

SECURITIES AND EXCHANGE COMMISSION  
 WASHINGTON, D.C. 20549

FORM S-1  
 REGISTRATION STATEMENT  
 UNDER  
 THE SECURITIES ACT OF 1933

COMFORT SYSTEMS USA, INC.  
 (EXACT NAME OF REGISTRANT AS SPECIFIED IN CHARTER)

DELAWARE  
 (STATE OR OTHER JURISDICTION OF  
 INCORPORATION OR ORGANIZATION)

1711  
 (PRIMARY STANDARD INDUSTRIAL  
 CLASSIFICATION CODE NUMBER)

76-0526487  
 (I.R.S. EMPLOYER  
 IDENTIFICATION NUMBER)

FRED M. FERREIRA  
 CHIEF EXECUTIVE OFFICER  
 4801 WOODWAY DRIVE  
 SUITE 300E  
 HOUSTON, TEXAS 77056  
 (800) 723-8430

(NAME AND ADDRESS, INCLUDING ZIP CODE, AND TELEPHONE NUMBER, INCLUDING  
 AREA CODE, OF REGISTRANT'S PRINCIPAL EXECUTIVE OFFICES AND AGENT FOR SERVICE)

COPIES TO:

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WILLIAM GEORGE  
 COMFORT SYSTEMS USA, INC.  
 4801 WOODWAY DRIVE  
 SUITE 300E  
 HOUSTON, TEXAS 77056

APPROXIMATE DATE OF COMMENCEMENT OF PROPOSED SALE TO THE PUBLIC: As soon  
 as practicable after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on  
 a delayed or continuous basis pursuant to Rule 415 under the Securities Act of  
 1933, check the following box.

If this Form is filed to register additional securities for an offering  
 pursuant to Rule 462(b) under the Securities Act, please check the following box  
 and list the Securities Act registration statement number of the earlier  
 effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c)  
 under the Securities Act, check the following box and list the Securities Act  
 registration statement number of the earlier effective registration statement  
 for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434,  
 please check the following box.

CALCULATION OF REGISTRATION FEE

TITLE OF EACH CLASS OF SECURITIES TO BE REGISTERED	AMOUNT TO BE REGISTERED	PROPOSED MAXIMUM OFFERING PRICE PER SHARE(1)	PROPOSED MAXIMUM AGGREGATE OFFERING PRICE(1)	AMOUNT OF REGISTRATION FEE
Common Stock, \$.01 par value per share.....	8,000,000	\$17.8125	\$142,500,000	\$43,182

(1) Estimated solely for the purpose of calculating the registration fee  
 pursuant to Rule 457(c).

THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATE OR  
 DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT SHALL  
 FILE A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THIS REGISTRATION  
 STATEMENT SHALL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8(A) OF  
 THE SECURITIES ACT OF 1933 OR UNTIL THIS REGISTRATION STATEMENT SHALL BECOME  
 EFFECTIVE ON SUCH DATE AS THE COMMISSION, ACTING PURSUANT TO SAID SECTION 8(A),  
 MAY DETERMINE.

[LOGO]

COMFORT SYSTEMS USA, INC.

COMMON STOCK

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THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

This Prospectus covers 8,000,000 shares of common stock, \$.01 par value (the "Common Stock"), which may be offered and issued by Comfort Systems USA, Inc. (the "Company", or "Comfort") from time to time in connection with merger or acquisition transactions entered into by the Company. It is expected that the terms of acquisitions involving the issuance of securities covered by this Prospectus will be determined by direct negotiations with the owners or controlling persons of the businesses or assets to be merged with or acquired by the Company, and that the shares of Common Stock issued will be valued at prices reasonably related to the market prices of Common Stock either at the time the terms of a merger or acquisition are agreed upon or at or about the time shares are delivered. No underwriting discounts or commissions will be paid, although finder's fees may be paid from time to time with respect to specific mergers or acquisitions. Any person receiving any such fees may be deemed to be an underwriter within the meaning of the Securities Act of 1933, as amended (the "Securities Act").

The Company currently has 20,975,774 shares of its Common Stock listed on the New York Stock Exchange, of which 7,015,000 are registered and available for unrestricted trading in the public markets unless owned by affiliates of the Company. Application will be made to list the shares of Common Stock offered hereby on the New York Stock Exchange. On July 29, 1997, the closing price of the Common Stock on the New York Stock Exchange was \$17.625 per share as published in THE WALL STREET JOURNAL on July 30, 1997. The Company is subject to the informational requirements of the Exchange Act of 1934 and in accordance therewith files reports and other information with the Securities and Exchange Commission.

All expenses of this offering will be paid by the Company. The Company is a Delaware corporation and all references herein to the Company refer to the Company and its subsidiaries. The executive offices of the Company are located at 4801 Woodway, 300E, Houston, Texas 77056, and its telephone number is (800) 723-8431.

SEE "RISK FACTORS" ON PAGE 9 FOR A DISCUSSION OF CERTAIN RISK FACTORS THAT SHOULD BE CONSIDERED BEFORE ACQUIRING THE COMMON STOCK OFFERED HEREBY.

INFORMATION CONTAINED HEREIN IS SUBJECT TO COMPLETION OR AMENDMENT. A REGISTRATION STATEMENT RELATING TO THESE SECURITIES HAS BEEN FILED WITH THE SECURITIES AND EXCHANGE COMMISSION. THESE SECURITIES MAY NOT BE SOLD NOR MAY OFFERS TO BUY BE ACCEPTED PRIOR TO THE TIME THE REGISTRATION STATEMENT BECOMES EFFECTIVE. THIS PROSPECTUS SHALL NOT CONSTITUTE AN OFFER TO SELL OR THE SOLICITATION OF AN OFFER TO BUY NOR SHALL THERE BE ANY SALE OF THESE SECURITIES IN ANY STATE IN WHICH SUCH OFFER, SOLICITATION OR SALE WOULD BE UNLAWFUL PRIOR TO REGISTRATION OR QUALIFICATION UNDER THE SECURITIES LAWS OF ANY SUCH STATE.

THE COMPANY INTENDS TO FURNISH ITS STOCKHOLDERS WITH ANNUAL REPORTS CONTAINING FINANCIAL STATEMENTS AUDITED BY INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS AND WITH QUARTERLY REPORTS CONTAINING UNAUDITED SUMMARY FINANCIAL INFORMATION FOR EACH OF THE FIRST THREE QUARTERS OF EACH FISCAL YEAR.

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THE DATE OF THIS PROSPECTUS IS , 1997

## PROSPECTUS SUMMARY

IN CONNECTION WITH ITS INITIAL PUBLIC OFFERING ON JULY 2, 1997 (THE "IPO"), COMFORT SYSTEMS USA, INC. ACQUIRED, IN SEPARATE MERGER OR SHARE EXCHANGE TRANSACTIONS (THE "Mergers") IN EXCHANGE FOR CASH AND SHARES OF ITS COMMON STOCK, 12 COMPANIES ENGAGED PRINCIPALLY IN THE HEATING, VENTILATION AND AIR CONDITIONING ("HVAC") BUSINESS (EACH A "FOUNDING COMPANY" AND, COLLECTIVELY, THE "FOUNDING COMPANIES"). UNLESS OTHERWISE INDICATED, ALL REFERENCES TO THE "COMPANY" HEREIN INCLUDE THE FOUNDING COMPANIES, AND REFERENCES HEREIN TO "COMFORT SYSTEMS" MEAN COMFORT SYSTEMS USA, INC. PRIOR TO THE CONSUMMATION OF THE MERGERS.

THE FOLLOWING SUMMARY IS QUALIFIED IN ITS ENTIRETY BY, AND SHOULD BE READ IN CONJUNCTION WITH, THE MORE DETAILED INFORMATION AND THE COMBINED, PRO FORMA COMBINED AND INDIVIDUAL HISTORICAL FINANCIAL STATEMENTS, INCLUDING THE NOTES THERETO, APPEARING ELSEWHERE IN THIS PROSPECTUS.

UNLESS OTHERWISE INDICATED, ALL REFERENCES HEREIN TO COMMON STOCK INCLUDE BOTH COMMON STOCK, \$0.01 PAR VALUE, AND RESTRICTED VOTING COMMON STOCK, \$0.01 PAR VALUE (THE "RESTRICTED COMMON STOCK") OF COMFORT SYSTEMS.(1)

### THE COMPANY

Comfort Systems was founded in 1996 to become a leading national provider of comprehensive HVAC installation services and maintenance, repair and replacement of HVAC systems, focusing primarily on the commercial and industrial markets. On July 2, 1997, the Company acquired in separate, concurrent transactions twelve companies engaged principally in the HVAC business. These Founding Companies are: Accurate Air Systems, Inc., located in Houston, Texas; Atlas Air Conditioning Co., located in Houston, Texas; C.S.I. / Bonneville, located in Salt Lake City, Utah; Eastern Heating and Cooling Inc., located in Albany, New York; Freeway Heating and Air Conditioning, Inc., located in Bountiful, Utah; Quality Air Heating and Cooling, Inc., located in Grand Rapids, Michigan; Seasonair, Inc., located in Rockville, Maryland; S. M. Lawrence Co., Inc., located in Jackson, Tennessee; Standard Heating and Air Conditioning Co., located in Birmingham, Alabama; Tech Heating and Air Conditioning, Inc., located in Solon, Ohio; Tri-City Mechanical, Inc., located in Phoenix, Arizona; and Western Building Services, Inc., located in Denver, Colorado. The Company's commercial and industrial applications include office buildings, retail centers, apartment complexes, hotels, manufacturing plants and government facilities. The Company also provides specialized HVAC applications such as process cooling, control systems, electronic monitoring and process piping. Approximately 90% of the Company's pro forma combined 1996 revenues of \$167.5 million was derived from commercial and industrial customers, with approximately 53% of combined revenues attributable to installation services and 47% attributable to maintenance, repair and replacement services. Combined revenues of the Founding Companies, which have been in business an average of 39 years, increased at a compound annual growth rate of approximately 16% from 1994 through 1996.

Based on available industry data, the Company believes that the HVAC industry is highly fragmented with over 40,000 companies, most of which are small, owner-operated businesses with limited access to capital for modernization and expansion. The overall HVAC industry, including the commercial, industrial and residential markets, is estimated to generate annual revenues in excess of \$75 billion, over \$35 billion of which is in the commercial and industrial markets. The Company believes there is a significant opportunity for a well-capitalized national company to provide comprehensive HVAC services and that the fragmented nature of the HVAC industry will provide it with significant opportunities to consolidate commercial, industrial and residential HVAC businesses.

(1) Notre Capital Ventures II, L.L.C. ("Notre") holds 2,742,912 shares of Restricted Common Stock, which are entitled to elect one member of the Company's Board of Directors and to 0.55 of one vote for each share held on all other matters on which they are entitled to vote. Restricted Common Stock is convertible into one share of Common Stock under certain circumstances. See "Description of Capital Stock -- Common Stock and Restricted Common Stock."

The Company's commercial and industrial installation business targets "design and build" projects where the Company is responsible for designing, engineering and installing a cost-effective, energy-efficient system, customized to meet the specific needs of the building owner. Management believes that the "design and build" segment represents a faster growing and more profitable segment of the HVAC business than traditional "plan and spec" installation, which is generally awarded based on a bid process. In recent years, the Company has undertaken a shift from "plan and spec" to "design and build" projects with "design and build" revenues increasing from approximately 65% of installation revenues in 1994 to approximately 80% in 1996.

The Company also provides maintenance, repair and replacement of HVAC systems. Growth in this segment is driven by a number of factors, particularly (i) the aging of the installed base, (ii) the increasing energy efficiency, sophistication and complexity of HVAC systems and (iii) the increasing restrictions on the use of refrigerants commonly used in older HVAC systems. The energy efficiency and sophistication of new HVAC systems are encouraging building owners to upgrade and reconfigure their current HVAC systems. Moreover, the increasing sophistication and complexity of these HVAC systems are leading many commercial and industrial building owners and property managers to outsource maintenance and repair through service agreements with HVAC service providers. Service agreements lead to better utilization of personnel, link the customer with the Company should a major repair or replacement be needed and result in recurring revenues. The Company believes there is also an opportunity to expand its presence in the highly-fragmented residential maintenance, repair and replacement market. The replacement segment of the residential HVAC market has grown significantly in recent years as a result of the aging of the installed base of residential HVAC systems, the introduction of more energy-efficient systems and the upgrading of older homes with central air conditioning.

The Company plans to achieve its goal of becoming a leading national provider of comprehensive HVAC services by improving operations, emphasizing continued internal growth and expanding through acquisitions.

**OPERATING STRATEGY.** The Company believes there are significant opportunities to increase its profitability and that of subsequently acquired businesses. The key elements of the Company's operating strategy are:

**FOCUS ON COMMERCIAL AND INDUSTRIAL MARKETS.** The Company believes that the commercial and industrial HVAC markets are attractive because of their growth opportunities, diverse customer base, attractive margins and potential for long-term relationships with building owners and managers, general contractors and architects.

**OPERATE ON DECENTRALIZED BASIS.** The Company believes that, while maintaining strong operating and financial controls, a decentralized operating structure will retain the entrepreneurial spirit present in each of the Founding Companies and will allow the Company to capitalize on the considerable local and regional market knowledge and customer relationships possessed by each Founding Company.

**ACHIEVE OPERATING EFFICIENCIES.** The Company intends to use its increased purchasing power to gain volume discounts in areas such as HVAC components, raw materials, service vehicles, advertising, bonding and insurance. In addition, the Company will identify "best practices" that can be successfully implemented throughout its operations.

**ATTRACT AND RETAIN QUALITY EMPLOYEES.** The Company intends 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) improved benefits packages.

INTERNAL GROWTH. A key component of the Company's strategy is to continue the internal growth at the Founding Companies and subsequently acquired businesses. The key elements of the Company's internal growth strategy are:

CAPITALIZE ON SPECIALIZED TECHNICAL AND MARKETING STRENGTHS. The Company believes it will be able to expand the services it offers in its local markets by leveraging the specialized technical and marketing strengths of individual Founding Companies.

ESTABLISH NATIONAL MARKET COVERAGE. The Company believes that significant demand exists from large national companies to utilize the services of a single HVAC service provider and believes existing local and regional relationships can be expanded as it develops a nationwide network.

ACQUISITIONS. The Company believes that, due to the highly fragmented nature of the HVAC industry, it has a significant opportunity to achieve its acquisition strategy. The Company anticipates that acquisition candidates in the commercial and industrial markets will typically have annual revenues ranging from \$5 million to \$35 million. The key elements of the Company's acquisition strategy are:

ENTER NEW GEOGRAPHIC MARKETS. The Company will pursue acquisitions that are located in new geographic markets, are financially stable, and which will have the customer base, technical skills and infrastructure necessary to be a core business into which other HVAC service operations can be consolidated.

EXPAND WITHIN EXISTING MARKETS. Once the Company has entered a market, it will seek to acquire other well-established HVAC businesses operating within that region and will also pursue "tuck-in" acquisitions of smaller companies, whose operations can be integrated into an existing operation to leverage the Company's infrastructure.

ACQUIRE COMPLEMENTARY BUSINESSES. The Company will focus on the HVAC industry and may also acquire companies providing complementary services to the same customer base, such as commercial and industrial process piping and plumbing and electrical companies.

## RECENT DEVELOPMENTS

During late 1996 and early 1997, members of the Company's management team and certain consultants were assembled to pursue the consolidation of the Founding Companies. Notre, a consolidator of highly-fragmented industries, provided the Company with expertise regarding the consolidation process and advanced the Company the funds needed to pay organizational and Offering expenses. In connection therewith, during 1996 and January and February 1997, Comfort Systems sold an aggregate of 1,269,935 shares of Common Stock to management of and consultants to the Company at a price of \$0.01 per share. As a result, the Company recorded a non-recurring, non-cash compensation charge of \$11.6 million (the "Compensation Charge") in the first quarter of 1997, representing the difference between the amount paid for the shares and the estimated fair value of the shares on the date of sale. This Compensation Charge of \$11.6 million is not included in pro forma combined net income.

On July 2, 1997, the Company consummated the IPO and the Mergers. In connection therewith, the Company issued 7,015,000 shares of Common Stock at a price of \$13.00 per share (less underwriting discounts and commissions).

The aggregate consideration paid by Comfort Systems in the Mergers consisted of \$45.3 million in cash and 9,720,927 shares of Common Stock, plus the assumption of \$19.7 million of existing debt of the Founding Companies. The consideration paid by Comfort Systems for each Founding Company was negotiated by the parties and was based primarily upon the pro forma adjusted net income of each Founding Company. For a more detailed description of these transactions, see "Certain Transactions -- Organization of the Company."

Between January 1, 1997 and the date of the Mergers, each Founding Company which was a C Corporation, except Atlas, distributed to its stockholders an amount equal to its net income for the period from January 1, 1997 through the date of the Mergers (the "Interim Earnings Distributions"). These aggregate distributions were \$1.5 million and were funded from the Founding Companies' cash and from borrowings from existing sources available to the Founding Companies.

Comfort Systems USA, Inc. was incorporated in 1996 in Delaware. The Company's executive offices are located at 4801 Woodway, Suite 300E, Houston, Texas 77056, and its telephone number is (800) 723-8431.

## RISK FACTORS

The Common Stock offered hereby involves a high degree of risk. See "Risk Factors".

SUMMARY PRO FORMA COMBINED FINANCIAL DATA  
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

Comfort Systems acquired the Founding Companies in connection with the IPO. For financial statement presentation purposes, Comfort Systems has been identified as the "accounting acquirer." The following table presents unaudited pro forma combined financial data for the Company, adjusted for (i) the effects of the Mergers, (ii) the effects of certain pro forma adjustments to the historical financial statements described below and (iii) the consummation of the IPO and the application of the net proceeds therefrom. See "Selected Financial Data," the Unaudited Pro Forma Combined Financial Statements and the Notes thereto and the historical Financial Statements for Comfort Systems and certain of the Founding Companies and the Notes thereto included elsewhere in this Prospectus.

	PRO FORMA COMBINED(1)	
	TWELVE MONTHS ENDED	THREE MONTHS ENDED
	DECEMBER 31, 1996	MARCH 31, 1997
<b>INCOME STATEMENT DATA:</b>		
Revenues.....	\$167,525	\$39,505
Gross profit.....	47,813	10,705
Selling, general and administrative expenses(2)....	27,814	7,814
Goodwill amortization(3).....	3,495	874
Income from operations.....	16,504	2,017
Interest and other income (expense), net(4).....	(961)	(250)
Income before income taxes.....	15,543	1,767
Net income(5).....	7,928	847
Net income per share.....	0.44	0.05
Shares used in computing pro forma net income per share(6).....	18,180,311	18,180,311

	MARCH 31, 1997	
	PRO FORMA COMBINED	AS ADJUSTED(8)
<b>BALANCE SHEET DATA:(7)</b>		
Working capital(4).....	\$ (31,197)(9)	\$ 48,678
Total assets.....	188,683	220,389
Long-term debt, net of current maturities(4).....	14,292	14,292
Stockholders' equity(4).....	101,118	180,993

(1) The pro forma combined income statement data assume that the Mergers and the IPO were consummated on January 1, 1996 and are not necessarily indicative of the results the Company would have obtained had these events actually then occurred or of the Company's future results.

(2) The pro forma combined income statement data reflect an aggregate of \$6.6 million for the twelve months ended December 31, 1996 and \$428,000 for the three months ended March 31, 1997 in pro forma reductions in salaries, bonuses and benefits to the owners of the Founding Companies to which they have agreed prospectively (the "Compensation Differential") and does not include the Compensation Charge of \$11.6 million recorded in the first quarter of 1997.

(3) Consists of amortization of goodwill to be recorded as a result of the Mergers over a 40-year period and computed on the basis described in the Notes to the Unaudited Pro Forma Combined Financial Statements.

(4) Several of the Founding Companies were S Corporations. In connection with the Mergers, these Founding Companies made distributions to their stockholders totalling \$16.8 million, representing substantially all of their previously taxed undistributed earnings through March 31, 1997 (the "S Corporation Distributions"). In order to fund these distributions, the Founding Companies borrowed \$11.0 million from existing sources. Accordingly, pro forma interest expense has been increased by \$935,000 for the twelve months ended December 31, 1996 and \$207,000 for the three months ended March 31, 1997, pro forma working capital has been reduced by \$1.9 million, pro forma long-term debt has been increased by \$11.0 million and pro forma stockholders' equity has been reduced by \$12.9 million. Quality has declared S Corporation Distributions of \$3.9 million which have been recorded as a dividend payable to shareholder and reduction of stockholders' equity in the pro forma combined balance sheet data. This \$3.9 million is included in the \$16.8 million of S Corporation Distributions.

(5) Assuming a corporate income tax rate of 40% and the non-deductibility of goodwill.

(6) Includes (i) 2,969,912 shares issued to Notre, (ii) 1,269,935 shares issued to management of and consultants to Comfort Systems, (iii) 9,720,927 shares issued to owners of the Founding Companies and (iv) 4,219,537 of the 7,015,000 shares sold in the IPO necessary to pay the cash portion of the Merger consideration and expenses of the IPO and excludes 915,000 shares of common stock purchased by the underwriters pursuant to an overallotment option.

(7) The pro forma combined balance sheet data assume that the Mergers were consummated on March 31, 1997.

(8) Adjusted for the sale of the 7,015,000 shares of Common Stock offered in the IPO and the application of the estimated net proceeds therefrom, which includes 915,000 shares of common stock purchased by the underwriters pursuant to an overallotment option.

(9) Includes a \$45.3 million note payable to owners of the Founding Companies, representing the cash portion of the Merger consideration paid from a portion of the net proceeds of the IPO.



SUMMARY INDIVIDUAL FOUNDING COMPANY FINANCIAL DATA  
(IN THOUSANDS)

The following table presents summary income statement data for the Founding Companies for each of their three most recent fiscal years. Income from operations has not been adjusted for the Compensation Differential or to take into account increased costs associated with the Company's new corporate management and with being a public company. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Introduction."

	FISCAL YEARS ENDED(1)			THREE MONTHS ENDED MARCH 31, (2)	
	1994	1995	1996	1996	1997
<b>QUALITY:</b>					
Revenues.....	\$ 24,434	\$ 32,594	\$ 29,597	\$ 6,315	\$ 8,766
Income from operations.....	2,154	4,953	4,490	416	1,300
<b>ATLAS:</b>					
Revenues.....	21,848	22,444	30,030	6,207	6,115
Income from operations.....	105	643	2,101	120	496
<b>TRI-CITY:</b>					
Revenues.....	16,883	25,030	24,237	6,482	6,791
Income from operations.....	393	2,539	1,773	374	278
<b>LAWRENCE:</b>					
Revenues.....	12,758	12,568	17,163	3,280	4,565
Income (loss) from operations.....	112	(51)	67	(93)	541
<b>ACCURATE:</b>					
Revenues.....	9,763	12,171	16,806	3,161	2,642
Income (loss) from operations.....	(122)	213	499	27	21
<b>EASTERN:</b>					
Revenues.....	7,348	6,067	7,944	1,525	1,284
Income (loss) from operations.....	274	117	431	20	(103)
<b>CSI/BONNEVILLE:</b>					
Revenues.....	6,502	6,361	7,842	1,369	1,562
Income from operations.....	881	448	981	75	59
<b>TECH:</b>					
Revenues.....	6,923	6,960	7,537	1,075	1,656
Income from operations.....	593	948	1,680	46	57
<b>SEASONAIR:</b>					
Revenues.....	5,168	5,942	6,737	1,128	1,831
Income (loss) from operations.....	189	451	134	(62)	22
<b>WESTERN:</b>					
Revenues.....	4,149	4,112	6,494	1,185	1,072
Income (loss) from operations.....	161	(151)	744	96	29
<b>ALL OTHER FOUNDING COMPANIES(3):</b>					
Revenues.....	8,934	12,264	13,138	3,072	3,221
Income (loss) from operations.....	266	321	531	48	(22)

(1) The fiscal years presented are as follows: Quality -- the fiscal years ended March 31, 1995 and 1996 and the year ended December 31, 1996; Atlas and Accurate -- the fiscal years ended June 30, 1994 and 1995 and the year ended December 31, 1996; Lawrence -- the fiscal years ended October 31, 1994, 1995 and 1996; and Tri-City, Eastern, CSI/Bonneville, Tech, Seasonair and Western -- the years ended December 31.

(2) Lawrence's revenues and income from operations are for the three months ended January 31, 1996 and 1997.

(3) The other Founding Companies are Standard and Freeway, and data presented are for the years ended December 31, 1994, 1995 and 1996, in the case of Standard, and the fiscal years ended March 31, 1995 and 1996 and the year ended December 31, 1996, in the case of Freeway.

