \$14.6 million for 1999, and \$17.7 million for 2000. The data available from administrators of the multi-employer pension plans is not sufficient to determine the accumulated benefit obligations, nor the net assets attributable to the multi-employer plans in which Company employees participate.

11. COMMITMENTS AND CONTINGENCIES:

LEASES

The Company leases certain facilities and equipment under noncancelable operating leases. Rent expense for the years ended December 31, 1998, 1999 and 2000 was \$6.7 million, \$17.5 million, and \$25.0 million, respectively. Concurrent with the acquisitions of certain acquired companies, the Company entered into various agreements with previous owners to lease land and buildings used in the Company's operations. The terms of these leases range from five to ten years and provide for certain escalations in the rental expenses each year. Included in the 1998, 1999 and 2000 rent expense above is approximately \$3.9 million, \$6.1 million and \$8.0 million of rent paid to these related parties, respectively. The following represents future minimum rental payments under noncancelable operating leases (in thousands):

Year ending December 31 --	
2001.....	\$17,193
2002.....	15,782
2003.....	12,950
2004.....	10,416
2005.....	8,487
Thereafter.....	16,349

	\$81,177
	=====

CLAIMS AND LAWSUITS

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

SELF-INSURANCE

The Company retains the risk for worker's compensation, employer's liability, auto liability, general liability and employee group health claims resulting from uninsured deductibles per accident or occurrence. Losses up to the deductible amounts are accrued based upon the Company's known claims incurred and an estimate of claims incurred but not reported. The accruals are based upon known facts and historical trends, and management believes such accruals to be adequate. A wholly-owned insurance company subsidiary reinsures a portion of the risk associated with surety bonds issued by a third party insurance company. Because no claims have been made against these financial instruments in the past, management does not expect these instruments will have a material effect on the Company's consolidated financial statements.

12. STOCKHOLDERS' EQUITY:

COMMON STOCK AND PREFERRED STOCK

On June 16, 1998, the Company completed a second public offering (the "Second Public Offering") of 400,000 shares of its Common Stock. The net

proceeds from this offering of \$7.6 million, after deducting underwriting commissions, were used to repay debt. On July 21, 1998, the underwriters exercised their overallotment option in connection with the Second Public Offering completed in June 1998. An additional 461,479 shares of Common Stock were sold and the net proceeds of \$8.8 million, after deducting underwriting commissions, were used to repay debt.

TREASURY STOCK

On October 5, 1999, the Company announced that its Board of Directors had approved a share repurchase program authorizing the Company to buy up to 4.0 million shares of its Common Stock. During 1999, the Company purchased approximately 1.8 million shares at a cost of approximately \$12.9 million. During 2000, the Company purchased approximately 0.2 million shares at a cost of approximately \$1.2 million. The Company does not expect further share repurchases under this program for the foreseeable future.

RESTRICTED COMMON STOCK

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

Each share of Restricted Voting Common Stock will automatically convert to Common Stock on a share-for-share basis (i) in the event of a disposition of such share of Restricted Voting Common Stock by the holder thereof (other than a distribution which is a distribution by a holder to its partners or beneficial owners, or a transfer to a related party of such holders (as defined in Sections 267, 707, 318 and/or 4946 of the Internal Revenue Code of 1986, as amended)), (ii) in the event any person acquires beneficial ownership of 15% or more of the total number of outstanding shares of Common Stock of the Company, or (iii) in the event any person offers to acquire 15% or more of the total number of outstanding shares of Common Stock of the Company. After July 1, 1998, the Board of Directors may elect to convert any remaining shares of Restricted Voting Common Stock into shares of Common Stock in the event 80% or more of the originally outstanding shares of Restricted Voting Common Stock have been previously converted into shares of Common Stock. As of December 31, 2000, there are 1,395,217 shares of Restricted Voting Common Stock remaining.

EARNINGS PER SHARE

Basic earnings per share ("EPS") is computed by dividing net income by the weighted average number of shares of common stock outstanding during the year. Diluted EPS is computed considering the dilutive effect of stock options and convertible subordinated notes. Options had an anti-dilutive effect for the year ended December 31, 2000 because the Company reported a net loss during this period, and therefore, are not included in the diluted EPS calculation. The Company would have included 175,767 shares related to the dilutive impact of stock options for the year ended December 31, 2000 if it were not for the net loss during the period. The Company has options outstanding to purchase 7.4 million shares of Common Stock at prices ranging from \$2.875 to \$21.438 per share as of December 31, 2000. Diluted EPS is also computed by adjusting both net earnings and shares outstanding as if the conversion of the convertible subordinated notes occurred on the first day of the year. The convertible subordinated notes had an anti-dilutive effect during the twelve

Outstanding at beginning of year.....	2,537,203	\$13.72	3,955,029	\$15.51	4,557,133	\$15.18
Granted.....	1,495,500	\$18.54	758,200	\$13.36	3,692,000	\$ 3.29
Exercised.....	(24,330)	\$13.45	(16,924)	\$13.00	--	\$ --
Forfeited.....	(53,344)	\$16.01	(139,172)	\$14.78	(892,974)	\$13.95
Expired.....	--	\$ --	--	\$ --	--	\$ --
-----	-----	-----	-----	-----	-----	-----
Outstanding at end of year....	3,955,029	\$15.51	4,557,133	\$15.18	7,356,159	\$ 9.35
-----	-----	-----	-----	-----	-----	-----
Options exercisable at year-end.....	518,281		1,287,229		1,838,099	
Weighted-average fair value of options granted during the year.....	\$ 7.33		\$ 6.26		\$ 2.46	

The following table summarizes information about fixed stock options outstanding at December 31, 2000:

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	NUMBER OUTSTANDING AT 12/31/00	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED-AVERAGE EXERCISE PRICE	NUMBER EXERCISABLE AT 12/31/00	WEIGHTED-AVERAGE EXERCISE PRICE
\$ 2.88- 7.63	3,717,700	9.44 years	\$ 3.34	37,040	\$ 7.15
\$11.75-16.88	2,417,067	4.03 years	\$13.82	1,270,142	\$13.76
\$17.88-21.44	1,221,392	4.50 years	\$18.79	530,917	\$18.77
-----	-----	-----	-----	-----	-----
\$ 2.88-21.44	7,356,159	6.84 years	\$ 9.35	1,838,099	\$15.08
-----	-----	-----	-----	-----	-----

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

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

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

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

	1998	1999	2000
	-----	-----	-----
Net Income (Loss)			
As reported.....	\$35,013	\$42,322	\$(16,853)
Pro forma for SFAS No. 123.....	\$33,341	\$39,519	\$(20,065)
Income (Loss) Per Share -- Basic			
As reported.....	\$ 1.06	\$ 1.10	\$ (0.45)
Pro forma for SFAS No. 123.....	\$ 1.01	\$ 1.02	\$ (0.54)
Income (Loss) Per Share -- Diluted			
As reported.....	\$ 1.04	\$ 1.09	\$ (0.45)
Pro forma for SFAS No. 123.....	\$ 0.97	\$ 1.01	\$ (0.54)

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

	1998	1999	2000
	-----	-----	-----
Expected dividend yield.....	0.00%	0.00%	0.00%
Expected stock price volatility.....	44.87%	65.63%	52.42%
Risk free interest rate.....	5.00%-6.15%	4.64%-5.87%	5.58-6.94%
Expected life of options.....	4 years	4 years	4 years

Employee Stock Purchase Plan -- The effects of applying SFAS No. 123 in the pro forma disclosure may not be indicative of future amounts as the granting of additional purchase rights is anticipated. Compensation cost associated with the stock purchase plan is recognized for the fair value of the employees' purchase rights, which is estimated using the Black-Scholes model with the following assumptions:

	1998	1999	2000
	-----	-----	-----
Expected dividend yield.....	0.00%	0.00%	0.00%
Expected volatility.....	42.10%	53.8%	76.24%
Risk free interest rate.....	5.19%-5.25%	4.56%-4.94%	6.00%-6.30%
Expected life of purchase rights.....	0.5 years	0.5 years	0.5 years

The weighted average fair values of the purchase rights granted in 1998, 1999 and 2000 were \$5.37 per share, \$4.88 per share and \$1.65 per share, respectively.

NON-EMPLOYEE DIRECTORS' STOCK PLAN

In March 1997, the Company's stockholders approved the 1997 Non-Employee Directors' Stock Plan (the "Directors' Plan"), which provides for the granting or awarding of stock options and stock appreciation rights to non-employees. The number of shares authorized and reserved for issuance under the Directors' Plan is 250,000 shares. The Directors' Plan provided for the automatic grant of options to purchase 10,000 shares to each non-employee director serving at the commencement of the initial public offering of the Company.

Each non-employee director will be granted options to purchase 10,000 shares at the time of the initial election. In addition, each non-employee director is automatically granted options to purchase an additional 5,000 shares at each annual meeting of the stockholders that is more than two months after the date of the director's initial election. All options are granted with an

exercise price equal to the fair market value at the date of grant and are immediately vested upon grant.

COMFORT SYSTEMS USA, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Either at the time of the initial public offering or upon election as a director, options were granted to four members of the board of directors to purchase in each case 10,000 shares of Common Stock at the initial public offering price or at the price in effect at the time of their election. Each of these directors received an option for 5,000 shares on the dates of the annual meetings which they have attended. In addition, directors who cease to be employees become eligible for the annual grant. One former employee received an annual grant in 2000. These options will expire at the earlier of 10 years from the date of grant or one year after termination of service as a director. As of December 31, 2000, 95,000 options were outstanding related to this plan.

The Directors' Plan allows non-employee directors to receive shares ("Deferred Shares") at future settlement dates in lieu of cash. The number of Deferred Shares will have an aggregate fair market value equal to the fees payable to the directors. No Deferred Shares have been issued as of December 31, 2000.

14. QUARTERLY RESULTS OF OPERATIONS (UNAUDITED):

Quarterly financial information for the years ended December 31, 1999 and 2000 is summarized as follows (in thousands, except per share data):

	YEAR ENDED DECEMBER 31, 1999			

	QUARTER ENDED			
	MARCH 31, 1999	JUNE 30, 1999	SEPTEMBER 30, 1999	DECEMBER 31, 1999
	-----	-----	-----	-----
Revenues.....	\$291,926	\$341,493	\$374,815	\$361,801
Gross profit.....	\$ 63,178	\$ 76,239	\$ 76,335	\$ 76,954
Operating income.....	\$ 15,536	\$ 30,023	\$ 27,559	\$ 20,086
Net income.....	\$ 6,564	\$ 14,645	\$ 12,868	\$ 8,245
Earnings per share:				
Basic.....	\$ 0.17	\$ 0.38	\$ 0.33	\$ 0.22
Diluted.....	\$ 0.17	\$ 0.37	\$ 0.33	\$ 0.22
	YEAR ENDED DECEMBER 31, 2000			

	QUARTER ENDED			
	MARCH 31, 2000	JUNE 30, 2000	SEPTEMBER 30, 2000	DECEMBER 31, 2000
	-----	-----	-----	-----
Revenues.....	\$362,566	\$404,970	\$423,922	\$399,608
Gross profit.....	\$ 70,867	\$ 70,638	\$ 71,084	\$ 71,661
Operating income (loss).....	\$ 12,856	\$ 10,802	\$ (47) (b)	\$ (3,184) (c)
Net income (loss).....	\$ 4,008	\$ (905) (a)	\$ (3,689) (b)	\$ (16,267) (c)
Earnings (loss) per share:				
Basic.....	\$ 0.11	\$ (0.02)	\$ (0.10)	\$ (0.44)
Diluted.....	\$ 0.11	\$ (0.02)	\$ (0.10)	\$ (0.44)

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

- (a) During the second quarter of 2000, the Company recorded a non-cash, pre-tax charge of approximately \$5.2 million primarily related to the impairment of certain non-operating assets.
- (b) During the third quarter of 2000, the Company recorded pre-tax restructuring charges of approximately \$10.0 million associated primarily with restructuring efforts at certain underperforming operations.
- (c) During the fourth quarter of 2000, the Company recorded an additional pre-tax charge of \$0.7 million related to the impairment of certain non-operating assets. In addition, during the fourth quarter of 2000, the Company recorded additional pre-tax restructuring charges of approximately \$15.0 million primarily related to restructuring efforts at certain underperforming operations and its decision to cease its e-commerce activities at Outbound Services.

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

None.

PART III

ITEMS 10 TO 13 INCLUSIVE

These items have been omitted in accordance with the instructions to Form 10-K. The Company will file with the Commission a definitive proxy statement including the information to be disclosed under the items in the 120 days following December 31, 2000.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

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

(1) Consolidated Financial Statements (Included Under Item 8): The Index to the Consolidated Financial Statements is included on page 19 of this report and is incorporated herein by reference.

(2) Financial Statement Schedules:

Report of Independent Public Accountants on Supplementary Data.

Schedule II -- Valuation and Qualifying Accounts.

All other schedules have been omitted since the required information is not significant or is included in the Consolidated Financial Statements or Notes thereto or is not applicable.

(b) Reports on Form 8-K

None.

(c) Exhibits

Reference is made to the Index of Exhibits beginning on page 46, which index is incorporated herein by reference.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS
ON SUPPLEMENTARY DATA

To Comfort Systems USA, Inc.:

We have audited in accordance with auditing standards generally accepted in the United States, the consolidated financial statements of Comfort Systems USA, Inc. and subsidiaries included in this Annual Report on Form 10-K and have issued our report thereon dated March 27, 2001, in which we expressed an unqualified opinion. Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The Valuation and Qualifying Accounts Schedule (Schedule II) listed in the index at Item 14(a) is the responsibility of the Company's management and is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements. This information has been subjected to the auditing procedures applied in our audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN LLP

Houston, Texas
March 27, 2001

COMFORT SYSTEMS USA, INC.

SCHEDULE II -- VALUATION AND QUALIFYING ACCOUNTS
(IN THOUSANDS)

	BALANCE AT BEGINNING OF PERIOD	ADDITIONS		DEDUCTIONS	BALANCE AT END OF PERIOD
		CHARGED TO COSTS AND EXPENSES	CHARGED TO OTHER ACCOUNTS		
Year ended December 31, 2000:					
Deducted from accounts receivable allowance for doubtful accounts.....	\$5,568	5,883	--	(4,662) (a), (b)	\$6,789
Accrued restructuring charges...	\$ --	5,407	--	(1,877)	\$3,530
Year ended December 31, 1999:					
Deducted from accounts receivable allowance for doubtful accounts.....	\$4,758	1,650	1,100 (c)	(1,940) (a)	\$5,568
Year ended December 31, 1998:					
Deducted from accounts receivable allowance for doubtful accounts.....	\$1,698	1,253	2,716 (c)	(909) (a)	\$4,758

-
- (a) Deductions for uncollectible receivables written off, net of recoveries.
- (b) Includes \$210 of allowance for doubtful accounts related to businesses sold or held for sale.
- (c) Allowance for doubtful accounts of purchased companies at date of acquisition.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COMFORT SYSTEMS USA, INC.

By: /s/ WILLIAM F. MURDY

 William F. Murdy
 Chief Executive Officer

Date: March 27, 2001

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, this report has been signed by the following persons in the capacities and on the date indicated.

SIGNATURE -----	TITLE -----	DATE ----
/s/ WILLIAM F. MURDY ----- William F. Murdy	Chairman of the Board and Chief Executive Officer	March 27, 2001
/s/ GARY E. HESS ----- Gary E. Hess	President, Chief Operating Officer and Director	March 27, 2001
/s/ J. GORDON BEITTENMILLER ----- J. Gordon Beittenmiller	Executive Vice President, Chief Financial Officer and Director (principal accounting officer)	March 27, 2001
/s/ HERMAN E. BULLS ----- Herman E. Bulls	Director	March 27, 2001
/s/ VINCENT J. COSTANTINI ----- Vincent J. Costantini	Director	March 27, 2001
/s/ ALFRED J. GIARDINELLI, JR. ----- Alfred J. Giardinelli, Jr.	Director	March 27, 2001
/s/ STEVEN S. HARTER ----- Steven S. Harter	Director	March 27, 2001
/s/ ROBERT J. POWERS ----- Robert J. Powers	Director	March 27, 2001
/s/ MARK P. SHAMBAUGH ----- Mark P. Shambaugh	Director	March 27, 2001

INDEX OF EXHIBITS

THE EXHIBIT INDICATED BELOW AND
TO THE FILING WITH THE
COMMISSION INDICATED BELOW

EXHIBIT NUMBER	DESCRIPTION OF EXHIBITS	EXHIBIT NUMBER	FILING OR FILE NUMBER
3.1	-- Second Amended and Restated Certificate of Incorporation of the Registrant.	3.1	333-24021
3.2	-- Certificate of Amendment dated May 21, 1998.	3.2	1998 Form 10-K
3.3	-- Bylaws of the Registrant, as amended.	3.3	1999 Form 10-K
4.1	-- Form of certificate evidencing ownership of Common Stock of the Registrant.	4.1	333-24021
10.1	-- Comfort Systems USA, Inc. 1997 Long-Term Incentive Plan.	10.1	333-24021
10.2	-- Comfort Systems USA, Inc. 1997 Non-Employee Directors' Stock Plan.	10.2	333-24021
10.3	-- Form of Employment Agreement between the Registrant and J. Gordon Beittenmiller.	10.4	333-24021
10.4	-- Form of Employment Agreement between the Registrant and William George, III.	10.5	333-24021
10.5	-- Form of Employment Agreement between the Registrant and Reagan S. Busbee.	10.6	333-24021
10.6	-- Form of Employment Agreement between the Registrant, Eastern Heating & Cooling, Inc. and Alfred J. Giardinelli, Jr.	10.10	333-24021
10.7	-- Employment Agreement between the Registrant, Shambaugh & Son, Inc. and Mark P. Shambaugh.	10.17	1998 Form 10-K
10.8	-- Form of Agreement among certain stockholders.	10.16	333-24021
10.9	-- Third Amended and Restated Credit Agreement among the Company and its subsidiaries, Bank One, Texas, N.A., as agent and the banks listed therein dated December 14, 1998.	10.25	333-38009
10.10	-- Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (Opportunity Drive).	10.28	1998 Form 10-K
10.11	-- Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (Di Salle Boulevard).	10.29	1998 Form 10-K
10.12	-- Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (Speedway Drive).	10.30	1998 Form 10-K
10.13	-- Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (South Bend).	10.31	1998 Form 10-K

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

EXHIBIT NUMBER	DESCRIPTION OF EXHIBITS	EXHIBIT NUMBER	FILING OR FILE NUMBER
10.14	-- Lease dated October 31, 1998, between Mark Shambaugh and Shambaugh & Sons, Inc. (Lafayette).	10.32	1998 Form 10-K
10.15	-- Form of Indemnity Agreement entered into by the Company with each of the following persons: J. Gordon Beittenmiller, Reagan S. Busbee, William George, III, Steven S. Harter, Robert J. Powers, Alfred J. Giardinelli, Jr., on June 27, 1997.	10.26	333-32595
10.16	-- Indemnity Agreement between the Company and Notre Capital Ventures II, L.L.C.	10.27	333-32595
10.17	-- Comfort Systems USA, Inc. 1998 Employee Stock Purchase Plan.	10.28	333-38009
10.18	-- Agreement Regarding Sale of Stock between Steve S. Harter and the Registrant dated October 31, 1997.	10.2	Third Quarter 1997 Form 10-Q
10.19	-- Agreement Regarding Sale of Stock between	10.3	Third Quarter 1997

	J. Gordon Beittenmiller and the Registrant dated October 31, 1997.		Form 10-Q
10.20	-- Agreement Regarding Sale of Stock between Alfred J. Giardinelli, Jr. and the Registrant dated October 31, 1997.	10.7	Third Quarter 1997 Form 10-Q
10.21	-- Agreement Regarding Sale of Stock between Robert J. Powers and the Registrant dated October 31, 1997.	10.8	Third Quarter 1997 Form 10-Q
10.22	-- Agreement Regarding Sale of Stock between Reagan S. Busbee and the Registrant dated October 31, 1997.	10.13	Third Quarter 1997 Form 10-Q
10.23	-- Agreement Regarding Sale of Stock between William George and the Registrant dated October 31, 1997.	10.14	Third Quarter 1997 Form 10-Q
10.24	-- Agreement and Plan of Merger dated November 15, 1998 by and among the Registrant, Shambaugh & Son, Inc.	2.1	November 1998 Form 8-K
10.25	-- First Amendment to Credit Agreement among the Company and its Subsidiaries, Bank One, Texas, N.A., as agent and the banks listed therein dated January 14, 2000.	10.63	1998 Form 10-K
10.26	-- Employment Agreement between the Registrant and Gary E. Hess dated January 1, 2001.		Filed Herewith
10.27	-- Lease dated April 1, 1998, between Gary E. and Susan B. Hess and Hess Mechanical Corporation.	10.53	1999 Form 10-K
10.28	-- Employment Agreement between William F. Murdy and the Registrant dated June 27, 2000.	10.2	Second Quarter 2000 Form 10-Q

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

EXHIBIT NUMBER	DESCRIPTION OF EXHIBITS	EXHIBIT NUMBER	FILING OR FILE NUMBER
10.29	-- Note Modification Agreement between Mark Shambaugh and the Registrant dated August 8, 2000.	10.3	Second Quarter 2000 Form 10-Q
10.30	-- Third Amendment to Credit Agreement dated as of August 11, 2000 amending the Third Amended and Restated Credit Agreement dated December 14, 1998 among the Registrant and its subsidiaries, Bank One, Texas, N.A., as agent and the banks listed therein.	10.5	Second Quarter 2000 Form 10-Q
10.31	-- Amendment to 1998 Employee Stock Purchase Plan dated May 18, 2000.	10.6	Second Quarter 2000 Form 10-Q
10.32	-- Comfort Systems USA, Inc. 2000 Incentive Plan.	10.7	Second Quarter 2000 Form 10-Q
10.33	-- Fourth Amendment to Credit Agreement dated as of November 13, 2000 amending the Third Amended and Restated Credit Agreement dated December 14, 1998 among the Registrant and its subsidiaries, Bank One, Texas, N.A., as agent and the banks listed therein.	10.1	Third Quarter 2000 Form 10-Q
10.34	-- Fourth Amended and Restated Credit Agreement dated as of March 22, 2001 among the Registrant and its subsidiaries, Bank One, Texas, N.A., as agent and the banks listed therein.		Filed Herewith
10.35	-- Employment Agreement between the Registrant and Milburn Honeycutt dated January 2, 2001.		Filed Herewith
21.1	-- List of subsidiaries of Comfort Systems USA, Inc.		Filed Herewith
23.1	-- Consent of Arthur Andersen LLP.		Filed Herewith

EMPLOYMENT AGREEMENT

This Employment Agreement (this "AGREEMENT") by and among COMFORT SYSTEMS USA (TEXAS), L.P., a Texas limited partnership (the "COMPANY"), and Gary E. Hess ("EMPLOYEE") is hereby entered into and effective as of the 2nd day of January, 2001.

R E C I T A L S

A. The Company is engaged primarily in the heating, ventilation, air conditioning, plumbing, electrical, fire protection and process piping industry.

B. Company desires to employ Employee hereunder in a confidential relationship wherein Employee, in the course of his employment, will become familiar with and aware of information as to the Company's customers, specific manner of doing business, processes, techniques and trade secrets and future plans with respect thereto, all of which have been and will be established and maintained at great expense to the Company, which information is a trade secret and constitutes the valuable good will of the Company; and

NOW, THEREFORE, in consideration of the mutual promises and covenants set forth herein, it is hereby agreed as follows:

A G R E E M E N T S

1. EMPLOYMENT AND DUTIES.

(a) Company hereby employs Employee to serve as President and Chief Operating Officer of the Company. As such, Employee shall have responsibilities, duties and authority customarily accorded to and expected of an officer holding such position directly with the Company. Employee hereby accepts this employment upon the terms and conditions herein contained and agrees to devote his full time, attention and efforts to promote and further the business of Company.

(b) Employee shall faithfully adhere to, execute and fulfill all policies established by Company from time to time.

2. COMPENSATION. For all services rendered by Employee, Company shall compensate Employee as follows:

(a) BASE SALARY. Effective as of the Effective Date, the base salary payable to Employee shall be \$250,000 per year, payable on a regular basis in accordance with Company's standard payroll procedures but not less frequently than monthly. On at least an annual basis, Company will review Employee's performance and

may, in its sole discretion, (i) make increases to such base salary; (ii) pay a performance bonus; or (iii) recommend Employee for the grant of Company stock options.

(b) EMPLOYEE PERQUISITES, BENEFITS AND OTHER COMPENSATION. Employee shall be entitled to receive additional benefits and compensation from Company in such form and to such extent as specified below:

(i) Coverage, subject to contributions required of executives of the

Company generally, for Employee and his dependent family members under health, hospitalization, disability, dental, life and other insurance plans that Company may have in effect from time to time. Benefits provided to Employee under this clause (i) shall be equal to such benefits provided to other Company employees of the same level.

(ii) Reimbursement for all business travel and other out-of-pocket expenses reasonably incurred by Employee in the performance of services pursuant to this Agreement. All reimbursable expenses shall be appropriately documented in reasonable detail by Employee upon submission of any request for reimbursement, and in a format and manner consistent with Company's expense reporting policy.

(iii) Company shall provide Employee with other employee perquisites as may be available to or deemed appropriate for Employee by Company and participation in all other Company-wide employee benefits as are available from time to time.

3. NONCOMPETITION AGREEMENT.

(a) Employee shall not, during the term of his employment hereunder, be engaged in any other business activity pursued for gain, profit or other pecuniary advantage if such activity interferes with Employee's duties and responsibilities hereunder. The foregoing limitations shall not be construed as prohibiting Employee from making personal investments in such form or manner as will neither require his services in the operation or affairs of the companies or enterprises in which such investments are made nor violate the terms of this paragraph 3. Employee will not, during the period of his employment by or with Company, and for a period of two (2) years immediately following the termination of his employment under this Agreement, except as provided below, directly or indirectly, for himself or on behalf of or in conjunction with any other person, persons, company, partnership, corporation or business of whatever nature:

(i) engage, as an officer, director, shareholder, owner, partner, joint venturer, or in a managerial capacity, whether as an employee, independent contractor, consultant or advisor, or as a sales representative, in any business in direct competition with Company or any of its subsidiaries and affiliates within 100 miles of where the Company or any of its subsidiaries and affiliates conduct

business, including any territory serviced by the Company or any of such subsidiaries (the "TERRITORY");

(ii) call upon any person who is, at that time, an employee of Company or any of its subsidiaries or affiliates sales or managerial capacity for the purpose or with the intent of enticing such employee away from or out of the employ of Company or any of its subsidiaries or affiliates or any its subsidiaries or affiliates;

(iii) call upon any person or entity which is, at that time, or which has been, within one (1) year prior to that time, a customer of the Company or any of its subsidiaries or affiliates for the purpose of soliciting or selling products or services in direct competition with the Company or any of its subsidiaries or affiliates; or

(iv) call upon any prospective acquisition candidate, on Employee's own behalf or on behalf of any competitor, which candidate was, to Employee's actual knowledge after due inquiry, either called upon by Company or any of its subsidiaries or affiliates or for which Employee participated in an acquisition analysis for the purpose of acquiring such entity or all or substantially all of such entity's assets.

Notwithstanding the above, the foregoing covenant shall not be deemed to prohibit Employee from acquiring as a passive investment not more than two percent (2%) of the capital stock of a competing business the stock of which is traded on a national securities exchange or on an over-the-counter or similar market.

(b) Because of the difficulty of measuring economic losses to Company or any of its subsidiaries or affiliates as a result of a breach of the foregoing covenant, and because of the immediate and irreparable damage that could be caused to Company or any of its subsidiaries or affiliates for which they would have no other adequate remedy, Employee agrees that the foregoing covenant may be enforced by Company or any of its subsidiaries or affiliates in the event of breach or threatened breach by Employee, by injunctions, restraining orders and other appropriate equitable relief.

(c) It is agreed by the parties that the foregoing covenants in this paragraph 3 impose a reasonable restraint on Employee in light of the activities and business of the Company on the date of the execution of this Agreement and the current plans of the Company or any of its subsidiaries or affiliates; but it is also the intent of the Company and Employee that such covenants be construed and enforced in accordance with the changing activities, business and locations of the Company or any of its subsidiaries or affiliates throughout the term of this covenant, whether before or after the date of termination of the employment of Employee. For example, if, during the term of this Agreement, the Company or any of its subsidiaries or affiliates engages in new and different activities, enters a new business or establishes new locations for its current activities or business in addition to or other than the activities or business enumerated under the Recitals above or the locations currently established therefor, then Employee

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will be precluded from soliciting the customers or Employees of such new activities or business or from such new location and from directly competing with such new business within 100 miles of its then-established operating location(s) through the term of this covenant.

It is further agreed by the parties hereto that, in the event that Employee shall cease to be employed hereunder, and shall enter into a business or pursue other activities not in competition with the Company or any of its subsidiaries or affiliates, or similar activities or business in locations the operation of which, under such circumstances, does not violate clause (i) of paragraph 3(a), Employee shall not be chargeable with a violation of this paragraph 3 if the Company or any of its subsidiaries or affiliates shall thereafter enter the same, similar or a competitive (i) business, (ii) course of activities or (iii) location, as applicable.

(d) The covenants in this paragraph 3 are severable and separate, and the unenforceability of any specific covenant shall not affect the provisions of any other covenant. Moreover, in the event any court of competent jurisdiction shall determine that the scope, time or territorial restrictions set forth herein are unreasonable, then it is the intention of the parties that such restrictions be enforced to the fullest extent which the court deems reasonable, and this Agreement shall thereby be reformed.

(e) All of the covenants in this paragraph 3 shall be construed as an agreement independent of any other provision in this Agreement, and the existence of any claim or cause of action of Employee against Company or any of its subsidiaries or affiliates, whether predicated on this Agreement or otherwise, shall not constitute a defense to the enforcement by Company or any of its subsidiaries or affiliates of such covenants. It is specifically agreed that the period of two (2) years following termination of employment stated at the beginning of this paragraph 3, during which the agreements and covenants of

Employee made in this paragraph 3 shall be effective, shall be computed by excluding from such computation any time during which Employee is in violation of any provision of this paragraph 3.

4. PLACE OF PERFORMANCE; RELOCATION RIGHTS.

(a) Employee understands that he may be requested by Company or any of its subsidiaries or affiliates to relocate from his present residence to another geographic location in order to more efficiently carry out his duties and responsibilities under this Agreement or as part of a promotion or other increase in duties and responsibilities. In such event, if Employee agrees to relocate, Company or any of its subsidiaries or affiliates will pay all relocation costs to move Employee, his immediate family and their personal property and effects. Such costs may include, by way of example, but are not limited to, pre-move visits to search for a new residence, investigate schools or for other purposes; temporary lodging and living costs prior to moving into a new permanent residence; duplicate home carrying costs; all closing costs on the sale of Employee's present residence and on the purchase of a comparable residence in the new location; and added income taxes that Employee may incur if any relocation costs are not deductible

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for tax purposes. The general intent of the foregoing is that Employee shall not personally bear any out-of-pocket cost as a result of the relocation, with an understanding that Employee will use his best efforts to incur only those costs which are reasonable and necessary to effect a smooth, efficient and orderly relocation with minimal disruption to the business affairs of Company or any of its subsidiaries or affiliates and the personal life of Employee and his family.

(b) Notwithstanding the above, if Employee is requested by Company to relocate his primary residence and Employee refuses, such refusal shall not constitute "CAUSE" for termination of this Agreement under the terms of paragraph 5(a) (iii).

5. TERM; TERMINATION; RIGHTS ON TERMINATION.

(a) TERM. The term of this Agreement shall begin on the date hereof and continue for three (3) years (the "INITIAL TERM") unless terminated sooner as herein provided, and shall automatically renew after the Initial Term on a year-to-year basis on the same terms and conditions contained herein in effect as of the time of renewal unless the Company notifies Employee at least 60 days prior to such expiration (the "TERM"). This Agreement and Employee's employment may be terminated in any one of the following ways:

- (i) TERMINATION AS A RESULT OF THE EMPLOYEE'S DEATH. The death of Employee shall immediately terminate this Agreement and upon such termination Employee's Estate shall receive from the Company, in a lump-sum payment, the base salary at the rate then in effect for one (1) year, provided, however, that such lump-sum payment shall be reduced by the amount, if any, of benefit payable under any life insurance policies to the extent such policies are procured and paid for by the Company.
- (ii) TERMINATION ON ACCOUNT OF DISABILITY. If, as a result of incapacity due to physical or mental illness or injury, Employee shall have been absent from his full-time duties hereunder for four (4) consecutive months, then thirty (30) days after receiving written notice (which notice may occur before or after the end of such four (4) month period, but which shall not be effective earlier than the last day of such four (4) month period), Company may terminate Employee's employment hereunder provided Employee is unable to resume his

full-time duties with or without reasonable accommodation at the conclusion of such notice period. Also, Employee may terminate his employment hereunder if his health should become impaired to an extent that makes the continued performance of his duties hereunder hazardous to his physical or mental health or his life, provided that Employee shall have furnished Company with a written statement from a qualified doctor to such effect and provided, further, that, at Company's request made within thirty (30) days of the date of such written statement, Employee shall submit to an examination by a doctor selected by Company who is reasonably

acceptable to Employee or Employee's doctor and such doctor shall have concurred in the conclusion of Employee's doctor. In the event this Agreement is terminated as a result of Employee's disability, Employee shall receive from Company, in a lump-sum payment due within ten (10) days of the effective date of termination, the base salary at the rate then in effect for whatever time period is remaining under the Initial Term of this Agreement or for one (1) year, whichever amount is greater; provided, however, that any such payments shall be reduced by the amount of any disability insurance payments payable to the Employee as a result of such disability.