## RISK FACTORS

AN INVESTMENT IN THE SHARES OF COMMON STOCK OFFERED BY THIS PROSPECTUS INVOLVES A HIGH DEGREE OF RISK. IN ADDITION TO THE OTHER INFORMATION IN THIS PROSPECTUS, THE FOLLOWING RISK FACTORS SHOULD BE CONSIDERED CAREFULLY IN EVALUATING AN INVESTMENT IN THE COMMON STOCK. THIS PROSPECTUS CONTAINS CERTAIN FORWARD-LOOKING STATEMENTS. ACTUAL RESULTS COULD DIFFER MATERIALLY FROM THOSE PROJECTED IN THE FORWARD-LOOKING STATEMENTS AS A RESULT OF ANY NUMBER OF FACTORS, INCLUDING THE RISK FACTORS SET FORTH BELOW AND ELSEWHERE IN THIS PROSPECTUS.

ABSENCE OF COMBINED OPERATING HISTORY. Comfort Systems was founded in 1996 but conducted no operations and generated no revenues prior to the Mergers on July 2, 1997. The Founding Companies operated as separate independent entities prior to the IPO, and there can be no assurance that the Company will be able to integrate the operations of these businesses successfully or to institute the necessary systems and procedures, including accounting and financial reporting systems, to manage the combined enterprise on a profitable basis. The Company's management group has been assembled only recently, and there can be no assurance that the management group will be able to effectively manage the combined entity or successfully implement the Company's operating strategy, internal growth strategy and acquisition program. The pro forma combined historical financial results of the Founding Companies cover periods when the Founding Companies and Comfort Systems were not under common control or management and, therefore, may not be indicative of the Company's future financial or operating results. The inability of the Company to integrate the Founding Companies successfully would have a material adverse effect on the Company's business, financial condition and results of operations and would make it unlikely that the Company's acquisition program will be successful. See "Business -- Strategy" and "Management."

RISKS RELATED TO THE COMPANY'S ACQUISITION STRATEGY. The Company intends to grow significantly through the acquisition of additional HVAC and complementary businesses. The Company expects to face competition for acquisition candidates, which may limit the number of acquisition opportunities and may lead to higher acquisition prices. There can be no assurance that the Company will be able to identify, acquire or manage profitably additional businesses or to integrate successfully any acquired businesses into the Company without substantial costs, delays or other operational or financial problems. Further, acquisitions involve a number of special risks, including failure of the acquired business to achieve expected results, diversion of management's attention, failure to retain key personnel of the acquired business and risks associated with unanticipated events or liabilities, some or all of which could have a material adverse effect on the Company's business, financial condition and results of operations. Customer dissatisfaction or performance problems at a single acquired company could have an adverse effect on the reputation of the Company generally and render ineffective the Company's national sales and marketing initiatives. The Company may consider acquiring complementary businesses in the electrical, process piping and plumbing industries, and there can be no assurance that these complementary businesses can be successfully integrated. In addition, there can be no assurance that the Founding Companies or other businesses acquired in the future will achieve anticipated revenues and earnings. See "Business -- Strategy."

RISKS RELATED TO ACQUISITION FINANCING. The timing, size and success of the Company's acquisition efforts and the associated capital commitments cannot be readily predicted. The Company currently intends to finance future acquisitions by using shares of its Common Stock for all or a substantial portion of the consideration to be paid. If the Common Stock does not maintain a sufficient market value, or if potential acquisition candidates are otherwise unwilling to accept Common Stock as part of the consideration for the sale of their businesses, the Company may be required to utilize more of its cash resources, if available, in order to initiate and maintain its acquisition program. As of the date of the Mergers, the Company had \$34.6 million of proceeds available for future acquisition and working capital. If the Company does not have sufficient cash resources, its growth could be limited unless it is able to obtain additional capital through debt or equity financings. The Company has obtained a bank line of credit of \$75.0 million from Bank One, Texas, NA ("Bank One") for working capital and acquisitions. As of July 28, 1997, borrowings under the line of credit were \$17.3 million, which was used to repay existing indebtedness of the Founding Companies. The line of credit is subject to customary financial covenants and drawing conditions. See

"Management's Discussion and Analysis of Financial Condition and Results of Operations -- Combined Liquidity and Capital Resources."

**RISKS RELATED TO OPERATING AND INTERNAL GROWTH STRATEGY.** Key elements of the Company's strategy are to improve the profitability of the Founding Companies and subsequently acquired businesses and to continue to expand the revenues of the Founding Companies and any subsequently acquired businesses. The Company intends to seek to improve the profitability of the Founding Companies and any subsequently acquired businesses by various means, including increased purchasing efficiencies and a reduction, in some cases, of duplicative operating costs and overhead. The Company's ability to increase the revenues of the Founding Companies and any subsequently acquired company will be affected by various factors, including demand for new or replacement HVAC systems, the level of new construction, the Company's ability to expand the range of services offered to customers of individual Founding Companies and other acquired businesses, the Company's ability to develop national accounts and other marketing programs in order to attract new customers and the Company's ability to attract and retain a sufficient number of qualified HVAC technicians and other necessary personnel. Many of these factors are beyond the control of the Company, and there can be no assurance that the Company's operating and internal growth strategies will be successful or that it will be able to generate cash flow adequate for its operation and to support internal growth. See "Business -- Strategy."

**COMPETITION.** The HVAC industry is highly competitive and is served by small, owner-operated private companies and several large companies. Certain of these competitors may have lower overhead cost structures and may, therefore, be able to provide their services at lower rates than the Company. The HVAC industry is currently undergoing rapid consolidation on both a national and a regional level by other companies which have acquisition objectives which are the same as or similar to the Company's objectives. These companies and other consolidators may have greater financial resources than the Company to finance acquisition and internal growth opportunities and might be willing to pay higher prices than the Company for the same acquisition opportunities. Additionally, HVAC equipment manufacturers and certain public utilities are beginning to enter the maintenance, repair and replacement segment of the HVAC industry. These companies generally are better capitalized, have greater name recognition and may be able to provide these services at a lower cost. Consequently, the Company may encounter significant competition in its efforts to achieve both its acquisition and internal growth objectives as well as its operating strategy to increase the profitability of the Founding Companies and subsequently acquired companies. See "Business -- Competition."

**AVAILABILITY OF HVAC TECHNICIANS.** 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. Accordingly, the Company's ability to increase its productivity and profitability will be limited by its ability to employ, train and retain the skilled technicians necessary to meet the Company's service requirements. From time to time, there are shortages of qualified HVAC technicians, and there can be no assurance that the Company will be able to maintain an adequate skilled labor force necessary to operate efficiently, that the Company's labor expenses will not increase as a result of a shortage in the supply of skilled technicians or that the Company will not have to curtail its planned internal growth as a result of labor shortages. See "Business -- Employees" and " -- Recruiting, Training and Safety."

**SEASONAL AND CYCLICAL NATURE OF THE HVAC INDUSTRY.** The HVAC industry is subject to seasonal variations. Specifically, the demand for new installations is generally lower during the winter months due to reduced construction activity during inclement weather and less use of air conditioning during colder months. Demand for HVAC maintenance, repair and replacement services is generally higher in the second and third calendar quarters due to the increased use of air conditioning during warmer months. Accordingly, the Company expects its revenues and operating results generally will be lower in the first and fourth quarters. 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.

REGULATION. HVAC systems are subject to various environmental statutes and regulations, including the Clean Air Act and those regulating the production, servicing and disposal of certain ozone depleting refrigerants used in HVAC systems. There can be no assurance that the regulatory environment in which the Company operates will not change significantly in the future. Various local, state and federal laws and regulations impose licensing standards on technicians who install and service HVAC systems. The Company's failure to comply with these laws and regulations could subject it to substantial fines and the loss of its licenses. See "Business -- Governmental Regulation and Environmental Matters."

RELIANCE ON KEY PERSONNEL. The Company will be highly dependent on the continuing efforts of its executive officers and the senior management of the Founding Companies, and the Company likely will depend on the senior management of any significant business it acquires in the future. The business or prospects of the Company could be affected adversely if any of these persons does not continue in his management role until the Company is able to attract and retain qualified replacements. See "Management."

CONTROL BY EXISTING MANAGEMENT AND STOCKHOLDERS. The Company's executive officers and directors, former stockholders of the Founding Companies and entities affiliated with them beneficially own approximately 66.6% of the outstanding shares of Common Stock. These persons, if acting in concert, would be able to exercise control over the Company's affairs, to elect the entire Board of Directors and to control the outcome of any matter submitted to a vote of stockholders. See "Principal Stockholders."

SUBSTANTIAL PROCEEDS OF OFFERING PAYABLE TO AFFILIATES OF FOUNDING COMPANIES. Of the net proceeds of the IPO, \$45.3 million, or approximately 53.4%, were paid as the cash portion of the purchase price for the Founding Companies. Some of the recipients of these funds are directors of the Company or holders of more than 5% of the Common Stock.

BENEFITS TO NOTRE AND MANAGEMENT. Notre, management and certain consultants to the Company own in the aggregate 4,239,847 shares of Common Stock. These stockholders acquired their Common Stock at a price of \$0.01 per share. These parties own, in the aggregate, approximately 20% of the outstanding Common Stock. Of these shares of Common Stock, 2,742,912 shares are Restricted Common Stock, which are entitled to elect one member of the Company's Board of Directors and to 0.55 of one vote for each share held on all other matters on which they are entitled to vote. Holders of Restricted Common Stock are not entitled to vote on the election of any other directors and control in the aggregate 8.8% of the votes of all shares of Common Stock. See "Principal Stockholders."

NO PRIOR PUBLIC MARKET AND DETERMINATION OF OFFERING PRICE. Prior to the IPO, there was no public market for the Common Stock. The offering prices for the Common Stock to be issued pursuant to this registration statement will be determined by negotiation between the Company and in each instance, certain owners of the company to be acquired and may bear no relationship to the price at which the Common Stock will trade after the respective acquisition transactions. The Common Stock is listed on The New York Stock Exchange; however, there can be no assurance that an active trading market will be sustained subsequent to the IPO or the acquisition transactions. After the acquisition transaction, the market price of the Common Stock may be subject to significant fluctuations in response to numerous factors, including the timing of any acquisitions by the Company, variations in the Company's annual or quarterly financial results or those of its competitors, changes by financial research analysts in their estimates of the future earnings of the Company, conditions in the economy in general or in the Company's industry in particular, unfavorable publicity or changes in applicable laws and regulations (or judicial or administrative interpretations thereof) affecting the Company or the HVAC, process piping and plumbing and electrical services industries. From time to time, the stock market experiences significant price and volume volatility, which may affect the market price of the Common Stock for reasons unrelated to the Company's performance.

POTENTIAL EFFECT OF SHARES ELIGIBLE FOR FUTURE SALE ON PRICE OF COMMON STOCK. After the consummation of the Mergers, 20,975,774 shares of Common Stock were outstanding. The 7,015,000 shares sold in the IPO (other than shares that may have been or that may subsequently be purchased by affiliates of the Company) are freely tradable. The remaining outstanding shares may be resold publicly only following their registration under the Securities Act of 1933, as amended (the "Securities Act"), or pursuant to an

available exemption from registration (such as provided by Rule 144 following a one year holding period for previously unregistered shares). The holders of these remaining shares have certain rights to have their shares registered in the future under the Securities Act, but may not exercise such registration rights, and have agreed with the Company that they will not sell, transfer or otherwise dispose of any of their shares for one year following the closing of the IPO. See "Shares Eligible for Future Sale." On completion of the IPO, the Company also had outstanding options to purchase up to a total of 2,174,954 shares of Common Stock. In addition, the 8,000,000 shares to be issued pursuant to this registration statement may be freely traded after their issuance by persons not affiliated with the Company unless the Company contractually restricts their resale. The market price of the Common Stock might be adversely affected by the sale, or availability for sale, of substantial amounts of the Common Stock in the public market as described above.

POSSIBLE ANTI-TAKEOVER EFFECT OF CERTAIN CHARTER PROVISIONS. Comfort Systems' Amended and Restated Certificate of Incorporation (the "Certificate of Incorporation"), authorizes the Board of Directors to issue, without stockholder approval, one or more series of preferred stock having such preferences, powers and relative, participating, optional and other rights (including preferences over the Common Stock respecting dividends and distributions and voting rights) as the Board of Directors may determine. The issuance of this "blank-check" preferred stock could render more difficult or discourage an attempt to obtain control of the Company by means of a tender offer, merger, proxy contest or otherwise. In addition, the Certificate of Incorporation provides for a classified Board of Directors, which may also have the effect of inhibiting or delaying a change in control of the Company. Certain provisions of the Delaware General Corporation Law may also discourage takeover attempts that have not been approved by the Board of Directors. See "Description of Capital Stock."

DILUTION. Purchasers of Common Stock will experience immediate, substantial dilution in the net tangible book value of their stock.

PRICE RANGE OF COMMON STOCK

The Company's Common Stock has traded on the New York Stock Exchange since June 27, 1997. On July 29, 1997, the last sale price of the Common Stock was \$17.625 per share, as published in THE WALL STREET JOURNAL on July 30, 1997. At July 29, 1997 there were approximately 84 stockholders of record of the Company's Common Stock. The following table sets forth the range of high and low sale prices for the Common Stock for the period from June 27, 1997, the date of the IPO, through June 30, 1997, and from July 1, 1997, through July 29, 1997.

	HIGH	LOW
	-----	-----
June 27-30, 1997.....	\$ 16.125	\$ 13.00
July 1-29, 1997.....	\$ 18.625	\$ 15.50

## THE COMPANY

Comfort Systems was founded in 1996 to become a leading national provider of comprehensive HVAC installation services and maintenance, repair and replacement of HVAC systems, focusing primarily on the commercial and industrial markets. In furtherance of this goal, Comfort Systems acquired the twelve Founding Companies on July 2, 1997. In 1996, the Founding Companies, which have been in business an average of 39 years, had pro forma combined revenues of \$167.5 million and served customers in 27 states. For a description of the transactions pursuant to which these businesses were acquired, see "Certain Transactions." The following is a description of the Founding Companies:

QUALITY AIR HEATING AND COOLING, INC. -- Quality Air Heating and Cooling, Inc. ("Quality"), headquartered in Grand Rapids, Michigan, was founded in 1968 and operates primarily in western Michigan. Quality focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems, primarily for medium and large commercial facilities. Quality operates a sheet metal and ductwork fabrication facility for its installation services. Quality had 1996 revenues of \$29.6 million and currently has 222 employees. Robert J. Powers, the President of Quality, has been employed by Quality for 16 years, has signed a five-year employment agreement with Quality to continue his present position and is a director of the Company.

ATLAS AIR CONDITIONING CO. -- Atlas Comfort Services USA, Inc., which does business as Atlas Air Conditioning Co. ("Atlas"), and is headquartered in Houston, Texas, was founded in 1947 and operates primarily in the southwest, northeast and mid-Atlantic regions of the United States. Atlas is a leading provider of HVAC installation services for apartment complexes, condominiums, hotels and elder care facilities in the United States and also provides maintenance, repair and replacement of HVAC systems. Atlas had 1996 revenues of \$30.0 million and currently has 205 employees. Brian S. Atlas and Michael Atlas, the Chief Executive Officer and Chief Operating Officer of Atlas, respectively, have been employed by Atlas for 22 and 20 years, respectively. They have signed five-year employment agreements with Atlas to continue their present positions following consummation of this Offering. Brian S. Atlas is a director of the Company.

TRI-CITY MECHANICAL, INC. -- Tri-City Mechanical, Inc. ("Tri-City"), headquartered in Tempe, Arizona, was founded in 1962 and operates in Arizona, California and Nevada. Tri-City focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems primarily for large commercial and industrial facilities, as well as process piping for industrial facilities. Tri-City operates a sheet metal and ductwork fabrication facility for its installation services. Tri-City had 1996 revenues of \$24.2 million and currently has 283 employees. Michael Nothum, Jr., the President of Tri-City, has been employed by Tri-City for 18 years, has signed a five-year employment agreement with Tri-City to continue his present position and is a director of the Company.

S. M. LAWRENCE CO., INC. -- S. M. Lawrence Co., Inc. and Lawrence Service, Inc. (together "Lawrence"), headquartered in Jackson, Tennessee, were founded in 1917 and operate primarily in Tennessee and the surrounding states. Lawrence focuses on providing "design and build" installation services and process piping primarily for industrial facilities and maintenance, repair and replacement of commercial and industrial HVAC systems. Lawrence operates a sheet metal and ductwork fabrication facility for its installation services. Lawrence had 1996 revenues of \$17.2 million and currently has 184 employees. Samuel M. Lawrence III and Frank F. Lawrence, the Chief Executive Officer and President of Lawrence, respectively, have been employed by Lawrence for 20 and 17 years, respectively, and have signed five-year employment agreements with Lawrence to continue their present positions. Samuel M. Lawrence III is a director of the Company.

ACCURATE AIR SYSTEMS, INC. -- Accurate Air Systems, Inc. ("Accurate"), headquartered in Houston, Texas, was founded in 1980 and operates primarily in Texas, Oklahoma and New Mexico. Accurate focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial facilities. Accurate operates a sheet metal and ductwork fabrication facility for its installation services. Accurate had 1996 revenues of \$16.8 million and currently has 115 employees. Thomas J. Beaty, President and founder of Accurate, has been employed by Accurate for 16 years, has

signed a five-year employment agreement with Accurate to continue his present position and is a director of the Company.

FREEWAY HEATING AND AIR CONDITIONING, INC. -- Freeway Heating and Air Conditioning, Inc. ("Freeway"), headquartered in Bountiful, Utah, was founded in 1947 and operates primarily in the Salt Lake City area. Freeway provides installation services and maintenance, repair and replacement of HVAC systems for commercial and residential facilities. Freeway had 1996 revenues of \$9.4 million and currently has 107 employees. Robert Arbuckle, President of Freeway, has been employed by Freeway for 22 years and has signed a five-year employment agreement with Freeway to continue his present position.

EASTERN HEATING AND COOLING INC. -- Eastern Heating and Cooling Inc. ("Eastern"), headquartered in Albany, New York, was founded in 1945 and operates primarily within a 75-mile radius of Albany, New York. Eastern focuses on providing "design and build" installation and maintenance, repair and replacement of HVAC systems for commercial and industrial facilities. Eastern also offers continuous monitoring and control services for commercial facilities. Eastern had 1996 revenues of \$7.9 million and currently has 57 employees. Alfred J. Giardenelli, Jr., President of Eastern, has been employed by Eastern for 26 years, has signed a five-year employment agreement with Eastern to continue his present position and is a director of the Company.

CSI/BONNEVILLE -- Contract Service Inc., which does business as C. S. I. Heating and Air Conditioning and Bonneville Heating and Cooling ("CSI/Bonneville") and is headquartered in Salt Lake City, Utah, was founded in 1969 and operates primarily in Utah. CSI/Bonneville focuses on providing maintenance, repair and replacement of HVAC systems for commercial and residential facilities. CSI/Bonneville had 1996 revenues of \$7.8 million and currently has 81 employees. John C. Phillips, President and co-founder of CSI/Bonneville, has been employed by CSI/Bonneville for 28 years, has signed a five-year employment agreement with CSI/Bonneville to continue his present position and is a director of the Company.

TECH HEATING AND AIR CONDITIONING, INC. -- Tech Heating and Air Conditioning, Inc. and Tech Mechanical, Inc. (together "Tech"), headquartered in Solon, Ohio, were founded in 1979 and operate primarily in the greater Cleveland, Ohio area. Tech focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial and industrial facilities. Tech also offers continuous monitoring and control services for commercial facilities. Tech had 1996 revenues of \$7.5 million and currently has 65 employees. Robert R. Cook, President and founder of Tech, has been employed by Tech for 18 years, has signed a five-year employment agreement with Tech to continue his present position and is a director of the Company.

SEASONAIR, INC. -- Seasonair, Inc. ("Seasonair"), headquartered in Rockville, Maryland, was founded in 1966 and operates primarily in Maryland, the District of Columbia and Virginia. Seasonair focuses on providing installation services and maintenance, repair and replacement of HVAC systems for light commercial facilities. Seasonair had 1996 revenues of \$6.7 million and currently has 62 employees. James C. Hardin, Sr., who became Chief Executive Officer of Seasonair upon consummation of the IPO, has been employed by Seasonair for 11 years and has signed a five-year employment agreement with Seasonair.

WESTERN BUILDING SERVICES, INC. -- Western Building Services, Inc. ("Western"), headquartered in Denver, Colorado, was founded in 1980 and operates primarily in Colorado. Western focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial facilities. Western also offers continuous monitoring and control services for commercial facilities. Western had 1996 revenues of \$6.5 million and currently has 53 employees. Charles W. Klapperich, President and founder of Western, has been employed by Western for 17 years, has signed a five-year employment agreement with Western to continue his present position and is a director of the Company.

STANDARD HEATING AND AIR CONDITIONING CO. -- Standard Heating and Air Conditioning Co. ("Standard"), headquartered in Birmingham, Alabama, was founded in 1939 and operates primarily in Alabama. Standard focuses on providing comprehensive maintenance, repair and replacement of HVAC systems for residential and light commercial facilities. Standard had 1996 revenues of \$3.7 million and currently has 38

employees. Thomas B. Kime, President of Standard, has been employed by Standard for over 20 years and has signed a five-year employment agreement with Standard to continue his present position with Standard.

#### DIVIDEND POLICY

The Company intends to retain all of its future earnings, if any, to finance the expansion of its business and for general corporate purposes, including future acquisitions, and does not anticipate paying any cash dividends on its Common Stock for the foreseeable future. In addition, the Company's credit facility includes restrictions on the ability of the Company to pay dividends without the consent of the lender.

#### CAPITALIZATION

The following table sets forth the current maturities of long-term obligations and capitalization at March 31, 1997 (i) of the Founding Companies combined; (ii) of Comfort Systems on a pro forma combined basis to give effect to the issuance of 1,269,935 shares of Common Stock to management of and consultants to Comfort Systems, the Mergers and the S Corporation Distributions; and (iii) of Comfort Systems, pro forma combined, as adjusted to give effect to the Mergers, the S Corporation Distributions, the IPO and the application of a portion of the net proceeds therefrom. This table should be read in conjunction with the Unaudited Pro Forma Combined Financial Statements of the Company and the Notes thereto included elsewhere in this Prospectus.

	MARCH 31, 1997		
	COMBINED	PRO FORMA COMBINED	AS ADJUSTED
	(IN THOUSANDS)		
Current maturities of long-term debt obligations(1).....	\$ 9,230	\$ 50,658(2)	\$ 5,355
Long-term obligations, less current maturities(1).....	\$ 3,267	\$ 14,292(3)	\$ 14,292
Stockholders' equity:			
Preferred Stock: \$0.01 par value, 5,000,000 shares authorized; none issued or outstanding.....	--	--	--
Common Stock: \$0.01 par value, 52,969,912 shares authorized; 14,875,774 shares issued and outstanding pro forma combined; and 20,975,774 shares issued and outstanding, as adjusted(4).....	433	140	210
Additional paid-in capital.....	12,149	100,978	180,783
Retained earnings.....	8,160	--	--
Treasury stock.....	(1,201)	--	--
Total stockholders' equity.....	19,541	101,118	180,993
Total capitalization.....	\$22,808	\$ 115,410	\$ 195,285

(1) For a description of the Company's debt, see the Notes to Unaudited Pro Forma Combined Financial Statements and Notes to the Founding Companies' Financial Statements.

(2) Includes a \$45.3 million note payable to owners of the Founding Companies, representing the cash portion of the Merger consideration that was paid from a portion of the net proceeds of the IPO.

(3) Includes \$11.0 million in long-term obligations to reflect that portion of the S Corporation Distributions that were funded through borrowings.

(4) Excludes 2,174,954 shares of Common Stock subject to options to be granted upon consummation of the IPO at an exercise price equal to the initial public offering price. See "Management -- 1997 Long-Term Incentive Plan" and "-- 1997 Non-Employee Directors' Stock Plan."



SELECTED FINANCIAL DATA  
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

Comfort Systems acquired the Founding Companies in connection with the consummation of the IPO. For financial statement presentation purposes, Comfort Systems has been identified as the "accounting acquirer." The following selected financial data for Comfort Systems as of December 31, 1996 has been derived from audited financial statements of Comfort Systems. The selected historical financial data as of March 31, 1997 and the three months ended March 31, 1997 have been derived from unaudited financial statements of Comfort Systems, which have been prepared on the same basis as the audited financial statements and, in the opinion of Comfort Systems, reflect all adjustments consisting of normal recurring adjustments, necessary for a fair presentation of such data. The selected unaudited pro forma combined financial data present data for the Company, adjusted for (i) the effects of the Mergers, (ii) the effects of certain pro forma adjustments to the historical financial statements described below and (iii) the consummation of the IPO and the application of the net proceeds therefrom. See the Unaudited Pro Forma Combined Financial Statements and the Notes thereto and the historical Financial Statements of Comfort Systems and certain of the Founding Companies and the Notes thereto included elsewhere in this Prospectus.