(iii) TERMINATION BY THE COMPANY FOR CAUSE. Company may terminate this Agreement immediately for "CAUSE," which shall be: (1) Employee's willful and material breach of this Agreement (which breach cannot be cured or, if capable of being cured, is not cured within ten (10) days after receipt of written notice to cure); (2) Employee's gross negligence in the performance or intentional nonperformance of any of Employee's material duties and responsibilities hereunder; (3) Employee's willful dishonesty, fraud or misconduct with respect to the business or affairs of Company or any of its subsidiaries or affiliates which materially and adversely affects the operations or reputation of Company or any of its subsidiaries or affiliates; (4) Employee's conviction of a felony crime; (5) Employee's confirmed positive illegal drug test result; (6) confirmed sexual harassment by Employee; or (7) Employee's material and willful violation of the Company's Compliance and Business Ethics Policies. In the event of a termination for Cause, as enumerated above, Employee shall have no right to any severance compensation.

(iv) TERMINATION WITHOUT CAUSE. At any time after the commencement of employment, either Employee or Company may, voluntarily or without cause, respectively, terminate this Agreement and Employee's employment, effective thirty (30) days after written notice is provided to the other. Should Employee be terminated by Company without Cause Employee shall receive from Company, in a lump-sum payment due on the effective date of termination, the base salary at the rate then in effect for one (1) year. Further, any termination without Cause by Company shall operate to shorten the period set forth in paragraph 3(a) and during which the terms of paragraph 3 apply to one (1) year from the date of termination of employment. Except as provided in paragraph 12 below, if Employee resigns or otherwise terminates this Agreement, the provisions of paragraph 3 hereof shall apply, except that Employee shall receive no severance compensation. If Employee is terminated by the Company without Cause, or if the Employee terminates

his employment for Good Reason pursuant to paragraph 12(c) below, then the Company shall make the insurance premium payments

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contemplated by COBRA for a period of twelve (12) months immediately following such termination.

(b) CHANGE IN CONTROL OF THE COMPANY. In the event of a Change in Control of the Company (as defined below) during the Term, paragraph 12 below shall apply.

(c) EFFECT OF TERMINATION. Upon termination of this Agreement for any reason provided above, Employee shall be entitled to receive all compensation earned and all benefits and reimbursements due through the effective date of termination. Additional compensation subsequent to termination, if any, will be due and payable to Employee only to the extent and in the manner expressly provided herein. All other rights and obligations of Company and Employee under this Agreement shall cease as of the effective date of termination, except that Company's obligations under paragraph 9 herein and Employee's obligations under paragraphs 3, 6, 7, 8 and 10 herein shall survive such termination in accordance with their terms.

(d) BREACH BY COMPANY. If termination of Employee's employment arises out of Company's material failure to pay Employee on a timely basis the amounts to which he is entitled under this Agreement or as a result of any other breach of this Agreement by Company, as determined by a court of competent jurisdiction or pursuant to the provisions of paragraph 16 below, Company shall pay all amounts and damages to which Employee may be entitled as a result of such breach, including interest thereon and all reasonable legal fees and expenses and other costs incurred by Employee to enforce his rights hereunder. Further, none of the provisions of paragraph 3 shall apply in the event this Agreement is terminated as a result of a breach by Company.

6. RETURN OF COMPANY PROPERTY. All records, designs, patents, business plans, financial statements, manuals, memoranda, lists and other property delivered to or compiled by Employee by or on behalf of the Company or its representatives, vendors or customers which pertain to the business of the Company shall be and remain the property of the Company and be subject at all times to its discretion and control. Likewise, all correspondence, reports, records, charts, advertising materials and other similar data pertaining to the business, activities or future plans of the Company which is collected by Employee shall be delivered promptly to the Company without request by it upon termination of Employee's employment.

7. INVENTIONS. Employee shall disclose promptly to the Company any and all significant conceptions and ideas for inventions, improvements and valuable discoveries, whether patentable or not, which are conceived or made by Employee, solely or jointly with another, during the period of employment or within one (1) year thereafter, and which are directly related to the business or activities of the Company and which

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Employee conveys as a result of his employment hereunder. Employee hereby assigns and agrees to assign all his interests therein to the Company or its nominee. Whenever requested to do so by the Company, Employee shall execute any and all applications, assignments or other instruments that the Company shall deem necessary to apply for and obtain Letters Patent of the United States or any foreign country or to otherwise protect the Company's interest therein.

8. TRADE SECRETS. Employee agrees that he will not, during or after the Term of this Agreement, disclose the specific terms of the Company's relationships or agreements with their respective significant vendors or customers or any other significant and material trade secret of the Company, whether in existence or proposed, to any person, firm, partnership, corporation or business for any reason or purpose whatsoever, except and only to the extent required by law or legal process following notice to the Company.

9. INDEMNIFICATION. In the event Employee is made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by Company against Employee), by reason of the fact that he is or was performing services under this Agreement, then Company shall indemnify Employee against all expenses (including attorneys' fees), judgments, fines and amounts paid in settlement, as actually and reasonably incurred by Employee in connection therewith, to the maximum extent permitted by applicable law. The advancement of expenses shall be mandatory to the extent permitted by applicable law. In the event that both Employee and Company are made a party to the same third-party action, complaint, suit or proceeding, Company agrees to engage counsel, and Employee agrees to use the same counsel, provided that if counsel selected by Company shall have a conflict of interest that prevents such counsel from representing Employee, Employee may engage separate counsel and Company shall pay all reasonable attorneys' fees of such separate counsel. Company shall not be required to pay the fees of more than one law firm except as described in the preceding sentence, and shall not be required to pay the fees of more than two law firms under any circumstances. Further, while Employee is expected at all times to use his best efforts to faithfully discharge his duties under this Agreement, Employee cannot be held liable to Company for errors or omissions made in good faith where Employee has not exhibited gross, willful and wanton negligence or misconduct or performed criminal or fraudulent acts.

10. NO PRIOR AGREEMENTS. Employee hereby represents and warrants to Company and the Company that the execution of this Agreement by Employee and his employment by Company and the performance of his duties hereunder will not violate or be a breach of any agreement with a former Company, client or any other person or entity. Further, Employee agrees to indemnify Company and the Company for any claim, including, but not limited to, attorneys' fees and expenses of investigation, by any such third party that such third party may now have or may hereafter come to have against Company or any of its subsidiaries or affiliates based upon or arising out of any noncompetition agreement, invention or secrecy agreement between Employee and such third party which was in existence as of the date of this Agreement.

11. ASSIGNMENT; BINDING EFFECT. Employee understands that he has been selected for employment by Company and/or the Company on the basis of his personal qualifications, experience and skills. Employee agrees, therefore, he cannot assign all or any portion of his performance under this Agreement. Subject to the preceding two (2) sentences and the express provisions of paragraph 12 below, this Agreement shall be binding upon, inure to the benefit of and be enforceable by the parties hereto and their respective heirs, legal representatives, successors and assigns.

12. CHANGE IN CONTROL.

- (a) Upon notice by Employee at any time during the 90 days following a Change in Control, the Employee may elect to terminate his employment and shall be entitled to receive in a lump-sum payment due upon the date of such termination the amount equal to two (2) times his annual base salary then in effect, and the noncompetition provisions of paragraph 3 shall apply for a period of one (1) year immediately following the effective date of termination.
- (b) Upon a Change in Control, any options outstanding to Employee that have not previously vested shall be immediately vested.
- (c) In any Change in Control situation, if Employee is terminated by Company without Cause at any time during the twelve (12) months immediately following the closing of the transaction giving rise to the Change in Control, or Employee terminates this Agreement for Good Reason (as defined below) at any time during the twelve (12) months immediately following the closing of the transaction giving rise to the Change in Control, Employee shall be entitled to receive in a lump-sum payment, due on the effective date of termination, the amount equal to two (2) times the greater of (i) his annual base salary then in effect or (ii) his annual base salary in effect immediately prior to the closing of the transaction giving rise to the Change in Control, and the noncompetition provisions of paragraph 3 shall apply for a period of one (1) year immediately following the effective date of termination. For purposes of this Agreement, Employee shall have "GOOD REASON" to terminate this Agreement and his employment hereunder if, without Employee's consent, (x) Employee is demoted by means of a reduction in authority, responsibilities, duties or title to a position of materially less stature or importance within the Company than as described in paragraph 1 hereof or (y) the Company breaches this Agreement in any material respect and fails to cure such breach within ten (10) days after Employee delivers written notice and a written description of such breach to the Company, which notice shall specifically refer to this section of this Agreement.
- (d) For purposes of applying paragraph 5 under the circumstances described in (b) above, the effective date of termination will be the closing date of the transaction giving rise to the Change in Control and all compensation, reimbursements and lump-sum payments due Employee must be paid in full

by Company at or prior to such closing. Further, Company shall ensure that Employee will be given sufficient time and opportunity to elect whether to exercise all or any of his vested options to purchase the Company's Common Stock, including any options with accelerated vesting under the provisions of the Company's 1998 Long-Term Incentive Plan (or other applicable plan then in effect), such that he may convert the options to shares of the Company's Common Stock at or prior to the closing of the transaction giving rise to the Change in Control, if he so desires.

- (e) A "CHANGE IN CONTROL" shall be deemed to have occurred if:
 - (i) any person, other than Comfort Systems USA, Inc., a

Delaware corporation and the beneficial owner of the Company ("CSUSA"), or an employee benefit plan of CSUSA, or any entity controlled by either, acquires directly or indirectly the Beneficial Ownership (as defined in Section 13(d) of the Securities Exchange Act of 1934, as amended) of any voting security of the CSUSA and immediately after such acquisition such Person is, directly or indirectly, the Beneficial Owner of voting securities representing fifty percent (50%) or more of the total voting power of all of the then-outstanding voting securities of CSUSA;

(ii) the following individuals no longer constitute a majority of the members of the Board of Directors of CSUSA: (A) the individuals who, as of the date hereof, constitute the Board of Directors of CSUSA (the "ORIGINAL DIRECTORS"); (B) the individuals who thereafter are elected to the Board of Directors of the CSUSA and whose election, or nomination for election, to the Board of Directors of CSUSA was approved by a vote of at least two-thirds (2/3) of the Original Directors then still in office (such directors becoming "ADDITIONAL ORIGINAL DIRECTORS" immediately following their election); and (C) the individuals who are elected to the Board of Directors of CSUSA and whose election, or nomination for election, to the Board of Directors of CSUSA was approved by a vote of at least two-thirds (2/3) of the Original Directors and Additional Original Directors then still in office (such directors also becoming "ADDITIONAL ORIGINAL DIRECTORS" immediately following their election);

(iii) the stockholders of CSUSA shall approve a merger, consolidation, recapitalization, or reorganization of CSUSA, a reverse stock split of outstanding voting securities, or consummation of any such transaction if stockholder approval is not obtained, other than any such transaction which would result in at least seventy-five percent (75%) of the total voting power represented by the voting securities of the surviving entity outstanding immediately after such transaction being Beneficially Owned by at least seventy-five percent (75%) of the holders of outstanding voting securities of CSUSA immediately prior to the transaction, with the voting power of each

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such continuing holder relative to other such continuing holders not substantially altered in the transaction; or

(iv) the stockholders of CSUSA shall approve a plan of complete liquidation of CSUSA or an agreement for the sale or disposition of all or a substantial portion of the CSUSA's assets (i.e., fifty percent (50%) or more of the total assets of CSUSA).

(v) Employee must be notified in writing by Company or any of its subsidiaries or affiliates at anytime that either Company or any of its subsidiaries or affiliates anticipates that a Change in Control may take place.

(f) If it shall be determined that any payment or distribution by Company, the Company or any other person to or for the benefit of the Employee (a "PAYMENT") would be subject to the excise tax imposed by Section 4999 of the Internal Revenue Code of 1986, as amended (the "EXCISE TAX"), as a result of the

termination of employment of the Employee in the event of a Change in Control, then Company, the Company or the successor to the Company shall pay an additional payment (a "GROSS-UP PAYMENT") in an amount such that after payment by the Employee of all taxes, including, without limitation, any income taxes and Excise Tax imposed on the Gross-Up Payment, the Employee retains an amount of the Gross-Up Payment equal to the Excise Tax imposed on the Payments. Such amount will be due and payable by Company, the Company or the successor to the Company within ten (10) days after the Employee delivers written request for reimbursement accompanied by a copy of the Employee's tax return(s) or other tax filings showing the excise tax actually incurred by the Employee.

13. COMPLETE AGREEMENT. This Agreement sets forth the entire agreement of the parties hereto relating to the subject matter hereof and supersedes any other employment agreements or understandings, written or oral, between or among Company, the Company and Employee. This Agreement is not a promise of future employment. Employee has no oral representations, understandings or agreements with Company or any of its subsidiaries or affiliates or any of its officers, directors or representatives covering the same subject matter as this Agreement. This Agreement is the final, complete and exclusive statement and expression of the agreement between Company and Employee and of all the terms of this Agreement, and it cannot be varied, contradicted or supplemented by evidence of any prior or contemporaneous oral or written agreements. This written Agreement may not be later modified except by a further writing signed by a duly authorized officer of Company and Employee, and no term of this Agreement may be waived except in writing signed by the party waiving the benefit of such term.

14. NOTICE. Whenever any notice is required hereunder, it shall be given in writing addressed as follows:

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To Company: Comfort Systems USA (Texas), L.P.
777 Post Oak Blvd, Suite 500
Houston, Texas 77056
Attention: Law Department

To Employee: William F. Murdy
5110 San Felipe 363W
Houston, TX 77056

Notice shall be deemed given and effective on the earlier of three (3) days after the deposit in the U.S. mail of a writing addressed as above and sent first class mail, certified, return receipt requested, or when actually received by means of hand delivery, delivery by Federal Express or other courier service, or by facsimile transmission. Either party may change the address for notice by notifying the other party of such change in accordance with this paragraph 14.1

15. SEVERABILITY; HEADINGS. If any portion of this Agreement is held invalid or inoperative, the other portions of this Agreement shall be deemed valid and operative and, so far as is reasonable and possible, effect shall be given to the intent manifested by the portion held invalid or inoperative. The paragraph headings herein are for reference purposes only and are not intended in any way to describe, interpret, define or limit the extent or intent of this Agreement or of any part hereof.

16. ARBITRATION. With the exception of paragraphs 3 and 7, any unresolved dispute or controversy arising under or in connection with this Agreement shall be settled exclusively by arbitration, conducted before a panel of three (3) arbitrators in Houston, Texas, in accordance with the National Rules for the Resolution of Employment Disputes of the American Arbitration Association

("AAA") then in effect, provided that Employee shall comply with Company's grievance procedures in an effort to resolve such dispute or controversy before resorting to arbitration, and provided further that the parties may agree to use arbitrators other than those provided by the AAA. The arbitrators shall not have the authority to add to, detract from, or modify any provision hereof nor to award punitive damages to any injured party. The arbitrators shall have the authority to order back-pay, severance compensation, vesting of options (or cash compensation in lieu of vesting of options), reimbursement of costs, including those incurred to enforce this Agreement, and interest thereon in the event the arbitrators determine that Employee was terminated without disability or Cause, as defined in paragraphs 5(a)(ii) and 5(a)(iii), respectively, or that Company has breached this Agreement in any material respect. A decision by a majority of the arbitration panel shall be final and binding. Judgment may be entered on the arbitrators' award in any court having jurisdiction. The direct expense of any arbitration proceeding shall be borne by Company.

17. GOVERNING LAW. This Agreement shall in all respects be construed according to the laws of the State of Texas.

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18. COUNTERPARTS. This Agreement may be executed simultaneously in two (2) or more counterparts, each of which shall be deemed an original and all of which together shall constitute but one and the same instrument.

19. THIRD-PARTY BENEFICIARY. The Company is intended to be a third-party beneficiary under this Agreement, and shall be entitled to enforce the provisions hereof benefiting the Company.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

COMFORT SYSTEMS USA (TEXAS), L.P.

By: Comfort Systems USA G.P., Inc.

By: /s/ William Murdy

William Murdy
Chief Executive Officer

COMFORT SYSTEMS USA, INC.

By: /s/ William Murdy

William Murdy
Chief Executive Officer

EMPLOYEE:

/s/ Gary E. Hess

Gary E. Hess

FOURTH AMENDED AND RESTATED CREDIT AGREEMENT

This FOURTH AMENDED AND RESTATED CREDIT AGREEMENT dated as of March 22, 2001 (this "Agreement") is among COMFORT SYSTEMS USA, INC., a Delaware corporation (the "Company"), the Subsidiaries of the Company listed on the signature pages hereto as Guarantors (together with each other person who subsequently becomes a Guarantor, collectively the "Guarantors"), the banks and other financial institutions listed on the signature pages hereto under the caption "Banks" (together with each other person who becomes a Bank, collectively the "Banks"), and BANK ONE, NA, formerly known as Bank One, Texas, N.A., individually as a Bank ("Bank One") and as administrative agent for the other Banks (in such capacity together with any other Person who becomes the administrative agent, the "Administrative Agent"), BANKERS TRUST COMPANY, individually as a Bank ("BTKo") and as syndication agent for the other Banks (in such capacity together with any other Person who becomes the syndication agent, the "Syndication Agent"), BANK OF AMERICA, N.A., individually as a Bank ("BoFA") and as documentation agent for the other Banks (in such capacity together with any other Person who becomes the documentation agent, the "Documentation Agent"; and together with the Administrative Agent and the Syndication Agent, the "Agents"), CREDIT LYONNAIS NEW YORK BRANCH, individually as a Bank and as Co-Agent, NATIONAL CITY BANK, individually as a Bank and as Co-Agent, and THE BANK OF NOVA SCOTIA, individually as a Bank and as Co-Agent (collectively, "Co-Agents").

WHEREAS, the Company, Guarantors, Bank One and the Administrative Agent are parties to the Existing Credit Agreement (this and other terms used in these recitals without definition being used as defined in Section 1.1 which provides for a revolving credit facility pursuant to which Bank One and the Banks named therein committed to make loans of up to \$280,000,000.00, including a letter of credit facility not to exceed \$10,000,000.00, to the Company for general corporate purposes, including working capital, financing permitted acquisitions and the issuance of letters of credit.

WHEREAS, the Company has requested the Banks to further amend and restate the Existing Credit Agreement to modify certain terms and conditions thereof, including, without limitation, to decrease the revolving credit facility to \$270,000,000.00, to increase the letter of credit facility to \$15,000,000, and to modify certain covenants, all as set forth herein.

NOW, THEREFORE, in consideration of the foregoing and the mutual covenants set forth herein, the Company, the Guarantors, the Agents and the Banks agree as follows:

ARTICLE I
DEFINITIONS; ACCOUNTING TERMS; INTERPRETATION

SECTION 1.1 Definitions. As used in this Agreement, the following terms shall have the following meanings:

"Account" has the meaning stated in the Texas Uniform Commercial Code.

"Administrative Agent" has the meaning specified in the introduction to this Agreement.

"Administrative Questionnaire" means the questionnaire attached hereto as Exhibit 1.1(a) to be completed by each Bank and returned to the Administrative Agent.

"Advance" means an advance, pursuant to a Notice of Advance, comprised of a single Type of Loans from all the Banks (or resulting from a conversion or conversions on the same date having, in the case of Eurodollar Rate Advances, the same Interest Period (except as otherwise provided in this Agreement)), made by all of the Banks concurrently to the Company.

"Advance Date" means, with respect to each Advance, the Business Day upon which the proceeds of such Advance are to be made available to the Company.

"Affiliate" means any other Person directly or indirectly controlling (including all directors and officers of such Person), controlled by, or under direct or indirect common control with such Person.

"Agents" has the meaning specified in the introduction to this Agreement.

"Agreement" has the meaning specified in the introduction to this Agreement.

"Alternate Base Rate" means, for any date, a rate per annum (rounded upwards, if necessary, to the next 1/16 of 1%) equal to the greater of (a) the Federal Funds Effective Rate in effect on such day plus 1/2 of 1% and (b) the Prime Rate in effect on such day. For purposes hereof, the term "Prime Rate" means, as of a particular date, the prime rate of Bank One most recently announced by Bank One and in effect on such date, automatically fluctuating upward or downward, as the case may be, with and at the time of each change therein without notice to the Company or any other Person, which prime rate may not necessarily represent the lowest or best rate actually charged to a customer. "Federal Funds Effective Rate" means, for any day, the weighted average of the rates on overnight federal funds transactions with members of the Federal Reserve System arranged by federal funds brokers, as published for such day (or, if such day is not a Business Day, for the next preceding Business Day) by the Federal Reserve Bank of New York, or, if such rate is not so published for any day which is a Business Day, the average of the quotations for such day on such transactions received by the Administrative Agent from three federal funds brokers of recognized standing selected by it. If, for any reason, the Administrative Agent shall have determined (which determination shall be conclusive absent manifest error) that it is unable to ascertain the Federal Funds Effective Rate, including the inability or failure of the Administrative Agent to obtain sufficient quotations in accordance with the terms hereof, the Alternate Base Rate shall be determined without regard to clause (a) of the first sentence of this definition until the circumstances giving rise to such inability no longer exist. Any change in the Alternate Base Rate due to a change in the Prime Rate or the Federal Funds Effective Rate shall be effective on the effective date of such change in the Prime Rate or the Federal Funds Effective Rate, respectively.

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"Alternate Base Rate Advance" means any Advance bearing interest at a rate determined by reference to the Alternate Base Rate in accordance with the provisions of Article II.

"Applicable Lending Office" means, with respect to each Bank, such Bank's Domestic Lending Office in the case of an Alternate Base Rate Advance and such Bank's Eurodollar Lending Office in the case of a Eurodollar Rate Advance.

"Application for Letter of Credit" means a letter of credit application in a form satisfactory to the Issuing Bank.

"Asset Sale" means the sale, transfer or other disposition for value, whether voluntary or involuntary, by the Company or any of its Subsidiaries to any Person other than the Company or any of its wholly-owned Subsidiaries of (i) any of the stock of any of the Company's Subsidiaries, (ii) substantially all of the Assets of any division or line of business of the Company and its Subsidiaries, or (iii) any other Assets of the Company or any of its Subsidiaries (other than (a) inventory and surplus or obsolete assets sold in the ordinary course of business and (b) any such other Assets to the extent that the aggregate value of such Assets sold in any single transaction or related series of transactions is equal to \$1,000,000 or less).

"Assets" (whether or not capitalized) means any interest in any kind of property or asset, whether real, personal or mixed, or tangible or intangible.

"Assignment and Acceptance" has the meaning specified in Section 12.10(c).

"Bank" has the meaning provided in the introduction to this Agreement.

"Bank One" means Bank One, NA, 910 Travis, 7th Floor, Houston, Texas 77002.

"Bankruptcy Code" has the meaning specified in Section 10.1(e).

"Board" means the Board of Governors of the Federal Reserve System of the United States (or any successor).

"BofA" means Bank of America, N.A., 700 Louisiana, Houston, Texas 77002.

"Borrowing Base" means as to the Company and its Guarantors on a consolidated basis at any time, an amount equal to the product of (a) eighty percent (80%), times (b) the Eligible Accounts Receivable plus or minus the Field Exam Adjustments, if any; provided that in the absence of a Borrowing Base Certificate, the Administrative Agent shall determine the Borrowing Base from time to time in its reasonable discretion, taking into account all information reasonably available to it, and the Borrowing Base from time to time so determined shall be the Borrowing Base for all purposes of this Agreement until a Borrowing Base Certificate is furnished to and accepted by the Administrative Agent.

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"Borrowing Base Certificate" means, as of any date, a certificate as to the Borrowing Base as of such date in the form of Exhibit 7.1(i).

"BTCO" means Bankers Trust, One Bankers Trust Plaza, 130 Liberty Street, New York, New York 10006.

"Business Day" means any day (other than a day which is a Saturday, Sunday or legal holiday in the State of Texas) on which most banks are open for business in Houston, Texas.

"Capitalized Lease Obligations" means all lease or rental obligations which, pursuant to GAAP, are capitalized for balance sheet purposes.

"CERCLA" means the comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended, state and local analogs, and all rules and regulations and requirements thereunder in each case as now or hereafter in effect.

"Change of Control" means any of (i) the acquisition by any Person (other than the shareholders on the Effective Date), or two or more Persons acting in concert, after the Effective Date of beneficial ownership of 50% or more of the outstanding shares of voting stock of the Company, (ii) during any period of 24 consecutive months, beginning on the Effective Date, the ceasing of those individuals (the "Continuing Directors") who (a) were directors of the Company on the first day of each such period or (b) subsequently became directors of the Company and whose initial nomination for election subsequent to that date was approved by a majority of the Continuing Directors then on the board of directors of the Company, to constitute a majority of the board of directors of the Company at any time during such period, (iii) all or substantially all of the assets of the Company and its Subsidiaries are sold in a single transaction or series of related transactions to any Persons or (iv) the Company merges or consolidates with or into any other Person except as permitted hereunder.

"Code" means the Internal Revenue Code of 1986 and the regulations promulgated thereunder.

"Collateral" means, collectively, all of the personal property (including capital stock) in which Liens are purported to be granted pursuant to the Collateral Documents as security for the Obligations.

"Collateral Account Agreement" means the Collateral Account Agreement executed and delivered by the Company and Administrative Agent on the Effective Date, substantially in the form of Exhibit 1.1(b) annexed hereto, as such Collateral Account Agreement may hereafter be amended, supplemented or otherwise modified from time to time.

"Collateral Documents" means the Collateral Account Agreement, the Company Pledge Agreement, the Company Security Agreement, the Subsidiary Pledge Agreements, the Subsidiary Security Agreements and all other instruments or documents delivered by the Company or any Guarantor pursuant to this Agreement or any of the

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other Loan Documents in order to grant to the Administrative Agent, on behalf of the Banks, a Lien on the Collateral as security for the Obligations.

"Commitment" and "Commitments" means the obligation of each of the Banks to enter into and perform this Agreement, to make available the Loans and to issue or participate in the Letters of Credit to the Company in the amounts shown on the signature page of each Bank hereto (as same are reduced pro rata by reductions to the Total Commitment) and all other duties and obligations of the Banks hereunder.

"Commitment Fee" has the meaning specified in Section 4.1(a).

"Company" has the meaning specified in the introduction to this Agreement.

"Company Pledge Agreement" means the Company Pledge Agreement executed and delivered by the Company on December 14, 1998, substantially in the form of Exhibit 1.1(c) annexed hereto, as such Company Pledge Agreement may thereafter be amended, supplemented or otherwise modified from time to time.

"Company Security Agreement" means the Company Security Agreement executed and delivered by the Company on December 14, 1998, substantially in the form of Exhibit 1.1(d) annexed hereto, as such Company Security Agreement may thereafter be amended, supplemented or otherwise modified from time to time.

"Compliance Certificate" means a certificate substantially in the form of Exhibit 1.1(e) annexed hereto delivered to the Administrative Agent and the Banks by the Company pursuant to Section 7.1(d).

"Consolidated Net Worth" means, at any date, an amount equal to the consolidated stockholders' equity of the Company and its subsidiaries determined in accordance with GAAP as of such date (including non-cash impairments to good will resulting from changes to financial accounting standards to be added to Consolidated Net Worth pursuant to Section 8.7).

"Conversion" or "Convert" (in each case whether or not capitalized) means the changing of a Eurodollar Rate Advance to an Alternate Base Rate Advance or vice versa in accordance with the provisions hereof.

"Credit Event" means the making of any Advance or the issuance or extension of any Letter of Credit.

"Cumulative Consolidated Net Income" means, as of any date of determination, (x) the consolidated net income (or loss) of the Company and its Subsidiaries, determined on a consolidated basis in accordance with GAAP, less (y) any Restricted Subordinated Debt Payments (other than interest payments) in respect of any Subordinated Debt existing on the Effective Date made during the period (taking as one accounting period) commencing on the Effective Date and ending on the last day of the most recent fiscal quarter for which financial statements have been delivered pursuant to Section 6.1.

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"Current Assets" and "Current Liabilities" means, as to the Company and its Subsidiaries determined on a consolidated basis, at any time the aggregate current assets or current liabilities (other than the repayment of the Loans) of the Company, each as determined in accordance with GAAP.

"Default" means the occurrence of any event which with or without the giving of notice or the passage of time or both could become an Event of Default.

"Default Rate" means the lesser of (i) the Highest Lawful Rate and (ii) with respect to (a) Alternate Base Rate Advances, the rate per annum which would otherwise be applicable plus two percent (2.00%), and (b) Eurodollar Rate Advances, the rate per annum which would otherwise be applicable plus three percent (3.00%).

"Designated Payment Date" means March 31, June 30, September 30 and December 31 of each year; provided, however, if a Designated Payment Date shall be a day which is not a Business Day, such Designated Payment Date shall be the next succeeding Business Day, and such extension of time shall be included in determining the amount to be paid on such date.

"Documentation Agent" has the meaning specified in the introduction to this Agreement.

"Domestic Lending Office" means, with respect to any Bank, the office of such Bank, designated from time to time as its "Domestic Lending Office" hereunder.

"EBITDA" means, for any period, the consolidated pre-tax income for such period, plus the aggregate amount which was deducted for such period in determining such consolidated, pre-tax income in respect of Interest Expense (including amortization of debt discount, imputed interest and capitalized interest), depreciation and amortization, provided, the calculation of EBITDA for any period shall include non-cash impairments to good will resulting from

changes to financing accounting standards to be added to EBITDA pursuant to Section 8.7; and further provided, the calculations of EBITDA after the acquisition of assets or entities permitted under Section 8.5(d) shall include pro forma adjustments consistent with the regulations and practices of the United States Securities and Exchange Commission (whether or not applicable) to account for such acquired entity's historical EBITDA for the relevant period or similar adjustments in the case of an asset acquisition. For fiscal year 2000, (and only for fiscal year 2000) the actual amount of pre-tax restructuring charges incurred by the Company during fiscal year 2000 (but in no event in excess of \$31,250,000.00 in the aggregate) may be added back in determining EBITDA, provided that such pre-tax restructuring charges may be added back to the extent, and only to the extent, that such pre-tax restructuring charges were deducted in calculating EBITDA.

"Effective Date" means the date on or before March 31, 2001, on which all conditions to make an Advance set forth in Section 5.1 are first met or waived in accordance with Section 12.1 hereof.

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"Eighty Percent Banks" means Banks holding at least 80% of the Advances outstanding under the Loans, or, if no Advances are outstanding, Banks holding such percentage of the Total Commitment (notwithstanding any reduction or termination of the Total Commitment) or if there are no Advances or Commitments outstanding, Banks holding such percentage of outstanding Letters of Credit.

"Eligible Accounts Receivable" means at any time an amount equal to the aggregate net invoice or ledger amount (net of any reserves) due on all trade Accounts of the Company and the Guarantors for goods sold or leased or services rendered upon which Borrower's and Guarantors' rights to receive payment are absolute and not contingent upon the fulfillment of any condition whatsoever; provided, however, that Eligible Accounts Receivable shall include any retainage due to the Company and the Guarantors with respect to jobs in progress.

"Eligible Assignee" means (a) any Bank; (b) a commercial bank organized under the laws of the United States, or any state thereof, and having total assets in excess of \$250,000,000.00; (c) a commercial bank organized under the laws of any other country which is a member of the Organization for Economic Cooperation and Development or any successor organization, or a political subdivision of any such country, and having total assets in excess of \$1,000,000,000.00; provided that such bank is acting through a branch or agency located in the country in which it is organized or another country which is also a member of the Organization for Economic Cooperation and Development or any successor organization; (d) the central bank of any country which is a member of the Organization for Economic Cooperation and Development or any successor organization; and (e) any other bank or similar financial institution approved by the Administrative Agent, the Majority Banks and the Company, which consent of the Company shall not be unreasonably withheld.

"Environmental Laws" means federal, state or local laws, rules or regulations, and any judicial or administrative interpretations thereof, including any judicial or administrative order, judgment, permit, approval, decision or determination pertaining to conservation or protection of the environment in effect at the time in question, including the Clean Air Act, CERCLA, the Federal Water Pollution Control Act, the Occupational Safety and Health Act, the Resource Conservation and Recovery Act, the Safe Drinking Water Act, the Toxic Substances Control Act, the Superfund Amendment and Reauthorization Act of 1986, the Hazardous Materials Transportation Act, and comparable state and local laws, and other environmental conservation and protection laws.

"ERISA" means the Employee Retirement Income Security Act of 1974 and

the regulations promulgated thereunder.

"ERISA Affiliate" means any trade or business (whether or not incorporated) which is either a member of the same "controlled group" or under "common control," within the meaning of Section 414 of the Code and the regulations thereunder, with the Company and (b) any Subsidiary of the Company.

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"Eurocurrency Liabilities" has the meaning specified in Regulation D as in effect from time to time.

"Eurodollar Lending Office" means, with respect to each Bank, the branches or affiliates of such Bank designated as its "Eurodollar Lending Office" from time to time hereunder.

"Eurodollar Rate" means, with respect to any Eurodollar Rate Advance, the rate (rounded to 1/16 of 1%) at which dollar deposits approximately equal in principal amount to the entire portion of such Advance and for a maturity equal to the applicable Interest Period are offered in immediately available funds to the Administrative Agent by prime banks in whatever Eurodollar interbank market may be selected by the Administrative Agent in its sole and absolute discretion at the time of determination and in accordance with the then usual practice in such market at approximately 10:00 a.m. (Houston, Texas time) two Business Days prior to the commencement of such Interest Period.

"Eurodollar Rate Advance" means any Advance bearing interest at a rate determined by reference to the Eurodollar Rate in accordance with the provisions of Article II.

"Events of Default" has the meaning specified in Section 10.1.

"Existing Credit Agreement" means that certain Credit Agreement by and among the Company, Guarantors, Bank One, the Administrative Agent and certain of the Banks dated as of July 2, 1997, as such credit agreement was amended and restated by that certain First Amended and Restated Credit Agreement dated as of September 22, 1997 and by that certain Second Amended and Restated Credit Agreement dated as of April 14, 1998, as such credit agreement was further amended by that certain First Amendment to Second Amended and Restated Credit Agreement dated as of June 30, 1998, and as such credit agreement was amended and restated by that certain Third Amended and Restated Credit Agreement dated as of December 14, 1998, as amended by that certain First Amendment dated as of January 14, 1999, that certain Second Amendment dated as of August 18, 1999, that certain Third Amendment dated as of August 11, 2000, and that certain Fourth Amendment dated as of November 13, 2000.

"Federal Funds Effective Rate" has the meaning specified in the definition of the term "Alternate Base Rate."

"Fees" has the meaning specified in Section 4.1.

"Field Exam Adjustments" means any increases or decreases to the Borrowing Base as determined by (i) the Administrative Agent in the exercise of its reasonable discretion, with respect to decreases, and (ii) the Majority Banks in the exercise of their reasonable collective discretion, with respect to increases, based on the results of the field exam of the Company's working capital assets required under Section 7.2.

"Financial Compliance" means that the Company has either (i) incurred Subordinated Debt (or other capital which is junior in right of payment to the

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Obligations) since the Effective Date with the approval of the Administrative Agent and the Banks in a principal amount of not less than \$25,000,000, with a maturity date of no less than five (5) years from its date of issuance and otherwise upon terms and conditions acceptable to the Administrative Agent and the Banks, or (ii) not permitted for at least two consecutive fiscal quarters, as of the last day of both of such fiscal quarters the ratio described in Section 8.11 to exceed 2.50 to 1.00.

"Financial Condition Certificate" means the certificate substantially in the form of Exhibit 1.1(f) annexed hereto, dated the Effective Date, delivered by the Company pursuant to Section 5.1(i).

"Financials" has the meaning specified in Section 5.1(h).

"First Priority" means, with respect to any Lien purported to be created in any Collateral pursuant to any Collateral Document, that (i) such Lien has priority over any other Lien on such Collateral (other than Permitted Liens which as a matter of statutory law have priority over any other Lien irrespective of the prior perfection or filing of such other Lien) and (ii) such Lien is the only Lien (other than Permitted Liens and Liens otherwise permitted pursuant to Section 8.4) to which such Collateral is subject.

"Funded Senior Debt" means all indebtedness for borrowed money evidenced by a written document and subject to required payments of interest and/or principal exclusive of Subordinated Debt.

"GAAP" means generally accepted accounting principles as in effect from time to time as set forth in the opinions, statements and pronouncements of the Accounting Principles Board of the American Institute of Certified Public Accountants, the Financial Accounting Standards Board and such other Persons who shall be approved by a significant segment of the accounting profession and concurred in by the independent certified public accountants certifying any audited financial statements of the Company.

"Guaranteed Obligations" has the meaning specified in Section 9.1.

"Guarantors" has the meaning provided in the introduction to this Agreement.

"Guaranty" means the obligations contained in Article IX hereof and in any document containing similar obligations executed by subsequent Guarantors.

"Hazardous Materials" means (a) hazardous waste as defined in the Resource Conservation and Recovery Act of 1976, or in any applicable federal, state or local law or regulation, (b) hazardous substances, as defined in CERCLA, or in any applicable state or local law or regulation, (c) gasoline, or any other petroleum product or by-product, (d) toxic substances, as defined in the Toxic Substances Control Act of 1976, or in any applicable federal, state or local law or regulation, (e) asbestos or asbestos containing materials, or (f) insecticides, fungicides, or rodenticides, as defined in the Federal Insecticide, Fungicide, and Rodenticide Act of 1975, or in any applicable federal, state or local law or regulation, as each such act, statute or regulation may be amended from time to time.

"Highest Lawful Rate" means, as to any Bank, the maximum nonusurious rate of interest that, under applicable law, may be contracted for, taken, reserved, charged or received by such Bank on the Loans or under the Loan Documents at any time or from time to time. If the maximum rate of interest which, under applicable law, any of the Banks are permitted to charge the Company on the Loans shall change after the date hereof, to the extent permitted by applicable law, the Highest Lawful Rate shall be automatically increased or decreased, as the case may be, as of the effective time of such change without notice to the Company or any other Person.

"Indebtedness" means, without duplication, (a) all indebtedness for borrowed money (whether by loan or the issuance and sale of debt securities or letters of credit issued under this facility, banker's acceptances or quasi equity issues) or for the deferred purchase price of property or services, (b) all indebtedness created or arising under any conditional sale or other title retention agreement with respect to property, (c) all Capitalized Lease Obligations, (d) hedge or swap agreements and Interest Rate Agreements (at a mark to market valuation); and (e) obligations under direct or indirect guaranties in respect of, and obligations (contingent or otherwise) to purchase or otherwise acquire, or otherwise to assure a creditor against loss in respect to indebtedness or obligations of another Person of the kinds referred to in clauses (a) through (d) above.

"Information Systems and Equipment" means all computer hardware, firmware and software, as well as other information processing systems, or any equipment containing embedded microchips, whether directly or owned, licensed, leased, operated or otherwise controlled by the Company or any of its Subsidiaries, including through third-party service providers, and which, in whole or in part, are used, operated, relied upon, or integral to, the Company's or any of its Subsidiaries' conduct of their business.

"Interest Expense" means, with respect to the Company and its Subsidiaries determined on a consolidated basis, for any period the total interest expense for such period determined in conformity with GAAP including any interest expense attributable to Capitalized Lease Obligations.

"Interest Period" has the meaning specified in Section 2.11.

"Interest Rate Agreement" means any interest rate swap agreement, interest rate cap agreement, interest rate collar agreement, interest rate hedging agreement or other similar agreement or arrangement designed to protect against fluctuations in interest rates to which the Company and any Bank are parties.

"Investment" means, as applied to any Person, any direct or indirect purchase or other acquisition by such Person of the assets, stock or other securities of any other Person, or any direct or indirect loan, advance or capital contribution by such Person to any other Person, and any other item which would be classified as an "investment" on a balance sheet of such Person in accordance with GAAP, including any direct or indirect contribution by such Person of property or assets to a joint venture, partnership or other business entity in which such Person retains an interest.

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"Issuing Bank" means, for each Letter of Credit, the Bank that agrees or is otherwise obligated to issue such Letter of Credit, determined as provided in Section 3.2(c).

"Letter of Credit" has the meaning specified in Section 3.1(a).

"Letter of Credit Fee" means the following computed on the undrawn face

amount of each Letter of Credit (i) a 1/8% per annum fronting fee payable to the Issuing Bank and (ii) a fee payable to the Issuing Bank for the ratable benefit of the Banks equal to the greater of (a) \$500.00 or (b) a rate per annum determined in accordance with the grid set forth below as a function of the ratio of Total Funded Debt on the last day of the immediately preceding fiscal quarter to EBITDA for the consecutive four fiscal quarters ending on the last day of such fiscal quarter:

TOTAL FUNDED DEBT/EBITDA RATIO	LETTER OF CREDIT FEE
-----	-----
-4.00	3.500%
-3.50 but <4.00	3.250%
-3.00 but <3.50	3.000%
-2.50 but <3.00	2.750%
<2.50	2.500%

Any Letter of Credit Fees expressed as a rate per annum shall be calculated on the basis of a 365 day-year.

"Letter of Credit Obligations" means at any time the sum of (a) the aggregate then undrawn and unexpired amount of outstanding Letters of Credit and (b) the aggregate amount of drawings under Letters of Credit not reimbursed pursuant to Section 3.3(c).

"Letter of Credit Request" has the meaning specified in Section 3.2(a).

"Lien" means, when used with respect to any Person, any mortgage, lien, charge, pledge, security interest, attachment or encumbrance of any kind (whether voluntary or involuntary and whether imposed or created by operation of law or otherwise) upon, or pledge of, any of its property or assets, whether now owned or hereafter acquired, or any lease intended as security, any capital lease in the nature of the foregoing, any conditional sale agreement or other title retention agreement, in each case, for the purpose, or having the effect, of protecting a creditor against loss or securing the payment or performance of an obligation.

"Loan" and "Loans" has the meaning assigned thereto in Section 2.1.

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"Loan Documents" means this Agreement, the Notes, the Letters of Credit (and any applications for, or reimbursement agreements or other documents or certificates executed by the Company in favor of an Issuing Bank relating to, the Letters of Credit), the Guaranty, the Collateral Documents, the Notice of Advance, and the corporate resolutions authorizing the Loan Documents.

"Majority Banks" means Banks holding at least 66.67% of the Advances outstanding under the Loans, or, if no Advances are outstanding, Banks holding such percentage of the Total Commitment (notwithstanding any reduction or termination of the Total Commitment) or if there are no Advances or Commitments outstanding, Banks holding such percentage of outstanding Letters of Credit.

"Margin" means with respect to any Advance, the percentage determined in accordance with the following table as a function of the ratio of Total Funded Debt on the last day of the immediately preceding fiscal quarter to EBITDA for the consecutive four fiscal quarters ending on the last day of such

fiscal quarter:

TOTAL FUNDED DEBT/ EBITDA RATIO	EURODOLLAR RATE ADVANCE	ALTERNATE BASE RATE ADVANCE
-----	-----	-----
-4.00	3.500%	2.000%
-3.50 but <4.00	3.250%	1.750%
-3.00 but <3.50	3.000%	1.500%
-2.50 but <3.00	2.750%	1.250%
<2.50	2.500%	1.000%

"Margin Period" means a period commencing on the date on which the quarterly or annual financial statements of the Company are required to be delivered pursuant to Section 7.1(a) or Section 7.1(b) as the case may be (or have been delivered pursuant to such Sections in the Existing Credit Agreement), and ending on the next date a financial statement is required to be so delivered.

"Material Adverse Effect" means, relative to any occurrence of whatever nature (including any adverse determination in any litigation, arbitration or governmental investigation or proceeding), (a) a material adverse effect on the business, operations, properties, assets or condition (financial or otherwise) of the Company and its Subsidiaries taken as a whole or (b) the impairment of the ability of the Company and the Guarantors to perform, or of any Agent or any Bank to enforce, the Obligations or the liens granted under the Collateral Documents.

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"Material Subsidiary" means a Subsidiary of the Company that has annual revenues or Assets with a book value of \$5,000,000 or more for the most recently ended fiscal year.

"Maturity Date" means January 1, 2003.

"Maximum Guaranteed Amount" means for each Guarantor the maximum amount which any Guarantor could pay under the Guaranty without having such payment set aside as a fraudulent transfer or conveyance or similar action under the Bankruptcy Code or any applicable state or foreign law.

"Multiemployer Plan" means any plan which is a "multiemployer plan" (as such term is defined in Section 4001(a)(3) of ERISA).

"Net Asset Sale Proceeds" means, with respect to any Asset Sale, cash payments (including any cash received by way of deferred payment pursuant to, or by monetization of, a note receivable or otherwise, but only as and when so received) received from such Asset Sale, net of any bona fide direct costs incurred in connection with Asset Sale, including (i) income taxes reasonably estimated to be actually payable within two years of the date of such Asset Sale as a result of any gain recognized in connection with such Asset Sale and (ii) payment of the outstanding principal amount of, premium or penalty, if any, and interest on any Indebtedness (other than the Loans) that is secured by a Lien on the stock or assets in question and that is required to be repaid under the terms thereof as a result of such Asset Sale.

"Net Cash Proceeds" means, with respect to the sale of any of the Company's vehicles, the proceeds thereof in the form of cash (including any such proceeds received by way of deferred payment of principal pursuant to a note or installment receivable or otherwise, but only as and when received) of such

sale, net of amounts required to be applied to the repayment of Indebtedness secured by a Lien expressly permitted hereunder (other than any Lien pursuant to a Loan Document) and other customary fees and expenses actually incurred in connection therewith and net of taxes paid or reasonably estimated to be payable as a result thereof.

"Note" and "Notes" have the meaning specified in Section 2.2.

"Notice of Advance" has the meaning provided in Section 2.3(a).

"Notice of Conversion" has the meaning provided in Section 2.5.

"Notice of Default" has the meaning specified in Section 10.2.

"Obligations" means all the obligations of every nature of the Company and each Guarantor owed to Agents, Banks or any of them now or hereafter existing under the Loan Documents, whether for principal, interest, Fees, expenses, indemnification or otherwise.

"Other Activities" has the meaning specified in Section 11.3.

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"Other Financings" has the meaning specified in Section 11.3.

"Other Hedging Agreement" shall mean any foreign exchange contract, currency swap agreements, commodity agreements or other similar agreements or arrangements designed to protect against the fluctuations in currency values to which the Company is a party.

"Payment Office" means the office of the Administrative Agent located at 910 Travis, Houston, Texas 77002, or such other office as the Administrative Agent may hereafter designate in writing as such to the other parties hereto.

"PBGC" means the Pension Benefit Guaranty Corporation or any entity succeeding to all or any of its functions under ERISA.

"Permitted Investments" means, as to any Person:

(a) securities issued or directly and fully guaranteed or insured by the United States or any agency or instrumentality thereof (provided, that the full faith and credit of the United States is pledged in support thereof) having maturities of not more than twelve months from the date of acquisition thereof,

(b) time deposits and certificates of deposit with maturities of not more than twelve months from the date of acquisition by such Person which deposits or certificates are either: (a) fully insured by the Federal Deposit Insurance Corporation or (b) in any Bank or other commercial bank incorporated in the United States or any U.S. branch of any other commercial bank, in each case having capital, surplus and undivided profits aggregating \$100,000,000.00 or more with a long-term unsecured debt rating of at least A- from Standard & Poor's Ratings Group or A3 from Moody's Investors Service,

(c) commercial paper issued by any Person incorporated in the United States rated at least A2 or the equivalent thereof by Standard & Poor's Ratings Group or at least P2 or the equivalent thereof by Moody's Investors

Service and, in each case, maturing not more than 270 days after the date of issuance,

(d) investments in money market mutual funds having assets in excess of \$2,000,000,000.00 substantially all of whose assets are comprised of securities of the types described in clauses (a) through (c) above, and

(e) repurchase or reverse purchase agreements respecting obligations with a term of not more than seven days for underlying securities of the types described in clause (a) above entered into with any bank listed in or meeting the qualifications specified in clause (b) above.

"Permitted Liens" shall mean: (a) Liens for taxes, assessments, levies or other governmental charges not yet due or which are being contested in good faith by appropriate proceedings and for which adequate reserves are maintained in accordance with GAAP; (b) Liens in connection with worker's compensation, unemployment

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insurance or other social security, old age pension or public liability obligations not yet due or which are being contested in good faith by appropriate proceedings and for which adequate reserves are maintained in accordance with GAAP; (c) operator's, vendors', carriers', warehousemen's, repairmen's, mechanics', workers', materialmen's or other like Liens arising by operation of law in the ordinary course of business (or deposits to obtain the release of any such Lien) and securing amounts not yet due or which are being contested in good faith by appropriate proceedings and for which adequate reserves are maintained in accordance with GAAP; (d) deposits to secure insurance in the ordinary course of business; (e) deposits to secure the performance of bids, tenders, contracts (other than contracts for the payment of money or the deferred purchase price of goods or services), leases, licenses, franchises, trade contracts, statutory obligations, surety and appeal bonds and performance bonds and other obligations of a like nature incurred in the ordinary course of business; (f) easements, rights of way, covenants, restrictions, reservations, exceptions, encroachments, zoning and similar restrictions and other similar encumbrances (other than to secure the payment of borrowed money or the deferred purchase price of goods or services) or title defects, in each case incurred in the ordinary course of business which, in the aggregate, are not substantial in amount, and which do not in any case singly or in the aggregate materially detract from the value or usefulness of the Property subject thereto for the business conducted by the Company and its Subsidiaries or materially interfere with the ordinary conduct of the business of the Company and its Subsidiaries; (g) bankers' liens arising by operation of law; and (h) inchoate Liens arising under ERISA to secure contingent liabilities of the Company and its Subsidiaries.

"Person" means an individual, partnership, corporation (including a business trust), limited liability company, joint stock company, trust, unincorporated association, joint venture or other entity, or a foreign or domestic state or political subdivision thereof or any agency of such state or subdivision.

"Plan" means any employee pension benefit plan (as defined in Section 3(2) of ERISA), subject to Title IV of ERISA or Section 412 of the Code, other than a Multiemployer Plan, with respect to which the Company or an ERISA Affiliate contributes or has an obligation or liability to contribute, including any such plan that may have been

terminated.

"Pledged Collateral" means, collectively, the "Pledged Collateral" as defined in the Company Pledge Agreement and the Subsidiary Pledge Agreements.

"Prescribed Forms" shall mean such duly executed form(s) or statement(s), and in such number of copies, which may, from time to time, be prescribed by law and which, pursuant to applicable provisions of the Code or an income tax treaty between the United States and the country of residence of the Bank providing the form(s) or statement(s), permit each of the Company and the Administrative Agent to make payments hereunder for the account of such Bank free of deduction or withholding of income and other taxes, or with deduction or withholding of income or other taxes at a reduced rate under an applicable tax treaty.

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"Prime Rate" has the meaning set forth in the definition of Alternate Base Rate.

"Property" (whether or not capitalized) means any interest in any kind of property or asset, whether real, personal or mixed, or tangible or intangible.

"Release" means any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping or disposing into the environment (including the abandonment or discarding of barrels, containers and other closed receptacles).

"Reportable Event" means an event described in Section 4043(b) of ERISA with respect to a Plan as to which the 30-day notice requirement has not been waived by the PBGC.

"Requirements of Environmental Laws" means, as to any Person, the requirements of any applicable Environmental Law relating to or affecting such Person or the condition or operation of such Person's business or its properties, both real and personal.

"Required Subordinated Debt Holders" means the holders of Subordinated Debt, the 2001 Subordinated Debt Principal for which totals at least ninety percent (90%) of all 2001 Subordinated Debt Principal.

"Reserve Percentage" means, for any Interest Period and for any Bank, the reserve percentage applicable during such Interest Period under regulations issued from time to time by the Board (or if more than one such percentage is so applicable, the daily average for such percentages for those days in such Interest Period during which any such percentage shall be so applicable) for determining the actual reserve requirement (including any marginal, supplemental or emergency reserves) for such Bank in respect of liabilities or assets consisting of or including Eurocurrency Liabilities.

"Responsible Officer" means, with respect to the Company, the chairman of the board of directors, president, any vice president, chief executive officer, chief operating officer, treasurer or chief financial officer of the Company.

"Restricted Subordinated Debt Payments" means any payment or prepayment of principal of, premium or penalty, if any, or interest on, or redemption, purchase, retirement, defeasance (including in-substance

or legal defeasance), sinking fund or similar payment (i) with respect to, any Subordinated Debt comprised in part of 2001 Subordinated Debt Principal which has not been restructured as referenced in Section 5.1(1); (ii) in excess of \$4,700,000 with respect to Subordinated Debt which has been restructured as referenced in Section 5.1(1), which prior to such restructuring had principal payments due in the calendar quarters ending December 31, 2000 or March 31, 2001; (iii) in excess of \$4,700,000 with respect to Subordinated Debt which has been restructured as referenced in Section 5.1(1), which prior to such restructuring had principal payments due during the last three calendar quarters of 2001; (iv) any such payment, other than regularly scheduled payments of interest on any Subordinated Debt, on which the first regularly scheduled payment of principal is not due until after the

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calendar year 2001; and (v) with respect to any Subordinated Debt when there is in existence a Default or an Event of Default.

"Sale and Leaseback Transaction" means any sale or other transfer of Property by any Person with the intent to lease such Property as lessee.

"Solvent" means, with respect to any Person, that as of the date of determination both (a) (i) the then fair saleable value of the property of such Person is (y) greater than the total amount of liabilities (including contingent liabilities) of such Person and (z) not less than the amount that will be required to pay the probable liabilities on such Person's then existing debts as they become absolute and matured considering all financing alternatives and potential asset sales reasonably available to such Person; (ii) such Person's capital is not unreasonably small in relation to its business or any contemplated or undertaken transaction; and (iii) such Person does not intend to incur, or believe (nor should it reasonably believe) that it will incur, debts beyond its ability to pay such debts as they become due; and (b) such Person is "solvent" within the meaning given that term and similar terms under applicable laws relating to fraudulent transfers and conveyances. For purposes of this definition, the amount of any contingent liability at any time shall be computed as the amount that, in light of all of the facts and circumstances existing at such time, represents the amount that can reasonably be expected to become an actual or matured liability.

"Subsidiary" means and includes, with respect to any Person, (a) any corporation more than 50% of whose stock of any class or classes having by the terms thereof ordinary voting power to elect a majority of the directors of such corporation (irrespective of whether or not at the time stock of any class or classes of such corporation shall have or might have voting power by reason of the happening of any contingency) is at the time owned by such Person, directly or indirectly and (b) any partnership, association, joint venture or other entity in which such Person, directly or indirectly, has greater than 50% of the equity interest. Unless otherwise provided or the context otherwise requires, the term "Subsidiary" or "Subsidiaries" shall mean a Subsidiary or Subsidiaries of the Company.

"Subsidiary Pledge Agreement" means each Subsidiary Pledge Agreement executed and delivered by an existing Guarantor on the Effective Date or executed and delivered by any additional Guarantor from time to time thereafter in accordance with Section 7.8, in each case substantially in the form of Exhibit 1.1(h) annexed hereto, as such Subsidiary Pledge Agreement may be amended, supplemented or

otherwise modified from time to time, and "Subsidiary Pledge Agreements" means all such Subsidiary Security Agreements.

"Subsidiary Security Agreement" means each Subsidiary Security Agreement executed and delivered by an existing Guarantor on the Effective Date or executed and delivered by any additional Guarantor from time to time thereafter in accordance with Section 7.8, in each case substantially in the form of Exhibit 1.1(i) annexed hereto, as such Subsidiary Security Agreement may be amended, supplemented or otherwise

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modified from time to time, and "Subsidiary Security Agreements" means all such Subsidiary Security Agreements.

"Subordinated Debt" means any Indebtedness of the Company or any subsidiary of the Company which is expressly and validly subordinated to the obligations of the Company hereunder and under the Notes and other Loan Documents pursuant to terms and conditions substantially in the form of the attached Exhibit 1.1(j).

"Syndication Agent" has the meaning specified in the introduction to this Agreement.

"Total Commitment" means the sum of the Commitments for each Bank totaling a maximum of \$270,000,000.00 for all Banks at all times prior to December 31, 2001, (ii) \$250,000,000.00 for all Banks from December 31, 2001 until June 29, 2002, and (iii) \$240,000,000.00 for all Banks at all times on and after June 30, 2002.

"Total Funded Debt" means Funded Senior Debt plus Subordinated Debt.

"2001 Subordinated Debt Principal" means the aggregate amount of all regularly scheduled principal payments due and payable on Subordinated Debt from October 1, 2000 to December 31, 2001.

"UCC" means the Uniform Commercial Code (or any similar or equivalent legislation) as in effect in any applicable jurisdiction.

"Unutilized Commitment" means the Total Commitment less Letter of Credit Obligations less the outstanding Advances under the Loan, as same may be reduced pursuant to Section 2.16.

SECTION 1.2 Types of Advances. Advances hereunder are distinguished by "Type." The Type of an Advance refers to the determination whether such Advance is a Eurodollar Rate Advance or an Alternate Base Rate Advance.

SECTION 1.3 Accounting Terms. All accounting terms not defined herein shall be construed in accordance with GAAP, as applicable, and all calculations required to be made hereunder and all financial information required to be provided hereunder shall be done or prepared in accordance with GAAP.

SECTION 1.4 Schedules. Schedules hereto may be updated by the Company from time to time to reflect transactions and other matters not prohibited by the Loan Documents.

SECTION 2.1 The Loans. Subject to the terms and conditions hereof, each Bank severally agrees at any time and from time to time on and after the Effective Date and prior to the Maturity Date, to make and maintain a loan or loans (together with any Advances under a Letter of Credit described in Article III, a "Loan" and collectively, the "Loans") to the Company

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not to exceed at any time outstanding the maximum amount of its Commitment, which Loans (i) shall, at the option of the Company, be made and maintained pursuant to one or more Advances comprised of Alternate Base Rate Advances or Eurodollar Rate Advances; provided that, except as otherwise specifically provided herein, all Advances made simultaneously under the Loan shall be of the same Type, (ii) in the case of Eurodollar Rate Advances, shall be made in the minimum amount of \$1,000,000.00 and integral multiples of \$100,000.00 and, in the case of Alternate Base Rate Advances, in the minimum amount of \$100,000.00 and integral multiples thereof, or, in either case, in the remaining balance of the lesser of (w) the Total Commitment, and (x) the Borrowing Base, (iii) may be repaid and, so long as no Default or Event of Default exists hereunder, reborrowed, at the option of the Company in accordance with the provisions hereof, and (iv) shall not, in the aggregate at any time outstanding and together with all Letter of Credit Obligations, exceed the lesser of (y) the Total Commitment, and (z) the Borrowing Base.

SECTION 2.2 The Notes. The Loans shall be evidenced by a Note in favor of each Bank (individually a "Note" and collectively, the "Notes"), substantially in the form of Exhibit 2.2(a).

SECTION 2.3 Notice of Advance.

(a) Whenever the Company desires an Advance, it shall give written notice thereof (a "Notice of Advance") (or telephonic notice promptly confirmed in writing) to the Administrative Agent (i) in the case of an Alternate Base Rate Advance, not later than 11:00 a.m. (Houston, Texas time) on the date of such Advance and (ii) in the case of a Eurodollar Rate Advance, not later than noon (Houston, Texas time) three Business Days prior to the date of such Advance. Each Notice of Advance shall be irrevocable and shall be in the form of Exhibit 2.3 hereto, specifying (i) the aggregate principal amount of the Advance to be made, (ii) the date of such Advance (which shall be a Business Day), (iii) whether it is to be an Alternate Base Rate Advance or a Eurodollar Rate Advance and (iv) if the proposed Advance is to be a Eurodollar Rate Advance, the initial Interest Period to be applicable thereto.

(b) The Administrative Agent shall promptly give the Banks written notice or telephonic notice (promptly confirmed in writing) of each proposed Advance, of each Bank's proportionate share thereof and of the other matters covered by each Notice of Advance.

SECTION 2.4 Disbursement of Funds for Loans.

(a) No later than 1:00 p.m. (Houston, Texas time) on any Advance Date for Loans, each Bank shall make available its pro rata portion of the amount of such Advance in U.S. dollars and in immediately available funds at the Payment Office. At such time, the Administrative Agent shall credit the amounts so received to the general deposit account of the Company maintained with the Administrative Agent in immediately available funds or as otherwise directed by the Company.

(b) Unless the Administrative Agent shall have been notified

by any Bank prior to disbursement of the Advance by the Administrative Agent that such Bank does not intend to make available to the Administrative Agent such Bank's portion of the

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Advance to be made on such date, the Administrative Agent may assume that such Bank has made such amount available to the Administrative Agent on such Advance Date and the Administrative Agent may, in reliance upon such assumption, make available to the Company a corresponding amount. If such corresponding amount is not in fact made available to the Administrative Agent by such Bank and the Administrative Agent has made available same to the Company, the Administrative Agent shall be entitled to recover such corresponding amount on demand from such Bank. If such Bank does not pay such corresponding amount forthwith upon the Administrative Agent's demand therefor, the Administrative Agent shall promptly notify the Company, and the Company shall pay such corresponding amount to the Administrative Agent within two (2) Business Days after demand therefor. The Administrative Agent shall also be entitled to recover from such Bank or the Company, as the case may be, interest on such corresponding amount from the date such corresponding amount was made available by the Administrative Agent to the Company to the date such corresponding amount is recovered by the Administrative Agent, at a rate per annum equal to (i) as to the Company, the Alternate Base Rate or the Eurodollar Rate plus the applicable Margin, as appropriate or (ii) as to any Bank, the Federal Funds Effective Rate on the date of such Advance for a period of three (3) days and thereafter at the Alternate Base Rate or the Eurodollar Rate plus the applicable Margin, as appropriate. Nothing herein shall be deemed to relieve any Bank from its obligation to fulfill its Commitments hereunder or to prejudice any rights which the Company may have against any Bank as a result of any default by such Bank hereunder.

SECTION 2.5 Conversions and Continuances. The Company shall have the option to convert or continue on any Business Day all or a portion of the outstanding principal amount of one Type of Advance for any Loan into another Type of Advance; provided, no Advances may be converted into or continued as Eurodollar Rate Advances if a Default or Event of Default is in existence on the date of the conversion or continuation. Any continuation of an Advance as the same Type of Advance in the same amount shall be effected by the Company giving notice to the Administrative Agent, in writing, or by telephone promptly confirmed in writing, of its intention to continue such Advance as an Advance of the same Type. Each such conversion shall be effected by the Company giving the Administrative Agent written notice (each a "Notice of Conversion"), substantially in the form of Exhibit 2.5 hereto, prior to noon (Houston, Texas time) at least (a) three (3) Business Days prior to the date of such conversion in the case of conversion into or continuance as Eurodollar Rate Advances and (b) prior to 11:00 a.m. (Houston, Texas time) one Business Day prior to the date of conversion in the case of a conversion into Alternate Base Rate Advances, specifying each Advance (or portions thereof) to be so converted and, if to be converted into or continued as Eurodollar Rate Advances, the Interest Period to be initially applicable thereto. The Administrative Agent shall thereafter promptly notify each Bank of such Notice of Conversion.

SECTION 2.6 Voluntary Prepayments. The Company shall have the right to voluntarily prepay any Loan in whole or in part at any time on the following terms and conditions: (a) no Eurodollar Rate Advance may be prepaid prior to the last day of its Interest Period unless, simultaneously therewith, the Company pays to the Administrative Agent for the benefit of the Banks, all sums necessary to compensate the Banks for all costs and expenses resulting from such prepayment, as reasonably determined by the Banks, including but not limited to

those costs

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described in Section 2.10(f), Section 2.14 and Section 2.15 hereof; and (b) each prepayment pursuant to this section shall be applied first, to the payment of accrued and unpaid interest, and then, to the outstanding principal of such Advances.

SECTION 2.7 Mandatory Repayments. The Loans shall be repaid and/or the Commitments shall be permanently reduced, in the amounts and under the circumstances set forth below, all such repayments and/or reductions to be applied as set forth below:

(a) Net Asset Sale Proceeds. No later than (i) the first Business Day following the date of receipt by the Company or any of its Subsidiaries of any Net Asset Sale Proceeds in respect of any Asset Sale (other than from a Sale and Leaseback Transaction permitted by Section 8.3(n)) in excess of \$5,000,000 for any single transaction or related series of transactions the Company shall repay the Loans and the Revolving Loan Commitments shall be permanently reduced in an aggregate amount equal to such Net Asset Sale Proceeds and (ii) the first Business Day following the 360th day after receipt by the Company or any Subsidiary of any Net Asset Sale Proceeds in respect of any Asset Sale of \$5,000,000 or less for any single transaction or related series of transactions the Company shall repay the Loans and the Revolving Loan Commitments shall be permanently reduced in an aggregate amount equal to the amount of such Net Asset Sale Proceeds that were not reinvested in the business of the Company or any of its Subsidiaries on or before such date;

(b) Loans and Letter of Credit Obligations in Excess of Total Commitment. The Company shall repay Loans on any day on which the aggregate outstanding principal amount of the Loans together with the outstanding Letter of Credit Obligations exceeds the lesser of (i) the Total Commitment, and (ii) the Borrowing Base, in the amount of such excess;

(c) Repayment Upon Maturity. The aggregate amount under the Notes (and all accrued, unpaid interest) shall be due and payable, and the Commitments shall terminate on the Maturity Date; and

(d) Sale and Leaseback Transaction Proceeds. The Company shall apply all net proceeds generated from the Sale and Leaseback Transaction permitted by Section 8.3(n) to permanently repay the Loans and irrevocably reduce the Commitments.

SECTION 2.8 Method and Place of Payment. Except as otherwise specifically provided herein, all payments under this Agreement due from the Company shall be made to the Administrative Agent for the benefit of the Banks not later than 11:00 a.m. (Houston, Texas time) on the date when due and shall be made in lawful money of the United States in immediately available funds at the Payment Office.

SECTION 2.9 Pro Rata Advances. All Advances under this Agreement shall be incurred from the Banks pro rata, on the basis of their respective Commitments. It is understood that no Bank shall be responsible for any default by any other Bank in its obligation to make Loans hereunder and that each Bank shall be obligated to make the Loans provided to be made by it hereunder, regardless of the failure of any other Bank to fulfill its commitments hereunder.

SECTION 2.10 Interest.

(a) Subject to Section 12.8, the Company agrees to pay interest on the total outstanding principal balance of all Alternate Base Rate Advances from the date of each respective Advance to maturity (whether by acceleration or otherwise) at a rate per annum which shall at all times be equal to the lesser of (i) the Highest Lawful Rate and (ii) the Alternate Base Rate in effect from time to time plus the Margin for Alternate Base Rate Advances, which Margin shall be adjusted on the first day of each Margin Period. If the Alternate Base Rate is based on the Prime Rate, interest shall be computed on the basis of the actual number of days elapsed over a year of 365 or 366 days, as the case may be. If the Alternate Base Rate is based on the Federal Funds Effective Rate, interest shall be computed on the basis of the actual number of days elapsed over a year of 360 days.