	TWELVE MONTHS ENDED DECEMBER 31, 1996	THREE MONTHS ENDED MARCH 31, 1997		
	-----	-----		
<b>INCOME STATEMENT DATA:</b>				
<b>COMFORT SYSTEMS</b>				
Revenues.....	\$ --	\$ --		
Gross profit.....	--	--		
Selling, general and administrative expenses(1).....	--	11,556		
	-----	-----		
Loss from operations.....	--	(11,556)		
Interest and other income (expense), net.....	--	--		
	-----	-----		
Net loss.....	\$ --	\$ (11,556)		
	=====	=====		
<b>PRO FORMA COMBINED(2)</b>				
Revenues.....	\$ 167,525	\$ 39,505		
Gross profit.....	47,813	10,705		
Selling, general and administrative expenses(3).....	27,814	7,814		
Goodwill amortization(4).....	3,495	874		
Income from operations.....	16,504	2,017		
Interest and other income (expense), net(5).....	(961)	(250)		
Income before income taxes.....	15,543	1,767		
Net income(6).....	7,928	847		
Net income per share.....	0.44	0.05		
Shares used in computing pro forma net income per share(7)...	18,180,311	18,180,311		
-----				
	COMFORT SYSTEMS	COMBINED COMPANIES		
	-----	-----		
	DECEMBER 31,	MARCH 31,	MARCH 31, 1997	
	-----	-----	-----	
	1996	1997	PRO FORMA COMBINED(8)	AS ADJUSTED(9)
	-----	-----	-----	-----
<b>BALANCE SHEET DATA:</b>				
Working capital(5).....	\$ 1	\$ 42	\$ (31,197)(10)	\$ 48,678
Total assets.....	178	2,908	188,683	220,389
Long-term debt, net of current maturities(5).....	--	--	14,292	14,292
Stockholders' equity(5).....	1	42	101,118	180,993

(FOOTNOTES ON FOLLOWING PAGE)

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- (1) Represents the non-recurring, non-cash Compensation Charge of \$11.6 million.
  - (2) The pro forma combined income statement data assume that the Mergers and the IPO were consummated on January 1, 1996 and are not necessarily indicative of the results the Company would have obtained had these events actually then occurred or of the Company's future results.
  - (3) The pro forma combined income statement data reflect the Compensation Differential of \$6.6 million for the twelve months ended December 31, 1996 and \$428,000 for the three months ended March 31, 1997 and does not include the Compensation Charge of \$11.6 million recorded in the first quarter of 1997.
  - (4) Consists of amortization of goodwill to be recorded as a result of the Mergers over a 40-year period and computed on the basis described in the Notes to the Unaudited Pro Forma Combined Financial Statements.
  - (5) Several of the Founding Companies were S Corporations. In connection with the Mergers, these Founding Companies made S Corporation Distributions totalling \$16.8 million through March 31, 1997. In order to fund these distributions, the Founding Companies borrowed \$11.0 million from existing sources. Accordingly, pro forma interest expense has been increased by \$935,000 for the twelve months ended December 31, 1996 and \$207,000 for the three months ended March 31, 1997, pro forma working capital has been reduced by \$1.9 million, pro forma long-term debt has been increased by \$11.0 million and pro forma stockholders' equity has been reduced by \$12.9 million. Quality declared S Corporation Distributions of \$3.9 million which have been recorded as a dividend payable to an affiliate and a reduction of stockholders' equity in the pro forma combined balance sheet data. This \$3.9 million is included in the \$16.8 million of S Corporation Distributions.
  - (6) Assuming a corporate income tax rate of 40% and the non-deductibility of goodwill.
  - (7) Includes (i) 2,969,912 shares issued to Notre, (ii) 1,269,935 shares issued to management of and consultants to Comfort Systems, (iii) 9,720,927 shares issued to owners of the Founding Companies and (iv) 4,219,537 of the 7,015,000 shares sold in the Offering necessary to pay the cash portion of the Merger consideration and expenses of the IPO and excludes 915,000 shares of common stock purchased by the underwriters pursuant to an overallotment option.
  - (8) The pro forma combined balance sheet data assume that the Mergers were consummated on March 31, 1997.
  - (9) Adjusted for the sale of the 7,015,000 shares of Common Stock offered in the IPO and the application of the estimated net proceeds therefrom.
  - (10) Includes a \$45.3 million note payable to owners of the Founding Companies, representing the cash portion of the Merger consideration paid from a portion of the net proceeds of the IPO.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with "Selected Financial Data" and the Founding Companies' Financial Statements and related Notes thereto appearing elsewhere in this Prospectus.

INTRODUCTION

The Company's revenues are derived from providing comprehensive HVAC installation services and maintenance, repair and replacement of HVAC systems primarily for commercial and industrial customers. The Company's commercial and industrial applications include office buildings, retail centers, apartment complexes, hotels, manufacturing plants and government facilities. The Company also provides specialized HVAC applications such as process cooling, control systems, electronic monitoring and process piping. Approximately 90% of the Company's pro forma combined 1996 revenues of \$167.5 million was derived from commercial and industrial customers, with approximately 53% of total revenues attributable to installation services and 47% attributable to maintenance, repair and replacement services.

Revenues related to commercial and industrial installation are of two types: "design and build" and "plan and spec." Approximately 80% of the commercial and industrial installation revenues for 1996 were generated from "design and build" projects, which generally yield higher margins than "plan and spec" projects because the Company is responsible for designing, engineering and installing a cost-effective, energy-efficient system that is customized to the specific needs of the building owner. This enables the Company to control the customer's cost and reduce overall design and installation time. Additionally, the costs and other terms of "design and build" projects are normally established through relationship-based negotiation with the building owner or its representative rather than through a competitive bid process. "Plan and spec" installation projects typically yield lower margins than "design and build" projects because the building's architect or consulting engineer designs the HVAC system and the installation project is put out for bid.

Most installation and reconfiguration projects are completed within one year. Generally, these contracts are accounted for under the percentage-of-completion method of accounting. Revenues are recorded based on the percentage of costs incurred during a particular period, in proportion to total estimated costs for each contract. Maintenance, repair and replacement service revenues are recorded as services are performed. Costs of services consist primarily of HVAC components, parts and materials related to new installation, equipment maintenance and rental, salaries and benefits payable to service and repair technicians, as well as supervisory and subcontract labor. Selling, general and administrative expenses consist primarily of compensation and benefits to owners as well as to sales and administrative employees, fees for professional services, depreciation of equipment and other general office expenses. Selling, general and administrative expenses also include incentive and discretionary bonuses paid to owners, significant portions of which were paid in lieu of S Corporation distributions to enable stockholders to meet their income tax obligations.

The Founding Companies have operated throughout the periods presented as independent, privately-owned entities, and their results of operations reflect varying tax structures (S Corporations or C Corporations) which have influenced the historical level of owners' compensation. Gross profit margins and selling, general and administrative expenses as a percentage of revenues may not be comparable among the individual Founding Companies. The owners of the Founding Companies have agreed to certain reductions in their compensation and benefits in connection with the organization of the Company. The Compensation Differential for 1996 of \$6.6 million has been reflected as a pro forma adjustment in the Unaudited Pro Forma Combined Statements of Operations.

The Company anticipates that following the Mergers it will realize savings from (i) greater volume discounts from suppliers of HVAC components, parts and raw materials; (ii) consolidation of insurance and bonding programs; (iii) other general and administrative areas such as training and advertising; and (iv) the Company's ability to borrow at lower interest rates than most of the Founding Companies. It is anticipated that these savings will be offset by costs related to the Company's new corporate management and by the

costs associated with being a public company. The Company believes that neither these savings nor the costs associated therewith can be quantified because the Mergers have not occurred, and there have been no combined operating results upon which to base any assumptions. As a result, they have not been included in the pro forma financial information included herein.

During January and February 1997, Comfort Systems sold an aggregate of 1,269,935 shares of Common Stock to management and consultants. As a result, the Company recorded a non-recurring, non-cash Compensation Charge of \$11.6 million in the first quarter of 1997, representing the difference between the amount paid for the shares and the estimated fair value of the shares on the date of sale. This Compensation Charge of \$11.6 million is not included in pro forma financial information or Combined Results of Operations.

In July 1996, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 97 ("SAB 97") relating to business combinations immediately prior to an initial public offering. SAB 97 requires that these combinations be accounted for using the purchase method of acquisition accounting. Under the purchase method, one of the companies must be designated as the accounting acquirer. For the remaining companies, \$139.8 million, representing the excess of the fair value of the Merger consideration received over the fair value of the net assets to be acquired, will be recorded as "goodwill" on the Company's balance sheet. Goodwill will be amortized as a non-cash charge to the income statement over a 40-year period. The pro forma impact of this amortization expense, which is non-deductible for tax purposes, is \$3.5 million per year on an after-tax basis. Prior to the issuance of SAB 97, goodwill and related amortization expense were not required to be recorded for most business combinations similar to the Mergers. See "Certain Transactions -- Organization of the Company."

#### COMBINED RESULTS OF OPERATIONS

The combined results of operations of the Founding Companies for the periods presented do not represent combined results of operations presented in accordance with generally accepted accounting principles, but are only a summation of the revenues, cost of services and selling, general and administrative expenses of the individual Founding Companies on a historical basis. The combined results also exclude the effect of pro forma adjustments and may not be comparable to, and may not be indicative of, the Company's post-combination results of operations because (i) the Founding Companies were not under common control or management during the periods presented; (ii) the Founding Companies used different tax structures (S Corporations or C Corporations) during the periods presented; (iii) the Company will incur incremental costs related to its new corporate management and the costs of being a public company; (iv) the Company will use the purchase method to record the Mergers, resulting in the recording of goodwill which will be amortized over 40 years; and (v) the combined data do not reflect the Compensation Differential and potential benefits and cost savings the Company expects to realize when operating as a combined entity.

The following table sets forth the combined results of operations of the Founding Companies on a historical basis and such results as a percentage of revenues.

	FISCAL YEARS ENDED(1)						THREE MONTHS ENDED MARCH 31, (3)			
	1994		1995(2)		1996(2)		1996		1997	
	(IN THOUSANDS)									
Revenues.....	\$ 124,710	100.0%	\$ 146,512	100.0%	\$ 167,525	100.0%	\$ 34,799	100.0%	\$ 39,505	100.0%
Cost of services.....	92,318	74.0	105,043	71.7	119,712	71.5	25,759	74.0	28,800	72.9
Gross profit.....	32,392	26.0	41,469	28.3	47,813	28.5	9,040	26.0	10,705	27.1
Selling, general and administrative expenses..	27,386	22.0	31,038	21.2	34,382	20.5	7,973	22.9	8,027	20.3
Income from operations.....	5,006	4.0	10,431	7.1	13,431	8.0	1,067	3.1	2,678	6.8

(1) The fiscal years presented are as follows: Quality -- the fiscal years ended March 31, 1995 and 1996 and the year ended December 31, 1996; Atlas and Accurate -- the fiscal years ended June 30, 1994 and 1995 and the year ended December 31, 1996; Lawrence -- the fiscal years ended October 31, 1994, 1995 and 1996; and Tri-City, Eastern, CSI/Bonneville, Tech, Seasonair and Western -- the years ended December 31 for all periods presented.

(2) The financial data for 1995 and 1996 both include Quality's results for the three months ended March 31, 1996 which were as follows: revenues of \$6.3 million, cost of services of \$4.3 million, and selling, general and administrative expenses of \$1.6 million.

(3) Lawrence's results of operations are presented for the three months ended January 31, 1996 and 1997.

COMBINED RESULTS FOR THE THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THE THREE MONTHS ENDED MARCH 31, 1996

REVENUES. Combined revenues increased approximately \$4.7 million, or 13.5%, from \$34.8 million for the three months ended March 31, 1996 to \$39.5 million for the three months ended March 31, 1997. The increase in revenues occurred primarily at Quality, Lawrence and Tech. Revenues at Quality increased \$2.5 million due to a \$1.5 million increase in installation revenues and a \$1.0 million increase in maintenance, repair and replacement revenues. Revenues increased \$1.3 million at Lawrence due primarily to a "design and build" installation project for a manufacturing facility in North Carolina. Revenues at Tech increased \$0.6 million due to an increase in commercial installation services because there were fewer days of inclement weather in the first three months of 1997 as compared to the prior comparable period. Four of the other Founding Companies reported an increase in revenues from the first quarter of 1996 compared to the first quarter of 1997, partially offset by a decline in revenues at Accurate and Eastern.

GROSS PROFIT. Combined gross profit increased \$1.7 million, or 18.4%, from \$9.0 million for the three months ended March 31, 1996 to \$10.7 million for the three months ended March 31, 1997, due primarily to increases of \$1.4 million at Quality, \$0.5 million at Atlas and \$0.3 million at Lawrence. As a percentage of revenues, combined gross profit increased from 26.0% in the three months ended March 31, 1996 to 27.1% in the three months ended March 31, 1997. Gross profit as a percentage of revenues at Quality increased from 32.1% in the three months ended March 31, 1996 to 38.7% in the three months ended March 31, 1997 as a result of Quality's ability to be more selective in accepting projects. Gross profit as a percentage of revenues at Atlas increased from 12.1% for the three months ended March 31, 1996 to 20.4% for the three months ended March 31, 1997. This improvement resulted from Atlas's ability to be more selective in accepting projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Combined selling, general and administrative expenses increased \$0.1 million, or 0.7%, from \$7.9 million for the three months ended March 31, 1996 to \$8.0 million for the three months ended March 31, 1997 due primarily to an increase in infrastructure needed to support increased volume, partially offset by a decrease in compensation to owners and incentive compensation to key employees totalling \$1.2 million. As a percentage of revenues, selling, general and administrative expenses decreased from 22.9% in the three months ended March 31, 1996 to 20.3% in the three months ended March 31, 1997.

COMBINED RESULTS FOR 1996 COMPARED TO 1995

REVENUES. Combined revenues increased approximately \$21.0 million, or 14.3%, from \$146.5 million in 1995 to \$167.5 million in 1996. The increase in combined revenues occurred primarily at Atlas, Accurate and Lawrence. This increase in combined revenues was primarily attributable to an increase in commercial and industrial "design and build" revenues of approximately 15% and an increase in maintenance, repair and replacement revenues of approximately 30%. Revenues for Atlas increased \$7.6 million from 1995 to 1996 due to increasing demand by several large national customers for HVAC "design and build" installation services provided by Atlas for multi-unit facilities. Revenues for Accurate increased \$4.6 million from 1995 to 1996 reflecting the success of an increased marketing effort along with the addition of sales personnel and project managers. Revenues at Lawrence increased by \$4.6 million from 1995 to 1996 due to a management decision in 1995 to expand the number of general contractors for which Lawrence provides industrial installation services and due to a large "design and build" installation contract obtained in 1996 for a food processing facility. Seven of the other Founding Companies reported an increase in revenues from 1995 and 1996, partially offset by a decline in revenues at Quality and Tri-City.

GROSS PROFIT. Combined gross profit increased \$6.3 million, or 15.3%, from \$41.5 million in 1995 to \$47.8 million in 1996, due principally to increases in gross profit of \$2.2 million at Atlas, \$1.5 million at Lawrence and \$1.1 million at Western. As a percentage of revenues, combined gross profit increased from 28.3% in 1995 to 28.5% in 1996. Gross profit as a percentage of revenues at Atlas increased from 12.5% of revenues in 1995 to 16.5% of revenues in 1996 as increasing demand for Atlas' specialized installation services enabled Atlas to earn higher margins. Gross profit as a percentage of revenues at Accurate decreased from 26.1% of revenues in 1995 to 21.0% of revenues in 1996 as a result of an increase in

overtime and subcontract labor necessary to support the increased number of "design and build" projects. Gross profit as a percentage of revenues at Western increased from 17.1% to 28.2% from 1995 to 1996, which resulted in part from Western's participation in an incentive program sponsored by the Public Service Company of Colorado during 1996. Western does not intend to participate in this program during 1997.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Combined selling, general and administrative expenses increased \$3.4 million, or 10.8%, from \$31.0 million in 1995 to \$34.4 million in 1996. Selling, general and administrative expenses increased \$1.4 million at Lawrence, approximately one-half of which was related to increases in salary and incentive compensation paid to the owners, and the other half of which was related to increases in incentive compensation and discretionary profit sharing contributions for employees. Selling, general and administrative expenses increased \$0.7 million at Tri-City as a result of a \$1.1 million increase in compensation to the owners in lieu of S Corporation distributions, offset by \$0.4 million of reductions in other overhead expenses. As a percentage of combined revenues, selling, general and administrative expenses decreased from 21.2% in 1995 to 20.5% in 1996.

#### COMBINED RESULTS FOR 1995 COMPARED TO 1994

REVENUES. Combined revenues increased approximately \$21.8 million, or 17.5%, from \$124.7 million in 1994 to \$146.5 million in 1995, primarily due to an increase in commercial and industrial "design and build" revenues of approximately 40% and an increase of approximately 10% in maintenance, repair and replacement revenues. Revenues at Quality increased \$8.2 million from 1994 to 1995 as a result of management's focus on obtaining more "design and build" projects and related service work. Revenues at Tri-City increased \$8.1 million from 1994 to 1995 as a result of a strategy implemented in late 1994 to focus on larger "design and build" projects and the related service relationships. To accomplish its strategy, Tri-City increased the size of its sales and project management staff.

GROSS PROFIT. Combined gross profit increased \$9.1 million, or 28.0%, from \$32.4 million in 1994 to \$41.5 million in 1995. Gross profit increased \$3.1 million at Tri-City and \$2.9 million at Quality. As a percentage of revenues, combined gross profit increased from 26.0% in 1994 to 28.3% in 1995. Gross profit as a percentage of revenues at Tri-City increased from 15.5% in 1994 to 22.9% in 1995 as a result of an increase in the number of higher-margin "design and build" installation projects. Gross profit as a percentage of revenues at Lawrence increased from 23.2% in fiscal 1994 to 27.3% in fiscal 1995 as management emphasized higher-margin "design and build" projects and successfully implemented an incentive program for project managers to control project costs.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Combined selling, general and administrative expenses increased \$3.6 million, or 13.3%, from \$27.4 million in 1994 to \$31.0 million in 1995. Selling, general and administrative expenses increased \$1.0 million at Tri-City from 1994 to 1995 primarily due to a \$0.8 million increase in compensation to its owners. Selling, general and administrative expenses at Lawrence increased \$0.6 million primarily due to an increase in salary and incentive compensation to its owners. As a percentage of combined revenues, combined selling, general and administrative expenses decreased from 22.0% in 1994 to 21.2% in 1995.

#### COMBINED LIQUIDITY AND CAPITAL RESOURCES

On a combined basis, the Founding Companies generated \$2.1 million of net cash from operating activities for the three months ended March 31, 1997, primarily at Quality, Tri-City and Seasonair. Net cash used in investing activities was \$0.8 million, primarily for equipment purchases. Net cash used in financing activities was \$0.4 million and consisted of increases in long-term debt of \$1.9 million offset by distributions to stockholders of \$2.3 million. At March 31, 1997, the combined Founding Companies had working capital of \$16.0 million and total debt of \$12.5 million, including \$5.1 million of debt to stockholders.

In connection with and prior to the Mergers, certain Founding Companies made S Corporation Distributions to their owners of substantially all of their previously-taxed undistributed earnings. The pro forma combined financial statements as of March 31, 1997 and for the three months then ended, included elsewhere in this Prospectus, reflect pro forma adjustments for the estimated amount of these S Corporation

Distributions and additional debt needed to fund these distributions had they occurred in their entirety as of March 31, 1997. These pro forma adjustments reflect \$16.8 million of S Corporation Distributions and \$11.0 million of additional debt.

On a combined basis, the Founding Companies generated \$9.0 million of net cash from operating activities during fiscal 1996, primarily at Quality, Tri-City and CSI/Bonneville. Net cash used in investing activities was \$3.0 million on a combined basis, primarily for equipment purchases. Net cash used in financing activities was \$7.3 million on a combined basis, consisting of net reductions in long-term debt of \$1.6 million and distributions to stockholders of \$5.7 million. At December 31, 1996, the combined Founding Companies had working capital of \$18.9 million and total debt of \$8.6 million, including debt to stockholders.

The Company intends to pursue acquisition opportunities. The Company expects to fund future acquisitions through the issuance of additional Common Stock, borrowings, including use of amounts available under its credit facility executed in connection with the IPO and cash flow from operations. The Company anticipates that its cash flow from operations will provide cash in excess of the Company's normal working capital needs, debt service requirements and planned capital expenditures for equipment. On a combined basis, the Founding Companies made capital expenditures of \$2.3 million in fiscal 1996.

The Company has obtained a revolving line of credit of \$75.0 million from Bank One. The facility will be used for acquisitions, capital expenditures, refinancing of debt not paid out of the proceeds of the IPO and for general corporate purposes. The credit facility requires the Company to comply with various loan covenants including (i) maintenance of certain financial ratios, (ii) restrictions on additional indebtedness, and (iii) restrictions on liens, guarantees, advances and dividends. As of July 28, 1997, borrowings under the line of credit were credit \$17.3 million, which was used to repay existing indebtedness of the Founding Companies.

#### QUALITY RESULTS OF OPERATIONS

Quality, headquartered in Grand Rapids, Michigan, was founded in 1968 and operates primarily throughout western Michigan. Quality focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems, primarily for medium and large commercial facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED MARCH 31,		YEAR ENDED DECEMBER 31,		NINE MONTHS ENDED DECEMBER 31,			
	1995	1996(1)	1996(1)	1995	1995	1995		
	(IN THOUSANDS)							
Revenues.....	\$ 24,434	100.0%	\$ 32,594	100.0%	\$ 29,597	100.0%	\$ 26,279	100.0%
Cost of services.....	15,634	64.0	20,850	64.0	18,467	62.4	16,559	63.0
Gross profit.....	8,800	36.0	11,744	36.0	11,130	37.6	9,720	37.0
Selling, general and administrative expenses.....	6,646	27.2	6,791	20.8	6,640	22.4	5,183	19.7
Income from operations.....	2,154	8.8	4,953	15.2	4,490	15.2	4,537	17.3
	THREE MONTHS ENDED MARCH 31,		THREE MONTHS ENDED MARCH 31,		THREE MONTHS ENDED MARCH 31,			
	1996	1996	1996	1997				
Revenues.....	\$ 23,282	100.0%	\$ 6,315	100.0%	\$ 8,766	100.0%		
Cost of services.....	14,176	60.9	4,291	67.9	5,372	61.3		
Gross profit.....	9,106	39.1	2,024	32.1	3,394	38.7		
Selling, general and administrative expenses.....	5,032	21.6	1,608	25.5	2,094	23.9		
Income from operations.....	4,074	17.5	416	6.6	1,300	14.8		

(1) The financial data for the year ended December 31, 1996 and the year ended March 31, 1996 both include results for the three months ended March 31, 1996, which were as follows: revenues of \$6.3 million, cost of services of \$4.3 million and selling, general and administrative expenses of \$1.6 million.

#### QUALITY RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

**REVENUES.** Revenues increased \$2.5 million, or 38.8%, from \$6.3 million for the three months ended March 31, 1996 to \$8.8 million for the three months ended March 31, 1997 due to a \$1.5 million increase in installation revenues and a \$1.0 million increase in maintenance, repair and replacement revenues.

**GROSS PROFIT.** Gross profit increased \$1.4 million, or 67.7%, from \$2.0 million for the three months ended March 31, 1996 to \$3.4 million for the three months ended March 31, 1997. As a percentage of





revenues, gross profit increased from 32.1% to 38.7% as a result of Quality's ability to be more selective in accepting projects.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses increased \$0.5 million, or 30.2%, from \$1.6 million for the three months ended March 31, 1996 to \$2.1 million for the three months ended March 31, 1997. The increase in selling, general and administrative expenses was primarily attributable to an increase in administrative costs associated with the higher sales volume. As a percentage of revenues, selling, general and administrative expenses decreased from 25.5% to 23.9% as Quality was able to increase its sales volume without a commensurate increase in overhead expenses.

**QUALITY RESULTS FOR NINE MONTHS ENDED DECEMBER 31, 1996 COMPARED TO NINE MONTHS ENDED DECEMBER 31, 1995**

**REVENUES.** Revenues decreased \$3.0 million, or 11.4%, from \$26.3 million for the nine months ended December 31, 1995 to \$23.3 million for the nine months ended December 31, 1996 due to a decrease in Quality's volume of commercial "design and build" installation projects. Quality's decline in revenues from 1995 to 1996 resulted from management's decision to be more selective in accepting installation projects. Management continues to emphasize project selectivity and expansion of capacity through the addition of technical staff and management rather than through subcontract labor and employee overtime.