(b) Subject to Section 12.8, the Company agrees to pay interest on the total outstanding principal balance of all Eurodollar Rate Advances from the date of each respective Advance to maturity (whether by acceleration or otherwise) at a rate per annum (computed on the basis of the actual number of days elapsed over a year of 360 days) which shall, during each Interest Period applicable thereto, be equal to the lesser of (i) the Highest Lawful Rate and (ii) the applicable Eurodollar Rate for such Interest Period plus the Margin for Eurodollar Rate Advances. The applicable Eurodollar Rate shall be fixed for each Interest Period and shall not change during said Interest Period, but the applicable Margin, which is added to said Eurodollar Rate to determine the total interest payable to the Banks, shall be adjusted, if applicable under the definition of "Margin," effective on the first day of each Margin Period, whether or not said adjustment occurs at a time other than the beginning of an Interest Period.

(c) Subject to Section 12.8, overdue principal and, to the extent permitted by law, overdue interest in respect of any Advance and all other overdue amounts owing hereunder shall bear interest for each day that such amounts are overdue at a rate per annum equal to the Default Rate.

(d) Interest on each Advance shall accrue from and including the date of such Advance to but excluding the date of any repayment thereof and shall be payable (i) in respect of Eurodollar Rate Advances (A) on the last day of the Interest Period (as defined below) applicable thereto and, in the case of any Interest Period in excess of three (3) months, the date that is three months after the commencement of such Interest Period, and (B) on the date of any voluntary or mandatory repayment or any conversion or continuance, (ii) in respect of Alternate Base Rate Advances (A) on each Designated Payment Date, and (B) on the date of any voluntary or mandatory repayment of such Advances on the principal amount repaid and (iii) in respect of each Advance, at maturity (whether by acceleration or otherwise) and, after maturity, on demand.

(e) The Administrative Agent, upon determining the Eurodollar Rate for any Interest Period shall notify the Company thereof. Each such determination shall, absent manifest error, be final and conclusive and binding on all parties hereto. In addition, prior to the due date for the payment of interest on any Advances set forth in the

immediately preceding paragraph, the Administrative Agent shall notify the Company of the amount of interest due by the Company on all outstanding Advances on the applicable due date, but any failure of the Administrative Agent to so notify the Company shall not reduce the Company's liability for the amount owed.

(f) The Company shall pay to the Administrative Agent for the account of each Bank, so long as such Bank shall be required under regulations of the Board to maintain reserves with respect to liabilities or assets consisting of or including Eurocurrency Liabilities, additional interest on the unpaid principal amount of such Bank's share of each Eurodollar Rate Advance, from the date of such Advance until such principal amount is paid in full, at an interest rate per annum equal at all times during the Interest Period for such Advance to the lesser of (i) the Highest Lawful Rate and (ii) the remainder obtained by subtracting (A) the Eurodollar Rate for such Interest Period from (B) the rate obtained by dividing such Eurodollar Rate referred to in clause (A) above by that percentage equal to 100% minus the Reserve Percentage of such Bank for such Interest Period. Such additional interest shall be determined by such Bank as incurred and shall be payable upon demand therefor by the Bank to the Company. Each determination by such Bank of additional interest due under this Section shall be conclusive and binding for all purposes in the absence of manifest error.

SECTION 2.11 Interest Periods.

(a) At the time the Company gives any Notice of Advance or Notice of Conversion or provides notice of its intent to continue a loan as the same Type in respect of the making of, or conversion into, a Eurodollar Rate Advance, the Company shall have the right to elect, by giving the Administrative Agent on the dates and at the times specified in Section 2.3 or Section 2.5, as the case may be, notice of the interest period (each an "Interest Period") applicable to such Eurodollar Rate Advance, which Interest Period shall be either a one, two, three or six month period; provided that:

(i) the initial Interest Period for any Eurodollar Rate Advance shall commence on the date of such Eurodollar Rate Advance (including the date of any conversion thereto or continuance thereof pursuant to Section 2.5); each Interest Period occurring thereafter in respect of such Eurodollar Rate Advance shall commence on the expiration date of the immediately preceding Interest Period;

(ii) if any Interest Period relating to a Eurodollar Rate Advance begins on a day for which there is no numerically corresponding day in the calendar month at the end of such Interest Period, such Interest Period shall end on the last Business Day of such calendar month;

(iii) if any Interest Period would otherwise expire on a day which is not a Business Day, such Interest Period shall expire on the next succeeding Business Day; provided, that if there are no more Business Days in that month, the Interest Period shall expire on the preceding Business Day;

(iv) no Interest Period for Advances shall extend beyond the applicable Maturity Date; and

(v) the Company shall be entitled to have a maximum of ten (10) separate Eurodollar Rate Advances hereunder for all Loans outstanding at any one time.

(b) If, upon the expiration of any Interest Period applicable to a Eurodollar Rate Advance, the Company has failed to elect a new Interest Period to be applicable to such Advance as provided above, the Company shall be deemed to have elected to convert such Advance into an Alternate Base Rate Advance effective as of the expiration date of such current Interest Period.

SECTION 2.12 Interest Rate Not Ascertainable. In the event that the Administrative Agent shall determine (which determination shall, absent manifest error, be final, conclusive and binding upon all parties) that on any date for determining the Eurodollar Rate for any Interest Period, by reason of any changes arising after the date of this Agreement affecting the Eurodollar interbank market or the Administrative Agent's position in such market, adequate and fair means do not exist for ascertaining the applicable interest rate on the basis provided for in the definition of Eurodollar Rate, then, and in any such event, the Administrative Agent shall forthwith give notice to the Company and to the Banks of such determination. Until the circumstances giving rise to the suspension described herein no longer exist, the obligations of the Banks to make Eurodollar Rate Advances shall be suspended.

SECTION 2.13 Change in Legality.

(a) Notwithstanding anything to the contrary herein contained, if any change in any law or regulation or in the interpretation thereof by any governmental authority charged with the administration or interpretation thereof shall make it unlawful for any Bank or its Eurodollar Lending Office to make or maintain any Eurodollar Rate Advance or to give effect to its obligations as contemplated hereby, then, by prompt written notice to the Company, such Bank may:

(i) declare that Eurodollar Rate Advances will not thereafter be made by such Bank hereunder, whereupon the Company shall be prohibited from requesting Eurodollar Rate Advances from such Bank hereunder unless such declaration is subsequently withdrawn, provided, such request for a Eurodollar Rate Advance shall, if the Company so indicates, be automatically converted (as to such Bank) into a request for an Alternate Base Rate Advance and the affected Bank or Banks shall respond thereto as provided herein; and

(ii) require that all outstanding Eurodollar Rate Advances made by such Bank be converted to Alternate Base Rate Advances, in which event (A) all such Eurodollar Rate Advances shall be automatically converted to Alternate Base Rate Advances as of the effective date of such notice as provided in paragraph (b) below if required by applicable law or regulation, or if not so required, at the end of the current Interest Period and (B) all payments and

prepayments of principal which would otherwise have been applied to repay the converted Eurodollar Rate Advances shall instead be applied to repay the Alternate Base Rate Advances resulting from the conversion of such Eurodollar Rate Advances.

(b) For purposes of this Section, a notice to the Company by the Administrative Agent pursuant to paragraph (a) above shall be effective on the date of receipt thereof by the Company.

SECTION 2.14 Increased Costs, Taxes or Capital Adequacy Requirements.

(a) If any change in the application or effectiveness of any applicable law or regulation or compliance by any Bank with any applicable guideline or request issued after the date hereof from any central bank or governmental authority having jurisdiction over such Bank (whether or not having the force of law) (i) shall change the basis of taxation of payments to such Bank of the principal or interest on any Eurodollar Rate Advance made by such Bank or any other fees or amounts payable hereunder with respect to Eurodollar Rate Advances (other than taxes imposed on the overall net income of such Bank or its Applicable Lending Office or franchise taxes imposed upon it by the jurisdiction in which such Bank or its Applicable Lending Office has an office), (ii) shall impose, modify or deem applicable any reserve, special deposit or similar requirement with respect to Eurodollar Rate Advances against assets of, deposits with or for the account of, or credit extended by, such Bank (without duplication of any amounts paid pursuant to Section 2.10(f) or (iii) shall impose on such Bank any other condition affecting this Agreement with respect to Eurodollar Rate Advances or any Eurodollar Rate Advance made by such Bank, and the result of any of the foregoing shall be to increase the cost to such Bank of maintaining its Commitment or of making or maintaining any Eurodollar Rate Advance or to reduce the amount of any sum received or receivable by such Bank hereunder (whether of principal, interest or otherwise) in respect thereof by an amount deemed in good faith by such Bank to be material, then the Company shall pay to such Bank such additional amount as will compensate it for such increase or reduction within ten (10) days after notice thereof pursuant to Section 2.14(c).

(b) If any Bank shall have determined in good faith that any change in any law, rule, regulation or guideline regarding capital adequacy, or any change therein or any change in the interpretation or administration thereof or compliance with any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or comparable agency has or would have the effect of reducing the rate of return on the capital of such Bank as a consequence of, or with reference to, such Bank's obligations hereunder to a level below that which it could have achieved but for such adoption, change or compliance by an amount deemed by such Bank to be material, then, from time to time, the Company shall pay to the Administrative Agent for the benefit of such Bank such additional amount as will reasonably compensate it for such reduction within ten (10) days after notice thereof pursuant to Section 2.14(c).

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(c) Each Bank will notify the Company through the Administrative Agent of any event occurring after the date of this Agreement which will entitle it to compensation pursuant to this Section, as promptly as practicable after it becomes aware thereof and

determines to request compensation and in any case, within 120 days after becoming aware thereof. A certificate setting forth in reasonable detail the amount necessary to compensate the Bank in question as specified in paragraph (a) or (b) above, as the case may be, and the calculation of such amount shall be delivered to the Company and shall be conclusive absent manifest error. The failure on the part of any Bank to demand increased compensation with respect to any Interest Period shall not constitute a waiver of the right to demand compensation thereafter within the 120 day time limit set forth above. Each Bank agrees, to the extent it may lawfully do so without incurring additional costs, to use its best efforts to minimize costs arising under this section by designating another lending office for the Loans affected, provided no Bank shall be required to do so.

(d) In the event any Bank gives a notice to the Company pursuant to Section 2.13 or Section 2.14 that it cannot fund certain Loans or that such funding will be at an increased cost, or is unable to deliver the Prescribed Forms as required by Section 2.17 below, the Company may give notice in response, with copies to the Administrative Agent, that it wishes to seek one or more banks to replace such Bank in accordance with the provisions set forth in Section 12.10. Each Bank giving such a notice agrees that, at the request of the Company, it will assign all of its interests hereunder and under the Notes and the Commitment to a designated, Eligible Assignee for the full amount then owing to it, all in accordance with Section 12.10. Thereafter, said assignee shall have all of the rights hereunder and obligations of the Assigning Bank (except as otherwise expressly set forth herein) and such Bank shall have no further obligations to the Company hereunder.

(e) Any notice given pursuant to this Section 2.14 shall be deemed to contain a representation by the Bank issuing such notice that the increased costs and charges are common to substantially all of the loan customers of such Bank and are not unique to the Company.

SECTION 2.15 Eurodollar Advance Prepayment and Default Penalties. Subject to Section 12.8, the Company shall indemnify each Bank against any loss or expense (excluding loss of anticipated profits) which it may sustain or incur as a consequence of (a) an Advance of, or a conversion from or into, Eurodollar Rate Advances that does not occur on the date specified therefor in a Notice of Advance or Notice of Conversion or (b) any payment, prepayment or conversion of a Eurodollar Rate Advance required by any other provision of this Agreement or otherwise made on a date other than the last day of the applicable Interest Period. Such loss or expense shall include an amount equal to the excess determined by each Bank of (i) its cost of obtaining the funds for the Advance being paid, prepaid or converted or not borrowed (based on the Eurodollar Rate) for the period from the date of such payment, prepayment or conversion or failure to borrow to the last day of the Interest Period for such Advance (or, in the case of a failure to borrow, the Interest Period for the Advance which would have commenced on the date of such failure to borrow) over (ii) the amount of interest (as determined by each Bank) that would be realized in reemploying the funds so paid, prepaid or converted or not borrowed for

such period or Interest Period, as the case may be. The Administrative Agent, on behalf of the Banks, will notify the Company of any loss or expense which will entitle the Banks to compensation pursuant to this Section, as promptly as possible after it becomes aware thereof, but failure to so notify shall not affect the Company's liability therefor. A certificate of any Bank setting forth any amount which it is entitled to receive pursuant to this Section shall be delivered to the Company and shall be conclusive absent manifest error if such determination is made on a reasonable basis. The Company shall pay to the

Administrative Agent for the account of the Banks the amount shown as due on any certificate within ten (10) days after its receipt of the same. Without prejudice to the survival of any other obligations of the Company hereunder, the obligations of the Company under this Section shall survive the termination of this Agreement and, with respect to the assigning Bank, the assignment of any of the Notes, in each case for one hundred and twenty (120) days.

SECTION 2.16 Voluntary Reduction of Commitment. Upon at least three (3) Business Days' prior written notice, the Company shall have the right, without premium or penalty, to reduce or terminate the Commitments, in whole or in part, in the amount of \$5,000,000.00 or integral multiples thereof.

SECTION 2.17 Tax Forms. With respect to any Bank which is organized under the laws of a jurisdiction outside the United States, on the date of the initial Advance hereunder or on the date it becomes a party hereto, and from time to time thereafter if requested by the Company or the Administrative Agent, each such Bank shall provide the Administrative Agent and the Company with the Prescribed Forms. Unless the Company and the Administrative Agent have received such Prescribed Forms, the Administrative Agent and the Company if required by applicable law or regulation, may withhold taxes from payments under the Loan Documents at the applicable rate in the case of payments to or for any Bank organized under the laws of a jurisdiction outside the United States; provided the Company shall, unless otherwise directed in writing by the Administrative Agent or unless otherwise required by law, make all payments in full to the Administrative Agent without deducting any withholding or similar taxes. If the Company is required by law to deduct or withhold any taxes from any Payment, the Company shall: (a) make such deduction or withholding; (b) pay the amount so deducted or withheld to the appropriate taxing authority not later than the date when due (irrespective of the rate of such deduction or withholding); (c) deliver to the relevant Administrative Agent or Bank, as the case may be, promptly and in any event within 30 days after the date on which such taxes become due, original tax receipts and other evidence satisfactory to such Administrative Agent or Bank, as the case may be, of the payment when due of the full amount of such taxes; and (d) pay to the respective Administrative Agent or Bank, forthwith upon any request by such Administrative Agent or Bank, therefor from time to time, such additional amounts as may be necessary so that such Administrative Agent or Bank, as the case may be, receives, free and clear of all taxes, the full amount of such Payment stated to be due under this Agreement, the Notes or the other Loan Documents as if no such deduction or withholding had been made. The Company hereby indemnifies each Agent and each Bank, and holds each of them harmless for, any taxes and any loss, cost, damage, penalty or expense whatsoever arising from any failure of the Company to make, or delay in making, any deduction or withholding of taxes, or its failure to pay when due the amount so deducted or withheld to the appropriate taxation authority or its failure otherwise to comply with the terms and conditions of this Section.

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ARTICLE III LETTERS OF CREDIT

SECTION 3.1 Letters of Credit.

(a) Subject to and upon the terms and conditions herein set forth, the Issuing Bank agrees that it will, at any time and from time to time on or after the Effective Date and prior to the Maturity Date, following its receipt of a Letter of Credit Request and Application for Letter of Credit, issue for the account of the Company and in support of the obligations of the Company or any of its Subsidiaries, one or more standby and/or commercial letters of credit (the "Letters of

Credit") payable on a sight basis, up to a maximum amount outstanding at any one time for all Letters of Credit of \$15,000,000.00; provided that the Issuing Bank shall not issue any Letter of Credit if at the time of such issuance: (i) Letter of Credit Obligations shall be greater than an amount which, when added to the sum of all Advances then outstanding plus Letter of Credit Obligations, would exceed the lesser of (x) the Total Commitment, and (y) the Borrowing Base; or (ii) the expiry date or, in the case of any Letter of Credit containing an expiry date that is extendable at the option of the Issuing Bank, the initial expiry date, of such Letter of Credit is a date that is later than the Maturity Date.

(b) The Issuing Bank shall neither renew or extend nor permit the renewal or extension of any Letter of Credit (which renewal or extension will not be for any period ending after the Maturity Date) if any of the conditions precedent to such renewal set forth in Section 5.2 are not satisfied or waived or, after giving effect to such renewal, the expiry date of such Letter of Credit would be a date that is later than five (5) Business Days prior to the Maturity Date.

SECTION 3.2 Letter of Credit Requests.

(a) Whenever the Company desires that a Letter of Credit be issued for its account or that the existing expiry date shall be extended, it shall give the Issuing Bank (with copies to be sent to the Administrative Agent and each Bank) (i) in the case of a Letter of Credit to be issued, at least five (5) Business Days' prior written request therefor and (ii) in the case of the extension of the existing expiry date of any Letter of Credit, at least five (5) Business Days prior to the date on which the Issuing Bank must notify the beneficiary thereof that the Issuing Bank does not intend to extend such existing expiry date. Each such request shall be executed by the Company and shall be in the form of Exhibit 3.2 attached hereto (each a "Letter of Credit Request") and shall be accompanied by an Application for Letter of Credit therefor, completed to the reasonable satisfaction of the Issuing Bank, and such other certificates, documents and other papers and information as the Issuing Bank or the Administrative Agent may reasonably request. Each Letter of Credit shall be denominated in U.S. dollars, shall expire no later than the date specified in Section 3.1, shall not be in an amount greater than is permitted under clause (i) of Section 3.1(a) and shall be in such form as may be reasonably approved from time to time by the Issuing Bank and the Company.

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(b) The making of each Letter of Credit Request shall be deemed to be a representation and warranty by the Company that such Letter of Credit may be issued in accordance with, and will not violate the requirements of this Agreement. Unless the Issuing Bank has received notice from any Bank before it issues the respective Letter of Credit or extends the existing expiry date of a Letter of Credit that one or more of the conditions specified in Article V are not then satisfied, or that the issuance of such Letter of Credit would violate this Agreement, then the Issuing Bank shall issue the requested Letter of Credit for the account of the Company in accordance with the Issuing Bank's usual and customary practices. Upon its issuance of any Letter of Credit or the extension of the existing expiry date of any Letter of Credit, as the case may be, the Issuing Bank shall promptly notify the Company and the Administrative Agent and the Administrative Agent shall notify each Bank of such issuance or extension, which notices shall be accompanied by a copy of the Letter of Credit actually issued or a copy

of any amendment extending the existing expiry date of any Letter of Credit, as the case may be.

(c) Upon receipt by a proposed Issuing Bank of a Letter of Credit Request pursuant to Section 3.2(a) requesting the issuance of a Letter of Credit, (a) in the event the Administrative Agent is the proposed Issuing Bank, the Administrative Agent shall be the Issuing Bank with respect to such Letter of Credit, notwithstanding the fact that the Letter of Credit Obligations with respect to such Letter of Credit and with respect to all other Letters of Credit issued by the Administrative Agent, when aggregated with the Administrative Agent's outstanding Loans, may exceed the Administrative Agent's Commitments; and (b) in the event any other Bank is the proposed Issuing Bank, such Bank shall promptly notify the Company and the Administrative Agent whether or not, in its sole discretion, it has elected to issue such Letter of Credit, and (1) if such Bank so elects to issue such Letter of Credit, it shall be the Issuing Bank with respect thereto and (2) if such Bank fails to so promptly notify the Company and the Administrative Agent or declines to issue such Letter of Credit, the Company may request the Administrative Agent or another Bank to be the Issuing Bank with respect to such Letter of Credit in accordance with the provisions of this Section 3.2.

SECTION 3.3 Letter of Credit Participations.

(a) All Letters of Credit issued subsequent hereto shall be deemed to have been sold and transferred by the Issuing Bank to each Bank, and each Bank shall be deemed irrevocably and unconditionally to have purchased and received from the Issuing Bank, without recourse or warranty, an undivided interest and participation, (to the extent of such Bank's percentage participation in the Commitment) in each such Letter of Credit (including extensions of the expiry date thereof), each substitute Letter of Credit, each drawing made thereunder and the obligations of the Company under this Agreement and the other Loan Documents with respect thereto, and any security therefor or guaranty pertaining thereto.

(b) In determining whether to pay under any Letter of Credit, the Issuing Bank shall have no obligation relative to the Banks other than to confirm that any documents required to be delivered under such Letter of Credit appear to have been

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delivered and that they appear to comply on their face with the requirements of such Letter of Credit.

(c) In the event that the Issuing Bank makes any payment under any Letter of Credit, the same shall be considered an Alternate Base Rate Advance without further action by any Person. The Issuing Bank shall promptly notify the Administrative Agent, which shall promptly notify each Bank thereof. Each Bank shall immediately pay to the Administrative Agent for the account of the Issuing Bank the amount of such Lender's percentage participation of such Advance. If any Bank shall not have so made its percentage participation available to the Administrative Agent, such Lender agrees to pay interest thereon, for each day from such date until the date such amount is paid at the lesser of (i) the Federal Funds Effective Rate and (ii) the Highest Lawful Rate.

(d) The Issuing Bank shall not be liable for, and the obligations of the Company and the Banks to make payments to the

Administrative Agent for the account of the Issuing Bank with respect to Letters of Credit shall not be subject to, any qualification or exception whatsoever, including any of the following circumstances:

(i) any lack of validity or enforceability of this Agreement or any of the other Loan Documents;

(ii) the existence of any claim, setoff, defense or other right which the Company may have at any time against a beneficiary named in a Letter of Credit, any transferee of any Letter of Credit, the Administrative Agent, any Issuing Bank, any Bank, or any other Person, whether in connection with this Agreement, any Letter of Credit, the transactions contemplated herein or any unrelated transactions (including any underlying transaction between the Company and the beneficiary named in any such Letter of Credit);

(iii) any draft, certificate or any other document presented under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect;

(iv) the surrender or impairment of any security for the performance or observance of any of the terms of any of the Loan Documents; or

(v) the occurrence of any Default or Event of Default.

(e) The Issuing Bank shall not be liable for any error, omission, interruption or delay in transmission, dispatch or delivery of any message or advice, however transmitted, in connection with any Letter of Credit, except for errors or omissions caused by such Issuing Bank's gross negligence or willful misconduct. IT IS THE EXPRESS INTENTION OF THE PARTIES HERETO THAT SUCH ISSUING BANK, ITS OFFICERS, DIRECTORS, EMPLOYEES AND AGENTS (OTHER THAN WITH RESPECT TO ANY CLAIMS BY THE ISSUING BANK AGAINST ANY SUCH OFFICER, DIRECTOR, EMPLOYEE OR AGENT THEREOF) SHALL BE INDEMNIFIED AND HELD HARMLESS FROM, SUBJECT TO THE SAME TYPE OF PROTECTIONS SET FORTH IN SECTION 11.5(B), ANY ACTION TAKEN OR OMITTED BY SUCH PERSON UNDER OR IN CONNECTION WITH ANY LETTER OF CREDIT OR ANY RELATED DRAFT OR DOCUMENT ARISING OUT OF OR RESULTING FROM

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SUCH PERSON'S SOLE OR CONTRIBUTORY NEGLIGENCE, BUT NOT FROM THE GROSS NEGLIGENCE OR WILLFUL MISCONDUCT OF SUCH PERSON AS DETERMINED BY A COURT OF COMPETENT JURISDICTION. The Company agrees that any action taken or omitted by the Issuing Bank under or in connection with any Letter of Credit or the related drafts or documents, if done in accordance with the standards of care specified in the Uniform Customs and Practice for Documentary Credits (1993 Revision), International Chamber of Commerce, Publication No. 500 (and any subsequent revisions thereof approved by a Congress of the International Chamber of Commerce and adhered to by the Issuing Bank) or any other comparable or successor publication or document and, to the extent not inconsistent therewith, the Uniform Commercial Code of the State of New York, shall not result in any liability of the Issuing Bank to the Company.

SECTION 3.4 Increased Costs.

(a) Notwithstanding any other provision herein, but subject to Section 12.8, if any Bank shall have determined in good faith that any

change after the Effective Date of any law, rule, regulation or guideline or the application or effectiveness of any applicable law or regulation or any change after the Effective Date in the interpretation or administration thereof, or compliance by any Bank (or any lending office of such Bank) with any applicable guideline or request from any central bank or governmental authority (whether or not having the force of law) issued after the Effective Date either (i) shall impose, modify or make applicable any reserve, deposit, capital adequacy or similar requirement against Letters of Credit issued, or participated in, by any Bank or (ii) shall impose on any Bank any other conditions affecting this Agreement or any Letter of Credit; and the result of any of the foregoing is to increase the cost to any Bank of issuing, maintaining or participating in any Letter of Credit, or reduce the amount received or receivable by any Bank hereunder with respect to Letters of Credit, by an amount deemed by such Lender to be material, then, from time to time, the Company shall pay to the Administrative Agent for the account of such Lender such additional amount or amounts as will reasonably compensate such Lender for such increased cost or reduction by such Lender.

(b) Each Bank will notify the Company through the Administrative Agent of any event occurring after the date of this Agreement which will entitle such Bank to compensation pursuant to Section 3.4(a) above, as promptly as practicable. A certificate of such Lender (i) stating that the compensation sought to be recovered pursuant to this Section 3.4 is generally being charged to other similarly situated customers and (ii) setting forth in reasonable detail such amount or amounts as shall be necessary to compensate such Bank as specified in Section 3.4(a) above may be delivered to the Company (with a copy to the Administrative Agent) and shall be conclusive absent manifest error. The Company shall pay to the Administrative Agent for the account of such Bank the amount shown as due on any such certificate upon demand; provided that with respect to events occurring prior to any notice given under this Section 3.4(b), such Bank shall only be entitled to recover compensation for such events occurring over a period of 120 days.

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(c) Except as expressly provided in Section 3.4(b), failure on the part of any Bank to demand compensation for any increased costs or reduction in amounts received or receivable or reduction in return on capital with respect to any Letter of Credit shall not constitute a waiver of such Bank's rights to demand compensation for any increased costs or reduction in amounts received or receivables or reduction in return on capital with respect to such Letter of Credit.

SECTION 3.5 Conflict between Applications and Agreement. To the extent that any provision of any application related to any Letter of Credit is inconsistent with the provisions of this Agreement, the provisions of this Agreement shall control.

ARTICLE IV FEES

SECTION 4.1 Fees. Subject to Section 12.8 hereof, the Company agrees to pay the following fees (the "Fees"):

(a) The Company agrees to pay to the Administrative Agent for the ratable account of the Banks a Commitment fee (the "Commitment Fee") for the period from and including the Effective Date to the

Maturity Date computed at a rate per annum determined by the grid set forth below and calculated on the basis of a 360 day-year on the daily average of the Unutilized Commitment of each Bank. The rate for the Commitment Fee shall be adjusted on the first day of each Margin Period. Commitment Fees shall be due and payable in arrears on each Designated Payment Date commencing on the first such date following the Effective Date and on the Maturity Date.

TOTAL FUNDED DEBT/EBITDA -----	COMMITMENT FEE RATE -----
-4.00x	0.500%
-3.50x and <4.00x	0.500%
-3.00x and <3.50x	0.500%
-2.50x and <3.00x	0.500%
<2.50x	0.375%

(b) The Letter of Credit Fees shall be due and payable at the time the Issuing Bank is to issue or renew any Letter of Credit. The Letter of Credit Fee shall be adjusted, if applicable under the definition of "Letter of Credit Fee," on the first day of each Margin Period.

(c) The fees described in those certain fee letters between the Company and BTCo, BofA and Bank One and any of their respective Affiliates.

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(d) A renewal fee payable to the Agent on the Effective Date for the ratable benefit of the Banks equal to 37.5 basis points multiplied by the Total Commitment.

ARTICLE V
CONDITIONS PRECEDENT

SECTION 5.1 Conditions Precedent to Effectiveness. The obligation of each Bank under the Agreement is subject to, in addition to the conditions precedent specified in Section 5.2, the prior or concurrent satisfaction of the following conditions:

(a) Loan and other Related Documents. On or before the Effective Date, the Company shall, and shall cause each Guarantor to, deliver to the Agents the following, all in form and substance satisfactory to the Agents, and, where relevant, executed by all appropriate parties:

(i) this Agreement (which includes the Guaranty) and all other Loan Documents;

(ii) one Note for each Bank;

(iii) a certificate of an officer and of the secretary or an assistant secretary of the Company and of each

Guarantor, as applicable, dated as of the Effective Date certifying, (i) true and complete copies of each of (1) the articles or certificate of incorporation, marked as filed with the applicable governmental authorities and as amended and in effect, of the Company and each of the Guarantors not party to the Existing Credit Agreement, (2) the bylaws, as amended and in effect, of the Company and each of the Guarantors not party to the Existing Credit Agreement and (3) the resolutions adopted by the board of directors of the Company and each of the Guarantors (A) authorizing the execution, delivery and performance by the Company and each of its Subsidiaries of this Agreement and the other Loan Documents to which it is or will be a party and, in the case of the Company, the Advances to be made hereunder, (B) approving the forms of the Loan Documents to which it is or will be a party and which will be delivered at or prior to the date of the initial Advance and (C) authorizing officers of the Company and each of its Subsidiaries to execute and deliver the Loan Documents to which it is or will be a party and any related documents, including, any agreement contemplated by this Agreement, in each case as being in full force and effect without modification or amendment, (ii) that the articles or certificate of incorporation and bylaws of each of the Guarantors party to the Existing Credit Agreement have not been amended, supplemented, or otherwise modified since April 14, 1998, except as attached to such certificate, (iii) the incumbency and specimen signatures of the officers of the Company and each of its Subsidiaries executing any documents on its behalf, and (iv) that since December 31, 1999 there has been no change in the businesses, operations, properties, assets, liabilities, condition (financial or otherwise) or prospects of the Company and its Subsidiaries taken as a whole which could reasonably be expected to have a Material Adverse Effect.

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(b) Security Interests in Personal Property. The Agents shall have received evidence satisfactory to them that the Company and the Guarantors shall have taken or caused to be taken all such actions, executed and delivered or caused to be executed and delivered all such agreements, documents and instruments, and made or caused to be made all such filings and recordings (other than the filing or recording of the items described in clauses (iii) and (iv) below) that may be necessary or, in the opinion of the Agents, desirable in order to create in favor of the Administrative Agent, for the benefit of the Banks, a valid and (upon such filing and recording) perfected First Priority security interest in the entire Collateral. Such actions shall include the following:

(i) Schedules to Collateral Documents. Delivery to the Administrative Agent of accurate and complete schedules to all of the applicable Collateral Documents;

(ii) Stock Certificates and Instruments. Delivery to the Administrative Agent of (a) certificates (which certificates shall be accompanied by irrevocable undated stock powers, duly endorsed in blank and otherwise satisfactory in form and substance to the Agents) representing substantially all capital stock pledged pursuant to the Company Pledge Agreement and the Subsidiary Pledge Agreements and (b)

substantially all promissory notes or other instruments (duly endorsed, where appropriate, in a manner satisfactory to the Agents) evidencing any Collateral;

(iii) Lien Searches and UCC Termination Statements. Delivery to the Administrative Agent of (a) the results of a recent search, by a Person satisfactory to the Agents, of all jurisdictions where filings to perfect are material or a material portion of the Collateral are located, together with copies of all such filings disclosed by such search; and (b) UCC termination statements duly executed by all applicable Persons for filing in all applicable jurisdictions as may be necessary to terminate any effective UCC financing statements or fixture filings disclosed in such search and affecting a material portion of the Collateral (other than any such financing statements or fixture filings in respect of Liens permitted to remain outstanding pursuant to the terms of this Agreement);

(iv) UCC Financing Statements. Delivery to the Administrative Agent of UCC financing statements duly executed by the Company and each applicable Guarantor with respect to all Collateral of the Company or such Guarantor, for filing in all jurisdictions as may be necessary or, in the opinion of the Agents, desirable to perfect the security interests created in such Collateral pursuant to the Collateral Documents; and

(v) Opinions of Local Counsel. Delivery to the Administrative Agent of an opinion of counsel (which counsel shall be reasonably satisfactory to the Agents) under the laws of Texas and such other jurisdictions as Agents may reasonably request, in each case with respect to the creation and perfection of the security interests in favor the Administrative Agent on behalf of the Banks in such Collateral and such other matters governed by the laws of such jurisdiction

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regarding such security interests as the Agents may reasonably request, in each case in form and substance reasonably satisfactory to the Agents.