**GROSS PROFIT.** Gross profit decreased \$0.6 million, or 6.3%, from \$9.7 million for the nine months ended December 31, 1995 to \$9.1 million for the nine months ended December 31, 1996. As a percentage of revenues, gross profit increased from 37.0% to 39.1% due to management's emphasis on project selection and a decrease in the use of subcontract labor, employee overtime and outside services.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses decreased \$0.2 million, or 2.9%, from \$5.2 million for the nine months ended December 31, 1995 to \$5.0 million for the nine months ended December 31, 1996. As a percentage of revenues, these expenses increased from 19.7% to 21.6% due to the decline in revenues.

**QUALITY RESULTS FOR YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED MARCH 31, 1996**

**REVENUES.** Revenues decreased \$3.0 million, or 9.2%, from \$32.6 million for the year ended March 31, 1996 to \$29.6 million for the year ended December 31, 1996, for the reasons described above.

**GROSS PROFIT.** Gross profit decreased \$0.6 million, or 5.2%, from \$11.7 million for the year ended March 31, 1996 to \$11.1 million for the year ended December 31, 1996. As a percentage of revenues, gross profit increased from 36.0% to 37.6% due to management's emphasis on project selection and a decrease in the use of subcontract labor, employee overtime and outside services.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses decreased \$0.2 million, or 2.2%, from \$6.8 million for the year ended March 31, 1996 to \$6.6 million for the year ended December 31, 1996. As a percentage of revenues, selling, general and administrative expenses increased from 20.8% to 22.4% due to the decline in revenues.

**QUALITY RESULTS FOR YEAR ENDED MARCH 31, 1996 COMPARED TO YEAR ENDED MARCH 31, 1995**

**REVENUES.** Revenues increased \$8.2 million, or 33.4%, from \$24.4 million for the fiscal year ended March 31, 1995 to \$32.6 for the fiscal year ended March 31, 1996. This increase in revenues was primarily attributable to management's emphasis on obtaining more "design and build" installation projects and the related service work.

**GROSS PROFIT.** Gross profit increased \$2.9 million, or 33.5%, from \$8.8 million for the fiscal year ended March 31, 1995 to \$11.7 million for the fiscal year ended March 31, 1996. As a percentage of revenues, gross profit remained unchanged at 36.0% as the benefits associated with higher revenues were offset by an increase in subcontract labor, employee overtime and outside services.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses increased \$0.2 million, or 2.2%, from \$6.6 million for the fiscal year ended March 31, 1995 to \$6.8 million for the fiscal year ended March 31, 1996. As a percentage of revenues, selling, general and administrative expenses

decreased from 27.2% to 20.8% as the Company successfully leveraged its infrastructure to support the significant increase in volume.

#### QUALITY LIQUIDITY AND CAPITAL RESOURCES

Quality generated \$1.5 million in net cash from operating activities for the three months ended March 31, 1997. Net cash used in investing activities was approximately \$0.1 million, principally for equipment purchases. Net cash used in financing activities was \$0.3 million, representing repayment of long-term debt.

At March 31, 1997, Quality had working capital of \$3.5 million and \$1.1 million of total debt outstanding.

Quality generated \$4.5 million in net cash from operating activities for the twelve months ended December 31, 1996. Net cash used in investing activities was approximately \$0.4 million, principally for equipment purchases. Net cash used in financing activities was \$4.4 million, of which \$3.5 million was distributed to shareholders and \$0.9 million was used to repay long-term debt.

At December 31, 1996, Quality had working capital of \$4.9 million and \$1.3 million of total debt outstanding.

#### ATLAS RESULTS OF OPERATIONS

Atlas, headquartered in Houston, Texas, was founded in 1947 and operates primarily in the southwest, northeast and mid-Atlantic regions of the United States. Atlas is a leading provider of HVAC installation services for apartment complexes, condominiums, hotels and elder care facilities in the United States and also provides maintenance, repair and replacement of HVAC systems.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED JUNE 30,						SIX MONTHS ENDED DECEMBER 31,	
	1994		1995		1996		1995	
(IN THOUSANDS)								
Revenues.....	\$ 21,848	100.0%	\$ 22,444	100.0%	\$ 29,174	100.0%	\$ 14,689	100.0%
Cost of services.....	19,657	90.0	19,635	87.5	25,449	87.2	12,886	87.7
Gross profit.....	2,191	10.0	2,809	12.5	3,725	12.8	1,803	12.3
Selling, general and administrative expenses.....	2,086	9.5	2,166	9.6	2,843	9.8	1,417	9.6
Income from operations..	105	0.5	643	2.9	882	3.0	386	2.7
THREE MONTHS ENDED MARCH 31,								
	1996		1996		1997			
Revenues.....	\$ 15,545	100.0%	\$ 6,207	100.0%	\$ 6,115	100.0%		
Cost of services.....	12,508	80.5	5,456	87.9	4,866	79.6		
Gross profit.....	3,037	19.5	751	12.1	1,249	20.4		
Selling, general and administrative expenses.....	1,432	9.2	631	10.2	753	12.3		
Income from operations..	1,605	10.3	120	1.9	496	8.1		

#### ATLAS RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARE D TO THREE MONTHS ENDED MARCH 31, 1996

**REVENUES.** Revenues decreased \$0.1 million, or 1.5%, from \$6.2 million for the three months ended March 31, 1996 to \$6.1 million for the three months ended March 31, 1997.

**GROSS PROFIT.** Gross profit increased \$0.4 million, or 66.3%, from \$0.8 million for the three months ended March 31, 1996 to \$1.2 million for the three months ended March 31, 1997. As a percentage of revenues, gross profit increased from 12.1% to 20.4% due to management's ability to be more selective in accepting projects.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses increased \$0.2 million, or 19.3%, from \$0.6 million for the three months ended March 31, 1996 to \$0.8 million for the three months ended March 31, 1997. As a percentage of revenues, selling, general and administrative expenses increased from 10.2% to 12.3% due to the addition of administrative personnel and related costs.

#### ATLAS RESULTS FOR SIX MONTHS ENDED DECEMBER 31, 1996 COMPARED TO SIX MONTHS ENDED DECEMBER 31, 1995

**REVENUES.** Revenues increased \$0.8 million, or 5.8%, from \$14.7 million for the six months ended December 31, 1995 to \$15.5 million for the six months ended December 31, 1996. This increase was primarily attributable to an increase in demand for Atlas' specialized services for multi-unit facilities.

**GROSS PROFIT.** Gross profit increased \$1.2 million, or 68.4%, from \$1.8 million for the six months ended December 31, 1995 to \$3.0 million for the six



revenues, gross profit increased from 12.3% to 19.5% due to an increase in the proportion of "design and build" projects and management's ability to be more selective in accepting projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses remained unchanged at \$1.4 million for the six months ended December 31, 1995 and the six months ended December 31, 1996. As a percentage of revenues, selling, general and administrative expenses decreased from 9.6% to 9.2% as Atlas was able to increase revenues without a commensurate increase in overhead expenses.

#### ATLAS RESULTS FOR YEAR ENDED JUNE 30, 1996 COMPARED TO YEAR ENDED JUNE 30, 1995

REVENUES. Revenues increased \$6.8 million, or 30.0%, from \$22.4 million for the year ended June 30, 1995 to \$29.2 million for the year ended June 30, 1996 due to an increase in demand for Atlas' specialized services for multi-unit facilities.

GROSS PROFIT. Gross profit increased \$0.9 million, or 32.6%, from \$2.8 million for the year ended June 30, 1995 to \$3.7 million for the year ended June 30, 1996. As a percentage of revenues, gross profit increased from 12.5% to 12.8%.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.6 million, or 31.3%, from \$2.2 million for the year ended June 30, 1995 to \$2.8 million for the year ended June 30, 1996, as Atlas increased its infrastructure to support higher volume. As a percentage of revenues, selling, general and administrative expenses increased from 9.6% to 9.8%.

#### ATLAS RESULTS FOR JUNE 30, 1995 COMPARED TO YEAR ENDED JUNE 30, 1994

REVENUES. Revenues increased \$0.6 million, or 2.7%, from \$21.8 million for the year ended June 30, 1994 to \$22.4 million for the year ended June 30, 1995.

GROSS PROFIT. Gross profit increased \$0.6 million, or 28.2%, from \$2.2 million for the year ended June 30, 1994 to \$2.8 million for the year ended June 30, 1995. As a percentage of revenues, gross profit increased from 10.0% to 12.5%. The increase in the gross profit percentage from 1994 to 1995 was primarily related to higher demand for Atlas' specialized installation services for multi-unit facilities and a decrease in lower-margin "plan and spec" projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.1 million, or 3.8%, from \$2.1 million for the twelve months ended June 30, 1994 to \$2.2 million for the twelve months ended June 30, 1995. As a percentage of revenues, selling, general and administrative expenses increased from 9.5% to 9.6%.

#### ATLAS LIQUIDITY AND CAPITAL RESOURCES

Atlas generated \$0.2 million in net cash from operating activities for the three months ended March 31, 1997. Net cash used in investing activities was approximately \$0.1 million, primarily for equipment purchases. Net cash provided by financing activities was \$0.2 million, representing borrowings on the line of credit.

At March 31, 1997, Atlas had working capital of \$2.8 million and total debt of \$2.0 million.

Atlas used \$0.3 million in net cash from operating activities for the twelve months ended June 30, 1996 primarily due to an increase in accounts receivable which were collected in subsequent periods. Net cash used in investing activities was approximately \$0.1 million for equipment purchases. Net cash provided by financing activities was \$0.3 million for the twelve months ended June 30, 1996, principally as a result of a net increase in long-term debt and notes payable.

At December 31, 1996, Atlas had working capital of \$2.7 million and total debt of \$1.8 million.

#### TRI-CITY RESULTS OF OPERATIONS

Tri-City, headquartered in Tempe, Arizona, was founded in 1962 and operates in Arizona, California and Nevada. Tri-City focuses on providing "design and build" installation services and maintenance, repair

and replacement of HVAC systems primarily for large commercial and industrial facilities, as well as process piping for industrial facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED DECEMBER 31,						THREE MONTHS ENDED	
	1994		1995		1996		MARCH 31,	
							1996	
	(IN THOUSANDS)							
Revenues.....	\$ 16,883	100.0%	\$ 25,030	100.0%	\$ 24,237	100.0%	\$ 6,482	100.0%
Cost of services.....	14,271	84.5	19,298	77.1	18,561	76.6	5,082	78.4
Gross profit.....	2,612	15.5	5,732	22.9	5,676	23.4	1,400	21.6
Selling, general and administrative expenses.....	2,219	13.2	3,193	12.8	3,903	16.1	1,026	15.8
Income from operations.....	393	2.3	2,539	10.1	1,773	7.3	374	5.8
	THREE MONTHS ENDED							
	MARCH 31,							
	1997							
Revenues.....	\$ 6,791	100.0%						
Cost of services.....	5,946	87.6						
Gross profit.....	845	12.4						
Selling, general and administrative expenses.....	567	8.3						
Income from operations.....	278	4.1						

TRI-CITY RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

REVENUES. Revenues increased \$0.3 million, or 4.8%, from \$6.5 million for the three months ended March 31, 1996 to \$6.8 million for the three months ended March 31, 1997 due primarily to an increase in "design and build" installation activity for a large medical institution. Tri-City pursued this project to expand its presence in its regional healthcare HVAC market. Tri-City was selected as the lead mechanical contractor on this project. Installation of the HVAC and process piping systems on this project began in October 1996 and accounted for approximately 45% of the revenues in the three months ended March 31, 1997. This particular project is for a nationally-known healthcare organization, and represents the first major facility on what is expected to be a medical campus covering more than 100 acres.

GROSS PROFIT. Gross profit decreased \$0.6 million, or 39.6%, from \$1.4 million for the three months ended March 31, 1996 to \$0.8 million for the three months ended March 31, 1997. As a percentage of revenues, gross profit decreased from 21.6% to 12.4%. In its role as lead mechanical contractor on this major healthcare project Tri-City is responsible for arranging a significant amount of subcontract work as well as for procuring most of the HVAC equipment on this project. Margins on subcontract work and procured equipment are typically lower than margins on work performed directly by Tri-City.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses decreased \$0.4 million, or 44.7%, from \$1.0 million for the three months ended March 31, 1996 to \$0.6 million for the three months ended March 31, 1997 due to a decrease in owners' compensation. As a percentage of revenues, selling, general and administrative expenses decreased from 15.8% to 8.3% due to the decrease in owners' compensation.

TRI-CITY RESULTS FOR YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED DECEMBER 31, 1995

REVENUES. Revenues decreased \$0.8 million, or 3.2%, from \$25.0 million in 1995 to \$24.2 million in 1996, primarily due to a decrease in "plan and spec" revenues from 1995 to 1996 of approximately \$2.0 million, partially offset by an increase of approximately \$1.2 million in commercial HVAC maintenance, repair and replacement service revenues.

GROSS PROFIT. Gross profit remained constant at \$5.7 million for 1995 and 1996. As a percentage of revenues, gross profit increased from 22.9% to 23.4%, due to a decrease in lower margin "plan and spec" projects in 1996.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.7 million, or 22.2%, from \$3.2 million in 1995 to \$3.9 million in 1996 due to a \$1.1 million increase in compensation to owners in lieu of S Corporation distributions, offset by a \$0.4 million reduction in other overhead expenses. As a percentage of revenues, selling, general and administrative expenses increased from 12.8% in 1995 to 16.1% in 1996, primarily as a result of the increase in owners' compensation.

TRI-CITY RESULTS FOR YEAR ENDED DECEMBER 31, 1995 COMPARED TO YEAR ENDED DECEMBER 31, 1994

REVENUES. Revenues increased \$8.1 million, or 48.2%, from \$16.9 million in 1994 to \$25.0 million in 1995 as a result of a strategy implemented in 1994 to emphasize "design and build" projects. To implement its strategy, Tri-City increased its sales and project management staff.

GROSS PROFIT. Gross profit increased \$3.1 million, or 119.4%, from \$2.6 million in 1994 to \$5.7 million in 1995. As a percentage of revenues, gross profit increased from 15.5% in 1994 to 22.9% in 1995 as a result of an increase in the proportion of "design and build" installation projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$1.0 million, or 43.9%, from \$2.2 million in 1994 to \$3.2 million in 1995. The increase in selling, general and administrative expenses in 1995 was primarily attributable to a \$0.8 million increase in compensation to owners in lieu of S Corporation distributions and an increase in the number of the sales personnel and project managers. As a percentage of revenues, selling, general and administrative expenses decreased from 13.2% in 1994 to 12.8% in 1995 as Tri-City was able to substantially increase its volume without a commensurate increase in overhead expenses.

TRI-CITY LIQUIDITY AND CAPITAL RESOURCES

Tri-City generated \$0.7 million in net cash from operating activities for the three months ended March 31, 1997. Investing and financing activities were immaterial during this period.

At March 31, 1997, working capital was \$5.8 million and there was no debt outstanding.

Tri-City generated \$1.4 million in net cash from operating activities in 1996. Net cash used in investing activities was approximately \$0.7 million, of which \$0.5 million was used for investments in U.S. Treasury obligations and \$0.2 million for equipment purchases. Net cash used in financing activities was \$1.2 million, primarily for distributions to shareholders.

At December 31, 1996, working capital was \$5.5 million and there was no debt outstanding.

LAWRENCE RESULTS OF OPERATIONS

Lawrence, headquartered in Jackson, Tennessee, was founded in 1917 and operates primarily in Tennessee and the surrounding states. Lawrence focuses on providing "design and build" installation services and process piping primarily for industrial facilities and maintenance, repair and replacement of commercial and industrial HVAC systems.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED OCTOBER 31,						SIX MONTHS ENDED	
	1994		1995		1996		APRIL 30	
							1996	
	(IN THOUSANDS)							
Revenues.....	\$ 12,758	100.0%	\$ 12,568	100.0%	\$ 17,163	100.0%	\$ 6,736	100.0%
Cost of services.....	9,797	76.8	9,142	72.7	12,211	71.1	4,958	73.6
Gross profit.....	2,961	23.2	3,426	27.3	4,952	28.9	1,778	26.4
Selling, general and administrative expenses.....	2,849	22.3	3,477	27.7	4,885	28.5	1,976	29.3
Income (loss) from operations.....	112	0.9	(51)	(0.4)	67	0.4	(198)	(2.9)
	SIX MONTHS ENDED							
	APRIL 30							
	1997							
Revenues.....	\$ 8,563	100.0%						
Cost of services.....	6,139	71.7						
Gross profit.....	2,424	28.3						
Selling, general and administrative expenses.....	1,630	19.0						
Income (loss) from operations.....	794	9.3						

LAWRENCE RESULTS FOR SIX MONTHS ENDED APRIL 30, 1997 COMPARED TO SIX MONTHS ENDED APRIL 30, 1996

REVENUES. Revenues increased \$1.9 million, or 27.1%, from \$6.7 million for the six months ended April 30, 1996 to \$8.6 million for the six months ended April 30, 1997 primarily due to both an increase in "design and build" installation revenues primarily related to a manufacturing facility in North Carolina and a \$0.6 million increase in maintenance, repair and replacement revenues.

GROSS PROFIT. Gross profit increased \$0.6 million, or 36.3%, from \$1.8 million for the six months ended April 30, 1996 to \$2.4 million for the six months ended April 30, 1997. As a percentage of revenues,



gross profit increased from 26.4% to 28.3% as a result of an increase in the proportion of "design and build" installation projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses decreased \$0.4 million, or 17.5%, from \$2.0 million for the six months ended April 30, 1996 to \$1.6 million for the six months ended April 30, 1997 primarily due to a decrease in discretionary bonuses to the owners of \$0.6 million. As a percentage of revenues, selling, general and administrative expenses decreased from 29.3% to 19.0% due to the increase in revenues and the decrease in owners' compensation.

LAWRENCE RESULTS FOR YEAR ENDED OCTOBER 31, 1996 COMPARED TO YEAR ENDED OCTOBER 31, 1995

REVENUES. Revenues increased \$4.6 million, or 36.6%, from \$12.6 million for the year ended October 31, 1995 to \$17.2 million for the fiscal year ended October 31, 1996 due to a management decision in 1995 to expand the number of general contractors for which Lawrence provides industrial installation services and due to a large "design and build" installation contract obtained in 1996 for a food processing facility in Tennessee.

GROSS PROFIT. Gross profit increased \$1.5 million, or 44.5%, from \$3.5 million for the fiscal year ended October 31, 1995 to \$5.0 million for the fiscal year ended October 31, 1996. As a percentage of revenues, gross profit increased from 27.3% to 28.9%, primarily as a result of an increase in the volume of "design and build" installation projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$1.4 million, or 40.5%, from \$3.5 million for the fiscal year ended October 31, 1995 to \$4.9 million for the fiscal year ended October 31, 1996. The increase in selling, general and administrative expenses in fiscal 1996 was primarily attributable to a \$0.6 million increase in salary and incentive compensation paid to the owners and a \$0.7 million increase in incentive compensation to employees and discretionary profit sharing contributions. As a percentage of revenues, selling, general and administrative expenses increased from 27.7% in fiscal 1995 to 28.5% in fiscal 1996.

LAWRENCE RESULTS FOR FISCAL YEAR ENDED OCTOBER 31, 1995 COMPARED TO FISCAL YEAR ENDED OCTOBER 31, 1994

REVENUES. Revenues decreased \$0.2 million, or 1.5%, from \$12.8 million the fiscal year ended October 31, 1994 to \$12.6 million for the fiscal year ended October 31, 1995.

GROSS PROFIT. Gross profit increased \$0.4 million, or 15.7%, from \$3.0 million for the fiscal year ended October 31, 1994 to \$3.4 million for the fiscal year ended October 31, 1995. As a percentage of revenues, gross profit increased from 23.2% to 27.3% as management emphasized higher-margin "design and build" projects and successfully implemented an incentive program for project managers designed to control project costs.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.7 million, or 22.0%, from \$2.8 million in fiscal 1994 to \$3.5 million in fiscal 1995 primarily due to an increase in salary and incentive compensation paid to the owners. As a percentage of revenues, selling, general and administrative expenses increased from 22.3% in fiscal 1994 to 27.7% in fiscal 1995 and, as a result, Lawrence incurred an operating loss in fiscal 1995.

LAWRENCE LIQUIDITY AND CAPITAL RESOURCES

Lawrence used \$0.2 million in net cash from operating activities for the six months ended April 30, 1997 primarily due to a decrease in accounts payable and accrued expenses. Net cash used in investing activities was approximately \$0.1 million, principally for equipment purchases.

Working capital as of April 30 1997 was \$1.8 million and there was no debt outstanding as of that date.

Lawrence generated \$0.1 million in net cash from operating activities for the fiscal year ended October 31, 1996. Net cash used in investing activities was approximately \$0.4 million, principally for equipment purchases and leasehold improvements.

Working capital as of October 31, 1996 was \$1.4 million and there was no debt outstanding as of that date.



ACCURATE RESULTS OF OPERATIONS

Accurate, headquartered in Houston, Texas, was founded in 1980 and operates primarily in Texas and Oklahoma. Accurate focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED JUNE 30,		YEAR ENDED		THREE MONTHS ENDED			
	1994	1995	DECEMBER 31,	1996	MARCH 31,	1996		
	(IN THOUSANDS)							
Revenues.....	\$ 9,763	100.0%	\$ 12,171	100.0%	\$ 16,806	100.0%	\$ 3,161	100.0%
Cost of services.....	7,204	73.8	8,998	73.9	13,270	79.0	2,450	77.5
Gross profit.....	2,559	26.2	3,173	26.1	3,536	21.0	711	22.5
Selling, general and administrative expenses.....	2,681	27.5	2,960	24.3	3,037	18.0	684	21.6
Income (loss) from operations.....	(122)	(1.3)	213	1.8	499	3.0	27	0.9
	THREE MONTHS ENDED							
	MARCH 31,							
	1997							
Revenues.....	\$ 2,642	100.0%						
Cost of services.....	2,095	79.3						
Gross profit.....	547	20.7						
Selling, general and administrative expenses.....	526	19.9						
Income (loss) from operations.....	21	0.8						

ACCURATE RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

REVENUES. Revenues decreased \$0.6 million, or 16.4%, from \$3.2 million for the three months ended March 31, 1996 to \$2.6 million for the three months ended March 31, 1997 due to a decrease in commercial installation services. This decrease resulted from a decrease in commercial installation services due to the greater number of days of inclement weather in Texas during the first three months of 1997 compared to the same period of the prior year.

GROSS PROFIT. Gross profit decreased \$0.2 million, or 23.1%, from \$0.7 million for the three months ended March 31, 1996 to \$0.5 million for the three months ended March 31, 1997. As a percentage of revenues, gross profit decreased from 22.5% to 20.7% due to the decrease in revenues.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses decreased \$0.2, or 23.1% from \$0.7 million for the three months ended March 31, 1996 to \$0.5 million for the three months ended March 31, 1997 primarily due to a decrease in owners' compensation. As a percentage of revenues, selling, general and administrative expenses decreased from 21.6% to 19.9%.

ACCURATE RESULTS FOR YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED JUNE 30, 1995

REVENUES. Revenues increased \$4.6 million, or 38.1%, from \$12.2 million for the year ended June 30, 1995 to \$16.8 million for the year ended December 31, 1996, reflecting the success of an increased marketing effort along with the addition of project management personnel who also have sales responsibility. These efforts resulted in an increase in commercial "design and build" installation revenues and an increase in replacement services.

GROSS PROFIT. Gross profit increased \$0.3 million, or 11.4%, from \$3.2 million for the year ended June 30, 1995 to \$3.5 million for the year ended December 31, 1996. As a percentage of revenues, gross profit decreased from 26.1% to 21.0%, primarily as a result of an increase in subcontract labor and employee overtime necessary to support the increased number of "design and build" projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses remained constant at \$3.0 million for the fiscal year ended June 30, 1995 and the year ended December 31, 1996. As a percentage of revenues, selling, general and administrative expenses decreased from 24.3% to 18.0% as Accurate was able to increase revenues without a commensurate increase in overhead expenses.

ACCURATE RESULTS FOR YEAR ENDED JUNE 30, 1995 COMPARED TO YEAR ENDED JUNE 30, 1994

REVENUES. Revenues increased \$2.4 million, or 24.7%, from \$9.8 million for the year ended June 30, 1994 to \$12.2 million for the fiscal year ended June 30, 1995. This increase was primarily attributable to a

new project for an existing customer to design and build an HVAC system for a correctional facility and an increase in maintenance and replacement services.