(c) Necessary Governmental Authorizations and Consents. The Company and its Subsidiaries shall have obtained all authorizations, consents, approvals, licenses or exemptions of or have made all filings or registrations with any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, and shall have obtained all consents of other Persons, in each case that are necessary or advisable in connection with the transactions contemplated hereby and the continued operation of the businesses conducted by the Company and its Subsidiaries in substantially the same manner as conducted prior to the Effective Date, and each shall be in full force and effect, in each case other than those the failure to obtain, which either individually or in the aggregate, would not be reasonably likely to have a Material Adverse Effect;

(d) Opinion of Bracewell & Patterson, L.L.P. The Banks shall have received originally executed copies of one or more favorable written opinions addressed to the Agents and the Banks from Bracewell & Patterson, L.L.P., counsel to the Company and the Guarantors dated as of the Effective Date, substantially in the form of Exhibit 5.1(d)

annexed hereto and such other matters as the Agents acting on behalf of the Banks may reasonably request;

(e) Intentionally deleted;

(f) Payment of Fees. The Company shall have paid to the Administrative Agent, for distribution as appropriate to the Agents and the Banks, the Fees payable on the Effective Date referred to in Section 4.1 and all reasonable fees and expenses (including the reasonable fees and expenses of Andrews & Kurth L.L.P.) agreed upon by such parties to be paid on the Effective Date;

(g) Good Standing and Related Certificates. On or prior to the Effective Date, the Agents shall have received certificates of appropriate public officials as to the existence, good standing and qualification to do business as a foreign corporation, as applicable, of the Company and its Subsidiaries in each jurisdiction in which the ownership of its properties or the conduct of its business requires such qualifications and where the failure to so qualify would have a Material Adverse Effect; and

(h) Financial Statements; Pro Forma Balance Sheet. On or prior to the Effective Date, the Banks shall have received from the Company (i) the audited financial statements of the Company and its Subsidiaries for the twelve (12) months ended December 31, 1999 consisting of a balance sheet and related consolidated statements of income, stockholders' equity and cash flows for such period, (ii) the unaudited financial statements of the Company and its Subsidiaries for the fiscal periods most recently ended prior to the Effective Date (including without limitation monthly income statements for any such period of less than three months), in each case consisting of a balance sheet and the related consolidated statements of income, stockholders' equity and cash flows for such periods, all in reasonably detail and certified by the chief financial officer of the

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Company that they fairly present the financial condition of the Company and its Subsidiaries for such periods and the results of their operations and their cash flows for such periods, subject to changes resulting from audit and normal year-end adjustments, (iii) pro forma consolidated balance sheets of the Company and its Subsidiaries as at January 31, 2001, prepared in accordance with GAAP and reasonably reflecting the transactions contemplated hereby, which pro forma financial statements shall be in form and substance reasonably satisfactory to the Agents, and (iv) projected consolidated financial statements of the Company and its Subsidiaries for the three-year period after the Effective Date consisting of a balance sheet and consolidated statements of income, shareholders' equity and cash flows, which projected financial statements shall be in form and substance reasonably satisfactory to the Agents (such financial statements and information described in clauses (i) through (iv) above are hereinafter collectively referred to as the "Financials");

(i) Solvency Assurances. On the Effective Date, as to the Company and its Subsidiaries, the Agents and the Banks shall have received a Financial Condition Certificate with appropriate attachments, demonstrating that, after giving effect to the consummation of the transactions contemplated hereby, the Company and its Subsidiaries will be Solvent;

(j) Due Diligence. The results of Agents' continuing financial, legal, tax and accounting due diligence investigations with

respect to the Company and its Subsidiaries and the other transactions contemplated hereunder shall be satisfactory in all respects to the Agents and the other Banks, and any supplemental business or financial due diligence that the Agents reasonably determine have become necessary shall not have disclosed information not previously disclosed to the Agents which causes the results of such diligences not to be satisfactory in all respects to the Agents and the other Banks. The Agents and the other Banks shall also have received any information reasonably necessary to conduct their continuing due diligence.

(k) Evidence of Insurance. Agents shall have received a certificate from the Company's insurance broker or other evidence satisfactory to them that all insurance required to be maintained pursuant to Section 7.3 is in full force and effect and that the Administrative Agent on behalf of the Banks has been named as additional insured and/or loss payee thereunder to the extent required under Section 7.3.

(l) Restructuring of Subordinated Debt. Evidence satisfactory to the Administrative Agent and the Banks that the Required Subordinated Debt Holders have restructured the payments of principal and interest owed on Subordinated Debt in a manner satisfactory to the Administrative Agent and the Banks.

The acceptance of the benefits of the initial Credit Event shall constitute a representation and warranty by the Company to the Administrative Agent and each of the Banks that, all of the conditions specified in this Section above shall have been satisfied or waived as of that time.

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SECTION 5.2 Conditions Precedent to Effectiveness and All Subsequent Credit Events. The obligation of the Banks under this Agreement and to make any Advance or issue any Letter of Credit after the Effective Date is subject to the further conditions precedent that on the date of such Credit Event:

(a) The representations and warranties set forth in Article VI and in each of the Collateral Documents shall be true and correct in all material respects as of, and as if such representations and warranties were made on, the date of the proposed Credit Event (unless such representation and warranty expressly relates to an earlier date or is no longer true and correct solely as a result of transactions permitted by the Loan Documents), and the Company shall be deemed to have certified to the Administrative Agent and the Banks that such representations and warranties are true and correct in all material respects by submitting a Notice of Advance or Letter of Credit Request.

(b) The Company shall have complied with the provisions of Section 2.3 hereof.

(c) No Default or Event of Default shall have occurred and be continuing or would result from such Credit Event.

(d) No Material Adverse Effect shall have occurred since the delivery of the most recent financial statements delivered pursuant to Section 7.1.

(e) The Administrative Agent shall have received such other approvals or documents as the Administrative Agent or the Banks may reasonably request.

The acceptance of the benefits of each such Credit Event shall constitute a representation and warranty by the Company to the Administrative Agent and each of the Banks that all of the conditions specified in this Section above exist as of that time.

SECTION 5.3 Delivery of Documents. All of the Notes, certificates, legal opinions and other documents and papers referred to in this Article V, unless otherwise specified, shall be delivered to the Administrative Agent for the account of each of the Banks and, except for the Notes, in sufficient counterparts for each of the Banks and shall be reasonably satisfactory in form and substance to the Banks.

ARTICLE VI REPRESENTATIONS AND WARRANTIES

The Company, as to itself and each of its Subsidiaries, makes, on or as of the occurrence of each Credit Event (except to the extent such representations or warranties relate to an earlier date or are no longer true and correct in all material respects solely as a result of transactions not prohibited by the Loan Documents), the following representations and warranties to the Administrative Agent and the Banks:

SECTION 6.1 Organization and Qualification. Each of the Company and its Subsidiaries (a) is duly formed or organized, validly existing and is in good standing under the laws of the state of its organization, (b) has the power to own its property and to carry on its business as now

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conducted, except where the failure to do so would not have a Material Adverse Effect and (c) is duly qualified to do business and is in good standing in every jurisdiction in which the failure to be so qualified would have a Material Adverse Effect.

SECTION 6.2 Authorization and Validity. Each of the Company and its Subsidiaries has the corporate power and authority to execute, deliver and perform its obligations hereunder and under the other Loan Documents to which it is a party and all such action has been duly authorized by all necessary corporate proceedings on its part. The Loan Documents to which each of the Company and its Subsidiaries is a party have been duly and validly executed and delivered by such Person and constitute a valid and legally binding agreement of such Person enforceable in accordance with the respective terms thereof, except, in each case, as such enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium, fraudulent transfer or other similar laws relating to or affecting the enforcement of creditors' rights generally, and by general principles of equity regardless of whether such enforceability is a proceeding in equity or at law.

SECTION 6.3 Governmental Consents. No authorization, consent, approval, license or exemption of or filing or registration with any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, is necessary for the valid execution, delivery or performance by the Company or any Subsidiary of any Loan Document.

SECTION 6.4 Conflicting or Adverse Agreements or Restrictions. Neither the Company nor any Subsidiary is a party to any contract or agreement or subject to any restriction which would reasonably be expected to have a Material Adverse Effect. Neither the execution nor delivery of the Loan Documents nor compliance with the terms and provisions hereof or thereof will be contrary to the provisions of, or constitute a default under (a) the charter or bylaws of the Company or any of its Subsidiaries or (b) any law, regulation, order, writ, injunction or decree of any court or governmental instrumentality that is

applicable to the Company or any of its Subsidiaries or (c) any material agreement to which the Company or any of its Subsidiaries is a party or by which it is bound or to which it is subject.

SECTION 6.5 Title to Assets. Each of the Company and its Subsidiaries has good title to all material personalty and good and indefeasible title to all material realty as reflected on the Company's and the Subsidiaries' books and records as being owned by them, except for properties disposed of in the ordinary course of business, subject to no Liens, except those permitted hereunder, except where the failure to do so could not reasonably be expected to have a Material Adverse Effect. All of such assets have been and are being maintained by the appropriate Person in good working condition in accordance with industry standards, except where the failure to do so could not reasonably be expected to have a Material Adverse Effect.

SECTION 6.6 Litigation. No proceedings against or affecting the Company or any Subsidiary are pending or, to the knowledge of the Company, threatened before any court or governmental agency or department which involve a reasonable material risk of having a Material Adverse Effect, individually or in the aggregate, except those listed on Schedule 6.6 hereof.

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SECTION 6.7 Financial Statements. Prior to the Effective Date, the Company has furnished to the Banks the Financials. The Financials have been prepared in conformity with GAAP consistently applied (except as otherwise disclosed in such financial statements) throughout the periods involved and present fairly, in all material respects, the consolidated financial condition of the Company and its consolidated Subsidiaries as of the dates thereof and the consolidated results of their operations for the periods then ended. As of the Effective Date, no Material Adverse Effect has occurred since December 31, 1999.

SECTION 6.8 Default. Neither the Company nor any Subsidiary is in default under any material provisions of any instrument evidencing any Indebtedness or of any agreement relating thereto, or in default in any respect under any order, writ, injunction or decree of any court, or in default in any respect under or in violation of any order, injunction or decree of any governmental instrumentality, in each case in such manner as to cause a Material Adverse Effect.

SECTION 6.9 Investment Company Act. Neither the Company nor any Subsidiary is, or is directly or indirectly controlled by or acting on behalf of any Person which is, an "investment company," as such term is defined in the Investment Company Act of 1940, as amended.

SECTION 6.10 Public Utility Holding Company Act. Neither the Company nor any Subsidiary is a non-exempt "holding company," or subject to regulation as such, or, to the knowledge of the Company's or such Subsidiary's officers, an "affiliate" of a "holding company" or a "subsidiary company" of a "holding company," within the meaning of the Public Utility Holding Company Act of 1935, as amended.

SECTION 6.11 ERISA. No accumulated funding deficiency (as defined in Section 412 of the Code or Section 302 of ERISA), that would cause a Material Adverse Effect whether or not waived, exists or is expected to be incurred with respect to any Plan. No liability to the PBGC (other than required premium payments) has been or is expected by the Company to be incurred with respect to any Plan by the Company or any ERISA Affiliate that would cause a Material Adverse Effect. Neither the Company nor any ERISA Affiliate has incurred any withdrawal liability under Title IV of ERISA with respect to any Multi-Employer

Plans.

SECTION 6.12 Tax Returns and Payments. Each of the Company and its Subsidiaries has filed all federal income tax returns and other tax returns, statements and reports (or obtained extensions with respect thereto) which are required to be filed and has paid or deposited or made adequate provision, in accordance with GAAP for the payment of all taxes (including estimated taxes shown on such returns, statements and reports) which are shown to be due pursuant to such returns, except for such taxes as are being contested in good faith and by appropriate proceedings.

SECTION 6.13 Environmental Matters. Each of the Company and its Subsidiaries (a) possesses all environmental, health and safety licenses, permits, authorizations, registrations, approvals and similar rights necessary under law or otherwise for the Company or such Subsidiary to conduct its operations as now being conducted (other than those with respect to which the failure to possess or maintain would not, individually or in the aggregate for the Company and such Subsidiaries, reasonably be expected to have a Material Adverse Effect) and (b) each of such licenses, permits, authorizations, registrations, approvals and similar rights is

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valid and subsisting, in full force and effect and enforceable by the Company or such Subsidiary, and each of the Company and its Subsidiaries is in compliance with all effective terms, conditions or other provisions of such permits, authorizations, registrations, approvals and similar rights except for such failure or noncompliance that, individually or in the aggregate for the Company and such Subsidiaries, would not reasonably be expected to have a Material Adverse Effect. Except as disclosed on Schedule 6.13, on the Effective Date, neither the Company nor any of its Subsidiaries has received any notices of any violation of, noncompliance with, or remedial obligation under, Requirements of Environmental Laws (which violation or non-compliance has not been cured), and there are no writs, injunctions, decrees, orders or judgments outstanding, or lawsuits, claims, proceedings, investigations or inquiries pending or, to the knowledge of the Company or any Subsidiary, threatened, relating to the ownership, use, condition, maintenance or operation of, or conduct of business related to, any property owned, leased or operated by the Company or such Subsidiary or other assets of the Company or such Subsidiary, other than those violations, instances of noncompliance, obligations, writs, injunctions, decrees, orders, judgments, lawsuits, claims, proceedings, investigations or inquiries that, individually or in the aggregate for the Company and such Subsidiaries, would not have a Material Adverse Effect. Except as disclosed on Schedule 6.13, there are no material obligations, undertakings or liabilities arising out of or relating to Environmental Laws to which the Company or any of its Subsidiaries has agreed, assumed or retained, or by which the Company or any of its Subsidiaries is adversely affected, by contract or otherwise and, further, except as disclosed on Schedule 6.13, neither the Company nor any of its Subsidiaries has received a written notice or claim to the effect that the Company or any of its Subsidiaries is or may be liable to any other Person as the result of a Release or threatened Release of a Hazardous Material which, in either case, could reasonably be expected to have a Material Adverse Effect.

SECTION 6.14 Purpose of Loans.

(a) The proceeds of the Loan will be used solely for general corporate purposes, including working capital, to finance acquisitions permitted hereunder, and for Letters of Credit.

(b) None of the proceeds of any Advance will be used directly or indirectly for the purpose of purchasing or carrying any "margin stock" within the meaning of Regulation U or for the purpose of reducing or retiring any indebtedness which was originally incurred to

purchase or carry any margin stock.

SECTION 6.15 Franchises and Other Rights. The Company and each of its Subsidiaries has all franchises, permits, licenses and other authority as are necessary to enable them to carry on their respective businesses as now being conducted and is not in default in respect thereof where the absence of such or any such default could reasonably be expected to have a Material Adverse Effect, individually or in the aggregate.

SECTION 6.16 Subsidiaries and Assets. The Subsidiaries listed on Schedule 6.16 are all of the Subsidiaries of the Company as of the Effective Date and the address given for such Guarantors is the correct mailing address as of the Effective Date. The Company shall update such Schedule 6.16 within thirty (30) days of new Subsidiaries being added.

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SECTION 6.17 Solvency. After giving effect to the initial Advance hereunder and all other Indebtedness of the Company existing at the time of such Advance, the Company and its Subsidiaries, viewed as a consolidated entity, is Solvent.

SECTION 6.18 Payment of Certain Indebtedness. The Company has (a) repaid in full all of the Indebtedness described on Schedule 8.3(b)(ii) and (b) obtained, and where applicable recorded in all appropriate locations, releases of Liens for all real and personal property securing same.

SECTION 6.19 Matters Relating to Collateral.

(a) Creation, Perfection and Priority of Liens. The execution and delivery of the Collateral Documents by the Company and the Guarantors, together with (i) the actions taken on or prior to the date hereof pursuant to Section 5.1(b) and (ii) the delivery to the Administrative Agent of any Pledged Collateral not delivered to the Administrative Agent at the time of execution and delivery of the applicable Collateral Document (all of which Pledged Collateral has been so delivered) are effective to create in favor of the Administrative Agent for the benefit of the Banks, as security for the respective Secured Obligations (as defined in the applicable Collateral Document in respect of any Collateral), a valid and perfected First Priority Lien on all of the Collateral, and all filings and other actions necessary or desirable to perfect and maintain the perfection and First Priority status of such Liens have been duly made or taken and remain in full force and effect, other than the filing of any UCC financing statements delivered to the Administrative Agent for filing (but not yet filed) and the periodic filing of UCC continuation statements in respect of UCC financing statements filed by or on behalf of the Administrative Agent.

(b) Governmental Authorizations. No authorization, approval or other action by, and no notice to or filing with, any governmental authority or regulatory body is required for either (i) pledge or grant by the Company or any Guarantor of the Liens purported to be created in favor of the Administrative Agent pursuant to any of the Collateral Documents or (ii) the exercise by the Administrative Agent of any rights or remedies in respect of any Collateral (whether specifically granted or created pursuant to any of the Collateral Documents or created or provided for by applicable law), except for filings or recordings contemplated by Section 6.19(a) and except as may be required, in connection with the disposition of any Pledged Collateral,

by laws generally affecting the offering and sale of securities.

(c) Absence of Third-Party Filings. Except such as may have been filed in favor of the Administrative Agent as contemplated by Section 6.19(a) or filed in connection with a Permitted Lien, no effective UCC financing statement, fixture filing or other instrument similar in effect covering a substantial portion of the Collateral is on file in any filing or recording office.

(d) Margin Regulations. The pledge of the Pledged Collateral pursuant to the Collateral Documents does not violate Regulation T, U or X of the Board of Governors of the Federal Reserve System.

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(e) Information Regarding Collateral. All information supplied to the Agents by or on behalf of the Company or any Guarantor with respect to any of the Collateral (in each case taken as a whole with respect to any particular Collateral) is accurate and complete in all material respects.

(f) Collateral Value. The fair value of the Collateral is equal to or greater than the amount of the Obligations taking into account all prior Liens on the Collateral securing Indebtedness other than the Obligations.

ARTICLE VII AFFIRMATIVE COVENANTS

The Company, as to itself and each of its Subsidiaries, covenants and agrees that on and after the date hereof and for so long as this Agreement is in effect and until the Obligations have been paid in full and the Commitments have terminated:

SECTION 7.1 Information Covenants. The Company will furnish to each Bank:

(a) As soon as available, and in any event within forty-five (45) days after the close of each fiscal quarter, the consolidated balance sheet of the Company and its Subsidiaries as of the end of such period and the related consolidated statements of income and cash flow for such period, setting forth, in each case, comparative consolidated figures for the related periods in the prior fiscal year, all of which shall be certified by the treasurer, chief financial officer, or chief executive officer of the Company as fairly presenting in all material respects, the financial position of the Company and its Subsidiaries as of the end of such period and the results of their operations for the period then ended in accordance with GAAP, subject to changes resulting from normal year-end audit adjustments. In addition to the foregoing, the Company shall also provide at such time: (i) summary balance sheet and operating income information with respect to each direct Subsidiary fairly representing in all material respects, the financial position of each direct Subsidiary as of the end of such period and the results of their operations for the period then ended, and (ii) a backlog report for the Company and its Subsidiaries for the fiscal quarter then ended.

(b) As soon as available, and in any event within ninety (90) days after the close of each fiscal year of the Company, the audited consolidated balance sheets of the Company as at the end of such fiscal year and the related consolidated and statements of income,

stockholders equity and cash flows for such fiscal year, setting forth. in each case comparative figures for the preceding fiscal year and certified by Arthur Andersen or other independent certified public accountants of recognized national standing, whose report shall be without limitation as to the scope of the audit and reasonably satisfactory in substance to the Banks. In addition to the foregoing, the Company shall cause each Subsidiary to deliver summary income statements within ninety (90) days after the close of each fiscal year of the Company.

(c) Promptly after any Responsible Officer of the Company obtains knowledge thereof, notice of:

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(i) any material violation of, noncompliance with, or remedial obligations under, Requirements of Environmental Laws that could cause a Material Adverse Effect;

(ii) any Release or threatened material Release of Hazardous Materials affecting any property owned, leased or operated by the Company or any of its Subsidiaries that could cause a Material Adverse Effect;

(iii) any event or condition which constitutes a Default or an Event of Default;

(iv) any condition or event which, in the opinion of management of the Company, would reasonably be expected to have a Material Adverse Effect;

(v) any Person having given any written notice to the Company or taken any other action with respect to a claimed material default or event under any material instrument or material agreement;

(vi) the institution of any litigation which might reasonably be expected in the good faith judgment of the Company either to have a Material Adverse Effect or result in a final, non-appealable judgment or award in excess of \$1,000,000.00 with respect to any single cause of action; and

(vii) all ERISA notices required by Section 7.7;

such notice shall specify the nature and period of existence thereof and specifying the notice given or action taken by such Person and the nature of any such claimed default, event or condition and, in the case of an Event of Default or Default, what action has been taken, is being taken or is proposed to be taken with respect thereto.

(d) At the time of the delivery of the financial statements provided for in Section 7.1(a) and Section 7.1(b), a Compliance Certificate of a Responsible Officer to the effect that, no Default or Event of Default exists or, if any Default or Event of Default does exist, specifying the nature and extent thereof and the action that is being taken or that is proposed to be taken with respect thereto, which certificate shall set forth the calculations required to establish (i) whether the Company was in compliance with the provisions of Section 8.10 through Section 8.15 as at the end of such fiscal period or year, as the case may be, and (ii) pro forma compliance with this Agreement

with respect to principal payments scheduled to be made during the next fiscal quarter of the Company on Subordinated Debt which has been restructured as required by Section 5.1(1).

(e) Promptly following request by the Administrative Agent such environmental reports, studies and audits of the Company's procedures and policies, assets and operations in respect of Environmental Laws as the Administrative Agent may reasonably request.

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(f) Promptly upon receipt thereof, a copy of any report or letter submitted to the Company by its independent accountants in connection with any regular or special audit of the Company's records.

(g) From time to time and with reasonable promptness, such other information or documents as the Administrative Agent or any Bank through the Administrative Agent may reasonably request.

(h) As soon as available, and in any event within thirty (30) days after the end of each calendar month (except at the close of a fiscal quarter or fiscal year of the Company, when Section 7.1(a) and Section 7.1(b), respectively, will apply), the consolidated balance sheet of the Company and its Subsidiaries as of the end of such month and the related consolidated statements of income for such period in comparison to the same period for the prior year, along with summaries of the accounts receivable, accounts payable balances and an accounts receivable aging report as of the end of such month, all of which shall be certified by the treasurer, chief financial officer, or chief executive officer of the Company as fairly presenting in all material respects, the financial position of the Company and its Subsidiaries as of the end of such month in accordance with GAAP. In addition to the foregoing, the Company shall also provide at such time a schedule and explanation of the top fifteen (15) jobs in progress for which projections indicate a negative deviation from the original anticipated margins, which report shall include the amount of underbillings for each such job.

(i) Within thirty (30) days after the end of each calendar month, a completed Borrowing Base Certificate calculating and certifying the Borrowing Base as of the last day of such calendar month, signed by an officer and the secretary of the company and in the form attached hereto as Exhibit 7.1(i).

(j) Promptly upon receipt, a copy of the Company's annual management letter from the Company's independent auditors.

SECTION 7.2 Books, Records and Inspections. The Company and its Subsidiaries will maintain, and will permit, or cause to be permitted, any Person designated by any Bank or the Banks to visit and inspect any of the properties of the Company and its Subsidiaries, to examine the corporate books and financial records of the Company and its Subsidiaries and make copies thereof or extracts therefrom and to discuss the affairs, finances and accounts of any such corporations with the officers of the Company and its Subsidiaries and with their independent public accountants, all at such reasonable times and as often as the Administrative Agent or such Bank may reasonably request. Such inspections shall include one field exam of the Company's working capital assets, which shall be completed on or before the one hundred twentieth (120th) day following the Effective Date. Such field exam shall be at the expense of the Company. Inspections other than such field exam shall be at the expense of the

Bank or Banks requesting same unless there is in existence a Default at the time of such request in which event such expense shall be at the expense of the Company.

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SECTION 7.3 Insurance and Maintenance of Properties.

(a) Each of the Company and its Subsidiaries will keep reasonably adequately insured by financially sound and reputable insurers all of its material property, which is of a character, and in amounts and against such risks, usually and reasonably insured by similar Persons engaged in the same or similar businesses, including, without limitation, insurance against fire, casualty and any other hazards normally insured against. Each of the Company and its Subsidiaries will at all times maintain insurance against its liability for injury to Persons or property, which insurance shall be by financially sound and reputable insurers and in such amounts and form as are customary for corporations of established reputation engaged in the same or a similar business and owning and operating similar properties. The Company shall provide the Administrative Agent a listing of all such insurance and such other certificates and other evidence thereof, on or prior to the Effective Date hereof and annually thereafter. Each policy of insurance that insures against loss or damage with respect to any Collateral or against losses due to business interruption shall name the Administrative Agent for the benefit of the Banks as the loss payee thereunder for any covered loss in excess of \$500,000 and shall provide for at least thirty (30) days (fifteen (15) days in the event of non-payment of premium) prior written notice to the Administrative Agent of any modification or cancellation of such policy.

(b) Each of the Company and its Subsidiaries will cause all of its material properties used or useful in the conduct of its business to be maintained and kept in good condition, repair and working order and supplied with all necessary equipment and will cause to be made all reasonably necessary repairs, renewals and replacements thereof, all as in the reasonable judgment of such Person may be reasonably necessary so that the business carried on in connection therewith may be properly conducted at all times, except where such failure could not reasonably be expected to have a Material Adverse Effect.

SECTION 7.4 Payment of Taxes. Each of the Company and its Subsidiaries will pay and discharge all taxes, assessments and governmental charges or levies imposed upon it or upon its income or profits, or upon any properties belonging to it, prior to the date on which penalties attach thereto, except for such amounts that are being contested in good faith and by appropriate proceedings, except where such failure could not reasonably be expected to have a Material Adverse Effect, individually or in the aggregate.

SECTION 7.5 Corporate Existence. Each of the Company and its Subsidiaries will do all things necessary to preserve and keep in full force and effect (a) the existence of the Company, and (b) unless the failure to do so would not reasonably be expected to have a Material Adverse Effect, individually or in the aggregate, the rights and franchises of each of the Company and its Subsidiaries.

SECTION 7.6 Compliance with Statutes. Each of the Company and its Subsidiaries will comply with all applicable statutes, regulations and orders of, and all applicable restrictions imposed by, all governmental bodies, domestic or foreign, in respect of the conduct of its

business and the ownership of its property, except to the extent the failure to do so would not reasonably be expected to have a Material Adverse Effect.

SECTION 7.7 ERISA. Promptly after any Responsible Officer of the Company or any of its Subsidiaries knows or has reason to know any of the following items are true the Company will deliver or cause to be delivered to the Banks a certificate of the chief financial officer of the Company setting forth details as to such occurrence and such action, if any, the Company or its ERISA Affiliate is required or proposes to take, together with any notices required or proposed to be given to or filed with or by the Company or its ERISA Affiliate with respect thereto: that a Reportable Event has occurred or that an application may be or has been made to the Secretary of the Treasury for a waiver or modification of the minimum funding standard; that a Multiemployer Plan has been or may be terminated, reorganized, partitioned or declared insolvent under Title IV of ERISA; that any required contribution to a Plan or Multiemployer Plan has not been or may not be timely made; that proceedings may be or have been instituted under Section 4069(a) of ERISA to impose liability on the Company or an ERISA Affiliate or under Section 4042 of ERISA to terminate a Plan or appoint a trustee to administer a Plan; that the Company or any ERISA Affiliate has incurred or may incur any liability (including any contingent or secondary liability) on account of the termination of or withdrawal from a Plan or a Multiemployer Plan; and that the Company or an ERISA Affiliate may be required to provide security to a Plan under Section 401(a)(29) of the Code.

SECTION 7.8 Additional Subsidiaries. The Company will cause any Person that becomes a Material Subsidiary subsequent to the Effective Date, within thirty (30) Business Days after becoming a Material Subsidiary, (A) to execute and deliver (i) a Guaranty or a counterpart of this Agreement and deliver same to the Administrative Agent (together with certificates and all other instruments for such Material Subsidiary as required by Section 5.1(a)(iii) hereof); (ii) a Subsidiary Pledge Agreement or a counterpart of a Subsidiary Pledge Agreement executed by each such new Guarantor; and (iii) a Subsidiary Security Agreement or a counterpart of a Subsidiary Security Agreement executed by each such new Guarantor; provided if said Material Subsidiary is not incorporated under the laws of the United States or one of its states or territories, no such Guaranty, Subsidiary Pledge Agreement or Subsidiary Security Agreement, will be required if the Company makes arrangements, satisfactory to the Administrative Agent, in its sole discretion, regarding restrictions on transfer of funds or other assets by the Company or any Subsidiary to said new foreign Material Subsidiary; and (B) to take all such other further actions and executed all such further documents and instruments (including actions, documents and instruments comparable to those described in Section 5.1(b)) as may be necessary or, in the opinion of the Administrative Agent, desirable to create in favor of the Administrative Agent, for the benefit of the Banks, a valid and perfected First Priority Lien on all of the personal property assets of such Subsidiary described in the applicable forms of the Collateral Documents.

SECTION 7.9 Additional Collateral. The Company and the Guarantors shall re-title or otherwise indicate the Administrative Agent's lien on behalf of the Banks on the certificate of title of any titled vehicles at such time as the Administrative Agent notifies the Company that such action is required.

SECTION 7.10 Outside Consultant.

(a) In the event that there shall occur an Event of Default as a result of a breach of Section 8.10 through Section 8.15 inclusive, the Administrative Agent and the Banks will appoint a consultant to review and opine on the Company's practices, procedures, systems and overall business operations.

(b) If the results of the field exam required under Section 7.2 are deemed unsatisfactory by the Majority Banks, the Administrative Agent and the Majority Banks will appoint a consultant to review and opine on the Company's practices, procedures, systems and overall business operations.

(c) In each of the cases (a) and (b) above, the reasonable fees, costs and expenses of said consultant, the Administrative Agent and the Banks in connection with said review, shall be at the expense of the Company, and the Company shall cooperate with such consultant in the manner described in Section 7.2. Upon completion of such review, the Company will diligently pursue in a commercially reasonable manner the incorporation of the recommendations of said consultant into its ordinary course of business.

ARTICLE VIII
NEGATIVE COVENANTS

The Company covenants and agrees, as to itself and, except as otherwise provided herein, each of its Subsidiaries, that on and after the date hereof and for so long as this Agreement is in effect and until the Obligations have been paid in full and the Commitments have terminated:

SECTION 8.1 Change in Business. The Company will not, and will not permit any of its Subsidiaries to, engage in any businesses not of the same general type or reasonably related thereto as those conducted by the Company on the Effective Date.

SECTION 8.2 Consolidation, Merger or Sale of Assets. Except as disclosed to the Administrative Agent on or before the Effective Date in writing, the Company will not, and will not permit any of its Subsidiaries to, wind up, liquidate or dissolve their affairs, or enter into any transaction of merger or consolidation, or enter into any Asset Sales, except for (a) mergers permitted under Section 8.5(d), so long as the Company is the surviving entity and so long as no Event of Default occurs immediately before or after such merger, (b) mergers by the Company with any of its wholly-owned Subsidiaries and mergers by the Company's wholly-owned Subsidiaries with another of the Company's wholly-owned Subsidiaries, so long as the Company is the surviving entity and so long as no Event of Default occurs immediately before or after such merger, (c) mergers by a wholly-owned Subsidiary of the Company with another Person in connection with an Investment permitted under Section 8.5(d), so long as the relevant Subsidiary is the surviving entity and so long as no Event of Default occurs immediately before or after such merger, (d) wind ups, liquidations, dissolutions, mergers or consolidations with respect to the Subsidiaries listed on Exhibit 8.2(d) attached hereto and incorporated herein by reference and Asset Sales with respect to the stock of such Subsidiaries and the assets owned by such

Subsidiaries as of the Effective Date; provided that all proceeds received from such transactions permitted by this Section 8.2(d) shall be applied to the

Obligations then outstanding under the Loan Documents, and (e) Sale and Leaseback Transactions permitted under Section 8.3(n). No amendment, modification, termination, waiver or consent shall be made with respect to this Section 8.2 or with respect to the definition of "Asset Sales" without the consent of Banks holding at least eighty percent (80%) of the Advances outstanding under the Loans, or, if no Advances are outstanding, Banks holding such percentage of the Total Commitment (notwithstanding any reduction or termination of the Total Commitment) or if there are no Advances or Commitments outstanding, Banks holding such percentage of outstanding Letters of Credit.

SECTION 8.3 Indebtedness. Neither the Company nor any Subsidiary of the Company will create, incur, assume or permit to exist any Indebtedness of the Company or any Subsidiary except:

(a) Indebtedness existing hereunder;

(b) Indebtedness existing on the Effective Date not otherwise permitted in this Section 8.3 listed on Schedule 8.3(b)(i) and (ii);

(c) Indebtedness arising as a result of the endorsement in the ordinary course of business of negotiable instruments in the course of collection;

(d) accounts payable and unsecured, current and long-term, liabilities (including accrued insurance related liabilities), not the result of indebtedness for borrowed money, to vendors, suppliers and other Persons for goods and services in the ordinary course of business;

(e) agreements to acquire any Person or assets entered into by the Company or any of its Subsidiaries in anticipation of acquiring such Person or assets if such acquisition is not prohibited by this Agreement, and so long as the Indebtedness represented by such agreements is not otherwise prohibited hereunder;

(f) intercompany Indebtedness of any Subsidiary of the Company to the Company or any other Subsidiary and Indebtedness of the Company to any Subsidiary of the Company provided that same is subordinate to the Obligations in the manner provided in Section 8.5 hereof;

(g) current and deferred taxes;

(h) other Indebtedness not in excess of \$10,000,000.00 in the aggregate at any time outstanding;

(i) Subordinated Debt incurred by the Company or any of its Subsidiaries solely in connection with Investments permitted by Section 8.5(d) and Subordinated Debt incurred to refinance the then outstanding aggregate principal amount of any such Subordinated Debt incurred solely in connection with Investments permitted by Section 8.5(d); provided that such refinancing Subordinated Debt (1) shall be in an aggregate

principal amount not to exceed the then outstanding aggregate principal amount of such Subordinated Debt to be refinanced plus the amount of accrued and unpaid interest thereon; (2) shall not mature earlier than twelve months after the Maturity Date; and (3) shall contain such other terms and conditions that are not more favorable to the holders of such refinancing Subordinated Debt than to the holders of the Subordinated Debt being refinanced;

(j) Indebtedness assumed or acquired in connection with Investments permitted under Section 8.5(d); provided that all of such Indebtedness in excess of three percent (3%) of the net book value of the assets acquired in any such Investment shall be retired within 60 days after the date of such Investment;

(k) renewals and extensions with the same lenders (in the same or lesser principal amount on similar terms and conditions) of any Indebtedness listed in Section 8.3(a) through Section 8.3(i) but excluding Section 8.3(h) above;

(l) vehicle leases not to exceed \$30,000,000.00 in face value;

(m) Indebtedness under Interest Rate Agreements and Other Hedging Agreements to which the Company and any Bank are parties; provided that the Company or any of its Subsidiaries may enter into Interest Rate Agreements and Other Hedging Agreements with lenders other than Banks so long as such Interest Rate Agreements and Other Hedging Agreements are unsecured and are entered into in the ordinary course of business for non-speculative purposes; and

(n) Sale and Leaseback Transactions in the ordinary course of business with respect to the Company's vehicles owned on the Effective Date; provided that one hundred percent (100%) of the Net Cash Proceeds generated from same is applied as set forth in Section 2.7(d).

SECTION 8.4 Liens and Related Matters.

(a) Prohibition on Liens. Neither the Company nor any Subsidiary of the Company will create, incur, assume or suffer to exist any Lien upon or with respect to any of its property or assets of any kind whether now owned or hereafter acquired, except:

(i) Liens existing on the Effective Date and listed on Schedule 8.4(a);

(ii) Liens existing on the Effective Date securing currently secured Indebtedness permitted under Section 8.3(b) or Section 8.3(h) above;

(iii) Permitted Liens;

(iv) Liens securing Indebtedness permitted under Section 8.3(h) and Section 8.3(j);

(v) Liens granted pursuant to the Collateral Documents; and

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(vi) any renewal, extension or replacement of any Lien referred to above with the same lenders; provided that no Lien arising or existing as a result of such extension, renewal or replacement shall be extended to cover any property not theretofore subject to the Lien being extended, renewed or replaced; and provided further that the principal amount of the Indebtedness secured thereby shall not exceed the principal amount of the Indebtedness so secured at the time of such extension, renewal or replacement.

(b) Equitable Lien in Favor of Lenders. If the Company or any

of its Subsidiaries shall create or assume any Lien upon any of its properties or assets, whether now owned or hereafter acquired, other than Liens excepted by the provisions of Section 8.4(a), it shall make or cause to be made effective provision whereby the Obligations will be secured by such Lien equally and ratably with any and all other Indebtedness secured thereby as long as any such Indebtedness shall be so secured; provided that, notwithstanding the foregoing, this covenant shall not be construed as a consent by Majority Banks to the creation or assumption of any such Lien not permitted by the provisions of Section 8.4(a).

(c) No Further Negative Pledges. Except with respect to specific property encumbered to secure payment of particular Indebtedness or to be sold pursuant to an executed agreement with respect to an Asset Sale, neither the Company nor any of its Subsidiaries shall enter into any agreement (other than an agreement prohibiting only the creation of Liens securing Subordinated Debt) prohibiting the creation or assumption on any Lien upon any of its properties or assets, whether now or owned or hereafter acquired.

SECTION 8.5 Investments. Neither the Company nor any Subsidiary will, directly or indirectly, make or own any Investment in any Person, except:

(a) Permitted Investments;

(b) Investments owned on the Effective Date as set forth on Schedule 8.5(b), including Investments in the Subsidiaries, direct and indirect;

(c) Investments arising out of loans and advances for expenses, travel per diem and similar items in the ordinary course of business to officers, directors and employees and intercompany Indebtedness permitted by Section 8.3(f);

(d) Provided that the Company has obtained the prior written consent of the Eighty Percent Banks with respect thereto, Investments in the stock, warrants, stock appreciation rights, other securities and/or other assets of domestic entities engaged in the same general type of business as the Company on the Effective Date, in which the Company or one of its wholly owned Subsidiaries is the surviving entity.

(e) other Investments having cost to the Company and its Subsidiaries not exceeding \$2,000,000.00 in the aggregate at any one time outstanding during the term of this Agreement,

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(f) Investments in the form of stock buybacks allowed under Section 8.6; and

(g) Investments in capital stock of wholly-owned Subsidiaries of the Company in existence on the Effective Date.

SECTION 8.6 Restricted Payments. The Company will not, without the prior written consent of the Majority Banks, pay any dividend or other distribution, direct or indirect, on account of, or redeem, retire, purchase or guaranty the value of or make any other acquisition, direct or indirect, of any shares of any class of stock of the Company, or of any warrants, rights or options to acquire any such shares, now or hereafter outstanding.

SECTION 8.7 Change in Accounting. The Company will not and will not permit any Subsidiary to, change its method of accounting including a change of the Company's fiscal year except for (a) changes permitted by GAAP in which the Company's auditors concur, (b) changes with respect to any Person or assets acquired by the Company to conform with the Company's policies and procedures and which are permitted by GAAP, (c) changes required by GAAP, or (d) changes required by regulatory agencies. The Company shall advise the Administrative Agent in writing promptly upon making any material change to the extent same is not disclosed in the financial statements required under Section 7.1 hereof. In the event of any such change, the Company, the Banks and the Administrative Agent agree to negotiate amendments to Section 8.10 through Section 8.14 hereof (and related definitions, if relevant) so as to equitably reflect such changes thereon with the intended result that the criteria for evaluating the financial condition of the Company and its Subsidiaries shall be substantially the same after such changes as before.

SECTION 8.8 Change of Certain Indebtedness. The Company will not, and will not permit any of its Subsidiaries, after the occurrence and during the continuance of any Default or Event of Default, to make any voluntary prepayments of principal or interest on any of the Company's Indebtedness other than Indebtedness evidenced by this Agreement.

SECTION 8.9 Transactions with Affiliates. The Company will not, directly or indirectly, engage in any transaction with any Affiliate, including the purchase, sale or exchange of assets or the rendering of any service, except in the ordinary course of business or pursuant to the reasonable requirements of its business and, in each case, upon terms that are no less favorable than those which might be obtained in an arm's-length transaction at the time from non-Affiliates.

SECTION 8.10 Funded Senior Debt to EBITDA Ratio. The Company will not, as of the last day of any fiscal quarter specified in the table below, permit the ratio of its total Funded Senior Debt on such day to EBITDA for the four consecutive fiscal quarters then ended to exceed the amounts set forth below:

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QUARTER ENDING DATE(S) -----	RATIO -----
3/31/01	3.55 to 1.00
6/30/01	3.25 to 1.00
9/30/01	3.00 to 1.00
all quarters ending after 9/30/01	2.50 to 1.00

For purposes of calculating the ratio in this Section 8.10, the calculation of Funded Senior Debt after the acquisition of assets or entities permitted under this Agreement shall include adjustments to account for the total Funded Senior Debt of or applicable to such acquired assets or entities during the relevant period.

SECTION 8.11 Total Funded Debt to EBITDA Ratio. The Company will not, as of the last day of any fiscal quarter specified in the table below, permit the ratio of (i) its Total Funded Debt on such day to (ii) EBITDA for the four consecutive fiscal quarters then ended to exceed the amounts set forth below:

FISCAL QUARTER DATE(S) -----	RATIO -----
3/31/01	4.40 to 1.00
6/30/01	4.00 to 1.00
9/30/01	3.50 to 1.00
all quarters ending after 9/30/01	3.00 to 1.00

For purposes of calculating the ratio in this Section 8.11, the calculation of Total Funded Debt after the acquisition of assets or entities permitted under this Agreement shall include adjustments to account for the Total Funded Debt of or applicable to such acquired assets or entities during the relevant period.

SECTION 8.12 Minimum Net Worth. The Company will not permit, as of the Effective Date, its Consolidated Net Worth to be less than \$360,419,000.00. The Company will not permit, as of the last day of any fiscal quarter commencing with fiscal quarter ending March 31, 2001, its Consolidated Net Worth to be less than the sum of (i) \$360,419,000 plus (ii) seventy-five percent (75%) of the cumulative quarterly consolidated net income of the Company for each such fiscal quarter during which the Company has positive consolidated net income plus (iii) one hundred percent (100%) of the net proceeds received by the Company from any sale or issuance of any equity securities of, or any other additions to capital by, the Company or its Subsidiaries.

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SECTION 8.13 Capital Expenditures. The Company will not permit total consolidated capital expenditures (including Capitalized Lease Obligations but exclusive of (x) Investments permitted under Section 8.5(d) and (y) consolidated capital expenditures with respect to casualty loss replacements) to be greater than the lesser of (i) \$22,000,000.00 or (ii) two percent (2.00%) of gross revenues (pro forma gross revenues with respect to permitted acquisitions) for any fiscal year during the term hereof.

SECTION 8.14 Interest Coverage Ratio. The Company will not, as of the last day of any fiscal quarter specified in the table below, permit the ratio of EBITDA for the four consecutive fiscal quarters then ended to cash Interest Expense for such period to be less than the amounts set forth below:

QUARTER ENDING DATE(S) -----	RATIO -----
3/31/01	2.15 to 1.00
6/30/01	2.25 to 1.00
9/30/01	2.50 to 1.00
12/31/01	2.80 to 1.00
quarters ending after 12/31/01	3.00 to 1.00

SECTION 8.15 Minimum EBITDA. The Company will not, as of the last day of any fiscal quarter specified in the table below, permit its EBITDA for the three (3) months then ended to be less than the amounts set forth below:

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QUARTER ENDING DATE(S) -----	QUARTERLY EBITDA -----
03/31/01	\$13,000,000.00
06/30/01	\$18,500,000.00
09/30/01	\$23,000,000.00
12/31/01	\$21,500,000.00
03/31/02	\$13,700,000.00
06/30/02	\$20,000,000.00
09/30/02	\$24,800,000.00
12/31/02 and quarters ending thereafter	\$23,200,000.00

SECTION 8.16 No Prepayment or Amendments to Subordinated Debt. The Company will not, and will not permit any of its Subsidiaries to:

(a) amend any material term (including, without limitation, interest, payment or subordination terms) of any promissory note, intercreditor agreement, restructuring agreement or any other document amending, evidencing or relating to payment of the Subordinated Debt without the prior written consent of the Administrative Agent and the Banks, except such amendments which do not make any material term less favorable to the Company or the Banks; and

(b) make any voluntary prepayments or defeasements of principal or interest on any Subordinated Debt that has been restructured as referenced in Section 5.1(1) other than as set forth immediately below in this Section 8.16(b). In the event that for two consecutive fiscal quarters (i) the ratio described in Section 8.10 does not exceed 2.00 to 1.00, and (ii) the ratio described in Section 8.11 does not exceed 3.00 to 1.00, and provided that such payment will not result in an Event of Default, the Company may pay Subordinated Debt that has been restructured as referenced in Section 5.1(1) as follows:

(i) During the first fiscal quarter after the above-referenced ratios have been so maintained, the Company may pay all principal due and payable during the period from October 1, 2000 through and including March 31, 2001 (x) on Subordinated Debt not payable to the Required Subordinated Debt Holders, and (y) which would have been due and payable on Subordinated Debt during such period to the Required Subordinated Debt Holders, but for the restructuring of the Subordinated Debt to such holders referenced in Section 5.1(1); and

(ii) During all fiscal quarters following the fiscal quarter referenced in Section 8.16(b)(i) above, and provided that the Company has continued to

maintain the ratios referred to in Section 8.16(b) above, the Company may pay the principal described in Section 8.16(b)(i)(x) and Section 8.16(b)(i)(y) attributable to the fiscal quarter in which such principal has remained unpaid for the greatest amount of time.

ARTICLE IX
GUARANTY

SECTION 9.1 Guaranty. In consideration of, and in order to induce the Banks to make the Loans and the Issuing Bank to issue Letters of Credit hereunder, the Guarantors hereby absolutely, unconditionally and irrevocably, jointly and severally, guarantee the punctual payment and performance when due, whether at stated maturity, by acceleration or otherwise, of the Obligations, and all other obligations and covenants of the Company now or hereafter existing under this Agreement, the Notes and the other Loan Documents whether for principal, interest (including interest accruing or becoming owing both prior to and subsequent to the commencement of any proceeding against or with respect to the Company under any chapter of the Bankruptcy Code), Fees, commissions, expenses (including reasonable attorneys' fees and expenses) or otherwise, and all reasonable costs and expenses, if any, incurred by the Administrative Agent or any Bank in connection with enforcing any rights under this Guaranty (all such obligations being the "Guaranteed Obligations,") and agree to pay any and all reasonable expenses incurred by each Bank and the Administrative Agent in enforcing this Guaranty; provided that notwithstanding anything contained herein or in any of the Loan Documents to the contrary, the maximum liability of each Guarantor hereunder and under the other Loan Documents shall in no event exceed such Guarantor's Maximum Guaranteed Amount, provided further, each Guarantor shall be unconditionally required to pay all amounts demanded of it hereunder prior to any determination of such Maximum Guaranteed Amount and the recipient of such payment, if so required by a final non-appealable order of a court of competent jurisdiction, shall then be liable for the refund of any excess amounts. If any such rebate or refund is ever required, all other Guarantors (and the Company) shall be fully liable for the repayment thereof to the maximum extent allowed by applicable law. This Guaranty is an absolute, unconditional, present and continuing guaranty of payment and not of collectibility and is in no way conditioned upon any attempt to collect from the Company or any other action, occurrence or circumstance whatsoever. Each Guarantor agrees that the Guaranteed Obligations may at any time and from time to time exceed the Maximum Guaranteed Amount of such Guarantor without impairing this Guaranty or affecting the rights and remedies of the Banks hereunder.

SECTION 9.2 Continuing Guaranty. Each Guarantor guarantees that the Guaranteed Obligations will be paid strictly in accordance with the terms of this Agreement, the Notes and the other Loan Documents. Each Guarantor agrees that the Guaranteed Obligations and Loan Documents may be extended or renewed, and Loans repaid and reborrowed in whole or in part, without notice to or assent by such Guarantor, and that it will remain bound upon this Guaranty notwithstanding any extension, renewal or other alteration of any Guaranteed Obligations or Loan Documents, or any repayment and reborrowing of Loans. To the maximum extent permitted by applicable law, the obligations of each Guarantor under this Guaranty shall be absolute, unconditional and irrevocable, and shall be performed strictly in accordance with the terms hereof under any circumstances whatsoever, including:

(a) any extension, renewal, modification, settlement, compromise, waiver or release in respect of any Guaranteed Obligations;

(b) any extension, renewal, amendment, modification, rescission, waiver or release in respect of any Loan Documents;

(c) any release, exchange, substitution, non-perfection or invalidity of, or failure to exercise rights or remedies with respect to, any direct or indirect security for any Guaranteed Obligations, including the release of any Guarantor or other Person liable on any Guaranteed Obligations;

(d) any change in the corporate existence, structure or ownership of the Company, any Guarantor, or any insolvency, bankruptcy, reorganization or other similar proceeding affecting the Company, such Guarantor, any other Guarantor or any of their respective assets;

(e) the existence of any claim, defense, set-off or other rights or remedies which such Guarantor at any time may have against the Company, or the Company or such Guarantor may have at any time against the Administrative Agent, any Bank, any other Guarantor or any other Person, whether in connection with this Guaranty, the Loan Documents, the transactions contemplated thereby or any other transaction other than by the payment in full by the Company of the Guaranteed Obligations after the termination of the Commitments of the Banks;

(f) any invalidity or unenforceability for any reason of this Agreement or other Loan Documents, or any provision of law purporting to prohibit the payment or performance by the Company, such Guarantor or any other Guarantor of the Guaranteed Obligations or Loan Documents, or of any other obligation to the Administrative Agent or any Bank; or

(g) any other circumstances or happening whatsoever, whether or not similar to any of the foregoing.

SECTION 9.3 Effect of Debtor Relief Laws. If after receipt of any payment of, or proceeds of any security applied (or intended to be applied) to the payment of all or any part of the Guaranteed Obligations, the Administrative Agent or any Bank is for any reason compelled to surrender or voluntarily surrenders such payment or proceeds to any Person (a) because such payment or application of proceeds is or may be avoided, invalidated, declared fraudulent, set aside, determined to be void or voidable as a preference, fraudulent conveyance, fraudulent transfer, impermissible set-off or a diversion of trust funds or (b) for any other similar reason, including (i) any judgment, decree or order of any court or administrative body having jurisdiction over the Administrative Agent, any Bank or any of their respective properties or (ii) any settlement or compromise of any such claim effected by the Administrative Agent or any Bank with any such claimant (including the Company), then the Guaranteed Obligations or part thereof intended to be satisfied shall be reinstated and continue, and this Guaranty shall continue in full force as if such payment or proceeds have not been received, notwithstanding any revocation thereof or the cancellation of any Note or any other instrument evidencing any

indemnify the Administrative Agent and the Banks and hold them harmless for the amount of such payment or proceeds so surrendered and all expenses (including reasonable attorneys' fees, court costs and expenses attributable thereto) incurred by the Administrative Agent or any Bank in the defense of any claim made against it that any payment or proceeds received by the Administrative Agent or any Bank in respect of all or part of the Guaranteed Obligations must be surrendered. The provisions of this paragraph shall survive the termination of this Guaranty, and any satisfaction and discharge of the Company by virtue of any payment, court order or any federal or state law.

SECTION 9.4 Waiver of Subrogation. Notwithstanding any payment or payments made by any Guarantor hereunder, or any set-off or application by the Administrative Agent or any Bank of any security or of any credits or claims, no Guarantor will assert or exercise any rights of the Administrative Agent or any Bank or of such Guarantor against the Company to recover the amount of any payment made by such Guarantor to the Administrative Agent or any Bank hereunder by way of any claim, remedy or subrogation, reimbursement, exoneration, contribution, indemnity, participation or otherwise arising by contract, by statute, under common law or otherwise, and such Guarantor shall not have any right of recourse to or any claim against assets or property of the Company, in each case unless and until the Obligations of the Company guaranteed hereby have been fully and finally satisfied. Until such time, each Guarantor hereby expressly waives any right to exercise any claim, right or remedy which such Guarantor may now have or hereafter acquire against the Company that arises under this Agreement or any other Loan Document or from the performance by any Guarantor of the Guaranty hereunder including any claim, remedy or right of subrogation, reimbursement, exoneration, contribution, indemnification or participation in any claim, right or remedy of the Administrative Agent or any Bank against the Company, or any security that the Administrative Agent or any Bank now has or hereafter acquires, whether or not such claim, right or remedy arises in equity, under contract, by statute, under common law or otherwise. If any amount shall be paid to a Guarantor by the Company or another Guarantor after payment in full of the Obligations, and the Obligations shall thereafter be reinstated in whole or in part and the Administrative Agent or any Bank forced to repay and sums received by any of them in payment of the Obligations, this Guaranty shall be automatically reinstated and such amount shall be held in trust for the benefit of the Administrative Agent and the Banks and shall forthwith be paid to the Administrative Agent to be credited and applied to the Guaranteed Obligations, whether matured or unmatured. The provisions of this paragraph shall survive the termination of this Guaranty, and any satisfaction and discharge of the Company by virtue of any payment, court order or any federal or state law.

SECTION 9.5 Subordination. If any Guarantor becomes the holder of any indebtedness payable by the Company or another Guarantor, each Guarantor hereby subordinates all indebtedness owing to it from the Company to all indebtedness of the Company to the Administrative Agent and the Banks, and agrees that during the continuance of any Event of Default it shall not accept any payment on the same until payment in full of the Obligations of the Company under this Agreement and the other Loan Documents after the termination of the Commitments of the Banks and shall in no circumstance whatsoever attempt to set-off or reduce any obligations hereunder because of such indebtedness. If any amount shall nevertheless be paid in violation of the foregoing to a Guarantor by the Company or another Guarantor prior to payment in full of the Guaranteed Obligations, such amount shall be held in trust for the benefit

of the Administrative Agent and the Banks and shall forthwith be paid to the Administrative Agent to be credited and applied to the Guaranteed Obligations, whether matured or unmatured.

SECTION 9.6 Waiver. Each Guarantor hereby waives promptness, diligence,

notice of acceptance and any other notice with respect to any of the Guaranteed Obligations and this Guaranty and waives presentment, demand of payment, notice of intent to accelerate, notice of dishonor or nonpayment and any requirement that the Administrative Agent or any Bank institute suit, collection proceedings or take any other action to collect the Guaranteed Obligations, including any requirement that the Administrative Agent or any Bank protect, secure, perfect or insure any Lien against any property subject thereto or exhaust any right or take any action against the Company or any other Person or any collateral (it being the intention of the Administrative Agent, the Banks and each Guarantor that this Guaranty is to be a guaranty of payment and not of collection). It shall not be necessary for the Administrative Agent or any Bank, in order to enforce any payment by any Guarantor hereunder, to institute suit or exhaust its rights and remedies against the Company, any other Guarantor or any other Person, including others liable to pay any Guaranteed Obligations, or to enforce its rights against any security ever given to secure payment thereof. Each Guarantor hereby expressly waives to the maximum extent permitted by applicable law each and every right to which it may be entitled by virtue of the suretyship laws of the State of Texas, including any and all rights it may have pursuant to Rule 31, Texas Rules of Civil Procedure, Section 17.001 of the Texas Civil Practice and Remedies Code and Chapter 34 of the Texas Business and Commerce Code. Each Guarantor hereby waives marshaling of assets and liabilities, notice by the Administrative Agent or any Bank of any indebtedness or liability to which such Bank applies or may apply any amounts received by such Bank, and of the creation, advancement, increase, existence, extension, renewal, rearrangement or modification of the Guaranteed Obligations. Each Guarantor expressly waives, to the extent permitted by applicable law, the benefit of any and all laws providing for exemption of property from execution or for valuation and appraisal upon foreclosure.

SECTION 9.7 Full Force and Effect. This Guaranty is a continuing guaranty and shall remain in full force and effect until all of the Obligations of the Company under this Agreement and the other Loan Documents and all other amounts payable under this Guaranty have been paid in full (after the termination of the Commitments of the Banks). All rights, remedies and powers provided in this Guaranty may be exercised, and all waivers contained in this Guaranty may be enforced, only to the extent that the exercise or enforcement thereof does not violate any provisions of applicable law which may not be waived.

ARTICLE X
EVENTS OF DEFAULT AND REMEDIES

SECTION 10.1 Events of Default. The following events shall constitute Events of Default ("Events of Default") hereunder:

(a) any installment of principal is not paid when due; or any payment of interest or Fees is not paid on the date on which such payment is due and such failure continues for a period of five (5) days; or

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(b) any representation or warranty made or deemed made by the Company or any Subsidiary herein or in any of the Loan Documents or other document, certificate or financial statement delivered in connection with this Agreement or any other Loan Document shall prove to have been incorrect in any material respect when made or deemed made or reaffirmed, as the case may be; or

(c) the Company shall fail to perform, comply or observe or cause any Subsidiary, to fail to perform, comply or observe (i) any

term, duty or covenant contained in Article VIII of this Agreement; or (ii) any other term, duty or covenant contained elsewhere in this Agreement or in any of the Loan Documents and such failure continues for a period of thirty (30) days after receipt by the Company and such Guarantor of notice from the Administrative Agent or any Bank of such default; or

(d) the Company or any Subsidiary shall (i) fail to make (whether as primary obligor or as guarantor or other surety) any principal payment of or interest or premium, if any, on any instruments of Indebtedness in excess of \$2,500,000 in the aggregate allowed hereunder outstanding beyond any period of grace provided with respect thereto or (ii) shall fail to duly observe, perform or comply with any agreement with any Person or any term or condition of any instrument of Indebtedness in excess of \$2,500,000 in the aggregate, if the effect of such failure is to cause, or to permit the holder or holders to cause, such obligations to become due prior to any stated maturity; provided that, the failure of the Company to make the Restricted Subordinated Debt Payments because it is not in Financial Compliance, as proscribed by Section 10.1(j) shall not constitute an Event of Default; or

(e) an involuntary proceeding shall be commenced or an involuntary petition shall be filed in a court of competent jurisdiction seeking (i) relief in respect of the Company or any Subsidiary, or of a substantial part of the property or assets of the Company or any Subsidiary, under Title 11 of the United States Code, as now or hereafter in effect, or any successor thereto (the "Bankruptcy Code"), or any other federal or state bankruptcy, insolvency, receivership or similar law, (ii) the appointment of a receiver, trustee, custodian, sequestrator, conservator or similar official for the Company or any Subsidiary or for a substantial part of the property or assets of the Company or any Subsidiary or (iii) the winding-up or liquidation of the Company or any Subsidiary; and such proceeding or petition shall continue undismissed for 60 days or an order or decree approving or ordering any of the foregoing shall be entered; or

(f) the Company or any Subsidiary shall (i) voluntarily commence any proceeding or file any petition seeking relief under the Bankruptcy Code or any other federal or state bankruptcy, insolvency, receivership or similar law, (ii) consent to the institution of, or fail to contest in a timely and appropriate manner, any proceeding or the filing of any petition described in clause (e) above, (iii) apply for or consent to the appointment of a receiver, trustee, custodian, sequestrator, conservator or similar official for the Company or any Subsidiary or for a substantial part of the property or assets of the Company or any Subsidiary, (iv) file an answer admitting the material allegations of a petition filed against it in any such proceeding, (v) make a general assignment for the benefit of creditors, (vi) become unable, or admit in writing its inability or fail generally

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to pay its debts as they become due or (vii) take any action for the purpose of effecting any of the foregoing; or

(g) a judgment or order (including any prejudgment orders), which with other outstanding judgments and orders against the Company and its Subsidiaries equal or exceed (i) with respect to matters other than Subordinated Debt, \$1,000,000.00 in the aggregate (to the extent not covered by insurance as to which the respective insurer has acknowledged coverage), and (ii) with respect to Subordinated Debt, \$200,000.00, shall be entered against the Company or any Subsidiary and, in each case, (A) within 30 days after entry thereof such judgment

or order shall not have been paid or discharged or execution thereof stayed pending appeal or, within 30 days after the expiration of any such stay, such judgment shall not have been paid or discharged or (B) any enforcement proceeding or remedy of any kind for the nonpayment of Indebtedness shall have been commenced (and not stayed) by any creditor or upon such judgment; or

(h) a Change of Control shall occur; or

(i) at any time after the execution and delivery thereof, (i) the Guaranty for any reason, other than the satisfaction in full of all Obligations, shall cease to be in full force and effect (other than in accordance with its terms) or shall be declared to be null and void, (ii) any Collateral Document shall cease to be in full force and effect (other than by reason of a release of Collateral thereunder in accordance with the terms hereof or thereof, the satisfaction in full of the Obligations or any other termination of such Collateral Document in accordance with the terms hereof or thereof) or shall be declared null and void, or the Administrative Agent shall not have or shall cease to have a valid and perfected First Priority Lien in any material amount of Collateral purported to be covered thereby, in each case for any reason other than the failure of the Administrative Agent or any Bank to take any action within its control, or (iii) the Company or any Guarantor shall contest the validity or enforceability of any Loan Document in writing or deny in writing that it has any further liability, including with respect to future Advances by the Banks, under any Loan Document to which it is a party; or

(j) The Company or any Subsidiary shall make any Restricted Subordinated Debt Payments (i) other than as permitted by Section 8.16, or (ii) unless such payment is made at a time when the Company is in Financial Compliance; provided that if the Company is in Financial Compliance by reason of complying solely with subsection (i) of the definition thereof, such payments may not be greater in the aggregate than the amount of Subordinated Debt (or other capital) incurred.

SECTION 10.2 Primary Remedies. In any such event, and at any time after the occurrence of any of the above described events, the Administrative Agent, if directed by the Majority Banks, shall by written notice to the Company (a "Notice of Default") take any or all of the following actions; provided, that if an Event of Default specified in Section 10.1(e) or Section 10.1(f) shall occur, the following shall occur automatically without the giving of any Notice of Default: (a) declare the Commitments terminated, whereupon the Commitments shall forthwith terminate immediately and any Commitment Fee and any other owing and unpaid Fee shall forthwith become due and payable without any other notice of any kind; (b) declare (i) the

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principal of and any accrued and unpaid interest in respect of all Advances, (ii) an amount equal to the maximum amount that may at any time be drawn under all Letters of Credit then outstanding (whether or not any beneficiary under any such Letter of Credit shall have presented, or shall be entitled at such time to present, the drafts or other documents or certificates required to draw under such Letter of Credit), and (iii) all other Obligations owing hereunder, to be, whereupon the same shall become, forthwith due and payable without presentment, demand, notice of demand or of dishonor and non-payment, protest, notice of protest, notice of intent to accelerate, declaration or notice of acceleration or any other notice of any kind (except as herein expressly provided), all of which are hereby waived by the Company; (c) set off any assets or money of the Company or any Guarantor in its or any Banks' possession against the Obligations; and (d) exercise any rights or remedies under any document securing any of the Loan Documents or under any applicable state or federal law. Any

amounts described in clause (b)(ii) above, when received by the Administrative Agent, shall be held by the Administrative Agent pursuant to the terms of the Collateral Account Agreement and shall be applied as therein provided.

SECTION 10.3 Other Remedies. Upon the occurrence and during the continuance of any Event of Default, the Administrative Agent may proceed to protect and enforce its and the Banks' rights, either by suit in equity or by action at law or both, whether for the specific performance of any covenant or agreement contained in this Agreement or in any other Loan Document or in aid of the exercise of any power granted in this Agreement or in any other Loan Document; or may proceed to enforce the payment of all amounts owing to the Banks under the Loan Documents and any accrued and unpaid interest thereon in the manner set forth herein or therein; it being intended that no remedy conferred herein or in any of the other Loan Documents is to be exclusive of any other remedy, and each and every remedy contained herein or in any other Loan Document shall be cumulative and shall be in addition to every other remedy given hereunder and under the other Loan Documents or now or hereafter existing at law or in equity or by statute or otherwise.

ARTICLE XI
THE AGENTS

SECTION 11.1 Authorization and Action. Each Bank hereby irrevocably appoints and authorizes each Agent to act on its behalf and to exercise such powers under this Agreement and the other Loan Documents as are specifically delegated to or required of such Agent by the terms hereof, together with such powers as are reasonably incidental thereto. Each Agent may perform any of its duties hereunder by or through its agents and employees. The duties of each Agent shall be mechanical and administrative in nature; no Agent shall have by reason of this Agreement or any other Loan Documents a fiduciary relationship in respect of any Bank; and nothing in this Agreement or any other Loan Document, expressed or implied is intended to, or shall be so construed as to, impose upon any Agent any obligations in respect of this Agreement or any other Loan Document except as expressly set forth herein or therein. As to any matters not expressly provided for by this Agreement, the Notes or the other Loan Documents (including enforcement or collection of the Notes), no Agent shall be required to exercise any discretion or take any action, but shall be required to act or to refrain from acting (and shall be fully protected in so acting or refraining from acting) upon the instructions of the Majority Banks, and such instructions shall be binding upon the Banks and all holders of Notes and the Obligations; provided, that no Agent shall be required to take any action which exposes such Agent to

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personal liability and shall not be required or entitled to take any action which is contrary to any of the Loan Documents or applicable law.

SECTION 11.2 Agents' Reliance.

(a) None of the Agents nor any of its directors, officers, agents or employees shall be liable to the Banks for any action taken or omitted to be taken by it or them under or in connection with this Agreement, the Notes or any of the other Loan Documents (i) with the consent or at the request of the Majority Banks or (ii) in the absence of its or their own gross negligence or willful misconduct, IT BEING THE EXPRESS INTENTION OF THE PARTIES HERETO THAT EACH AGENT AND ITS DIRECTORS, OFFICERS, AGENTS AND EMPLOYEES SHALL HAVE NO LIABILITY TO THE BANKS FOR ACTIONS AND OMISSIONS UNDER THIS SECTION RESULTING FROM THEIR SOLE ORDINARY OR CONTRIBUTORY NEGLIGENCE.

(b) Without limitation of the generality of the foregoing, each Agent: (i) may treat the payee of each Note and the Obligations as

the holder thereof until the Administrative Agent receives written notice of the assignment or transfer thereof signed by such payee and in form satisfactory to the Agents; (ii) may consult with legal counsel (including counsel for the Company), independent public accountants and other experts selected by it and shall not be liable for any action taken or omitted to be taken in good faith by it in accordance with the advice of such counsel, accountants or experts; (iii) makes no warranty or representation to any Bank and shall not be responsible to any Bank for any statements, warranties or representations made in or in connection with this Agreement, any Note or any other Loan Document; (iv) except as otherwise expressly provided herein, shall not have any duty to ascertain or to inquire as to the performance or observance of any of the terms, covenants or conditions of this Agreement, any Note or any other Loan Document or to inspect the property (including the books and records) of the Company; (v) shall not be responsible to any Bank for the due execution, legality, validity, enforceability, collectibility, genuineness, sufficiency or value of this Agreement, any Note, any other Loan Document or any other instrument or document furnished pursuant hereto or thereto; (vi) shall not be responsible to any Bank for the perfection or priority of any Lien securing the Obligations; and (vii) shall incur no liability under or in respect of this Agreement, any Note or any other Loan Document by acting upon any notice, consent, certificate or other instrument or writing (which may be by telegram, telecopier or cable) reasonably believed by it to be genuine and signed or sent by the proper party or parties.