**GROSS PROFIT.** Gross profit increased \$0.6 million, or 24.0%, from \$2.6 million for the fiscal year ended June 30, 1994 to \$3.2 million for the fiscal year ended June 30, 1995. As a percentage of revenues, gross profit remained stable over these periods.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses increased \$0.3 million, or 10.4%, from \$2.7 million in fiscal 1994 to \$3.0 million in fiscal 1995. As a percentage of revenues, selling, general and administrative expenses decreased from 27.5% to 24.3% as Accurate was able to increase revenues without a commensurate increase in overhead expenses.

#### ACCURATE LIQUIDITY AND CAPITAL RESOURCES

Accurate used \$0.1 million of net cash for operating activities for the three months ended March 31, 1997. Net cash provided by financing activities of \$0.2 million resulted from an increase in long-term debt used to fund working capital needs.

Working capital at March 31, 1997 was \$0.2 million and total debt outstanding was \$1.5 million, of which \$0.6 million was owed to a shareholder.

Accurate generated \$0.2 million in net cash from operating activities for the year ended December 31, 1996. Net cash used in investing activities was approximately \$0.1 million for equipment purchases.

Working capital at December 31, 1996 was \$0.2 million and total debt outstanding was \$1.3 million, of which \$0.6 million was owed to a shareholder.

#### CSI/BONNEVILLE RESULTS OF OPERATIONS

CSI/Bonneville, headquartered in Salt Lake City, Utah, was founded in 1969 and operates primarily in Utah. CSI/Bonneville focuses on providing maintenance, repair and replacement of HVAC systems for commercial and residential facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED DECEMBER 31,						THREE MONTHS ENDED	
	1994		1995		1996		MARCH 31,	
							1996	
	(IN THOUSANDS)							
Revenues.....	\$ 6,502	100.0%	\$ 6,361	100.0%	\$ 7,842	100.0%	\$ 1,369	100.0%
Cost of services.....	4,393	67.6	4,413	69.4	5,201	66.3	926	67.6
Gross profit.....	2,109	32.4	1,948	30.6	2,641	33.7	443	32.4
Selling, general and administrative expenses.....	1,228	18.9	1,500	23.6	1,660	21.2	368	26.9
Income from operations.....	881	13.5	448	7.0	981	12.5	75	5.5
	THREE MONTHS ENDED							
	MARCH 31,							
	1997							
Revenues.....	\$ 1,562	100.0%						
Cost of services.....	1,045	66.9						
Gross profit.....	517	33.1						
Selling, general and administrative expenses.....	458	29.3						
Income from operations.....	59	3.8						

#### CSI/BONNEVILLE RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

**REVENUES.** Revenues increased \$0.2 million, or 14.1%, from \$1.4 million for the three months ended March 31, 1996 to \$1.6 million for the three months ended March 31, 1997 primarily due to an increase in commercial and residential maintenance, repair and replacement services.

**GROSS PROFIT.** Gross profit increased \$0.1 million, or 16.7%, from \$0.4 million for the three months ended March 31, 1996 to \$0.5 million for the three months ended March 31, 1997. As a percentage of revenues, gross profit increased from 32.4% to 33.1%.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses increased \$0.1 million, or 24.5%, from \$0.4 million for the three months ended March 31, 1996 to \$0.5 million for the three months ended March 31, 1997 as a result of an increase in administrative personnel. As a percentage of revenues, selling, general and administrative expenses increased from 26.9% to 29.3%.

CSI/BONNEVILLE RESULTS FOR YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED DECEMBER 31, 1995

REVENUES. Revenues increased \$1.4 million, or 23.3%, from \$6.4 million in 1995 to \$7.8 million in 1996, primarily as a result of an increase in both commercial and residential maintenance, repair and replacement services due to an increase in the number of sales and marketing personnel in 1995 and 1996. Revenues declined in 1995 due to the deployment of operating personnel to a move to a new facility in that year.

GROSS PROFIT. Gross profit increased \$0.7 million, or 35.6%, from \$1.9 million in 1995 to \$2.6 million in 1996. As a percentage of revenues, gross profit increased from 30.6% in 1995 to 33.7% in 1996. The lower gross profit in 1995 was due to the deployment of operating personnel to a move to a new facility.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.2 million, or 10.7%, from \$1.5 million in 1995 to \$1.7 million in 1996. As a percentage of revenues, selling, general and administrative expenses decreased from 23.6% in 1995 to 21.2% in 1996.

CSI/BONNEVILLE RESULTS FOR YEAR ENDED DECEMBER 31, 1995 COMPARED TO YEAR ENDED DECEMBER 31, 1994

REVENUES. Revenues decreased from \$6.5 million in 1994 to \$6.4 million in 1995 as a result of CSI/Bonneville's move into a new facility during 1995.

GROSS PROFIT. Gross profit decreased \$0.2 million, or 7.6%, from \$2.1 million in 1994 to \$1.9 million in 1995. As a percentage of revenues, gross profit declined from 32.4% in 1994 to 30.6% in 1995 as a result of CSI/Bonneville's move into a new facility during 1995.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.3 million, or 22.1%, from \$1.2 million in 1994 to \$1.5 million in 1995. As a percentage of revenues, selling, general and administrative expenses increased from 18.9% in 1994 to 23.6% in 1995. This percentage increase was primarily attributable to rent, depreciation and related costs associated with the new facility occupied in 1995.

CSI/BONNEVILLE LIQUIDITY AND CAPITAL RESOURCES

CSI/Bonneville's operating activities were breakeven on a cash-flow basis for the three months ended March 31, 1997. Net cash used in investing activities was \$0.1 million, principally for equipment purchases.

Working capital at March 31, 1997 was \$0.5 million and total debt outstanding was \$0.5 million, all of which was owed to shareholders.

CSI/Bonneville generated \$1.1 million in net cash from operating activities in 1996. Net cash used in investing activities was \$0.2 million, principally for equipment purchases. Net cash used in financing activities was \$0.8 million, primarily for distributions to shareholders.

Working capital at December 31, 1996 was \$0.5 million and total debt outstanding was \$0.5 million, all of which was owed to shareholders.

TECH RESULTS OF OPERATIONS

Tech, headquartered in Solon, Ohio, was founded in 1979 and operates primarily in the greater Cleveland, Ohio area. Tech focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial and industrial facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED DECEMBER 31,				THREE MONTHS ENDED MARCH 31,			
	1995		1996		1996		1997	
	(IN THOUSANDS)							
Revenues.....	\$ 6,960	100.0%	\$ 7,537	100.0%	\$ 1,075	100.0%	\$ 1,656	100.0%
Cost of services.....	4,212	60.5	3,996	53.0	639	59.4	1,034	62.4
Gross profit.....	2,748	39.5	3,541	47.0	436	40.6	622	37.6
Selling, general and administrative expenses.....	1,800	25.9	1,861	24.7	390	36.3	565	34.1
Income from operations.....	948	13.6	1,680	22.3	46	4.3	57	3.5

TECH RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

REVENUES. Revenues increased \$0.6 million, or 54.0%, from \$1.1 million for the three months ended March 31, 1996 to \$1.7 million for the three months ended March 31, 1997 due primarily to an increase in commercial installation services because there were fewer days of inclement weather in the first three months of 1997 as compared to the prior comparable period.

GROSS PROFIT. Gross profit increased \$0.2 million, or 42.7%, from \$0.4 million for the three months ended March 31, 1996 to \$0.6 million for the three months ended March 31, 1997. As a percentage of revenues, gross profit decreased from 40.6% to 37.6% due to a decrease in the proportion of maintenance, repair and replacement revenues, which typically have higher margins than installation.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.2 million, or 44.9%, from \$0.4 million for the three months ended March 31, 1996 to \$0.6 million for the three months ended March 31, 1997 due to an increased marketing effort, including an increase in marketing personnel. As a percentage of revenues, selling, general and administrative expenses declined from 36.3% to 34.1% as Tech was able to substantially increase its volume without a commensurate increase in overhead expenses.

TECH RESULTS FOR YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED DECEMBER 31, 1995

REVENUES. Revenues increased \$0.5 million, or 8.3%, from \$7.0 million in 1995 to \$7.5 million in 1996. This increase was primarily attributable to an increase in commercial "design and build" installation projects and related service work.

GROSS PROFIT. Gross profit increased \$0.8 million, or 28.9%, from \$2.7 million in 1995 to \$3.5 million in 1996. As a percentage of revenues, gross profit increased from 39.5% to 47.0%, primarily due to an increase in "design and build" versus "plan and spec" installation projects.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses remained relatively unchanged from 1995 to 1996. As a percentage of revenues, selling, general and administrative expenses decreased from 25.9% in 1995 to 24.7% in 1996 as Tech successfully leveraged its infrastructure to achieve revenue growth.

TECH LIQUIDITY AND CAPITAL RESOURCES

Tech generated \$0.6 million in net cash from operating activities for the three months ended March 31, 1997. Net cash used in financing activities was \$0.9 million, principally for distributions to shareholders of \$1.6 million offset by borrowings of long-term debt of \$0.7 million.

Total debt outstanding at March 31, 1997 was \$1.0 million.

Tech generated \$0.9 million in net cash from operating activities in 1996. Net cash used in investing activities was \$0.3 million for equipment purchases. Net cash used in financing activities was \$0.4 million, principally for distributions to shareholders.

Working capital at December 31, 1996 was \$1.6 million and total debt outstanding was \$0.3 million.

WESTERN RESULTS OF OPERATIONS

Western, headquartered in Denver, Colorado, was founded in 1980 and operates primarily in Colorado. Western focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED DECEMBER 31,				THREE MONTHS ENDED MARCH 31,			
	1995		1996		1996		1997	
	(IN THOUSANDS)							
Revenues.....	\$ 4,112	100.0%	\$ 6,494	100.0%	\$ 1,185	100.0%	\$ 1,072	100.0%
Cost of services.....	3,408	82.9	4,662	71.8	857	72.3	812	75.7
Gross profit.....	704	17.1	1,832	28.2	328	27.7	260	24.3
Selling, general and administrative expenses.....	855	20.8	1,088	16.7	232	19.6	231	21.6
Income (loss) from operations.....	(151)	(3.7)	744	11.5	96	8.1	29	2.7

WESTERN RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

REVENUES. Revenues decreased \$0.1 million, or 9.5%, from \$1.2 million for the three months ended March 31, 1996 to \$1.1 million for the three months ended March 31, 1997.

GROSS PROFIT. Gross profit was \$0.3 million for the three months ended March 31, 1996 and the three months ended March 31, 1997. As a percentage of revenues, gross profit decreased from 27.7% to 24.3% due primarily to the decline in revenues.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses remained constant at \$0.2 million for the three months ended March 31, 1996 and the three months ended March 31, 1997. As a percentage of revenues, selling, general and administrative expenses increased from 19.6% to 21.6% due to the decline in revenues.

WESTERN RESULTS FOR YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED DECEMBER 31, 1995

REVENUES. Revenues increased \$2.4 million, or 57.9%, from \$4.1 million in 1995 to \$6.5 million in 1996. This increase was primarily attributable to an increase in commercial replacement revenues of \$1.5 million related to the Demand Side Management ("DSM") incentive program developed by the Public Service Company of Colorado ("PSC"). This program provided incentives for commercial PSC customers to replace existing HVAC systems with more energy-efficient systems and ended in November 1996. Management believes that a significant portion of the revenues generated under the DSM program can be replaced by redeploying Western's sales force to emphasize installation of commercial control systems and commercial maintenance, repair and replacement services. Western does not intend to participate in this program during 1997.

GROSS PROFIT. Gross profit increased \$1.1 million, or 160.2%, from \$0.7 million in 1995 to \$1.8 million in 1996. As a percentage of revenues, gross profit increased from 17.1% in 1995 to 28.2% in 1996, primarily due to an increase in maintenance, repair and replacement revenues, including revenues generated under the DSM program.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses increased \$0.2 million in 1995, or 27.3%, from \$0.9 million in 1995 to \$1.1 million in 1996. As a percentage of revenues, selling, general and administrative expenses decreased from 20.8% to 16.7% as a result of the substantial revenue increase without a commensurate increase in overhead expenses.

WESTERN LIQUIDITY AND CAPITAL RESOURCES

Western used \$0.1 million in net cash from operating activities in the three months ended March 31, 1997 primarily due to a decrease in accounts payable and accrued expenses.

Working capital at March 31, 1997 was \$0.3 million and total long-term debt outstanding was \$0.2 million.

Western generated \$0.6 million in net cash from operating activities in 1996. Net cash used in investing activities was approximately \$0.1 million, principally for equipment purchases. Net cash used in financing activities was \$0.4 million, as a result of distributions to shareholders and net repayments of long-term debt.

Working capital at December 31, 1996 was \$0.4 million and total long-term debt outstanding was \$0.3 million.

SEASONAIR RESULTS OF OPERATIONS

Seasonair, headquartered in Rockville, Maryland, was founded in 1966 and operates primarily in Maryland, the District of Columbia and Virginia. Seasonair focuses on providing installation services and maintenance, repair and replacement of HVAC systems for light commercial facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED DECEMBER 31, 1996		THREE MONTHS ENDED MARCH 31,			
			1996		1997	
Revenues.....	\$ 6,737	100.0%	\$ 1,128	100.0%	\$ 1,831	100.0%
Cost of services.....	4,006	59.5	586	52.0	1,165	63.6
Gross profit.....	2,731	40.5	542	48.0	666	36.4
Selling, general and administrative expenses.....	2,597	38.5	604	53.5	644	35.2
Income (loss) from operations.....	134	2.0	(62)	(5.5)	22	1.2

SEASONAIR RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

REVENUES. Revenues increased \$0.7 million, or 62.3%, from \$1.1 million for the three months ended March 31, 1996 to \$1.8 million for the three months ended March 31, 1997 due to an increase in maintenance, repair and replacement services resulting from management's decision to expand the business more rapidly.

GROSS PROFIT. Gross profit increased \$0.2 million, or 22.9%, from \$0.5 million for the three months ended March 31, 1996 to \$0.7 million from the three months ended March 31, 1997. As a percentage of revenues, gross profit decreased from 48.0% to 36.4%.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Selling, general and administrative expenses were \$0.6 million for the three months ended March 31, 1996 and the three months ended March 31, 1997. As a percentage of revenues, selling, general and administrative expenses decreased from 53.5% to 35.2% due to management's ability to increase revenues without a commensurate increase in overhead expenses.

SEASONAIR LIQUIDITY AND CAPITAL RESOURCES

Seasonair generated \$0.1 million in net cash from operating activities for the three months ended March 31, 1997 due to a decrease in prepaid expenses and other current assets and an increase in accounts payable and accrued expenses. Net cash provided by financing activities was \$0.1 million from borrowings on the line of credit.

Working capital at March 31, 1997 was \$0.5 million and total debt outstanding was \$0.2 million.

Seasonair used \$0.2 million in net cash from operating activities in 1996 primarily due to an increase in prepaid expenses and other current assets. Net cash provided by investing activities was \$0.1 million

from proceeds on sale of equipment. Net cash used in financing activities was \$0.1 million to repay long-term debt.

Working capital at December 31, 1996 was \$0.5 million and total debt outstanding was \$0.1 million.

#### EASTERN RESULTS OF OPERATIONS

Eastern, headquartered in Albany, New York, was founded in 1945 and operates primarily within a 75 mile radius of Albany, New York. Eastern focuses on providing "design and build" installation and maintenance, repair and replacement of HVAC systems for commercial and industrial facilities. Eastern also offers continuous monitoring and control services for commercial facilities.

The following table sets forth selected statement of operations data and such data as a percentage of revenues for the periods indicated:

	YEAR ENDED DECEMBER 31, 1996		THREE MONTHS ENDED MARCH 31,			
			1996		1997	
Revenues.....	\$ 7,944	100.0%	\$ 1,525	100.0%	\$ 1,284	100.0%
Cost of services.....	5,276	66.4	973	63.8	805	62.7
Gross profit.....	2,668	33.6	552	36.2	479	37.3
Selling, general and administrative expenses.....	2,237	28.2	532	34.9	582	45.3
Income (loss) from operations.....	431	5.4	20	1.3	(103)	(8.0)

#### EASTERN RESULTS FOR THREE MONTHS ENDED MARCH 31, 1997 COMPARED TO THREE MONTHS ENDED MARCH 31, 1996

**REVENUES.** Revenues decreased \$0.2 million, or 15.8% from \$1.5 million for the three months ended March 31, 1996 to \$1.3 million for the three months ended March 31, 1997 due primarily to a decrease in maintenance, repair and replacement services. As a result of a mild winter season in the first three months of 1997 in the Albany, New York area, the need for service work on heating equipment decreased.

**GROSS PROFIT.** Gross profit decreased \$0.1 million, or 13.2%, from \$0.6 million for the three months ended March 31, 1996 to \$0.5 million for the three months ended March 31, 1997. As a percentage of revenues, gross profit increased from 36.2% to 37.3%.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, general and administrative expenses increased \$0.1 million, or 9.4%, from \$0.5 million for the three months ended March 31, 1996 to \$0.6 million for the three months ended March 31, 1997. As a percentage of revenues, selling, general and administrative expenses increased from 34.9% to 45.3% due to the higher expenses and the decrease in revenues.

#### EASTERN LIQUIDITY AND CAPITAL RESOURCES

Eastern generated \$0.1 million in net cash from operating activities primarily from a net decrease in accounts receivables of \$0.3 million. Cash flows used for financing activities were \$0.1 million for distributions to shareholders and \$0.1 million for repayment of long-term debt. Cash flows used in financing activities was \$0.2 million of borrowings on the line of credit.

As of March 31, 1997, Eastern had a working capital deficit of \$0.2 million and total debt outstanding of \$1.0 million. Eastern has historically funded its operations with cash flow from operations and debt from lenders and shareholders. The Company believes that Eastern has adequate financing alternatives to fund its operations.

Eastern generated \$0.5 million in net cash from operating activities in 1996 primarily due to \$0.4 million in net income. Net cash used in investing activities was \$0.2 million for the purchase of property and equipment. Net cash used in financing activities in 1996 was \$0.3 million for distributions to shareholders.

Working capital at December 31, 1996 was \$0.1 million and total debt outstanding was \$0.9 million of which \$0.3 million is payable to the former owner.

#### SEASONAL AND CYCLICAL NATURE OF THE HVAC INDUSTRY

The HVAC industry is subject to seasonal variations. Specifically, the demand for new installations is generally lower during the winter months due to reduced construction activities 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 quarters due to the 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 quarters. 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.

#### INFLATION

Inflation did not have a significant effect on the results of operations of the combined Founding Companies for 1994, 1995 or 1996 or the three months ended March 31, 1997.



## BUSINESS

Comfort Systems was founded in 1996 to become a leading national provider of comprehensive HVAC installation services and maintenance, repair and replacement of HVAC systems, focusing primarily on the commercial and industrial markets. Comfort Systems acquired the twelve Founding Companies on July 2, 1997. The Company's commercial and industrial applications include office buildings, retail centers, apartment complexes, hotels, manufacturing plants and government facilities. The Company also provides specialized HVAC applications such as process cooling, control systems, electronic monitoring and process piping. Approximately 90% of the Company's pro forma combined 1996 revenues of \$167.5 million was derived from commercial and industrial customers, with approximately 53% of combined revenues attributable to installation services and 47% attributable to maintenance, repair and replacement services. Combined revenues of the Founding Companies, which have been in business an average of 39 years, increased at a compound annual growth rate of approximately 16% from 1994 through 1996.

### INDUSTRY OVERVIEW

Based on available industry data, the Company believes that the HVAC industry is highly fragmented with over 40,000 companies, most of which are small, owner-operated businesses with limited access to capital for modernization and expansion. The overall HVAC industry, including the commercial, industrial and residential markets, is estimated to generate annual revenues in excess of \$75 billion, over \$35 billion of which is in the commercial and industrial markets. HVAC systems have become 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 addressing air quality concerns and injecting fresh air. Older industrial facilities often have poor air quality as well as inadequate air conditioning, factors which are causing industrial facility owners to consider replacement options. Operation of older HVAC systems represents a significant cost due to their energy inefficiency. 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 the effectiveness of the HVAC system and air quality.

Growth in the HVAC industry is being 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 and (iii) the increasing restrictions on the use of refrigerants commonly used in older HVAC systems. These factors are expected to increase demand for the reconfiguration or replacement of existing HVAC systems. These factors also mitigate the effect on the HVAC industry of the cyclicity inherent in the traditional construction industry.

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

**INSTALLATION SEGMENT.** The installation segment consists 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 meet 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, 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 an architect or a consulting engineer designs the HVAC system 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 and the bid process often take months to complete. Furthermore, in "plan and spec" projects, the HVAC firm is not responsible for project design and changes must be approved by several parties, thereby increasing overall project time and cost.

**MAINTENANCE, REPAIR AND REPLACEMENT SEGMENT.** This segment includes the maintenance, repair, replacement, reconfiguration and monitoring of previously installed HVAC systems and controls. Growth in

this segment has been fueled by the aging of the installed base of HVAC systems and the increasing demand for more efficient, sophisticated and complex systems and controls. The increasing sophistication and complexity of these HVAC systems is leading many commercial and industrial building owners and property managers 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 air quality concerns, are expected to increase demand for the reconfiguration and replacement of existing HVAC systems. State-of-the-art control and monitoring systems feature electronic sensors and microprocessors and require specialized training to install, maintain and repair, which the typical building engineer does not have. 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.

The Company believes that the majority of business owners in the HVAC industry have limited access to capital for expansion of their businesses and that few have attractive liquidity options. In addition, the increasing complexity of HVAC systems has led to a need for better trained technicians to install, monitor and service these systems. The cost of recruiting, training and retaining a sufficient number of qualified technicians makes it more difficult for smaller HVAC companies to expand their businesses. The Company believes that significant opportunities exist for a well-capitalized, national company operating in the commercial, industrial and residential markets of the HVAC industry and that the highly fragmented nature of this industry should allow it to consolidate existing HVAC businesses.

#### STRATEGY

The Company plans to achieve its goal of becoming a leading national provider of comprehensive HVAC services by implementing its operating strategy, emphasizing continued internal growth and expanding through acquisitions.

**OPERATING STRATEGY.** The Company believes there are significant opportunities to increase the profitability of the Founding Companies and subsequently acquired businesses. The key elements of the Company's operating strategy are:

**FOCUS ON COMMERCIAL AND INDUSTRIAL MARKETS.** The Company intends to focus principally on the commercial and industrial markets with particular emphasis on the "design and build" installation and the maintenance, repair and replacement segments. The Company believes that the commercial and industrial HVAC markets are attractive because of their growth opportunities, diverse customer base, attractive margins and potential for long-term relationships with building owners and managers, general contractors and architects.

**OPERATE ON DECENTRALIZED BASIS.** The Company intends to manage the Founding Companies on a decentralized basis, with local management assuming responsibility for the day-to-day operations, profitability and growth of the business. The Company believes that, while maintaining strong operating and financial controls, a decentralized operating structure will retain the entrepreneurial spirit present in each of the Founding Companies and will allow the Company to capitalize on the considerable local and regional market knowledge and customer relationships possessed by each Founding Company.

**ACHIEVE OPERATING EFFICIENCIES.** The Company believes there are significant opportunities to achieve operating efficiencies and cost savings through purchasing economies and the adoption of "best practices" operating programs. The Company intends to use its increased purchasing power to gain volume discounts in areas such as HVAC components, raw materials, service vehicles, advertising, bonding and insurance. Moreover, the Company will review its operations and training programs at the local and regional operating levels in order to identify those "best practices" that can be successfully implemented throughout its operations.

**ATTRACT AND RETAIN QUALITY EMPLOYEES.** The Company intends 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) improved benefits packages.

**INTERNAL GROWTH.** A key component of the Company's strategy is to continue the internal growth at the Founding Companies and subsequently acquired businesses. The key elements of the Company's internal growth strategy are:

**CAPITALIZE ON SPECIALIZED TECHNICAL AND MARKETING STRENGTHS.** The Company believes it will be able to expand the services it offers in its markets by leveraging the specialized technical and marketing strengths of individual Founding Companies. For example, one of the Founding Companies has developed significant industry recognition for its technical expertise within apartment complexes, condominiums, hotels and elder care facilities which may be transferable to other Founding Companies. A number of Founding Companies currently focus primarily on installation and, therefore, have only limited maintenance, repair and replacement operations. The Company believes there are significant opportunities for these Founding Companies to provide maintenance, repair and replacement services, particularly by offering those services to its "design and build" customers. Several of the Founding Companies have specific expertise in HVAC control and monitoring systems, process cooling, replacement and other service strengths, many of which can be shared with other Founding Companies and subsequently acquired businesses.

**ESTABLISH NATIONAL MARKET COVERAGE.** The Company believes that significant demand exists from large national companies to utilize the services of a single HVAC service company capable of providing comprehensive commercial and industrial services on a regional or national basis. Many of the Founding Companies already provide local or regional coverage to companies with nationwide locations, such as commercial real estate developers and managers, retailers and manufacturers. The Company believes these existing relationships can be expanded as it develops a nationwide network since these customers often desire a single source for all of their HVAC needs to promote consistency, improve control and reduce cost.