SECTION 11.3 Agent and Affiliates. Without limiting the right of any other Bank to engage in any business transactions with the Company or any of its Affiliates, with respect to their Commitments, the Loans made by them and the Notes issued to them, Bank One, BTCo and BofA and each other Bank who may become the Administrative Agent, Syndication Agent or Documentation Agent, as the case may be, shall have the same rights and powers under this Agreement and its Notes as any other Bank and may exercise the same as though it was not an Agent; and the term "Bank" or "Banks" shall, unless otherwise expressly indicated, include Bank One, BTCo and BofA and any such other Bank, in their individual capacities. Bank One, BTCo and BofA, each other Person who becomes the Administrative Agent, the Syndication Agent or the Documentation Agent, as the case may be, and their respective Affiliates may be engaged in,

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or may hereafter engage in, one or more loan, letter of credit, leasing or other financing activity not the subject of this Agreement (collectively, the "Other Financings") with the Company, any Subsidiary or any of its Affiliates, or may act as trustee on behalf of, or depositary for, or otherwise engage in other business transactions with the Company, any Subsidiary or any of its Affiliates (all Other Financings and other such business transactions being collectively, the "Other Activities") with no responsibility to account therefor to the Banks. Without limiting the rights and remedies of the Banks specifically set forth herein, no other Bank by virtue of being a Bank hereunder shall have any interest in (a) any Other Activities, (b) any present or future guaranty by or for the account of the Company not contemplated or included herein, (c) any present or future offset exercised by an Agent in respect of any such Other Activities, (d) any present or future property taken as security for any such Other Activities or (e) any property now or hereafter in the possession or control of any Agent which may be or become security for the Obligations of the Company hereunder and under the Notes by reason of the general description of indebtedness secured, or of property contained in any other agreements, documents or instruments related to such Other Activities; provided, however, that if any payment in respect of such guaranties or such property or the proceeds thereof shall be applied to reduction of the Obligations evidenced hereunder and by the Notes, then each Bank shall be entitled to share in such

application according to its pro rata portion of such Obligations.

SECTION 11.4 Bank Credit Decision. Each Bank acknowledges and agrees that it has, independently and without reliance upon any Agent or any other Bank and based on the financial statements referred to in Section 7.1 and such other documents and information as it has deemed appropriate, made its own credit analysis and decision to enter into this Agreement. Each Bank also acknowledges and agrees that it will, independently and without reliance upon any Agent or any other Bank and based on such documents and information as it shall deem appropriate at the time, continue to make its own credit decisions in taking or not taking action under this Agreement and the other Loan Documents.

SECTION 11.5 Agents' Indemnity.

(a) No Agent shall be required to take any action hereunder or to prosecute or defend any suit in respect of this Agreement, the Notes or any other Loan Document unless indemnified to Agents' satisfaction by the Banks against loss, cost, liability and expense. If any indemnity furnished to the Agents shall become impaired, it may call for additional indemnity and cease to do the acts indemnified against until such additional indemnity is given. In addition, the Banks agree to indemnify the Agents (to the extent not reimbursed by the Company), ratably according to the respective aggregate principal amounts of the Notes then held by each of them (or if no Notes are at the time outstanding, ratably according to the respective amounts of the Commitments), from and against any and all liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses or disbursements of any kind or nature whatsoever which may be imposed on, incurred by, or asserted against any Agent in any way relating to or arising out of this Agreement or any action taken or omitted by any Agent under this Agreement, the Notes and the other Loan Documents. Without limitation of the foregoing, each Bank agrees to reimburse each Agent promptly upon demand for its ratable share of any out-of-pocket expenses (including reasonable counsel fees) incurred by such Agent in connection with the preparation, execution, administration, or enforcement of, or legal

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advice in respect of rights or responsibilities under, this Agreement, the Notes and the other Loan Documents to the extent that such Agent is not reimbursed for such expenses by the Company. The provisions of this Section shall survive the termination of this Agreement, the payment of the Obligations and/or the assignment of any of the Notes.

(b) Notwithstanding the foregoing, no Bank shall be liable under this Section to any Agent for any portion of such liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses or disbursements due to any Agent resulting from such Agent's gross negligence or willful misconduct. Each Bank agrees, however, that it expressly intends, under this Section, to indemnify each Agent ratably as aforesaid for all such liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses and disbursements arising out of or resulting from such Agent's sole ordinary or contributory negligence.

SECTION 11.6 Successor Agents. Each Agent may resign at any time by giving written notice thereof to the Banks and the Company and may be removed as an Agent under this Agreement, the Notes and the other Loan Documents at any time with or without cause by the Majority Banks. Upon any such resignation or removal, the Majority Banks shall have the right to appoint a successor Agent with, so long as no Event of Default exists, the consent of the Company, which will not be unreasonably withheld. If no successor Agent shall have been so

appointed by the Majority Banks, and shall have accepted such appointment, within 30 calendar days after the retiring Agent's giving of notice of resignation or the Majority Banks' removal of the retiring Agent, then the retiring Agent may, on behalf of the Banks, appoint a successor Agent, which shall be an Eligible Assignee. Upon the acceptance of any appointment as an Agent hereunder and under the Notes and the other Loan Documents by a successor Agent, such successor Agent shall thereupon succeed to and become vested with all the rights, powers, privileges and duties of the retiring Agent, and the retiring Agent shall be discharged from its duties and obligations under this Agreement, the Notes and the other Loan Documents. After any retiring Agent's resignation or removal as an Agent hereunder and under the Notes and the other Loan Documents, the provisions of this Article XI shall inure to its benefit as to any actions taken or omitted to be taken by it while it was an Agent under this Agreement, the Notes and the other Loan Documents.

SECTION 11.7 Notice of Default. No Agent shall be deemed to have knowledge or notice of the occurrence of any Default or Event of Default hereunder unless such Agent shall have received notice from a Bank or the Company referring to this Agreement, describing such Default or Event of Default and stating that such notice is a "notice of default." If an Agent receives such notice, such Agent shall give notice thereof to the Banks; provided however, if such notice is received from a Bank, such Agent also shall give notice thereof to the Company. Each Agent shall be entitled to take action or refrain from taking action with respect to such Default or Event of Default as provided in Section 10.1 and Section 10.2.

SECTION 11.8 Collateral Documents and Guaranties. Each Bank hereby further authorizes the Administrative Agent, on behalf of and for the benefit of the Banks, to enter into each Collateral Document as secured party and to be the agent for and representative of the Banks under the Guaranty, and each Bank agrees to be bound by the terms of each Collateral Document and the Guaranty; provided that the Administrative Agent shall not (i) enter into or

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consent to any material amendment, modification, termination or waiver of any provision contained in any Collateral Document or the Guaranty or (ii) release any Collateral (except as otherwise expressly permitted or required pursuant to the terms of this Agreement or the applicable Collateral Document), in each case without the prior consent of Majority Banks (or, if required pursuant to Section 12.1, all Banks); provided further, however, that, without further written consent or authorization from the Banks, the Administrative Agent may execute any documents or instruments necessary to (a) release any Lien encumbering any item of Collateral that is the subject of a sale or other disposition of assets permitted by this Agreement or to which Majority Banks have otherwise consented or (b) release any Guarantor from the Guaranty if all of the capital stock of such Guarantor is sold to any Person (other than an Affiliate of the Company) pursuant to a sale or other disposition permitted hereunder or to which Majority Banks have otherwise consented. Anything contained in any of the Loan Documents to the contrary notwithstanding, the Company, the Agents and each Bank hereby agree that (X) no Bank shall have any right individually to realize upon any of the Collateral under any Collateral Document or to enforce the Guaranty, it being understood and agreed that all powers, rights and remedies under the Collateral Documents and the Guaranty may be exercised solely by the Administrative Agent for the benefit of the Banks in accordance with the terms thereof, and (Y) in the event of a foreclosure by the Administrative Agent on any of the Collateral pursuant to a public or private sale, any Agent or any Bank may be the purchaser of any or all of such Collateral at any such sale and the Administrative Agent, as agent for and representative of Banks (but not any Bank or Banks in its or their respective individual capacities unless Majority Banks shall otherwise agree in writing) shall be entitled, for the purpose of bidding and making settlement or payment of the purchase price for all or any portion of the Collateral sold at any such public sale, to use and apply any of

the Obligations as a credit on account of the purchase price for any Collateral payable by the Administrative Agent at such sale.

SECTION 11.9 Co-Agents. None of the Banks identified on the facing page, preamble or signature pages of this Agreement as a "Co-Agent" shall have any right, power, obligation, liability, responsibility or duty under this Agreement other than those applicable to all Banks as such. Each Bank acknowledges that it has not relied, and will not rely, on any of the Banks so identified in deciding to enter into this Agreement or in taking or not taking action hereunder.

ARTICLE XII
MISCELLANEOUS

SECTION 12.1 Amendments. No amendment, modification, termination or waiver of any provision of this Agreement or of the Notes, or consent to any departure by the Company therefrom, shall in any event be effective without the written concurrence of Majority Banks; provided that no such amendment, modification, termination, waiver or consent shall, without the consent of each Bank (with Obligations directly affected in the case of the following clause (i)): (i) extend the scheduled final maturity of any Loan or Note, or extend the stated expiration date of any Letter of Credit beyond the Maturity Date, or reduce the rate of interest (other than any waiver of any increase in the interest rate applicable to any of the Loans pursuant to the Default Rate) or fees thereon, or extend the time of payment of interest, principal or fees thereon, or reduce the principal amount thereof, (ii) release all or substantially all of the Collateral, release all or substantially all of the Subsidiaries that are party to the Guaranty from the Guaranty

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except as expressly provided in the Loan Documents, (iii) amend, modify, terminate or waive any provision of this Section 12.1, (iv) reduce the percentage specified in the definition of Majority Banks or Eighty Percent Banks (or amend, modify, terminate or waive any provision requiring consent of the Eighty Percent Banks without the consent of the Eighty Percent Banks), (v) consent to the assignment or transfer by the Company of any of its respective rights and obligations under this Agreement, or (vi) amend, modify, terminate or waive the requirement under Section 7.10(a) and Section 7.10(b) that the Company's business practices be reviewed by an outside consultant; provided further that no such amendment, modification, termination or waiver shall (1) increase the Commitments of any Bank over the amount thereof then in effect without the consent of such Bank (it being understood that amendments, modifications or waivers of conditions precedent, covenants, Events of Default or of a mandatory reduction of the Commitments shall not constitute an increase of the Commitment of any Bank, and that an increase in the available portion of any Commitment of any Bank shall not constitute an increase in the Commitment of such Bank), (2) no amendment, modification, termination or waiver relating to the obligations of Banks relating to the purchase or participation in Letters of Credit shall be effective without the written concurrence of each Issuing Bank having a Letter of Credit then outstanding or which has not been reimbursed for a drawing under a Letter of Credit issued by it and of the Administrative Agent, and (3) no amendment, modification, termination or waiver of any provision of Article XI or of any provision of this Agreement which, by its terms, expressly requires the approval or concurrence of any Agent shall be effective without the written concurrence of such Agent. The Administrative Agent may, but shall have no obligation to, with the concurrence of any Bank, execute amendments, modifications, waivers or consents on behalf of that Bank. Any waiver or consent shall be effective only in the specific instance and for the specific purpose for which it was given. No notice to or demand on the Company in any case shall entitle the Company to any other or further notice or demand in similar or other circumstances. Any amendment, modification, termination, waiver or consent effected in accordance with this Section 12.1 shall be binding upon each Bank at

the time outstanding, each future Bank and, if signed by the Company, on the Company.

SECTION 12.2 Notices. Except with respect to telephone notifications specifically permitted pursuant to Article II, all notices, consents, requests, approvals, demands and other communications provided for herein shall be in writing (including telecopy communications) and mailed, telecopied, sent by overnight courier or delivered:

(a) If to the Company and the Guarantors:

Comfort Systems USA, Inc.
777 Post Oak Boulevard, Suite 500
Houston, Texas 77056
Telephone No.: (713) 830-9600
Telecopy No.: (713) 830-9676
Attention: J. Gordon Beittenmiller

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(b) If to the Administrative Agent:

Bank One, NA
910 Travis, 7th Floor
Houston, Texas 77002
Telephone No.: (713) 751-3838
Telecopy No.: (713) 751-6777
Attention: Greg Smothers

or, in the case of any party hereto, such other address or telecopy number as such party may hereafter specify for such purpose by notice to the other parties.

(c) If to any Bank, to the address shown on the signature page hereof or specified by such Bank (or the Administrative Agent on behalf of any Bank) to the Company.

All communications shall, when mailed, telecopied or delivered, be effective when mailed by certified mail, return receipt requested to any party at its address specified above, or telecopied to any party to the telecopy number set forth above, or delivered personally to any party at its address specified above; provided, that communications to the Administrative Agent pursuant to Article II shall not be effective until actually received by the Administrative Agent, and provided further that communications sent by telecopy after 5:00 p.m., Houston, Texas time, shall be effective on the next succeeding Business Day.

SECTION 12.3 No Waiver; Remedies. No failure on the part of any Bank or the Administrative Agent to exercise, and no delay in exercising, any right hereunder, under any Note or under any other Loan Document shall operate as a waiver thereof; nor shall any single or partial exercise of any such right, or any abandonment or discontinuance of any steps to enforce such right, preclude any other or further exercise thereof or the exercise of any other right. No notice to or demand on the Company in any case shall entitle the Company to any other or further notice or demand in similar or other circumstances. The remedies herein are cumulative and not exclusive of any other remedies provided by law, at equity or in any other agreement.

SECTION 12.4 Costs, Expenses and Taxes. The Company agrees to pay on demand: (a) all reasonable out-of-pocket costs and expenses of the Syndication Agent in connection with the preparation, execution and delivery of this

Agreement, the Notes, the other Loan Documents and the other documents to be delivered hereunder, including the reasonable fees and out-of-pocket expenses of counsel for the Syndication Agent with respect thereto and with respect to advising the Syndication Agent as to its rights and responsibilities under this Agreement, the Notes and the other Loan Documents, and any modification, supplement or waiver of any of the terms of this Agreement or any other Loan Document, (b) all reasonable costs and expenses of any Bank and any other holder of an interest in the Notes, and the Obligations of the Company hereunder and under the Loan Documents, including reasonable legal fees and expenses, in connection with the enforcement of this Agreement, the Notes and the other Loan Documents and (c) reasonable costs and expenses incurred in connection with third party professional services required by the Syndication Agent, such as appraisers, environmental consultants, accountants or similar Persons; provided that prior to any Event of Default

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hereunder, such Agent will first obtain the consent of the Company to such expense, which consent shall not be unreasonably withheld. Without prejudice to the survival of any other obligations of the Company hereunder and under the Notes, the obligations of the Company under this Section shall survive the termination of this Agreement or the replacement of any Agent and each assignment of the Notes.

SECTION 12.5 Indemnity.

(a) The Company shall and hereby does indemnify each Agent and each Bank and each Affiliate thereof and their respective directors, officers, employees and agents from, and hold each of them harmless against, any and all losses, liabilities, claims or damages (including reasonable legal fees and expenses) to which any of them may become subject, insofar as such losses, liabilities, claims or damages arise out of or result from any actual or proposed use by the Company of the proceeds of any extension of credit hereunder or any investigation, litigation or other proceeding (including any threatened investigation or proceeding) relating to the foregoing or any of the other Loan Documents, including, without limitation, any of the foregoing relating to the violations of, noncompliance with or liability under any Environmental Law applicable to the operations of the Company, any of its Subsidiaries or any of their respective Property, and the Company shall reimburse each Agent, each Bank and each Affiliate thereof and their respective directors, officers, employees and agents, upon demand for any expenses (including legal fees) reasonably incurred in connection with any such investigation or proceeding; but excluding any such losses, liabilities, claims, damages or expenses incurred by reason of the gross negligence or willful misconduct of the Person to be indemnified (the "Indemnified Obligations").

(b) WITHOUT LIMITING ANY PROVISION OF THIS AGREEMENT, IT IS THE EXPRESS INTENTION OF THE PARTIES HERETO THAT EACH PERSON TO BE INDEMNIFIED HEREUNDER SHALL BE INDEMNIFIED AND HELD HARMLESS AGAINST ANY AND ALL INDEMNIFIED OBLIGATIONS: (i) ARISING OUT OF OR RESULTING FROM THE ORDINARY SOLE OR CONTRIBUTORY NEGLIGENCE OF SUCH PERSON OR (ii) IMPOSED UPON SAID PARTY UNDER ANY THEORY OF STRICT LIABILITY. Without prejudice to the survival of any other obligations of the Company hereunder and under the other Loan Documents, the obligations of the Company under this Section shall survive the termination of this Agreement and the other Loan Documents and the payment of the Obligations or the assignment of the Notes.

SECTION 12.6 Right of Setoff. Without limiting the remedies provided for in Article X, each Bank is hereby authorized at any time and from time to

time, to the fullest extent permitted by law, to set off and apply any and all deposits held and other indebtedness owing by such Bank, or any branch, subsidiary or Affiliate, to or for the credit or the account of the Company against any and all the Obligations of the Company now or hereafter existing under this Agreement and the other Loan Documents and other obligations of the Company held by such Bank, irrespective of whether or not such Bank shall have made any demand under this Agreement, its Note or the Obligations and although the Obligations may be unmatured. The rights of each Bank under this Section are in addition to other rights and remedies (including other rights of setoff) which such Bank may have.

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SECTION 12.7 Governing Law. This Agreement, all Notes, the other Loan Documents and all other documents executed in connection herewith shall be deemed to be contracts and agreements executed by the Company and each Bank under the laws of the State of New York and of the United States of America and for all purposes shall be construed in accordance with, and governed by, the laws of said state and of the United States of America. Without limitation of the foregoing, nothing in this Agreement, or in the Notes or in any other Loan Document shall be deemed to constitute a waiver of any rights which any Bank may have under applicable federal legislation relating to the amount of interest which such Bank may contract for, take, receive or charge in respect of the Loan and the Loan Documents, including any right to take, receive, reserve and charge interest at the rate allowed by the law of the state where any Bank is located. Each Agent, each Bank and the Company further agree that insofar as the provisions of V.T.C.A., Finance Code, Chapter 303, as amended, are applicable to the determination of the Highest Lawful Rate with respect to the Notes and the Obligations hereunder and under the other Loan Documents, the indicated rate ceiling of such Article shall be applicable; provided, however, that to the extent permitted by such Article, the Administrative Agent may from time to time by notice to the Company revise the election of such interest rate ceiling as such ceiling affects the then current or future balances of the Loans. The provisions of V.T.C.A., Finance Code, Chapter 346, do not apply to this Agreement, any Note issued hereunder or the other Loan Documents.

SECTION 12.8 Interest. Each provision in this Agreement and each other Loan Document is expressly limited so that in no event whatsoever shall the amount paid, or otherwise agreed to be paid, to the Administrative Agent or any Bank, or charged, contracted for, reserved, taken or received by the Administrative Agent or any Bank, for the use, forbearance or detention of the money to be loaned under this Agreement or any Loan Document or otherwise (including any sums paid as required by any covenant or obligation contained herein or in any other Loan Document which is for the use, forbearance or detention of such money), exceed that amount of money which would cause the effective rate of interest to exceed the Highest Lawful Rate, and all amounts owed under this Agreement and each other Loan Document shall be held to be subject to reduction to the effect that such amounts so paid or agreed to be paid, charged, contracted for, reserved, taken or received which are for the use, forbearance or detention of money under this Agreement or such Loan Document shall in no event exceed that amount of money which would cause the effective rate of interest to exceed the Highest Lawful Rate. Anything in any Note or any other Loan Document to the contrary notwithstanding, the Company shall not be required to pay unearned interest on any Note and the Company shall not be required to pay interest on the Obligations at a rate in excess of the Highest Lawful Rate, and if the effective rate of interest which would otherwise be payable under such Note and such Loan Documents would exceed the Highest Lawful Rate, or if the holder of such Note shall receive any unearned interest or shall receive monies that are deemed to constitute interest which would increase the effective rate of interest payable by the Company under such Note and the other Loan Documents to a rate in excess of the Highest Lawful Rate,

then (a) the amount of interest which would otherwise be payable by the Company shall be reduced to the amount allowed under applicable law and (b) any unearned interest paid by the Company or any interest paid by the Company in excess of the Highest Lawful Rate shall in the first instance be credited on the principal of the Obligations of the Company (or if all such Obligations shall have been paid in full, refunded to the Company). It is further agreed that, without limitation of the foregoing, all calculations of the rate of interest contracted for, reserved, taken, charged or received by any

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Bank under the Notes and the Obligations and under the other Loan Documents are made for the purpose of determining whether such rate exceeds the Highest Lawful Rate, and shall be made, to the extent permitted by usury laws applicable to such Bank, by amortizing, prorating and spreading in equal parts during the period of the full stated term of the Notes and this Agreement all interest at any time contracted for, charged or received by such Bank in connection therewith. Furthermore, in the event that the maturity of any Note or other obligation is accelerated or in the event of any required or permitted prepayment, then such consideration that constitutes interest under applicable law may never include more than the maximum amount allowed by applicable law and excess interest, if any, provided for in this Agreement, any Note or otherwise shall be canceled automatically as of the date of such acceleration or prepayment and, if theretofore paid, shall be refunded to the Company.

SECTION 12.9 Survival of Representations and Warranties. All representations, warranties and covenants contained herein or made in writing by the Company in connection herewith and the other Loan Documents shall survive the execution and delivery of this Agreement, the Notes and the other Loan Documents, the termination of the Commitments of the Banks and will bind and inure to the benefit of the respective successors and assigns of the parties hereto, whether so expressed or not, provided, that the Commitments of the Banks shall not inure to the benefit of any successor or assign of the Company.

SECTION 12.10 Successors and Assigns; Participations.

(a) All covenants, promises and agreements by or on behalf of the Company or the Banks that are contained in this Agreement shall bind and inure to the benefit of their respective permitted successors and assigns. Neither the Company nor any Guarantor may assign or transfer any of its rights or obligations hereunder.

(b) Any of the Banks may assign to or sell participations to one or more banks of all or a portion of its rights and obligations under this Agreement and the other Loan Documents (including all or a portion of its Commitment, the Advances and the Obligations of the Company owing to it and the Notes); provided, that the participating banks or other entities shall be entitled to the cost protection provisions contained in Article II and Section 12.4 and the Company shall continue to deal solely and directly with the Administrative Agent in connection with its rights and obligations under this Agreement and the other Loan Documents. Except with respect to cost protections provided to a participant pursuant to this paragraph and the items listed in Section 12.1 hereof, no participant shall be a third party beneficiary of this Agreement nor shall it be entitled to enforce any rights provided to the Banks against the Company under this Agreement. Notwithstanding the foregoing, no Bank shall transfer or grant any participation under which the participant shall have rights to approve any amendment to or waiver of this Agreement or any other Loan Document except to the extent such amendment or waiver would (i) extend the final scheduled maturity of any Loan, Note or Letter of Credit (unless such Letter of Credit is not extended beyond the Maturity Date) in which such participant is participating, or reduce

the rate or extend the time of payment of interest or fees thereon (except in connection with a waiver of applicability of any post-default increase in interest rates) or reduce the principal amount thereof, or increase the amount of the participant's participation over the amount thereof then in

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effect (it being understood that a waiver of any Default or Event of Default or of a mandatory reduction in the Total Commitment, shall not constitute a change in the terms of such participation, and that an increase in Commitment or any Loan shall be permitted without the consent of any participant if the participant's participation is not increased as a result thereof).

(c) A Bank may assign to any other Bank or Banks or to any Affiliate of a Bank and, with the prior written consent of the Company (so long as no Event of Default exists) and the Administrative Agent (which consent shall not be unreasonably withheld), a Bank may assign to one or more other Eligible Assignees all or a portion of its interests, rights, and obligations under this Agreement and the other Loan Documents (including all or a portion of its Commitment and the same portion of the Loans and other Obligations of the Company at the time owing to it and the Note held by it); provided, however, that (i) each such assignment shall be in a minimum principal amount of not less than \$5,000,000.00, or 100% of such Bank's outstanding Loans, all Types of Loans and shall be of a constant, and not a varying, percentage of all the assigning Bank's Commitment, rights and obligations under this Agreement, (ii) the parties to each such assignment shall execute and deliver to the Administrative Agent, for its acceptance, an Assignment and Acceptance, substantially in the form of Exhibit 12.10(c) hereto, in form and substance satisfactory to the Administrative Agent (an "Assignment and Acceptance") and any Note subject to such assignment and (iii) no assignment shall be effective until receipt by the Administrative Agent of a reasonable service fee from the assignee in respect of said assignment equal to \$2,000.00. Upon such execution, delivery, acceptance and recording, from and after the effective date specified in each Assignment and Acceptance, which effective date (unless otherwise agreed to by the assigning Bank, the Eligible Assignee thereunder and the Administrative Agent) shall be at least five Business Days after the execution thereof, (x) the Eligible Assignee thereunder shall be a party hereto and to the other Loan Documents and, to the extent provided in such Assignment and Acceptance, have the rights and obligations of a Bank hereunder and under the other Loan Documents and (y) the assignor Bank thereunder shall, to the extent provided in such Assignment and Acceptance, be released from its obligations under this Agreement and the other Loan Documents (and, in the case of an Assignment and Acceptance covering all of the remaining portion of an assigning Bank's rights and obligations under this Agreement and the other Loan Documents, such Bank shall cease to be a party hereto).

(d) Notwithstanding any other provision herein, any Bank may, in connection with any assignment or participation or proposed assignment or participation pursuant to this section, disclose to the assignee or participant or proposed assignee or participant, any information relating to the Company furnished to such Bank by or on behalf of the Company.

SECTION 12.11 Confidentiality. Each Bank agrees to exercise its best efforts to keep any information delivered or made available by the Company to it which is clearly indicated to be confidential information, confidential from anyone other than Persons employed or retained by such Bank who are or are

expected to become engaged in evaluating, approving, structuring or administering the Loans; provided that nothing herein shall prevent any Bank from

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disclosing such information (a) to any other Bank, (b) pursuant to subpoena or upon the order of any court or administrative agency, (c) upon the request or demand of any regulatory agency or authority having jurisdiction over such Bank, (d) which has been publicly disclosed, (e) to the extent reasonably required in connection with any litigation to which the Administrative Agent, any Bank, the Company or its respective Affiliates may be a party, (f) to the extent reasonably required in connection with the exercise of any remedy hereunder, (g) to such Bank's legal counsel and independent auditors and (h) to any actual or proposed participant or assignee of all or part of its rights hereunder which has agreed in writing to be bound by the provisions of this Section. Each Bank will promptly notify the Company of any information that it is required or requested to deliver pursuant to clause (b) or (c) of this Section and, if the Company is a party to any such litigation, clause (e) of this Section.

SECTION 12.12 Pro Rata Treatment.

(a) Except as otherwise specifically permitted hereunder, each payment or prepayment of principal, if permitted under this Agreement, and each payment of interest with respect to an Advance shall be made pro rata among the Banks.

(b) Each Bank agrees that if, through the exercise of a right of banker's Lien, setoff or claim of any kind against the Company as a result of which the unpaid principal portion of the Notes and the Obligations held by it shall be proportionately less than the unpaid principal portion of the Notes and Obligations held by any other Bank, it shall be deemed to have simultaneously purchased from such other Bank a participation in the Notes and Obligations held by such other Bank, in the amount required to render such amounts proportional; provided, however, that if any such purchase or purchases or adjustments shall be made pursuant to this Section and the payment giving rise thereto shall thereafter be recovered, such purchase or purchases or adjustments shall be rescinded to the extent of such recovery and the purchase price or prices or adjustments restored without interest. Each Bank purchasing participations pursuant to this clause may exercise all rights of collection, set-off and banker's liens with respect to such participations as if such Bank were a holder of a direct Loan to the Company.

SECTION 12.13 Separability. Should any clause, sentence, paragraph or Section of this Agreement be judicially declared to be invalid, unenforceable or void, such decision will not have the effect of invalidating or voiding the remainder of this Agreement, and the parties hereto agree that the part or parts of this Agreement so held to be invalid, unenforceable or void will be deemed to have been stricken herefrom and the remainder will have the same force and effectiveness as if such part or parts had never been included herein.

SECTION 12.14 Execution in Counterparts. This Agreement may be executed in any number of counterparts and by different parties hereto in separate counterparts, each of which when so executed shall be deemed to be an original and all of which taken together shall constitute one and the same agreement. Any Subsidiary of the Company that executes this Agreement after the date of this Agreement shall, upon such execution, become a party hereto as a Guarantor.

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SECTION 12.15 Interpretation.

(a) In this Agreement, unless a clear contrary intention appears:

(i) the singular number includes the plural number and vice versa;

(ii) reference to any gender includes each other gender;

(iii) the words "herein," "hereof" and "hereunder" and other words of similar import refer to this Agreement as a whole and not to any particular Article, Section or other subdivision;

(iv) reference to any Person includes such Person's successors and assigns but, if applicable, only if such successors and assigns are permitted by this Agreement, and reference to a Person in a particular capacity excludes such Person in any other capacity or individually, provided at nothing in this clause is intended to authorize any assignment not otherwise permitted by this Agreement;

(v) except as expressly provided to the contrary herein, reference to any agreement, document or instrument (including this Agreement) means such agreement, document or instrument as amended, supplemented or modified and in effect from time to time in accordance with the terms thereof and, if applicable, the terms hereof, and reference to any Note or other note includes any Note issued pursuant hereto in extension or renewal thereof and in substitution or replacement therefor;

(vi) unless the context indicates otherwise, reference to any Article, Section, Schedule or Exhibit means such Article or Section hereof or such Schedule or Exhibit hereto;

(vii) the words "including" (and with correlative meaning "include") means including, without limiting the generality of any description preceding such term;

(viii) with respect to the determination of any period of time, except as expressly provided to the contrary, the word "from" means "from and including" and the word "to" means "to but excluding"; and

(ix) reference to any law, rule or regulation means such as amended, modified, codified or reenacted, in whole or in part, and in effect from time to time.

(b) The Article and Section headings herein and the Table of Contents are for convenience only and shall not affect the construction hereof.

(c) No provision of this Agreement shall be interpreted or construed against any Person solely because that Person or its legal representative drafted such provision.

(d) In the event of any conflict between the specific provisions of this Agreement and the provisions of any application pertaining to any Letter of Credit, the terms of this Agreement shall control.

SECTION 12.16 SUBMISSION TO JURISDICTION.

(a) ANY LEGAL ACTION OR PROCEEDING WITH RESPECT TO THIS AGREEMENT AND THE OTHER LOAN DOCUMENTS MAY BE BROUGHT IN THE COURTS OF THE STATE OF NEW YORK, IN NEW YORK COUNTY OR OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK AND, BY EXECUTION AND DELIVERY OF THIS AGREEMENT, EACH OF THE COMPANY AND EACH GUARANTOR HEREBY IRREVOCABLY ACCEPTS FOR ITSELF AND IN RESPECT OF ITS PROPERTY, UNCONDITIONALLY, THE JURISDICTION OF THE AFORESAID COURTS WITH RESPECT TO ANY SUCH ACTION OR PROCEEDING. THE COMPANY AND EACH GUARANTOR FURTHER IRREVOCABLY CONSENT TO THE SERVICE OF PROCESS OUT OF ANY OF THE AFOREMENTIONED COURTS IN ANY SUCH ACTION OR PROCEEDING BY THE MAILING OF COPIES THEREOF BY REGISTERED OR CERTIFIED MAIL, POSTAGE PREPAID, TO IT AT ITS ADDRESS PROVIDED IN Section 12.2 AND WITH RESPECT TO ANY GUARANTOR, AT THE ADDRESS PROVIDED ON SCHEDULE 6.16 HERETO, SUCH SERVICE TO BECOME EFFECTIVE THIRTY (30) DAYS AFTER SUCH MAILING. NOTHING HEREIN SHALL AFFECT THE RIGHT OF THE ADMINISTRATIVE AGENT OR ANY BANK TO SERVE PROCESS IN ANY OTHER MANNER PERMITTED BY LAW OR TO COMMENCE LEGAL PROCEEDINGS OR OTHERWISE PROCEED AGAINST THE COMPANY IN ANY OTHER JURISDICTION. THE SUBMISSION TO JURISDICTION CONTAINED IN THIS SECTION IS NON-EXCLUSIVE.

(b) EACH OF THE COMPANY AND THE GUARANTORS HEREBY IRREVOCABLY WAIVES ANY OBJECTION WHICH IT MAY NOW OR HEREAFTER HAVE TO THE LAYING OF VENUE OF ANY OF THE AFORESAID ACTIONS OR PROCEEDINGS ARISING OUT OF OR IN CONNECTION WITH THIS AGREEMENT BROUGHT IN THE COURTS REFERRED TO IN Section 12.16(A) ABOVE AND HEREBY FURTHER IRREVOCABLY WAIVES AND AGREES NOT TO PLEAD OR CLAIM IN ANY SUCH COURT THAT ANY SUCH ACTION OR PROCEEDING BROUGHT IN ANY SUCH COURT HAS BEEN BROUGHT IN AN INCONVENIENT FORUM.

SECTION 12.17 WAIVER OF JURY TRIAL. EACH OF THE COMPANY AND EACH GUARANTOR HEREBY WAIVES, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ANY RIGHT TO A TRIAL BY JURY IN ANY ACTION OR PROCEEDING TO ENFORCE OR DEFEND ANY RIGHTS UNDER THIS AGREEMENT OR UNDER ANY AMENDMENT, INSTRUMENT, DOCUMENT OR AGREEMENT DELIVERED OR WHICH MAY IN THE FUTURE BE DELIVERED IN CONNECTION HERewith OR ARISING FROM OR RELATING TO ANY BANKING RELATIONSHIP EXISTING IN CONNECTION WITH THIS AGREEMENT, AND AGREES, TO THE

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EXTENT PERMITTED BY APPLICABLE LAW, THAT ANY SUCH ACTION OR PROCEEDING SHALL BE TRIED BEFORE A COURT AND NOT BEFORE A JURY.