**ACQUISITIONS.** The Company believes the HVAC industry is highly fragmented with over 40,000 companies, most of which are small, owner-operated businesses with limited access to adequate capital for modernization and expansion. The Company anticipates that acquisition candidates in the commercial and industrial markets will typically have annual revenues ranging from \$5 million to \$35 million. The key elements of the Company's acquisition strategy are:

**ENTER NEW GEOGRAPHIC MARKETS.** In new markets, the Company intends to target one or more leading local or regional companies providing HVAC or complementary services. The acquisition target will have the customer base, technical skills and infrastructure necessary to be a core business into which other HVAC service operations can be consolidated. The Company will choose businesses that are located in attractive markets, are financially stable, are experienced in the industry and have management willing to participate in the future growth of the Company.

**EXPAND WITHIN EXISTING MARKETS.** Once the Company has entered a market, it will seek to acquire other well-established HVAC businesses to expand its market penetration and range of services offered. The Company also will pursue "tuck-in" acquisitions of smaller companies, whose operations can be integrated into an existing Company operation to leverage the existing infrastructure.

**ACQUIRE COMPLEMENTARY BUSINESSES.** The Company will focus on its traditional markets in the HVAC industry and may acquire companies providing complementary services to the same customer base, such as commercial and industrial process piping and plumbing as well as electrical companies. This will enable the Company to offer, on a comprehensive basis and from a single provider, HVAC, mechanical and electrical services in certain markets.

#### ACQUISITION PROGRAM

The Company believes it will be regarded by acquisition candidates as an attractive acquirer because of: (i) the Company's strategy for creating a national, comprehensive and professionally managed HVAC

service provider that capitalizes on cross-marketing and business development opportunities; (ii) the Company's decentralized operating strategy; (iii) the Company's increased visibility and access to financial resources as a public company; (iv) the potential for increased profitability due to certain centralized administrative functions, enhanced systems capabilities and access to increased marketing resources; and (v) the potential for the owners of the businesses being acquired to participate in the Company's planned internal growth and growth through acquisitions, while realizing liquidity.

The Company believes the management teams of the Founding Companies will be instrumental in identifying and completing future acquisitions. The Company's visibility within the HVAC industry will increase the awareness and interest of acquisition candidates in the Company and its acquisition program. Within the past several months, the Company has contacted the owners of a number of acquisition candidates, several of whom have expressed interest in having their business acquired by the Company. The Company currently has no binding agreements to effect any acquisition other than the Founding Companies.

As consideration for future acquisitions, the Company intends to use various combinations of its Common Stock, cash and notes. The consideration for each future acquisition will vary on a case-by-case basis. The major factors in establishing the purchase price for each acquisition will be historical operating results, future prospects of the acquiree and the ability of that business to complement the services offered by the Company. Management believes that companies providing commercial and industrial HVAC services are larger than those providing residential services, with commercial and industrial companies generating annual revenues ranging from \$5 million to \$35 million, compared to companies providing residential HVAC services which generally have annual revenues ranging from \$500,000 to \$3 million.

#### OPERATIONS AND SERVICES PROVIDED

The Company provides a wide range of installation, maintenance, repair and replacement services for HVAC systems in commercial, industrial and residential properties. Daily operations are managed on a local basis by the management team at each Founding Company. In addition to senior management, the Founding Companies' personnel generally include design engineers, sales personnel, customer service personnel, installation service technicians, sheet metal and prefabrication technicians, estimators and administrative personnel. Upon consummation of the Mergers, the Company will manage the Founding Companies on a decentralized basis, with local management being responsible for day-to-day operating decisions. The Company intends to centralize certain administrative functions to enable the management of each Founding Company to focus on pursuing new business opportunities and to improve operating efficiencies. Administrative functions which the Company expects to centralize include Company-wide training and safety programs, accounting programs, risk management programs, purchasing programs and employee benefits.

**INSTALLATION SEGMENT.** The Company's installation business comprised approximately 53% of the Company's 1996 revenues. This segment consists of the design, engineering, integration, installation and start-up of HVAC systems. The commercial and industrial installation services performed by the Company consist primarily of "design and build" systems for office buildings, retail centers, apartment complexes, hotels, manufacturing plants and government 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 sales and engineering personnel to prepare a specific design for the HVAC system. The Company determines the needed capacity, energy efficiency and type of 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. Materials and equipment for a typical commercial or industrial project include ductwork, compressors, blowers, chillers, cooling towers, air handling equipment and the associated pumps and piping necessary to complete the system. The Company utilizes CAD/CAM systems in the design and engineering phases of the project to calculate the material and labor costs of the project based on previously established Company standards and to generate mechanical drawings for each project. The drawings are prepared in a format appropriate for submission to local building inspectors. 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.

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, thereby eliminating the need to subcontract ductwork or piping fabrication. The Company's CAD/CAM systems are capable of automatically cutting ductboard, sheet metal and piping, thereby reducing the amount of labor necessary to produce the ductwork and piping for the system. Project specific components are then fabricated at the Company's facilities in sections small enough to be transported to the job site. This enables the Company to limit the amount of field work required for installation, reduce the labor associated with the actual installation process and meet the shorter time requirements increasingly demanded by commercial and industrial customers. 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 \$25,000 to \$2,000,000 per project. These projects are generally billed periodically as costs are incurred throughout the project, with a 10% retainage until completion and successful start-up of the HVAC system.

Atlas, one of the Founding Companies, specializes in the design and installation of HVAC systems for apartment complexes, condominiums, hotels and elder care facilities. Because the room layouts in these types of buildings are typically very similar, Atlas is able to design a single HVAC system, or a few systems, suitable for installation in all units within the project. This permits Atlas to prepare a "kit" containing all parts for an individual unit and ship all of the kits for a particular project to the job site, thereby significantly decreasing installation time.

The Company also performs selected "plan and spec" installation services when a bidder prequalification process has been used by the customer to limit the number of potential bidders for an attractive project. The Company may use these projects when "design and build" projects are in lower demand and to provide additional on-the-job training to apprentice or less-experienced technicians.

The Company also installs process cooling systems, control 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. Control systems are used in HVAC and process cooling systems in order to maintain pre-established temperature or climate standards for commercial or industrial facilities. These systems use direct digital technology integrated with computer terminals. HVAC 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. Monitoring can be performed on-site or remotely through a PC-based communications system. The monitoring system will sound an alarm when the HVAC 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 materials, support utilities and finished products.

The Company's residential services consist of installing complete central HVAC systems in new and existing homes, often through agreements with housing developers. In 1996, residential installation comprised approximately 2% of the Company's revenues.

The Founding Companies generally warrant their labor for the first year after installation on new HVAC systems and for 30 days after servicing of existing HVAC systems. A reserve for warranty costs is recorded based on a percentage of material costs.

**MAINTENANCE, REPAIR AND REPLACEMENT SEGMENT.** The Company's maintenance, repair and replacement segment comprised approximately 47% of the Company's 1996 combined revenues and includes the maintenance, repair, replacement, reconfiguration and monitoring of HVAC systems and industrial process piping. Over one-half of the Company's maintenance, repair and replacement segment 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 communications technology to process orders, arrange service calls, communicate with customers, dispatch technicians and invoice customers. Service technicians work out of service vans 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, and typically provide fees from \$3,000 to \$20,000 per year. The Company also provides remote monitoring of temperature, pressure, humidity and air flow for HVAC systems for commercial and industrial customers. 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, as appropriate. Residential service agreements generally have one year terms, automatic renewal provisions and provide annual fees between \$100 and \$200 per 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 take a month or more to obtain. Chillers for large units typically have the longest delivery time and generally have lead times of up to six months. The major components of 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 control systems are Honeywell Inc., Johnson Controls Inc., York and Andover Control Corporation. The Company believes that it will be able to reduce costs on raw materials and components through volume purchases. The Company does not currently have any significant contracts for the supply of raw materials or components.

#### SALES AND MARKETING

The Company has a diverse customer base, with no single customer accounting for more than 4% of the Company's pro forma combined 1996 revenues. Management and a dedicated sales force at the Founding Companies have been responsible for developing and maintaining successful long-term relationships with key customers. Customers of the Founding Companies 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 will receive additional technical and sales training to enhance the comprehensive selling skills necessary to serve the HVAC needs of its customers.

The Company also intends to capitalize on cross-marketing and business development opportunities that management believes will be available to the Company as a national provider of comprehensive commercial, industrial and residential HVAC services. Management believes that it will be able to leverage the diverse technical and marketing strengths of individual Founding Companies to expand the services offered in other local markets. Eventually, the Company intends to offer comprehensive services from many of its regional locations.

#### EMPLOYEES

As of July 29, 1997 the Company had 1,482 employees, including 98 management personnel, 1,160 engineers and service and installation technicians, 67 sales personnel and 157 administrative personnel. The Company does not anticipate any reductions in staff as a result of the recent consolidation of the Founding Companies. Rather, as it implements its internal growth and acquisition strategies, the Company expects

that the number of employees will increase. Three of the Founding Companies have collective bargaining agreements which cover, in the aggregate, fewer than 50 employees. Under these agreements, these Founding Companies make payments to multi-employer pension plans. The Company has not experienced any strikes or work stoppages and believes its relationship with its employees and union representatives is satisfactory.

#### RECRUITING, TRAINING AND SAFETY

The Company's 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 recruits at local technical schools and community colleges where students focus on learning basic HVAC and related skills, and provides on-the-job training, apprenticeship programs, improved benefit packages, steady employment and opportunities for advancement.

The Company intends to establish "best practices" throughout its operations to ensure that all technicians comply with safety standards established by the Company, its insurance carriers and federal, state and local laws and regulations. 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. The Company believes that these employment criteria effectively identify potential employees committed to safety and quality. Additionally, the Company intends to implement a "best practices" safety program throughout its operations, which will provide employees with incentives to improve safety performance and decrease workplace accidents. The Company intends to implement job site safety meetings and instruct personnel in proper lifting techniques and eye safety in an effort to reduce the number of preventable accidents.

#### FACILITIES AND VEHICLES

All of the Company's facilities are leased. See "Certain Transactions -- Leases of Real Property by Founding Companies."

The Founding Companies collectively lease approximately 250,000 square feet of commercial property, which they utilize for office, warehouse, fabrication and storage space. Leased premises range in size from 50,200 square feet, in the case of Quality, to 7,000 square feet and 6,500 square feet in the case of Eastern and Seasonair, respectively. In addition, Atlas currently leases 14 one-bedroom apartments for technicians and installation crews working on projects around the country. The Company believes that the opportunities for some of the Founding Companies to use fabrication and storage facilities of other Founding Companies for sheet metal cutting, equipment fabrication and inventory storage will increase operating efficiencies for the Company as a whole. The Company believes that its facilities are sufficient for its current needs.

The Company operates a fleet of approximately 600 owned or leased service trucks, vans and support vehicles. It believes these vehicles generally are well-maintained and adequate for the Company's current operations. The Company expects it will be able to purchase vehicles at lower prices due to its increased purchasing volume.

The Company leases its principal executive and administrative offices in Houston, Texas and is currently in the process of relocating within Houston, Texas.

#### RISK MANAGEMENT, INSURANCE AND LITIGATION

The primary risks in the Company's operations are bodily injury, property damage and injured workers' compensation. The Company has obtained and intends to maintain liability insurance for bodily injury and third party property damage which it considers sufficient to insure against these risks, subject to self-insured amounts. The workers' compensation insurance policies held by the Founding Companies generally provide for first dollar coverage.

The Company is, from time to time, a party to litigation arising in the normal course of its business, most of which involves claims for personal injury and property damage incurred in connection with its operations. The Company is not currently involved in any litigation, nor is the Company aware of any threatened litigation, that the Company believes is likely to have a material adverse effect on its financial condition or results of operations.

The Company generally offers one year warranties on labor it performs and passes to the customer warranties on equipment purchased from manufacturers. The Company does not expect warranty claims to have a material effect on its results of operations or financial condition.

#### 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 believes its strategy of becoming a leading national provider of comprehensive HVAC installation services as well as maintenance, repair and replacement of HVAC systems directly addresses these factors. Specifically, the Company's strategy to focus on the highly consultative "design and build" installation segment and the maintenance, repair and replacement segment, as well as its strategy to operate on a decentralized basis, should promote the development and strengthening of long-term customer relationships. In addition, the Company's focus on attracting, training and retaining quality employees by utilizing professionally managed recruiting, training and benefits programs should allow it to offer high quality, comprehensive HVAC services at a competitive price.

Most of the Company's competitors are small, owner-operated companies that typically operate in a limited geographic area. There are a few public companies focused on providing HVAC services in some of the same services lines provided by the Company. In addition, there are a number of private companies attempting to consolidate HVAC companies on a regional or national basis. In the future, competition may be encountered from new entrants, such as public utilities and HVAC manufacturers. Certain of the Company's competitors and potential competitors may have greater financial resources than the Company to finance acquisition and development opportunities, to pay higher prices for the same opportunities or to develop and support their own 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 the Company's service technicians who work in the state or county that issued the permit or license. The Company intends to implement 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. As a result, the number of conversions of existing HVAC systems which use CFCs to systems using alternative refrigerants is expected to increase.

Prior to entering into the agreements relating to the Mergers, the Company evaluated the properties owned or leased by the Founding Companies and engaged an independent environmental consulting firm to conduct or review assessments of environmental conditions at these properties. No material environmental problems were discovered in these reviews, and the Company is not aware of any material environmental liabilities associated with these properties.

MANAGEMENT

DIRECTORS, EXECUTIVE OFFICERS AND KEY EMPLOYEES

The following table sets forth information concerning the Company's directors, executive officers and key employees.

NAME ----	AGE ---	POSITION -----
Fred M. Ferreira.....	54	Chairman of the Board, Chief Executive Officer and President
Michael Nothum, Jr.....	43	Chief Operating Officer (acting), President of Tri-City, Director
J. Gordon Beittenmiller.....	38	Senior Vice President, Chief Financial Officer and Director
Reagan S. Busbee.....	33	Senior Vice President
William George, III.....	32	Vice President, General Counsel and Secretary
Milburn E. Honeycutt.....	33	Vice President and Controller
S. Craig Lemmon.....	45	Vice President -- Acquisitions
Brian J. Vensel.....	36	Vice President -- Acquisitions
Brian S. Atlas.....	45	Chief Executive Officer of Atlas, Director
Thomas J. Beaty.....	43	President of Accurate, Director
Robert R. Cook.....	42	President of Tech, Director
Alfred J. Giardenelli, Jr.....	50	President of Eastern, Director
Charles W. Klapperich.....	50	President of Western, Director
Samuel M. Lawrence III.....	45	Chief Executive Officer of Lawrence, Director
John C. Phillips.....	55	President of CSI/Bonneville, Director
Robert J. Powers.....	57	President of Quality, Director
Steven S. Harter.....	35	Director
Larry Martin.....	55	Director
John Mercadante, Jr.....	52	Director
Robert Arbuckle.....	47	President of Freeway
James C. Hardin, Sr.....	35	Chief Executive Officer of Seasonair
Thomas B. Kime.....	50	President of Standard

Fred M. Ferreira has served as Chairman of the Board, Chief Executive Officer and President of Comfort Systems since January 1997. Mr. Ferreira was responsible for introducing the consolidation opportunity in the commercial and industrial HVAC industry to Notre and has been primarily responsible for the organization of Comfort Systems, the acquisition of the Founding Companies and this Offering. From 1995 through 1996, Mr. Ferreira was a private investor. He served as Chief Operating Officer and a director of Allwaste, Inc., a publicly-traded environmental services company ("Allwaste"), from 1994 to 1995, and was President of Allwaste Environmental Services, Inc., the largest division of Allwaste, from 1991 to 1994. From 1989 to 1990, Mr. Ferreira served as President of Allied Waste Industries, Inc., an environmental services company. Prior to that time, Mr. Ferreira served as Vice President -- Southern District and in various other positions with Waste Management, Inc., an environmental services company.

Michael Nothum, Jr. is a director of the Company and its Chief Operating Officer (acting). He has been employed by Tri-City since 1979, serving as President since 1992. Mr. Nothum currently serves on the Education and Training Committee of Associated Builders and Contractors and on the Legislative Committee of the Air Conditioning Contractors Association. It is anticipated that Mr. Nothum will return full-time to his duties at Tri-City when a permanent Chief Operating Officer joins the Company.

J. Gordon Beittenmiller has served as Senior Vice President, Chief Financial Officer and a director of Comfort Systems since February 1997. 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 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 company. From August 1986 to May 1992, he was a certified public accountant with Arthur Andersen LLP.

William George, III has served as Vice President, General Counsel and Secretary of Comfort Systems since March 1997. From October 1995 to March 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 law firm.

Milburn E. Honeycutt has served as Vice President and Controller of Comfort Systems since February 1997. 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. Mr. Honeycutt is a Certified Public Accountant.

S. Craig Lemmon is Vice President -- Acquisitions. Mr. Lemmon has been a consultant to Comfort Systems since its inception in December 1996. From 1993 to 1996, he served as Manager of Mergers and Acquisitions of Allwaste Environmental Services, Inc. From 1992 to 1993, he served as Vice President -- Acquisitions and Vice President -- Southern Region of United Waste Systems, Inc., an environmental services company. Prior thereto, Mr. Lemmon held various positions in the transportation and solid waste industries.

Brian J. Vensel has served as Vice President -- Acquisitions of the Company since February 1997. From September 1996 through January 1997, Mr. Vensel served as Projects Director of the Liquids Business Unit of NGC Corporation, a publicly-traded gas marketer and processor. From April 1996 through August 1996, Mr. Vensel served as Corporate Controller and an officer of Phoenix Energy Products, Inc., a privately-owned, oilfield service company. From 1982 through March 1996, Mr. Vensel held various positions, primarily with Price Waterhouse LLP and Arthur Andersen LLP. Mr. Vensel is a Certified Public Accountant.

Brian S. Atlas is a director of the Company. He has been employed by Atlas since 1974, serving as its Chief Executive Officer since 1983.

Thomas J. Beaty is a director of the Company. He founded and has served as President of Accurate since 1980.

Robert R. Cook is a director of the Company. He founded and has served as President of Tech since 1979.

Alfred J. Giardenelli, Jr. is a director of the Company. He has been the President of Eastern since 1982.

Charles W. Klapperich is a director of the Company. He founded and has served as President of Western since 1980.

Samuel M. Lawrence III is a director of the Company. He has been employed by Lawrence since 1977, serving as its Chairman and Chief Executive Officer since 1991.

John C. Phillips is a director of the Company. He co-founded CSI/Bonneville in 1969, serving as President and General Manager since 1969. Mr. Phillips was President of the Utah Heating and Air Conditioning Contractors Association from 1981 to 1982 and is currently a director of that association.

Robert J. Powers is a director of the Company. He has been employed by Quality since 1977, serving as President since 1988.

Steven S. Harter has been a director of the Company since December 1996 and is the director elected by the holders of the Restricted Common Stock. Mr. Harter is President of Notre, a consolidator of highly-fragmented industries. Prior to becoming the President of Notre, Mr. Harter was Senior Vice President of Notre Capital Ventures, Ltd. ("Notre I") from June 1993 through July 1995 and was the Notre I principal primarily responsible for the initial public offerings of US Delivery Systems, Inc., a consolidator of the local delivery industry, and Physicians Resource Group, Inc., a consolidator of eye care physician management companies. From April 1989 to June 1993, Mr. Harter was Director of Mergers and Acquisitions for Allwaste. From May 1984 to April 1989, Mr. Harter was a certified public accountant with Arthur Andersen LLP. Mr. Harter also serves as a director of Coach USA, Inc. ("Coach").

Larry Martin is a director of the Company. Mr. Martin, a co-founder of Sanifill, Inc., an environmental services provider ("Sanifill"), served as its Vice Chairman from March 1992 through August 1996. From July 1991 to February 1992, he was President of Sanifill, and from October 1989 to July 1991, he served as its President and Co-Chief Executive Officer. Prior to that time, Mr. Martin served in various positions in the environmental services and contracting industries. Mr. Martin currently serves on the Board of Directors of USA Waste Services, Inc., an environmental services company.

John Mercadante, Jr. is a director of the Company. Mr. Mercadante co-founded Leisure Time Tours, Inc. in 1970 and was President of Cape Transit Corp. both of which are motor coach companies that were acquired by Coach at the time of Coach's initial public offering in May 1996. Mr. Mercadante has served as President, Chief Operating Officer and a director of Coach since its initial public offering.

Robert Arbuckle has been employed by Freeway since 1975, serving as its President since 1987.

James C. Hardin, Sr. has been employed by Seasonair since 1986, serving initially as a service technician, as field supervisor from 1988 to 1990, as service manager from 1990 to 1993 and as Vice President of Operations from 1993 to March 1997. Mr. Hardin currently serves as Chief Executive Officer of Seasonair

Thomas B. Kime has been employed by Standard since 1977, serving as its President since 1996.

The Board of Directors is divided into three classes of four, five and five directors, respectively, with directors serving staggered three-year terms, expiring at the annual meeting of stockholders in 1998, 1999 and 2000, respectively. At each annual meeting of stockholders, one class of directors will be elected for a full term of three years to succeed that class of directors whose terms are expiring. All officers serve at the discretion of the Board of Directors.

The Board of Directors has established an Audit Committee, a Compensation Committee and an Executive Committee. The members of the Audit Committee and the Compensation Committee are Messrs. Harter, Mercadante and Martin. The members of the Executive Committee have yet to be selected and will include at least one outside director.

#### DIRECTORS' COMPENSATION

Directors who are also employees of the Company or one of its subsidiaries will not receive additional compensation for serving as directors. Each director who is not an employee of the Company or one of its subsidiaries will receive a fee of \$2,000 for attendance at each Board of Directors' meeting and \$1,000 for each committee meeting (unless held on the same day as a Board of Directors' meeting). In addition, under the Company's 1997 Non-Employee Directors' Stock Plan, each non-employee director will automatically be granted an option to acquire 10,000 shares of Common Stock upon such person's initial election as a director, and an annual option to acquire 5,000 shares at each annual meeting of the Company's stockholders thereafter at which such director is re-elected or remains a director, unless such annual meeting is held within three months of such person's initial election as a director. Each non-employee director also may elect to receive shares of Common Stock or credits representing "deferred shares" in lieu of cash directors' fees. See " -- 1997 Non-Employee Directors' Stock Plan." Directors are also reimbursed for out-of-pocket expenses incurred in attending meetings of the Board of Directors or committees thereof.

The Company was incorporated in December 1996 and did not pay any of its executive officers compensation during 1996. The Company anticipates that during 1997 its five most highly compensated executive officers will be Messrs. Ferreira, Beittenmiller, George, Nothum and Powers.

Each of Messrs. Ferreira, Beittenmiller and George has entered into an employment agreement with the Company providing for an annual base salary of \$150,000. Each employment agreement is for a term of three years, and unless terminated or not renewed by the Company or not renewed by the employee, the term will continue thereafter on a year-to-year basis on the same terms and conditions existing at the time of renewal. Each of these agreements provides that, in the event of a termination of employment by the Company without cause, the employee will be entitled to receive from the Company an amount equal to one year's salary, payable in one lump sum on the effective date of termination. In the event of a change in control of the Company (as defined in the agreement) during the initial three-year term, if the employee is not given at least five days' notice of such change in control, the employee may elect to terminate his employment and receive in one lump sum three times the amount he would receive pursuant to a termination without cause during such initial term. The non-competition provisions of the employment agreement do not apply to a termination without such notice. In the event the employee is given at least five days' notice of such change in control, the employee may elect to terminate his employment and receive in one lump sum three times the amount he would receive pursuant to a termination without cause during such initial term. In such event, the non-competition provisions of the employment agreement would apply for two years from the effective date of termination. Each employment agreement contains a covenant not to compete with the Company for a period of two years immediately following termination of employment or, in the case of a termination by the Company without cause in the absence of a change in control, for a period of one year following termination of employment.

Each of Messrs. Nothum and Powers has entered into an employment agreement with their respective Founding Company providing for an annual base salary of \$150,000. Each employment agreement is for a term of five years, and unless terminated or not renewed by the Founding Company or not renewed by the employee, the term will continue thereafter on a year-to-year basis on the same terms and conditions existing at the time of renewal. Each of these agreements provides that, in the event of a termination of employment by the Founding Company without cause during the first three years of the employment term (the "Initial Term"), the employee will be entitled to receive from the Founding Company an amount equal to his then current salary for the remainder of the Initial Term or for one year, whichever is greater. In the event of a termination of employment with cause during the final two years of the initial five year term of the employment agreement, the employee will be entitled to receive an amount equal to his then current salary for one year. In either case, payment is due in one lump sum on the effective date of termination. In the event of a change in control of the Company (as defined in the agreement) during the Initial Term, if the employee is not given at least five days' notice of such change in control, the employee may elect to terminate his employment and receive in one lump sum three times the amount he would receive pursuant to a termination without cause during the Initial Term. The non-competition provisions of the employment agreement do not apply to a termination without such notice. In the event the employee is given at least five days' notice of such change in control, the employee may elect to terminate his employment agreement and receive in one lump sum two times the amount he would receive pursuant to a termination without cause during the Initial Term. In such event, the non-competition provisions of the employment agreement would apply for two years from the effective date of termination. Each employment agreement contains a covenant not to compete with the Company for a period of two years immediately following termination of employment or, in the case of a termination by the Company without cause in the absence of a change in control, for a period of one year following termination of employment.

At least one principal executive officer of each of the other Founding Companies has entered into an employment agreement, containing substantially the same provisions, including a covenant not to compete, as Messrs. Nothum's and Power's employment agreements.

#### 1997 LONG-TERM INCENTIVE PLAN

No stock options were granted to, or exercised by or held by any executive officer in 1996. In March 1997, the Board of Directors and the Company's stockholders approved the Company's 1997 Long-Term Incentive Plan (the "Plan"). The purpose of the Plan is to provide directors, officers, key employees, consultants and other service providers with additional incentives by increasing their ownership interests in the Company. Individual awards under the Plan may take the form of one or more of: (i) either incentive stock options ("ISOs") or non-qualified stock options ("NQSOs"), (ii) stock appreciation rights ("SARs"), (iii) restricted or deferred stock, (iv) dividend equivalents and (v) other awards not otherwise provided for, the value of which is based in whole or in part upon the value of the Common Stock.

The Compensation Committee will administer the Plan and select the individuals who will receive awards and establish the terms and conditions of those awards. The maximum number of shares of Common Stock that may be subject to outstanding awards, determined immediately after the grant of any award, may not exceed the greater of 2,500,000 shares or 13% of the aggregate number of shares of Common Stock outstanding. Shares of Common Stock which are attributable to awards which have expired, terminated or been canceled or forfeited are available for issuance or use in connection with future awards.

The Plan will remain in effect until terminated by the Board of Directors. The Plan may be amended by the Board of Directors without the consent of the stockholders of the Company, except that any amendment, although effective when made, will be subject to stockholder approval if required by any Federal or state law or regulation or by the rules of any stock exchange or automated quotation system on which the Common Stock may then be listed or quoted.

At the closing of the IPO, NQSOs to purchase a total of 675,000 shares of Common Stock were granted as follows: 200,000 shares to Mr. Ferreira, 100,000 shares to Mr. Beittenmiller, 100,000 shares to Mr. Busbee, 100,000 shares to Mr. Lemmon, 75,000 shares to Mr. George, 50,000 shares to Mr. Honeycutt and 50,000 shares to Mr. Vensel. In addition, at the closing of the IPO, options to purchase 1,469,953 shares were granted to certain employees of the Founding Companies and to other key employees of the Company. Each of the foregoing options has an exercise price equal to the initial public offering price per share. These options will vest at the rate of 20% per year, commencing on the first anniversary of the IPO and will expire at the earlier of seven years from the date of grant or three months following termination of employment.

#### 1997 NON-EMPLOYEE DIRECTORS' STOCK PLAN

The Company's 1997 Non-Employee Directors' Stock Plan (the "Directors' Plan"), which was adopted by the Board of Directors and approved by the Company's stockholders in March 1997, provides for (i) the automatic grant to each non-employee director serving at the consummation of the IPO of an option to purchase 10,000 shares, (ii) the automatic grant to each non-employee director of an option to purchase 10,000 shares upon such person's initial election as a director and (iii) an automatic annual grant to each non-employee director of an option to purchase 5,000 shares at each annual meeting of stockholders thereafter at which such director is re-elected or remains a director, unless such annual meeting is held within three months of such person's initial election as a director. All options have an exercise price per share equal to the fair market value of the Common Stock on the date of grant and are immediately vested and expire on the earlier of ten years from the date of grant or one year after termination of service as a director. The Directors' Plan also permits non-employee directors to elect to receive, in lieu of cash directors' fees, shares or credits representing "deferred shares" at future settlement dates, as selected by the director. The number of shares or deferred shares received will equal the number of shares of Common Stock which, at the date the fees would otherwise be payable, will have an aggregate fair market value equal to the amount of such fees.

CERTAIN TRANSACTIONS

ORGANIZATION OF THE COMPANY

In connection with the formation of Comfort Systems, Comfort Systems issued to Notre a total of 2,969,912 shares of Common Stock for an aggregate cash consideration of \$29,699. Mr. Harter is the President of Notre and a director of the Company. In March 1997, Notre exchanged 2,742,912 shares of Common Stock for an equal number of shares of Restricted Common Stock. Notre advanced \$1.4 million to provide funds necessary to effect the Mergers and the IPO. All of Notre's advances were repaid from the net proceeds of the IPO.

In January and February 1997, the Company issued a total of 902,435 shares of Common Stock at \$.01 per share to various members of management, as follows: Mr. Ferreira -- 479,435 shares, Mr. Beittenmiller -- 116,000 shares, Mr. Busbee -- 116,000 shares, Mr. George -- 75,000 shares, Mr. Honeycutt -- 58,000 shares and Mr. Vensel -- 58,000 shares. The Company also issued 116,000 shares to Mr. Lemmon and 251,500 shares of Common Stock to other consultants to the Company at \$.01 per share. The Company also granted options to purchase 10,000 shares of Common Stock under the Directors' Plan, effective upon the consummation of the IPO, to Mr. Harter, a Director of the Company, and to Messrs. Mercadante and Martin, who became directors of the Company upon the closing of the IPO.

In connection with the IPO, Comfort Systems acquired by merger or share exchange all of the issued and outstanding stock of the Founding Companies, each of which is now a wholly-owned subsidiary of the Company. The aggregate consideration paid by Comfort Systems in the Mergers consisted of \$45.3 million in cash and 9,720,927 shares of Common Stock. In addition, prior to the Mergers, Accurate distributed to Thomas J. Beaty real property having a net book value of approximately \$370,000.

The following table sets forth the consideration paid and total debt assumed by Comfort Systems for each of the Founding Companies:

	CASH	SHARES OF COMMON STOCK	TOTAL DEBT
(DOLLARS IN THOUSANDS)			
Quality.....	\$ 10,082	2,207,158	\$ 7,389
Tri-City.....	8,680	1,557,962	3,479
Atlas.....	6,864	1,432,000	1,540
Lawrence.....	4,500	1,197,796	300
Tech.....	3,997	717,408	1,906
Accurate.....	3,145	564,537	985
CSI/Bonneville.....	1,813	493,672	1,385
Western.....	2,022	362,939	777
Freeway.....	1,039	319,698	203
Seasonair.....	1,516	272,084	154
Standard.....	947	291,457	433
Eastern.....	698	304,216	1,138
Total.....	\$ 45,303	9,720,927	\$ 19,689

Additionally, prior to the Mergers, the Founding Companies which are C Corporations, except Atlas, made Interim Earnings Distributions to their stockholders in the amount of \$1.5 million.

In connection with the Mergers, and as consideration for their interests in the Founding Companies, certain officers, directors, key employees and holders of more than 5% of the outstanding shares of the Company, together with their spouses and trusts for which they act as trustees, received cash and shares of Common Stock of the Company as follows:

NAME	CASH	SHARES OF COMMON STOCK
(DOLLARS IN THOUSANDS)		
Robert J. Powers.....	\$ 8,143	1,461,496
Michael Nothum, Jr.....	4,236	760,287
Robert R. Cook.....	3,997	717,408
Brian S. Atlas.....	3,432	716,000
Thomas J. Beaty.....	3,145	564,537
John C. Phillips.....	1,310	403,305
Samuel M. Lawrence III.....	1,031	317,307
Alfred J. Giardenelli, Jr.....	698	304,216
Charles W. Klapperich.....	1,423	255,401

Pursuant to the agreements entered into in connection with the Mergers, the stockholders of the Founding Companies have agreed not to compete with the Company for five years, commencing on the date of consummation of the IPO.

#### LEASES OF REAL PROPERTY BY FOUNDING COMPANIES

Atlas leases its office space in Houston, Texas, as well as mobile homes located in Austin, Texas; Phoenix, Arizona; and Antioch, Tennessee. These properties are owned by M & B Interests, Inc. ("M & B"), a corporation wholly-owned by Mr. Brian S. Atlas, who is a director of the Company, and his brother, Mr. Michael Atlas. The lease for the real property in Houston expires on September 30, 1997 and provides for an annual rental of \$90,000. The three single family residences are leased on a month-to-month basis, at an annual aggregate rental of \$36,780. The Company has also agreed to enter into an agreement with M & B to lease a newly constructed office and warehouse facility to be constructed by M & B in Houston for an annual rental of \$204,000. When construction is completed, this new office and warehouse facility will replace Atlas' existing facility. The Company believes that the rent for these properties does not exceed fair market value.

Tri-City leases its office space in Tempe, Arizona from Mr. Nothum, Jr. and his father. Mr. Nothum, Jr. is a trustee of a family trust that is a stockholder of Tri-City and will become a director of the Company upon consummation of this Offering. The lease expires on June 30, 1998 and provides for an annual rental of \$120,000. Additionally, Tri-City provides liability insurance on the property and is responsible for any increases in real property taxes due to its improvement of the leased property. Tri-City has entered into an agreement with a limited liability corporation owned by Mr. Nothum, Jr. and his father to lease office, operations and warehouse facilities which are being constructed, for a ten year term at annual rental of \$530,100. The Company believes that the rent for these properties does not and will not exceed fair market value.

Lawrence leases its office space and fabrication facility in Jackson, Tennessee from the father of Mr. Samuel M. Lawrence III, who is Lawrence's Chief Executive Officer and a director of the Company. The lease expires on October 31, 1997 and provides for an annual rental of \$110,400. Additionally, Lawrence provides liability insurance on the property and pays its proportionate share of ad valorem taxes, utilities and maintenance costs. The Company believes that the rent for this property does not exceed fair market value.



Accurate leases two parcels of real property in Houston, Texas owned by Mr. Beaty, who is a director of the Company. One of the leased premises is used by Accurate for office and warehouse space. The lease on one of these premises expires on June 30, 2002 and provides for an annual rental of \$38,000. The other leased premise is used by Accurate as a sheet metal shop under a lease dated July 1, 1997, that will expire on June 30, 2002 and will provide for an annual rental of \$46,700. The rental rate on these premises in subsequent years of the lease term will be adjusted in accordance with the Consumer Price Index. Additionally, Accurate will pay all utility, taxes and insurance costs on both leased premises. Accurate has options to renew each lease for two additional five-year terms. The Company believes that the rent for both properties does not and will not exceed fair market value. Accurate previously owned the property it uses for its sheet metal shop. Prior to the Mergers, Accurate distributed this property having a net book value of approximately \$370,000 to Mr. Beaty.

Eastern leases its office and warehouse space in Albany, New York from 60 Loudonville Road Associates ("Loudonville"), a partnership of Mr. Alfred J. Giardenelli, Jr., who is a director of the Company, and his brother. The lease provides for annual rental of \$55,000 and payment by Eastern of taxes, maintenance, repairs, utilities and insurance costs on the leased premises. The Company believes that the rent for this property does not exceed the fair market value. The lease expires on December 31, 1999. Prior to expiration, however, Eastern intends to enter into a 10-year lease with Loudonville for a new building and to terminate the existing lease. Eastern has agreed to install the HVAC systems in the new building at a price which the Company believes to be at a fair market value. The Company's annual rental in the new building will be at fair market value, as determined by an appraisal.

CSI/Bonneville leases its office and warehouse space in Salt Lake Valley, Utah from J & J Investments, a joint venture partly owned by Mr. Phillips, who is a director of the Company. This lease expires on February 28, 2002 and provides for an annual rental in 1997 of \$120,720, increasing annually by 5%. CSI/Bonneville is responsible for ad valorem taxes, maintenance, insurance and third-party management costs related thereto. CSI/Bonneville has options to renew the lease for two additional five-year terms at a fair market value, as determined by an appraisal. The Company believes that the rent for this property does not exceed fair market value.

Tech leases its office and warehouse space in Solon, Ohio from Mr. Cook, who is a director of the Company. The lease expires on April 2, 2000, and provides for an annual rental of \$84,000. Tech is responsible for its utility costs, 15% of common utility costs and 50% of the landlord's cost of servicing and maintaining the premises and providing comprehensive liability insurance for the leased premises. The Company believes that the rent for such property does not exceed fair market value.

Quality leases its warehouse facility in Grand Rapids, Michigan from Mr. Powers, who is a director of the Company. Construction of the warehouse facility was financed with the proceeds of a public bond issue. The lease expires on April 30, 2005, and provides for an annual rental of the greater of \$216,000 or Mr. Powers' costs for the leased warehouse, including bond debt service or mortgage payments, utilities, insurance, ad valorem taxes, maintenance and repairs. Quality has an option to renew the lease for one additional three-year term on the same terms. The Company believes that the rent for such property does not exceed fair market value. Quality has guaranteed the payment of two series of public bonds issued in 1985 and 1990, respectively, by the Michigan Strategic Fund on behalf of two real property development entities owned by Mr. Powers, the proceeds of which were used to fund the construction of Quality's leased warehouse facility and a second adjacent warehouse. As of March 1997, approximately \$1.6 million of the bond debt remained outstanding.

The Company has adopted a policy that, whenever possible, it will not own any real estate. Accordingly, in connection with future acquisitions, the Company may require the distribution of real property owned by acquired companies to its stockholders and the leaseback of such property at fair market value.

## OTHER TRANSACTIONS

Prior to the IPO, Atlas owed \$78,000 to Sid Atlas, the father of Brian and Michael Atlas, payable in monthly installments of \$5,500, including interest at the rate of 10%, through March 1998. Atlas was also the obligor on two promissory notes payable to Brian S. Atlas and Michael Atlas in the outstanding principal amount of \$63,537 to each, providing for aggregate monthly installments of \$4,812, including interest at the rate of 10%, through June 1999. Shortly after the IPO the Company paid and retired all such indebtedness.

On October 31, 1996, Lawrence loaned \$75,000 to Charles Lawrence at an interest rate of 8%. This note was payable on demand or October 31, 2001, and was repaid shortly following the IPO. Charles Lawrence is a brother of Samuel M. Lawrence III, who is a director of the Company on consummation of this Offering.

On December 27, 1996, Accurate borrowed \$630,000 from Mr. Beaty. Interest was payable monthly at the rate of 9% on the outstanding balance. The note matured on June 30, 1997 and was repaid at that time.

CSI/Bonneville owed Messrs. Phillips and another stockholder of CSI/Bonneville \$424,000 and \$105,000, respectively. Two of the promissory notes, payable to Mr. Phillips and the other stockholder, are in the principal amount of \$80,000 and \$20,000, respectively, and are payable on demand. The remaining eight promissory notes are each payable ten years from the date of the note, and mature at various times from 2002 to 2006. All of the notes bear interest at 10%, with interest payable monthly and principal payable at maturity. In 1996, CSI/Bonneville made interest payments to Mr. Phillips and the other stockholder in the amount of \$35,000 and \$6,000, respectively.

During 1996, Mr. Klapperich, who is a director of the Company, received advances from Western aggregating \$173,500. On December 31, 1996, Western credited against this amount a portion of a dividend payable in the amount of \$210,315, discharging the indebtedness of Mr. Klapperich to Western.

On January 2, 1996, Standard loaned Mr. Kime \$480,000 under a promissory note at an interest rate of 7.67%. Mr. Kime has repaid the balance of this note. The note was formerly secured by a pledge of his shares of stock in Standard; however, Standard released its security interest in such stock on March 6, 1997 in anticipation of consummation of the Mergers.

The Company has agreed to pay up to an aggregate of \$150,000 of the legal fees of the owners of the Founding Companies.

The Company has agreed to indemnify Notre for liabilities arising in connection with actions taken by it in connection with its role as a promoter prior to and during the IPO.

## COMPANY POLICY

Any future transactions with directors, officers, employees or affiliates of the Company or its subsidiaries are anticipated to be minimal and will be approved in advance by a majority of disinterested members of the Board of Directors.

PRINCIPAL STOCKHOLDERS

The following table sets forth information regarding the beneficial ownership of the Common Stock, after giving effect to the Mergers and the IPO, by (i) each person known to own beneficially more than 5% of the outstanding shares of Common Stock; (ii) each Company director and person who has consented to be named as a director ("named directors"); (iii) each named executive officer; and (iv) all executive officers, directors and named directors as a group. All persons listed have an address c/o the Company's principal executive offices and have sole voting and investment power with respect to their shares unless otherwise indicated.

NAME	SHARES BENEFICIALLY OWNED(1)	
	NUMBER	PERCENT
Notre Capital Ventures II, L.L.C.....	2,969,912	14.2%
Steven S. Harter(2).....	2,979,912	14.2
Robert J. Powers.....	1,461,915	7.0
Michael Nothum, Jr.(3).....	778,981	3.7
Robert R. Cook.....	717,408	3.4
Brian S. Atlas.....	716,000	3.4
Thomas J. Beaty.....	564,537	2.7
Fred M. Ferreira.....	479,535	2.3
John C. Phillips.....	403,305	1.9
Samuel M. Lawrence III.....	317,307	1.5
Alfred J. Giardenelli, Jr.....	304,216	1.5
Charles W. Klapperich.....	255,401	1.2
J. Gordon Beittenmiller.....	116,000	*
Reagan S. Busbee.....	116,000	*
William George, III.....	75,000	*
Larry Martin(4)(5).....	27,692	*
John Mercadante, Jr.(4)(5).....	27,692	*
All executive officers, directors and named directors as a group (16 persons).....	9,340,901	44.5

\* Less than 1%.

- (1) Shares shown do not include shares that could be acquired upon exercise of options which do not vest within 60 days.
- (2) Includes 10,000 shares of Common Stock issuable upon exercise of options granted under the Directors' Plan and 2,969,912 shares of Common Stock issued to Notre. Mr. Harter is the President of Notre.
- (3) Includes an aggregate of 18,694 shares which are held in irrevocable trusts for Mr. Nothum's minor children and of which he is trustee.
- (4) Includes 10,000 shares of Common Stock issuable upon exercise of options granted under the Directors' Plan.
- (5) Includes 7,692 shares of Common Stock issuable on conversion of a convertible note issued by Notre which is convertible into Common Stock of the Company owned by Notre.

## DESCRIPTION OF CAPITAL STOCK

### GENERAL

The authorized capital stock of the Company consists of 57,969,912 shares of capital stock, consisting of 50,000,000 shares of Common Stock, 2,969,912 shares of Restricted Common Stock and 5,000,000 shares of Preferred Stock. The Company has outstanding 20,975,774 shares of Common Stock, which includes 2,742,912 shares of Restricted Common Stock and no shares of Preferred Stock. The following discussion is qualified in its entirety by reference to the Restated Certificate of Incorporation of Comfort Systems, which is included as an exhibit to the Registration Statement of which this Prospectus is a part.

### COMMON STOCK AND RESTRICTED COMMON STOCK

The holders of Common Stock are each entitled to one vote for each share held on all matters to which they are entitled to vote, including the election of directors. The holders of Restricted Common Stock, voting together as a single class, are entitled to elect one member of the Company's Board of Directors and to 0.55 of one vote for each share held on all other matters on which they are entitled to vote. Holders of Restricted Common Stock are not entitled to vote on the election of any other directors. Upon consummation of this Offering, the Board of Directors will be classified into three classes as nearly equal in number as possible, with the term of each class expiring on a staggered basis. The classification of the Board of Directors may make it more difficult to change the composition of the Board of Directors and thereby may discourage or make more difficult an attempt by a person or group to obtain control of the Company. Cumulative voting for the election of directors is not permitted. Any director, or the entire Board of Directors, may be removed at any time, with cause, by a majority of the aggregate number of votes which may be cast by the holders of all of the outstanding shares of Common Stock and Restricted Common Stock entitled to vote for the election of directors, except that only the holder of the Restricted Common Stock may remove the director such holder is entitled to elect.

Subject to the rights of any then outstanding shares of Preferred Stock, holders of Common Stock and Restricted Common Stock are together entitled to participate pro rata in such dividends as may be declared in the discretion of the Board of Directors out of funds legally available therefor. Holders of Common Stock and Restricted Common Stock together are entitled to share ratably in the net assets of the Company upon liquidation after payment or provision for all liabilities and any preferential liquidation rights of any Preferred Stock then outstanding. Holders of Common Stock and holders of Restricted Common Stock have no preemptive rights to purchase shares of stock of the Company. Shares of Common Stock are not subject to any redemption provisions and are not convertible into any other securities of the Company. Shares of Restricted Common Stock are not subject to any redemption provisions and are convertible into Common Stock as described below. All outstanding shares of Common Stock and Restricted Common Stock are, and the shares of Common Stock to be issued pursuant to this Offering will be, upon payment therefor, fully paid and non-assessable.

Each share of Restricted 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 Common Stock by the holder thereof (other than 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, or (iii) in the event any person offers to acquire 15% or more of the total number of outstanding shares of Common Stock. After July 1, 1998, the Board of Directors may elect to convert any remaining shares of Restricted Common Stock into shares of Common Stock in the event 80% or more of the originally outstanding shares of Restricted Common Stock have been previously converted into shares of Common Stock.

The Common Stock is listed on The New York Stock Exchange under the symbol "FIX." The Restricted Common Stock is not listed on any exchange.

## PREFERRED STOCK

The Preferred Stock may be issued from time to time by the Board of Directors in one or more series. Subject to the provisions of the Company's Certificate of Incorporation and limitations prescribed by law, the Board of Directors is expressly authorized to adopt resolutions to issue the shares, to fix the number of shares and to change the number of shares constituting any series and to provide for or change the voting powers, designations, preferences and relative, participating, optional or other special rights, qualifications, limitations or restrictions thereof, including dividend rights (including whether dividends are cumulative), dividend rates, terms of redemption (including sinking fund provisions), redemption prices, conversion rights and liquidation preferences of the shares constituting any series of the Preferred Stock, in each case without any further action or vote by the stockholders. The Company has no current plans to issue any shares of Preferred Stock.

One of the effects of undesignated Preferred Stock may be to enable the Board of Directors to render more difficult or to discourage an attempt to obtain control of the Company by means of a tender offer, proxy contest, merger or otherwise, and thereby to protect the continuity of the Company's management. The issuance of shares of the Preferred Stock pursuant to the Board of Directors' authority described above may adversely affect the rights of the holders of Common Stock. For example, Preferred Stock issued by the Company may rank prior to the Common Stock and Restricted Common Stock as to dividend rights, liquidation preference or both, may have full or limited voting rights and may be convertible into shares of Common Stock. Accordingly, the issuance of shares of Preferred Stock may discourage bids for the Common Stock or may otherwise adversely affect the market price of the Common Stock.

## STATUTORY BUSINESS COMBINATION PROVISION

The Company is subject to Section 203 of the DGCL which, with certain exceptions, prohibits a Delaware corporation from engaging in any of a broad range of business combinations with any "interested stockholder" for a period of three years following the date that such stockholder became an interested stockholder, unless: (i) prior to such date, the Board of Directors of the corporation approved either the business combination or the transaction which resulted in the stockholder becoming an interested stockholder, (ii) upon consummation of the transaction which resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced, excluding for purposes of determining the number of shares outstanding those shares owned (a) by persons who are directors and officers and (b) by employee stock plans in which employee participants do not have the right to determine confidentially whether shares held subject to the plan will be tendered in a tender or exchange offer, or (iii) on or after such date, the business combination is approved by the Board of Directors and authorized at an annual or special meeting of stockholders by the affirmative vote of at least 66 2/3% of the outstanding voting stock which is not owned by the interested stockholder. An "interested stockholder" is defined as any person that is (a) the owner of 15% or more of the outstanding voting stock of the corporation or (b) an affiliate or associate of the corporation and was the owner of 15% or more of the outstanding voting stock of the corporation at any time within the three-year period immediately prior to the date on which it is sought to be determined whether such person is an interested stockholder.

## CERTAIN PROVISIONS OF THE CERTIFICATE OF INCORPORATION AND BYLAWS

Pursuant to the Company's Certificate of Incorporation and as permitted by Delaware law, directors of the Company are not liable to the Company or its stockholders for monetary damages for breach of fiduciary duty, except for liability in connection with a breach of duty of loyalty, for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, for dividend payments or stock repurchases illegal under Delaware law or any transaction in which a director has derived an improper personal benefit.

Additionally, the Certificate of Incorporation of the Company provides that directors and officers of the Company shall be, and at the discretion of the Board of Directors non-officer employees and agents may be, indemnified by the Company to the fullest extent authorized by Delaware law, as it now exists or may in

the future be amended, against all expenses and liabilities actually and reasonably incurred in connection with service for or on behalf of the Company, and further permits the advancing of expenses incurred in defense of claims.