SECTION 12.18 Acknowledgment and Consent. The Company is a party to certain Collateral Documents pursuant to which the Company has created Liens in favor of the Agents on certain Collateral to secure the Obligations. Each of the Guarantors party hereto is a party to certain Collateral Documents and the Guaranty, pursuant to which each such Guarantor has (i) guaranteed the Obligations and (ii) created Liens in favor of the Administrative Agent on certain Collateral to secure the Guaranteed Obligations of such Guarantor under the Guaranty. The Guarantors party hereto are collectively referred to herein as

the "Credit Support Parties," and the Collateral Documents and the Guaranty are collectively referred to herein as the "Credit Support Documents."

Each Credit Support Party hereby acknowledges that it has reviewed the terms and provisions of this Agreement, the Collateral Documents and the Guaranty, and consents to the amendment and restatement of the Existing Credit Agreement effected pursuant to this Agreement. Each Credit Support Party and the Company hereby confirms that each of the Credit Support Documents to which it is a party or otherwise bound and all Collateral encumbered thereby will continue to guaranty or secure, as the case may be, to the fullest extent possible the payment and performance of all "Obligations," "Guaranteed Obligations" and "Secured Obligations," as the case may be (in each case as such terms are defined in the applicable Credit Support Document), including without limitation the payment and performance of all such "Obligations," "Guaranteed Obligations" or "Secured Obligations," as the case may be, in respect of the Obligations of the Company now or hereafter existing under or in respect of this Agreement, the Notes and the other Loan Documents.

Each Credit Support Party and the Company acknowledges and agrees that any of the Credit Support Documents to which it is a party or otherwise bound shall continue in full force and effect and that all of its obligations thereunder shall be valid and enforceable and shall not be impaired or limited by the execution or effectiveness of this Agreement. Each Credit Support Party and the Company represents and warrants that all representations and warranties contained in this Agreement and the other Credit Support Documents to which it is a party or otherwise bound are true, correct and complete in all material respects on and as of the Effective Date to the same extent as though made on and as of that date, except to the extent such representations and warranties specifically relate to an earlier date, in which case they were true, correct and complete in all material respects on and as of such earlier date.

Each Credit Support Party acknowledges and agrees that (i) notwithstanding the conditions to effectiveness set forth in this Agreement, such Credit Support Party is not required by the terms of this Agreement or any other Loan Document to consent to the amendments to the Existing Credit Agreement effected pursuant to this Agreement, and (ii) nothing in this Agreement or any other Loan Document shall be deemed to require the consent of such Credit Support Party to any future amendments to this Agreement.

SECTION 12.19 FINAL AGREEMENT OF THE PARTIES. THIS AGREEMENT (INCLUDING THE SCHEDULES AND EXHIBITS HERETO), THE NOTES AND THE OTHER LOAN DOCUMENTS CONSTITUTE A "LOAN AGREEMENT" AS

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DEFINED IN SECTION 26.02(a) OF THE TEXAS BUSINESS AND COMMERCE CODE, AND REPRESENT THE FINAL AGREEMENT BETWEEN THE PARTIES RELATING TO THE SUBJECT MATTER HEREOF AND THEREOF AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES. THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN THE PARTIES.

[Remainder of page intentionally left blank]

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IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed by their respective officers thereunto duly authorized as of the date first above written.

COMPANY:

COMFORT SYSTEMS USA, INC.

By:

J. Gordon Beittenmiller
Senior Vice President and
Chief Financial Officer

CREDIT SUPPORT PARTIES AND GUARANTORS:

AARON MECHANICAL, INC.
ACI MECHANICAL, INC.
A.C.I. MECHANICAL USA, INC.
ACCU-TEMP GP, INC.
ACCU-TEMP LP, INC.
ACCU-TEMP, LLC, by Accu-Temp LP, Inc.,
managing member
AIR SOLUTIONS USA, INC.
AMERICAN MECHANICAL INC.
AMERICAN REFRIGERATION CONTRACTORS, INC.
BATCHELOR'S MECHANICAL CONTRACTORS, INC.
BCM CONTROLS CORPORATION
CARSON BROTHERS, INC.
CEL, INC. (Casey Electric)
CENTRAL MECHANICAL CONSTRUCTION CO., INC.
CENTRAL MECHANICAL, INC.
CLIMATE CONTROL, INC.
COMFORT SYSTEMS USA G.P., INC.
COMFORT SYSTEMS USA (ARKANSAS), INC.
(fka River City Mechanical, Incorporated)
COMFORT SYSTEMS USA (BRISTOL), INC.
(fka Fred Hayes Mechanical Contractors, Inc.)
COMFORT SYSTEMS USA (CLEVELAND), INC.
(fka Tech Heating and Air Conditioning, Inc.)

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COMFORT SYSTEMS USA (HARTFORD), INC.
(fka The Harvey Robbin Company)
COMFORT SYSTEMS USA (PHILADELPHIA), INC.
(fka Lower Bucks Cooling and Heating
Corporation)
COMFORT SYSTEMS USA (SYRACUSE), INC.
(fka Armani Plumbing & Mechanical, Inc.)
COMFORT SYSTEMS USA (TEXAS), L.P., by
Comfort Systems USA G.P., Inc., sole
general partner
Comfort Systems USA (Intermountain), Inc.
CS44 ACQUISITION CORP. (Edmonds/Service
Refrigeration)
DESIGN MECHANICAL INCORPORATED
EASTERN HEATING & COOLING, INC.
EASTERN REFRIGERATION CO., INC.
EDS, INC. (Energy Development Services)
E.L. PRUITT COMPANY
ESS ENGINEERING, INC.

F&G MECHANICAL CORPORATION
GOTHAM AIR CONDITIONING SERVICE, INC.
GULFSIDE MECHANICAL, INC.
H & H PLUMBING & HEATING, INC.
H & M MECHANICAL, INC.
HELM CORPORATION
HELM CORPORATION SAN DIEGO
HESS MECHANICAL CORPORATION
HILLCREST SHEET METAL, INC.
INDUSTRIAL COOLING INC.
J & J MECHANICAL, INC.
JAMES AIR CONDITIONING ENTERPRISE INC.
KILGUST MECHANICAL, INC.
KUEMPEL SERVICE, INC.
LOWRIE ELECTRIC COMPANY, INC.
MANDELL MECHANICAL CORPORATION
MARTIN HEATING, INC.
MAXIMUM REFRIGERATION & AIR CONDITIONING
CORP.
MEADOWLANDS FIRE PROTECTION CORP.
MECHANICAL SERVICE GROUP, INC. (Page)
MJ MECHANICAL SERVICES, INC.
NEEL MECHANICAL CONTRACTORS, INC.
NOGLE & BLACK MECHANICAL, INC.
NORTH AMERICAN MECHANICAL, INC.

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NORTH JERSEY MECHANICAL CONTRACTORS, INC.
OK SHEET METAL AND AIR CONDITIONING, INC.
PLANT SERVICES INCORPORATED
QUALITY AIR HEATING & COOLING, INC.
RIVER CITY MECHANICAL, INC.
ROSS & ASSOCIATES, INC.
S&K AIR CONDITIONING CO., INC.
S.I. GOLDMAN COMPANY, INC.
S.M. LAWRENCE COMPANY, INC.
SA ASSOCIATES, INC. (formerly Salmon &
Alder, Inc.)
SALMON & ALDER, LLC, by SA Associates, Inc.,
sole member
SEASONAIR, INC.
SOUTHERN BLUEGRASS MECHANICAL, INC.
STANDARD HEATING & AIR CONDITIONING COMPANY
SUPERIOR MECHANICAL SYSTEMS
TARGET CONSTRUCTION, INC.
TEMP-RIGHT SERVICE, INC.
TEMPRITE AIR CONDITIONING AND
REFRIGERATION, INC.
THE CAPITAL REFRIGERATION COMPANY
THE FAGAN COMPANY
TRI-CITY MECHANICAL, INC.
TROOST SERVICE CO.
WALKER-J-WALKER, INC.
WEATHER ENGINEERING, INC.
WESTERN BUILDING SERVICES, INC.

By:

J. Gordon Beittenmiller, Vice President

ATLAS-ACCURATE HOLDINGS, L.L.C.
ATLAS-ACCURATE HOLDINGS, L.L.C., as the sole
general partner of
Accurate Air Systems, L.P. (restructure of
Accurate Air Systems, Inc.)
Atlas Air Conditioning Company, L.P.
(restructure of Atlas Air
Conditioning Company and Atlas Comfort
Services USA, Inc.)

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Border Electric, L.P.
Border Mechanical, L.P.
Mechanical Technical, L.P.
Shambaugh & Son, L.P. (restructure of
Shambaugh & Son,
Inc./Shambaugh & Son Conversion
Corporation)
United Environmental Services, L.P.
(restructure of United
Environmental Services, Inc./UES Conversion
Corporation)

By: CS48 ACQUISITION CORP., sole member

By:

J. Gordon Beittenmiller, Vice President

ADMINISTRATIVE AGENT/BANK:

Amount of Commitment
on the Effective
Date: \$40,500,000.00

BANK ONE, NA,
as Administrative Agent and Individually
as a Bank

By:

Name:

Title:

SYNDICATION AGENT/BANK:

Amount of Commitment
on the Effective
Date: \$31,500,000.00

BANKERS TRUST COMPANY,
as Syndication Agent and Individually as a Bank

By:

Name:

Title:

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DOCUMENTATION AGENT/BANK:

Amount of Commitment
on the Effective
Date: \$38,250,000.00

BANK OF AMERICA, N.A. (formerly known as
NationsBank, N.A.), as Documentation Agent
and Individually, as a Bank

By: _____
Name: _____
Title: _____

CO-AGENT/BANK:

Amount of Commitment
on the Effective
Date: \$22,500,000.00

CREDIT LYONNAIS NEW YORK BRANCH,
as Co-Agent and Individually, as a Bank

By: _____
Name: _____
Title: _____

CO-AGENT/BANK:

Amount of Commitment
on the Effective
Date: \$22,500,000.00

NATIONAL CITY BANK,
as Co-Agent and Individually, as a Bank

By: _____
Name: _____
Title: _____

CO-AGENT/BANK:

Amount of Commitment
on the Effective
Date: \$22,500,000.00

THE BANK OF NOVA SCOTIA, as Co-Agent and
Individually, as a Bank

By: _____
Name: _____
Title: _____

Amount of Commitment
on the Effective
Date: \$18,000,000.00

BANK:

UNION BANK OF CALIFORNIA, N.A.

By: -----

Name: -----

Title: -----

BANK:

Amount of Commitment
on the Effective
Date: \$13,500,000.00

COMERICA BANK

By: -----

Name: -----

Title: -----

BANK:

Amount of Commitment
on the Effective
Date: \$4,500,000.00

BANK POLSKA, KASA OPIEKI S.A., PEKOA
S.A. GROUP, New York Branch

By: -----

Name: -----

Title: -----

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BANK:

Amount of Commitment
on the Effective
Date: \$27,000,000.00

FIRSTAR BANK, NATIONAL ASSOCIATION

By: -----

Name: -----

Title: -----

BANK:

Amount of Commitment
on the Effective
Date: \$18,000,000.00

LASALLE BANK NATIONAL ASSOCIATION

By: -----
Name: -----
Title: -----

Amount of Commitment
on the Effective
Date: \$11,249,999.00

BANK:
GENERAL ELECTRIC CAPITAL
CORPORATION

By: -----
Name: -----
Title: -----

EMPLOYMENT AGREEMENT

THIS EMPLOYMENT AGREEMENT (this "Agreement") between COMFORT SYSTEMS USA, INC., a Delaware corporation (referred to herein individually as "Comfort" and collectively with its subsidiaries and affiliates as the "Company"), and Milburn E. Honeycutt ("Executive") is entered into and effective as of the 1st day of January, 1998. This Agreement supersedes any other employment agreements or understandings, written or oral, between the Company and Executive.

R E C I T A L S

The following statements are true and correct:

As of the date of this Agreement, the Company is engaged in the business of mechanical contracting services, including heating, ventilation and air conditioning, plumbing, piping, electrical and related services ("Services").

Executive is employed hereunder by the Company in a confidential relationship wherein Executive, in the course of Executive's employment with the Company, has and will continue to become familiar with and aware of information as to the Company's and its customers' specific manner of doing business, including the processes, techniques and trade secrets utilized by the Company, and future plans with respect thereto, all of which has been and will be established and maintained at great expense to the Company. This information is a trade secret and constitutes the valuable goodwill of the Company.

NOW, THEREFORE, in consideration of the mutual promises, terms, covenants and conditions set forth herein and the performance of each, the Company and Executive hereby agree as follows:

A G R E E M E N T S

1. Employment and Duties.

(a) The Company hereby employs Executive in an executive position and Executive hereby accepts this employment upon the terms and conditions herein contained. Executive agrees to devote substantially all of Executive's business time, attention and efforts to promote and further the business of the Company.

(b) Executive shall faithfully adhere to, execute and fulfill all lawful policies established by the Company, including the Company's Corporate Compliance Policy.

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(c) Executive shall not, during the term of Executive's employment hereunder, be engaged in any other business activity pursued for gain, profit or other pecuniary advantage if such activity interferes in any material respect with Executive's duties and responsibilities hereunder. The foregoing limitations shall not be construed as prohibiting Executive from making personal investments in such form or manner as will neither require Executive's services in the operation or affairs of the companies or enterprises in which such

investments are made nor violate the terms of Section 4 hereof.

2. Compensation. For all services rendered by Executive, the Company shall compensate Executive as follows:

(a) Base Salary. Effective the date hereof, the base salary payable to Executive shall be \$110,00 per year, payable on a regular basis in accordance with the Company's standard payroll procedures, but not less often than monthly. On at least an annual basis, the Company will review Executive's performance and may make increases to such base salary if, in its discretion, any such increase is warranted.

(b) Executive Perquisites, Benefits and Other Compensation. Executive shall be entitled to receive additional benefits and compensation from the Company in such form and to the extent specified below:

(i) Coverage, subject to contributions required of employees generally, for Executive and Executive's dependent family members under health, hospitalization, disability, dental, life and other insurance plans that the Company may have in effect from time to time for the benefit of its employees.

(ii) Reimbursement for all business travel and other out-of-pocket expenses reasonably incurred by Executive in the performance of Executive's services pursuant to this Agreement. Reimbursable expenses shall be appropriately documented in reasonable detail by Executive, and shall be in a format consistent with the Company's expense reporting policy.

3. Confidentiality.

(a) Confidential Information. As used herein, the term "Confidential Information" means any information, technical data or know-how of the Company, including, but not limited to, that which relates to customers, business affairs, business plans, financial matters, financial plans and projections, pending and proposed acquisitions, operational and hiring matters, contracts and agreements, marketing, sales and pricing, prospects of the Company, and any information, technical data or know-how that contain or reflect any of the foregoing, whether prepared by the Company, Executive or any other person or entity; provided, however, that the term "Confidential Information" shall not include information, technical data or know-how that Executive can demonstrate is generally available to the public not as a result of any breach of this Agreement by Executive.

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(b) No Disclosure. Except in the performance of Executive's duties as an employee of the Company, Executive will not, during or after the term of Executive's engagement with the Company, disclose to any person or entity or use, for any reason whatsoever, any Confidential Information.

4. Non-Competition Agreement.

(a) Competition. Executive will not, during the period of Executive's employment by or with the Company, and for a period of twelve months immediately following the termination of Executive's employment, for any reason whatsoever, directly or indirectly, on behalf of Executive or on behalf of or in conjunction with any other

person, company, partnership, corporation or business of whatever nature:

(i) engage, as an officer, director, shareholder, owner, partner, joint venturer, or in a managerial capacity, whether as an employee, independent contractor, consultant or advisor, or as a sales representative, or make or guarantee loans or invest in or for any business engaged in Services in competition with the Company within 100 miles of where the Company conducts or has conducted business during the Term (the "Territory");

(ii) call upon any person who is, at that time, within the Territory, an employee of the Company in a technical, managerial or sales capacity for the purpose or with the intent of enticing such employee away from or out of the employ of the Company;

(iii) call upon any person or entity which is, at that time, or which has been, within two (2) years prior to that time, a customer of the Company for the purpose of soliciting or selling Services;

(iv) call upon any prospective acquisition candidate, on Executive's own behalf or on behalf of any competitor, which candidate was either called upon by the Executive on behalf of the Company or for which the Executive made an acquisition analysis on behalf of the Company for the purpose of acquiring such entity.

Notwithstanding the above, the foregoing covenants shall not be deemed to prohibit Executive from acquiring as an investment not more than one percent (1%) of the capital stock of a competing business whose stock is traded on a national securities exchange or on an over-the-counter or similar market.

(b) No Violation. It is specifically agreed that the period during which the agreements and covenants of Executive made in this Section 4 shall be effective shall be

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computed by excluding from such computation any time during which Executive is in violation of any provision of this Section 4.

5. Term; Termination; Rights on Termination. The term of this Agreement shall begin on the date hereof and continue for two (2) (the "Term"), unless terminated sooner as herein provided. Beginning on the second anniversary and thereafter on each anniversary this Agreement shall renew for consecutive one-year terms unless either party shall give the other notice at least 30 days prior to such anniversary. This Agreement and Executive's employment may be terminated in any one of the following ways:

(a) Death. The death of Executive shall immediately terminate this Agreement with no severance compensation due to Executive's estate.

(b) Disability. If, as a result of incapacity due to physical or mental illness or injury, Executive shall have been absent from Executive's full-time duties hereunder for four (4) consecutive months, then thirty (30) days after receiving written notice (which notice may occur before or after the end of such four (4) month period, but which shall not be effective earlier than the last day of such four (4) month

period), the Company may terminate Executive's employment hereunder, provided Executive is unable to resume Executive's full-time duties at the conclusion of such notice period. In the event this Agreement is terminated as a result of Executive's disability, Executive shall receive from the Company Executive's base salary at the rate then in effect for the lesser of the time period remaining under the Term of this Agreement or for one (1) year, and such amount shall be payable during such period in a manner consistent with Company's standard pay practices. The amount payable hereunder shall be decreased by the amount of benefits otherwise actually paid by the Company to Executive or on Executive's behalf or under any insurance procured by the Company.

(c) Good Cause. The Company may terminate this Agreement ten (10) days after written notice to Executive for good cause, which shall be any of the following: (1) Executive's willful or material breach of this Agreement; (2) Executive's gross negligence in the performance or intentional nonperformance of any of Executive's material duties and responsibilities hereunder; (3) Executive's willful dishonesty, fraud or misconduct with respect to the business or affairs of the Company; (4) Executive's conviction of a felony crime; (5) Executive's confirmed positive illegal drug test result; (6) sexual harassment by Executive; or (7) willful or material failure by Executive to comply with the Company's Corporate Compliance Policy or other Company policies. In the event of a termination for good cause, as enumerated above, Executive shall have no right to any severance compensation.

(d) Without Cause. At any time after the commencement of Executive's employment, Executive or the Company may, without cause, terminate this Agreement and Executive's employment, effective thirty (30) days after receipt of written notice. Should Executive be terminated by the Company without cause, Executive shall receive from the Company Executive's base salary at the rate then in effect for the greater of the

time period remaining under the Term or for one (1) year, and such amount shall be payable during such period in a manner consistent with the Company's standard pay practices. If Executive resigns or otherwise terminates Executive's employment, Executive shall receive no severance compensation, provided, however, at any time after a change of control of the Company (i.e. a sale of a majority of the Comfort's capital stock, substantially all of Comfort's assets, or other transaction of similar effect), Executive may resign during the nine-month period immediately following consummation of such transaction if Executive's duties or compensation are materially diminished in any way, and in such event Executive shall be entitled to severance as if Executive had been terminated without cause.

6. Return of Company Property. All records, plans, manuals, "field guides", memoranda, lists, documents, statements and other property delivered to Executive by or on behalf of the Company, by any customer of the Company (including but not limited to, any such customers obtained by Executive), by any acquisition candidate of the Company, and all records compiled by Executive which pertain to the business or activities of the Company shall be and remain the property of the Company and shall be subject at all times to its discretion and control. Likewise, all correspondence with customers, representatives or acquisition candidates, reports, records, charts, advertising materials, and any data collected by Executive, or by or on behalf of the Company or any representative of the Company shall be delivered promptly to the Company without request by it upon termination of Executive's engagement with the Company.

7. Inventions. Executive shall disclose promptly to the Company any and

all significant conceptions and ideas for inventions, improvements and valuable discoveries, whether patentable or not, which are conceived or made by Executive, solely or jointly with another, during the period of Executive's employment or within one (1) year thereafter, and which are directly related to the business or activities of the Company or which Executive conceives as a result of Executive's employment by the Company. Executive hereby assigns and agrees to assign all Executive's interests therein to the Company or its nominee. Whenever requested to do so by the Company, Executive shall execute any and all applications, assignments or other instruments that the Company shall deem necessary to apply for and obtain Letters Patent of the United States or any foreign country or to otherwise protect the Company's interest therein.

8. Trade Secrets. Executive agrees that Executive will not, during or after the Term, disclose the specific terms of the Company's relationships or agreements with significant vendors or customers or any other significant and material trade secret of the Company, whether in existence or proposed, to any person, firm, partnership, corporation or business for any reason or purpose whatsoever.

9. No Prior Agreements. Executive hereby represents and warrants to the Company that the execution of this Agreement by Executive and Executive's employment by the Company and the performance of Executive's duties hereunder will not violate or be a breach of any agreement with a former employer, client or any other person or entity. Further, Executive agrees to indemnify the Company for any claim, including, but not limited to, attorneys' fees and

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expenses of investigation, by any such third party that such third party may now have or may hereafter come to have against the Company based upon or arising out of any non-competition agreement, invention or secrecy agreement between Executive and such third party which was in existence as of the date of this Agreement.

10. Assignment; Binding Effect. Executive understands that Executive has been selected for employment by the Company on the basis of Executive's personal qualifications, experience and skills. Executive agrees, therefore, that Executive cannot assign all or any portion of Executive's performance under this Agreement. Executive, Executive's spouse and the estates of each shall not have any right to encumber or dispose of any right to receive payments hereunder, it being understood that such payments and the right thereto are nonassignable and nontransferable; provided, however in the event of the death of Executive, any payments that Executive is entitled to receive may be assigned to the beneficiaries of Executive's estate. Subject to the preceding three (3) sentences and the express provisions of Section 11 below, this Agreement shall be binding upon, inure to the benefit of and be enforceable by the parties hereto and their respective heirs, legal representatives, successors and assigns.

11. Complete Agreement. Executive has no oral representations, understandings or agreements with the Company or any of its officers, directors or representatives covering the same subject matter as this Agreement. This Agreement is the final, complete and exclusive statement and expression of the agreement between the Company and Executive and of all the terms of this Agreement, and it cannot be varied, contradicted or supplemented by evidence of any prior or contemporaneous oral or written agreements.

12. Amendment; Waiver. This Agreement may not be modified except in writing signed by the parties, and no term of this Agreement may be waived except by a writing signed by the party waiving the benefit of such terms. No waiver by the parties hereto of any default or breach of any term, condition or covenant of this Agreement shall be deemed to be a waiver of any subsequent default or breach of the same or any other term, condition or covenant contained

herein.

13. Notice. Whenever any notice is required hereunder, it shall be given in writing addressed as follows:

To the Company: Comfort Systems USA, Inc.
 Three Riverway, Suite 200
 Houston, TX 77056
 Attention: General Counsel

To Executive: Milburn E. Honeycutt
 815 Buckeye Place
 Missouri City, Texas 77459

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Notice shall be deemed given and effective on the earlier of five (5) days after the deposit in the U.S. mail of a writing addressed as above and sent first class mail, certified, return receipt requested, or when actually received. Either party may change the address for notice by notifying the other party of such change in accordance with this Section 13.

14. Severability; Enforceability. If any portion of this Agreement is held invalid or inoperative, the other portions of this Agreement shall be deemed valid and operative and, so far as is reasonable and possible, effect shall be given to the intent manifested by the portion held invalid or inoperative. Moreover, in the event any court of competent jurisdiction shall determine that the scope, time or territorial restrictions set forth in any covenant contained herein are unreasonable, then it is the intention of the parties that such restrictions be enforced to the fullest extent which the court deems reasonable, and this Agreement shall thereby be reformed. Each of the covenants contained in this Agreement shall be construed as an agreement independent of any other provision in this Agreement, and the existence of any claim or cause of action of Executive against the Company, whether predicated on this Agreement or otherwise, shall not constitute a defense to the enforcement by the Company of such covenants.

15. Survival. The provisions and covenants of Sections 3, 4, 6, 7 and 8 shall survive termination of this Agreement.

16. Specific Performance. Because of the difficulty of measuring economic losses to the Company as a result of a breach of the covenants contained in Sections 3, 4, 6, 7 and 8 and because of the immediate and irreparable damage that could be caused to the Company for which it would have no other adequate remedy, Executive agrees that the Company shall be entitled to specific performance and that such covenants may be enforced by the Company in the event of any breach or threatened breach by Executive, by injunctions, restraining orders and other appropriate equitable relief. Executive further agrees to waive any requirement for the securing or posting of any bond in excess of \$50,000 in connection with the obtaining of any such injunctive or any other equitable relief.

17. Arbitration. With the exception of Sections 4 and 8, any unresolved dispute or controversy arising under or in connection with this Agreement shall be settled exclusively by arbitration, conducted by a single arbitrator in Houston, Texas, in accordance with the National Rules for the Resolution of Employment Disputes of the American Arbitration Association ("AAA") then in effect, provided that the parties may agree to use arbitrators other than those provided by the AAA. The arbitrators shall not have the authority to add to, detract from, or modify any provision hereof nor to award punitive damages to any injured party. The arbitrators shall have the authority to order back pay, severance compensation, reimbursement of costs, including those incurred to

enforce this Agreement, and interest thereon. A decision by the arbitrator shall be final and binding. Judgment may be entered on the arbitrator's award in any court having jurisdiction. Responsibility for bearing the cost of the arbitration shall be determined by the arbitrator and shall be proportional to the arbitrator's decision on the merits.

18. Attorney's Fees. If any litigation is instituted to enforce or interpret the provisions of this Agreement or the transactions described herein, the prevailing party in such action shall be

entitled to recover such party's reasonable attorneys' fees and other costs from the other party hereto.

19. Governing Law. This Agreement shall be governed by and construed in accordance with the internal laws of the State of Texas.

20. Counterparts. This Agreement may be executed in multiple counterparts, each of which shall be deemed to be an original and all of which together shall constitute one and the same instrument.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

EXECUTIVE:

COMPANY:

COMFORT SYSTEMS USA, INC.

/s/ Milburn Honeycutt

/s/ J. Gordon Beittenmiller

Milburn E. Honeycutt

J. Gordon Beittenmiller
Senior Vice President

COMFORT SYSTEMS USA, INC.
LIST OF SUBSIDIARIES

ENTITY NUMBER -----	NAME OF ENTITY -----	STATE OF ORGANIZATION -----
1.	Aaron Mechanical, Inc.	Michigan
2.	ACI Mechanical, Inc.	Delaware
3.	A.C.I. Mechanical USA, Inc.	Delaware
4.	Accurate Air Systems, L.P.	Texas
5.	Accu-Temp GP, Inc.	Delaware
6.	Accu-Temp LP, Inc.	Delaware
7.	Accu-Temp, LLC	Indiana
8.	Air Solutions USA, Inc.	Delaware
9.	Air Temp, Inc.	Delaware
10.	American Mechanical Inc.	Michigan
11.	American Refrigeration Contractors, Inc.	Delaware
12.	Atlas-Accurate Holdings, L.L.C.	Delaware
13.	Atlas Air Conditioning Company, L.P.	Texas
14.	Batchelor's Mechanical Contractors, Inc.	Alabama
15.	BCM Controls Corporation	Massachusetts
16.	Border Electric Co., L.P.	Texas
17.	Border Mechanical Co., L.P.	Texas
18.	Carson Brothers, Inc.	Montana
19.	CEL, Inc. (Casey Electric)	Delaware
20.	Central Mechanical Construction Co. , Inc.	Delaware
21.	Central Mechanical, Inc.	Delaware
22.	Climate Control, Inc.	Delaware
23.	Comfort Systems USA (Arkansas), Inc.	Delaware
24.	Comfort Systems USA (Bristol), Inc.	Delaware
25.	Comfort Systems USA (Cleveland), Inc.	Ohio
26.	Comfort Systems USA (Florida), Inc.	Florida
27.	Comfort Systems USA G.P., Inc.	Delaware
28.	Comfort Systems USA (Hartford), Inc.	
29.	Comfort Systems USA (Intermountain), Inc. Utah	
30.	Comfort Systems USA National Service Organization, Inc.	Delaware
31.	Comfort Systems USA (Philadelphia), Inc.	Pennsylvania
32.	Comfort Systems USA (Syracuse), Inc.	New York
33.	Comfort Systems USA (Texas), L.P.	Texas
34.	CS44 Acquisition Corp. [Edmonds/Service Refrigeration]	Delaware
35.	CS48 Acquisition Corp.	Delaware
36.	Design Mechanical Incorporated	Delaware
37.	Eastern Heating & Cooling, Inc.	New York
38.	Eastern Refrigeration Co., Inc.	New York
39.	EDS, Inc. [Energy Development Services]	Minnesota

ENTITY NUMBER -----	NAME OF ENTITY -----	STATE OF ORGANIZATION -----
40.	E.L. Pruitt Company	Delaware
41.	ESS Engineering, Inc.	Delaware
42.	F&G Mechanical Corporation	Delaware
43.	FIX Reinsurance Corporation	Vermont
44.	Fred Hayes Mechanical Contractors, Inc.	Virginia
45.	Gotham Air Conditioning Service, Inc.	Delaware
46.	Gulfside Mechanical, Inc.	Delaware
47.	H & H Plumbing & Heating, Inc.	Delaware
48.	H & M Mechanical, Inc.	Delaware
49.	Helm Corporation	Colorado
50.	Helm Corporation San Diego	California
51.	Hess Mechanical Corporation	Delaware
52.	Hillcrest Sheet Metal, Inc.	Delaware
53.	Industrial Cooling Inc.	Delaware
54.	J & J Mechanical, Inc.	Kentucky
55.	James Air Conditioning Enterprise Inc.	Puerto Rico
56.	Kilgust Mechanical, Inc.	Delaware
57.	Kuempel Service, Inc.	Ohio
58.	Lowrie Electric Company, Inc.	Tennessee
59.	MDC Service Corporation	California
60.	Mandell Mechanical Corporation	New York
61.	Martin Heating, Inc.	Wyoming
62.	Maximum Refrigeration & Air Conditioning Corp.	Delaware
63.	Meadowlands Fire Protection Corp.	New Jersey
64.	Mechanical Service Group, Inc. [Page]	Delaware
65.	Mechanical Technical Services, L.P.	Texas
66.	MJ Mechanical Services, Inc.	Delaware
67.	Neel Mechanical Contractors, Inc.	Delaware
68.	NJM Service Co.	New Jersey
69.	Nogle & Black Mechanical, Inc.	Delaware
70.	North American Mechanical, Inc.	Delaware
71.	North Jersey Mechanical Contractors, Inc.	New Jersey
72.	OK Sheet Metal and Air Conditioning, Inc.	Delaware
73.	Outbound Services, Inc.	Delaware
74.	Plant Services Incorporated	Iowa
75.	Quality Air Heating & Cooling, Inc.	Michigan
76.	River City Mechanical, Inc.	Michigan
77.	RMC2 Mechanical Systems, Inc.	California
78.	Ross & Associates, Inc.	Delaware
79.	S&K Air Conditioning Co., Inc.	Georgia
80.	S. I. Goldman Company, Inc.	Delaware
81.	S.M. Lawrence Company, Inc.	Tennessee

COMFORT SYSTEMS USA, INC.
LIST OF SUBSIDIARIES

ENTITY NUMBER -----	NAME OF ENTITY -----	STATE OF ORGANIZATION -----
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82.	SA Associates, Inc.	Utah
83.	Salmon & Alder, LLC	Utah
84.	Seasonair, Inc.	Maryland
85.	Shambaugh & Son, L.P.	Texas
86.	Sheren Plumbing & Heating, Inc.	Delaware
87.	Southern Bluegrass Mechanical, Inc.	Delaware
88.	Standard Heating & Air Conditioning Company	Alabama
89.	Superior Mechanical Systems, Inc.	Delaware
90.	Target Construction, Inc.	Delaware
91.	Temp-Right Service, Inc.	Delaware
92.	Temprite Air Conditioning and Refrigeration, Inc.	Delaware
93.	The Capital Refrigeration Company	Delaware
94.	The Fagan Company	Kansas
95.	Tri-City Mechanical, Inc.	Arizona
96.	Troost Service Co.	Michigan
97.	United Environmental Services, L.P.	Texas
98.	Walker-J-Walker, Inc.	Tennessee
99.	Weather Engineering, Inc.	Delaware
100.	Western Building Services, Inc.	Colorado

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation of our report included in this Form 10-K, into the Company's previously filed Registration Statement on Form S-8 on October 16, 1997, File No. 333-38011, the Company's previously filed Registration Statement on Form S-4 on April 2, 1999, File No. 333-75595 and the Company's previously filed Registration Statements on Form S-8 on August 23, 2000, File No. 333-44356, File No. 333-44354, and File No. 333-44352.

ARTHUR ANDERSEN LLP

Houston, Texas
March 27, 2001