The Certificate of Incorporation also provides that any action required or permitted to be taken by the stockholders of the Company at an annual or special meeting of stockholders must be effected at a duly called meeting and may not be taken or effected by a written consent of stockholders in lieu thereof. The Company's Bylaws provide that a special meeting of stockholders may be called only by the Chief Executive Officer, by a majority of the Board of Directors, or by a majority of the Executive Committee of the Board of Directors. The Bylaws provide that only those matters set forth in the notice of the special meeting may be considered or acted upon at that special meeting. To amend or repeal the Company's Bylaws, an amendment or repeal thereof must first be approved by the Board of Directors or by affirmative vote of the holders of at least 66 2/3% of the total votes eligible to be cast by holders of voting stock with respect to such amendment or repeal.

The Company's Bylaws establish an advance notice procedure with regard to the nomination, other than by or at the direction of the Board of Directors or a committee thereof, of candidates for election as directors (the "Nomination Procedure") and with regard to other matters to be brought by stockholders before an annual meeting of stockholders of the Company (the "Business Procedure"). The Nomination Procedure requires that a stockholder give prior written notice, in proper form, of a planned nomination for the Board of Directors to the Secretary of the Company. The requirements as to the form and timing of that notice are specified in the Company's Bylaws. If the Chairman of the Board of Directors determines that a person was not nominated in accordance with the Nomination Procedure, such person will not be eligible for election as a director. Under the Business Procedure, a stockholder seeking to have any business conducted at an annual meeting must give prior written notice, in proper form, to the Secretary of the Company. The requirements as to the form and timing of that notice are specified in the Company's Bylaws. If the Chairman of the Board of Directors determines that the other business was not properly brought before such meeting in accordance with the Business Procedure, such business will not be conducted at such meeting.

Although the Company's Bylaws do not give the Board of Directors any power to approve or disapprove stockholder nominations for the election of directors or of any other business desired by stockholders to be conducted at an annual or any other meeting, the Company's Bylaws (i) may have the effect of precluding a nomination for the election of directors or precluding the conduct of business at a particular meeting if the proper procedures are not followed or (ii) may discourage or deter a third party from conducting a solicitation of proxies to elect its own slate of directors or otherwise attempting to obtain control of the Company, even if the conduct of such solicitation or such attempt might be beneficial to the Company and its stockholders.

#### TRANSFER AGENT AND REGISTRAR

The Transfer Agent and Registrar for the Common Stock is American Stock Transfer & Trust Company, 40 Wall Street, New York, New York, 10005.

## SHARES ELIGIBLE FOR FUTURE SALE

The Company has outstanding 20,974,774 shares of Common Stock. The 7,015,000 shares sold in the IPO will be freely tradeable without restriction unless acquired by affiliates of the Company. None of the remaining outstanding shares of Common Stock or Restricted Common Stock have been registered under the Securities Act, which means that they may be resold publicly only upon registration under the Securities Act or in compliance with an exemption from the registration requirements of the Securities Act, including the exemption provided by Rule 144 thereunder.

In general, under Rule 144, if a period of at least one year has elapsed between the later of the date on which restricted securities were acquired from the Company or the date on which they were acquired from an affiliate, the holder of such restricted securities (including an affiliate) is entitled to sell a number of shares within any three-month period that does not exceed the greater of (i) one percent of the then outstanding shares of the Common Stock (approximately 209,758 shares upon completion of the IPO) or (ii) the average weekly reported volume of trading of the Common Stock during the four calendar weeks preceding such sale. Sales under Rule 144 are also subject to certain requirements pertaining to the manner of such sales, notices of such sales and the availability of current public information concerning the Company. Affiliates may sell shares not constituting restricted securities in accordance with the foregoing volume limitations and other requirements but without regard to the one year holding period. Under Rule 144(k), if a period of at least two years has elapsed between the later of the date on which restricted securities were acquired from the Company and the date on which they were acquired from an affiliate, a holder of such restricted securities who is not an affiliate at the time of the sale and has not been an affiliate for a least three months prior to the sale is entitled to sell the shares immediately without regard to the volume limitations and other conditions described above.

The Company and its officers, directors and certain stockholders, who beneficially own 4,239,947 shares in the aggregate, have agreed not to sell or otherwise dispose of any shares of Common Stock or Restricted Common Stock for a period of 180 days after the date of this Prospectus without the prior written consent of Alex. Brown & Sons Incorporated, except that the Company may issue Common Stock in connection with acquisitions, in connection with its 1997 Long-Term Incentive Plan and its 1997 Non-Employee Directors' Stock Plan (the "Plans") or upon conversion of shares of the Restricted Common Stock. See "Underwriting." In addition, all of the stockholders of the Founding Companies, the Company's officers and directors and certain stockholders, holding in the aggregate 13,960,874 shares of Common Stock, have agreed with the Company that they will not sell any of their shares for a period of one year after the closing of the IPO. These stockholders, however, have the right, in the event the Company proposes to register under the Securities Act any Common Stock for its own account or for the account of others, subject to certain exceptions, to require the Company to include their shares in the registration, subject to the right of the Company to exclude some or all of the shares in the offering upon the advice of the managing underwriter. In addition, certain of such stockholders have certain limited demand registration rights to require the Company to register shares held by them following the first anniversary of the closing of the IPO.

The Company is hereby registering 8,000,000 shares of its Common Stock under the Securities Act for use by the Company in connection with future acquisitions. After the effective date of such registration, any such shares that may be issued will generally be freely tradeable, unless acquired by persons who become affiliates of the Company. In some instances, however, the Company may contractually restrict the sale of shares issued in connection with future acquisitions. The piggyback registration rights described above do not apply to the registration statement relating to these 8,000,000 shares.

No prediction can be made as to the effect, if any, that the sale of shares or the availability of shares for sale will have on the market price for the Common Stock prevailing from time to time. Nevertheless, sales, or the availability for sale of, substantial amounts of the Common Stock in the public market could adversely affect prevailing market prices and the future ability of the Company to raise equity capital and complete any additional acquisitions for Common Stock.

#### LEGAL MATTERS

The validity of the Common Stock offered hereby will be passed on for the Company by Bracewell & Patterson, L.L.P., Houston, Texas.

#### EXPERTS

The audited financial statements included in this Prospectus and elsewhere in the registration statement have been audited by Arthur Andersen LLP, independent public accountants, as indicated in their reports with respect thereto, and are included herein in reliance upon the authority of said firm as experts in giving said reports.

#### ADDITIONAL INFORMATION

The Company has filed with the SEC a Registration Statement (which term shall encompass any and all amendments thereto) on Form S-1 (the "Registration Statement") under the Securities Act of 1933, as amended (the "Securities Act"), with respect to the Common Stock offered hereby. This Prospectus, which is part of the Registration Statement, does not contain all the information set forth in the Registration Statement and the exhibits and schedules thereto, certain items of which are omitted in accordance with the rules and regulations of the SEC. Statements made in this Prospectus as to the contents of any contract, agreement or other document referred to are not necessarily complete. With respect to each such contract, agreement or other document filed as an exhibit to the Registration Statement, reference is hereby made to the exhibit for a more complete description of the matter involved, and each such statement shall be deemed qualified in its entirety by such reference. For further information with respect to the Company, reference is hereby made to the Registration Statement and such exhibits and schedules filed as a part thereof, which may be inspected, without charge, at the Public Reference Section of the SEC at Room 1024, Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. 20549, and at the regional offices of the SEC located at Seven World Trade Center, 13th Floor, New York, New York 10048 and at Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. The SEC maintains a web site that contains reports, proxy and information statements regarding registrants that file electronically with the SEC. The address of this web site is (<http://www.sec.gov>). Copies of all or any portion of the Registration Statement may be obtained from the Public Reference Section of the SEC, upon payment of the prescribed fees.

The Common Stock is listed on the New York Stock Exchange. Proxy statements, reports and other information concerning the Company that are filed under the Exchange Act can be inspected at the offices of the New York Stock Exchange, Inc., 20 Broad Street, New York, New York 10005.



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COMFORT SYSTEMS USA, INC. AND FOUNDING COMPANIES  
UNAUDITED PRO FORMA COMBINED FINANCIAL STATEMENTS  
BASIS OF PRESENTATION

The following unaudited pro forma combined financial statements give effect to the acquisitions by Comfort Systems USA, Inc. ("Comfort Systems") of the outstanding capital stock of Quality, Atlas, Tri-City, Lawrence, Accurate, Eastern, CSI/Bonneville, Seasonair, Tech, Western, Freeway and Standard (together, the "Founding Companies"). These acquisitions (the "Mergers") occurred concurrently with the closing of Comfort Systems' initial public offering (the "IPO") and were accounted for using the purchase method of accounting. Comfort Systems has been identified as the accounting acquirer for financial statement presentation purposes.

The unaudited pro forma combined balance sheet gives effect to the Mergers and the IPO as if they had occurred on March 31, 1997. The unaudited pro forma combined statements of operations give effect to these transactions as if they had occurred on January 1, 1996.

Comfort Systems has preliminarily analyzed the savings that it expects to be realized from reductions in salaries and certain benefits to the owners. To the extent the owners of the Founding Companies have agreed prospectively to reductions in salary, bonuses and benefits, these reductions have been reflected in the pro forma combined statements of operations. With respect to other potential cost savings, Comfort Systems has not and cannot quantify these savings until completion of the combination of the Founding Companies. It is anticipated that these savings will be offset by costs related to Comfort Systems' new corporate management and by the costs associated with being a public company. However, because these costs cannot be accurately quantified at this time, they have not been included in the pro forma financial information of Comfort Systems.

The pro forma adjustments are based on estimates, available information and certain assumptions and may be revised as additional information becomes available. The pro forma financial data do not purport to represent what Comfort Systems' financial position or results of operations would actually have been if such transactions in fact had occurred on those dates and are not necessarily representative of the Comfort Systems' financial position or results of operations for any future period. Since the Founding Companies were not under common control or management, historical combined results may not be comparable to, or indicative of, future performance. The unaudited pro forma combined financial statements should be read in conjunction with the other financial statements and notes thereto included elsewhere in this Prospectus. See "Risk Factors" included elsewhere herein.

COMFORT SYSTEMS USA, INC.  
 UNAUDITED PRO FORMA COMBINED BALANCE SHEET  
 MARCH 31, 1997  
 (AMOUNTS IN THOUSANDS)

	QUALITY	ATLAS	TRI-CITY	LAWRENCE	ACCURATE	EASTERN	CSI/BONNEVILLE	TECH
<b>ASSETS</b>								
Cash and cash equivalents.....	\$ 3,778	\$ 356	\$2,665	\$--	\$ 104	\$ 131	\$ 103	\$ 249
Restricted cash and investments.....	--	--	828	--	--	--	--	--
Accounts receivable.....	6,512	4,764	4,532	3,706	2,330	921	743	1,261
Less allowance.....	80	100	30	--	28	25	21	45
Accounts receivable, net.....	6,432	4,664	4,502	3,706	2,302	896	722	1,216
Other receivables.....	6	--	66	76	85	27	--	20
Inventories.....	601	1,676	218	255	141	97	491	193
Prepaid expenses and other.....	50	56	2	31	--	--	4	20
Costs in excess of billings.....	595	314	380	262	228	48	129	--
Other.....	692	145	--	--	--	--	--	--
Total current assets.....	12,154	7,211	8,661	4,330	2,860	1,199	1,449	1,698
Property and equipment, net.....	774	598	643	716	932	607	690	484
Goodwill, net.....	--	22	--	--	--	--	--	--
Other noncurrent assets.....	--	88	--	237	--	174	15	--
Total assets.....	\$12,928	\$7,919	\$9,304	\$5,283	\$3,792	\$1,980	\$ 2,154	\$2,182
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>								
Current maturities of long-term debt.....	\$ 695	\$ 800	\$--	\$ 450	\$ 716	\$ 607	\$ 101	\$ 969
Accounts payable and accrued expenses.....	2,654	3,037	2,408	1,241	1,197	759	657	701
Payable to shareholder/affiliate.....	3,875	--	--	--	630	--	--	--
Billings in excess of costs and earnings.....	988	570	435	890	97	53	218	--
Deferred income taxes.....	--	--	--	217	--	--	--	--
Other.....	391	--	--	--	--	--	--	--
Total current liabilities.....	8,603	4,407	2,843	2,798	2,640	1,419	976	1,670
Deferred income taxes.....	--	--	--	--	--	--	--	--
Long-term debt, net of current maturities.....	362	1,174	--	--	149	353	4	32
Payable to shareholder/affiliate.....	--	75	--	--	--	--	430	--
Total liabilities.....	8,965	5,656	2,843	2,798	2,789	1,772	1,410	1,702
Commitments and contingencies.....	--	--	--	--	--	--	--	--
Stockholders' equity:								
Common stock.....	22	1	25	161	1	50	9	1
Additional paid-in-capital.....	6	--	105	--	--	--	--	--
Retained earnings.....	4,833	2,262	6,331	2,339	1,002	158	735	482
Treasury stock.....	(898)	--	--	(15)	--	--	--	(3)
Total stockholders' equity.....	3,963	2,263	6,461	2,485	1,003	208	744	480
Total liabilities and stockholders' equity.....	\$12,928	\$7,919	\$9,304	\$5,283	\$3,792	\$1,980	\$ 2,154	\$2,182

	SEASONAIR	WESTERN	OTHER FOUNDING COMPANIES	COMFORT SYSTEMS	PRO FORMA ADJUSTMENTS	PRO FORMA COMBINED	POST MERGER ADJUSTMENTS	AS ADJUSTED
<b>ASSETS</b>								
Cash and cash equivalents.....	\$ 221	\$ 34	\$ 227	\$ 42	\$ (5,760)	\$ 2,150	\$ 34,572	\$36,722
Restricted cash and investments.....	--	--	--	--	--	828	--	828
Accounts receivable.....	922	641	1,677	--	--	28,009	--	28,009
Less allowance.....	9	--	69	--	--	407	--	407
Accounts receivable, net.....	913	641	1,608	--	--	27,602	--	27,602
Other receivables.....	40	6	443	--	--	769	--	769
Inventories.....	187	86	519	--	--	4,464	--	4,464
Prepaid expenses and other.....	49	9	82	--	--	303	--	303
Costs in excess of billings.....	89	91	--	--	--	2,136	--	2,136
Other.....	104	--	--	2,866	--	3,807	(2,866)	941
Total current assets.....	1,603	867	2,879	2,908	(5,760)	42,059	31,706	73,765
Property and equipment, net.....	61	189	288	--	--	5,982	--	5,982
Goodwill, net.....	--	--	--	--	139,790	139,812	--	139,812
Other noncurrent assets.....	110	174	32	--	--	830	--	830
Total assets.....	\$ 1,774	\$1,230	\$ 3,199	\$ 2,908	\$ 134,030	\$188,683	\$ 31,706	\$220,389
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>								
Current maturities of long-term debt.....	\$ 91	\$ 97	\$ 199	\$ --	\$ --	\$ 4,725	\$ --	\$ 4,725
Accounts payable and accrued expenses.....	866	437	1,548	2,866	--	18,371	(2,866)	15,505
Payable to shareholder/affiliate.....	--	--	--	--	41,428	45,933	(45,303)	630
Billings in excess of costs and earnings.....	134	21	44	--	--	3,450	--	3,450
Deferred income taxes.....	--	--	49	--	--	266	--	266
Other.....	--	--	120	--	--	511	--	511

Total current liabilities.....	1,091	555	1,960	2,866	41,428	73,256	(48,169)	25,087
Deferred income taxes.....	17	--	--	--	--	17	--	17
Long-term debt, net of current maturities.....	9	241	370	--	11,025	13,719	--	13,719
Payable to shareholder/affiliate.....	68	--	--	--	--	573	--	573
Total liabilities.....	1,185	796	2,330	2,866	52,453	87,565	(48,169)	39,396
Commitments and contingencies.....	--	--	--	--	--	--	--	--
Stockholders' equity:								
Common stock.....	78	1	42	42	(293)	140	70	210
Additional paid-in-capital.....	1	62	419	11,556	88,829	100,978	79,805	180,783
Retained earnings.....	745	371	458	(11,556)	(8,160)	--	--	--
Treasury stock.....	(235)	--	(50)	--	1,201	--	--	--
Total stockholders' equity.....	589	434	869	42	81,577	101,118	79,875	180,993
Total liabilities and stockholders' equity.....	\$ 1,774	\$1,230	\$ 3,199	\$ 2,908	\$ 134,030	\$188,683	\$ 31,706	\$220,389

COMFORT SYSTEMS USA, INC.  
 UNAUDITED PRO FORMA COMBINED STATEMENTS OF OPERATIONS  
 YEAR ENDED DECEMBER 31, 1996  
 (IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	QUALITY	ATLAS	TRI-CITY	LAWRENCE	ACCURATE	EASTERN	CSI/BONNEVILLE
REVENUES.....	\$29,597	\$ 30,030	\$24,237	\$17,163	\$16,806	\$7,944	\$ 7,842
COST OF SERVICES.....	18,467	25,071	18,561	12,211	13,270	5,276	5,201
Gross profit.....	11,130	4,959	5,676	4,952	3,536	2,668	2,641
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	6,640	2,858	3,903	4,885	3,037	2,237	1,660
GOODWILL AMORTIZATION.....	--	--	--	--	--	--	--
INCOME FROM OPERATIONS.....	4,490	2,101	1,773	67	499	431	981
OTHER INCOME (EXPENSE):							
Interest income.....	--	--	152	47	--	--	--
Interest expense.....	(154 )	(292)	--	--	(80)	(87 )	(29)
Other.....	97	65	89	8	14	40	51
INCOME BEFORE INCOME TAXES.....	4,433	1,874	2,014	122	433	384	1,003
PROVISION FOR INCOME TAXES.....	--	750	--	60	--	--	--
NET INCOME.....	\$ 4,433	\$ 1,124	\$ 2,014	\$ 62	\$ 433	\$ 384	\$ 1,003
NET INCOME PER SHARE.....							
SHARES USED IN COMPUTING PRO FORMA NET INCOME PER SHARE(1).....							

  

	TECH	SEASONAIR	WESTERN	OTHER FOUNDING COMPANIES	COMFORT SYSTEMS	PRO FORMA ADJUSTMENTS	PRO FORMA COMBINED
REVENUES.....	\$ 7,537	\$6,737	\$6,494	\$ 13,138	\$--	\$ --	\$ 167,525
COST OF SERVICES.....	3,996	4,006	4,662	8,991	--	--	119,712
Gross profit.....	3,541	2,731	1,832	4,147	--	--	47,813
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	1,861	2,597	1,088	3,616	--	(6,568)	27,814
GOODWILL AMORTIZATION.....	--	--	--	--	--	3,495	3,495
INCOME FROM OPERATIONS.....	1,680	134	744	531	--	3,073	16,504
OTHER INCOME (EXPENSE):							
Interest income.....	--	--	--	17	--	--	216
Interest expense.....	(18)	(21)	(51)	--	--	(935)	(1,667 )
Other.....	31	82	(21)	34	--	--	490
INCOME BEFORE INCOME TAXES.....	1,693	195	672	582	--	2,138	15,543
PROVISION FOR INCOME TAXES.....	--	69	--	49	--	6,687	7,615
NET INCOME.....	\$ 1,693	\$ 126	\$ 672	\$ 533	\$--	\$ (4,549)	\$ 7,928
NET INCOME PER SHARE.....							\$ 0.44
SHARES USED IN COMPUTING PRO FORMA NET INCOME PER SHARE(1).....							18,180,311

(1) Includes (i) 2,969,912 shares issued to Notre, (ii) 1,269,935 shares issued to management of and consultants to Comfort Systems, (iii) 9,720,927 shares issued to owners of the Founding Companies and (iv) 4,219,537 of the 7,015,000 shares sold in the IPO necessary to pay the cash portion of the Merger consideration and expenses of the IPO. The 2,795,463 shares excluded reflects 1,880,463 shares for the net cash proceeds to Comfort Systems from the IPO, and 915,000 shares purchased by the underwriters pursuant to an overallotment option.

COMFORT SYSTEMS USA, INC.  
 UNAUDITED PRO FORMA COMBINED STATEMENTS OF OPERATIONS  
 THREE MONTHS ENDED MARCH 31, 1997  
 (IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	QUALITY	ATLAS	TRI-CITY	LAWRENCE	ACCURATE	EASTERN	CSI/BONNEVILLE
REVENUES.....	\$ 8,766	\$ 6,115	\$ 6,791	\$ 4,565	\$ 2,642	\$1,284	\$ 1,562
COST OF SERVICES.....	5,372	4,866	5,946	3,326	2,095	805	1,045
Gross profit.....	3,394	1,249	845	1,239	547	479	517
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	2,094	753	567	698	526	582	458
GOODWILL AMORTIZATION.....	--	--	--	--	--	--	--
INCOME (LOSS) FROM OPERATIONS.....	1,300	496	278	541	21	(103 )	59
OTHER INCOME (EXPENSE):							
Interest income.....	38	--	25	--	1	--	2
Interest expense.....	(29 )	(54)	--	--	(33)	(20 )	(17)
Other.....	(34 )	17	9	2	7	--	9
INCOME (LOSS) BEFORE INCOME TAXES....	1,275	459	312	543	(4)	(123 )	53
PROVISION FOR INCOME TAXES.....	--	188	--	217	--	--	--
NET INCOME (LOSS).....	\$ 1,275	\$ 271	\$ 312	\$ 326	\$ (4)	\$ (123 )	\$ 53
NET INCOME PER SHARE.....							
SHARES USED IN COMPUTING PRO FORMA NET INCOME PER SHARE(1).....							

  

	TECH	SEASONAIR	WESTERN	OTHER FOUNDING COMPANIES	COMFORT SYSTEMS	PRO FORMA ADJUSTMENTS	PRO FORMA COMBINED
REVENUES.....	\$ 1,656	\$1,831	\$1,072	\$ 3,221	\$ --	\$ --	\$ 39,505
COST OF SERVICES.....	1,034	1,165	812	2,334	--	--	28,800
Gross profit.....	622	666	260	887	--	--	10,705
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	565	644	231	909	11,556	(11,769)	7,814
GOODWILL AMORTIZATION.....	--	--	--	--	--	874	874
INCOME (LOSS) FROM OPERATIONS.....	57	22	29	(22)	(11,556 )	10,895	2,017
OTHER INCOME (EXPENSE):							
Interest income.....	--	--	--	6	--	--	72
Interest expense.....	(10)	(3)	(11)	--	--	(207)	(384 )
Other.....	11	28	(2)	15	--	--	62
INCOME (LOSS) BEFORE INCOME TAXES....	58	47	16	(1)	(11,556 )	10,688	1,767
PROVISION FOR INCOME TAXES.....	--	23	--	--	--	492	920
NET INCOME (LOSS).....	\$ 58	\$ 24	\$ 16	\$ (1)	\$ (11,556)	\$ 10,196	\$ 847
NET INCOME PER SHARE.....							\$ 0.05
SHARES USED IN COMPUTING PRO FORMA NET INCOME PER SHARE(1).....							18,180,311

(1) Includes (i) 2,969,912 shares issued to Notre, (ii) 1,269,935 shares issued to management of and consultants to Comfort Systems, (iii) 9,720,927 shares issued to owners of the Founding Companies and (iv) 4,219,537 of the 7,015,000 shares sold in the IPO necessary to pay the cash portion of the Merger consideration and expenses of the IPO. The 2,795,463 shares excluded reflects 1,880,463 shares for the net cash proceeds to Comfort Systems from the IPO, and 915,000 shares purchased by the underwriters pursuant to an overallotment option.

COMFORT SYSTEMS USA, INC. AND FOUNDING COMPANIES  
NOTES TO UNAUDITED PRO FORMA COMBINED FINANCIAL STATEMENTS

1. GENERAL:

Comfort Systems USA, Inc. ("Comfort Systems") was founded to become a leading national provider of comprehensive heating, ventilation and air conditioning ("HVAC") installation services as well as maintenance, repair and replacement of HVAC systems, focusing primarily on commercial and industrial markets. Comfort Systems conducted no operations prior to the IPO and acquired the Founding Companies concurrently with and as a condition to the closing of the Offering.

The historical financial statements reflect the financial position and results of operations of the Founding Companies and were derived from the respective Founding Companies' financial statements where indicated. The periods included in these financial statements for the individual Founding Companies are as of and for the three months ended March 31, 1997 and for the year ended December 31, 1996, with the exception of Lawrence for which the period is as of and for the three months ended January 31, 1997 and for the fiscal year ended October 31, 1996. The audited historical financial statements included elsewhere herein have been included in accordance with Securities and Exchange Commission ("SEC") Staff Accounting Bulletin No. 80.

2. ACQUISITION OF FOUNDING COMPANIES:

Concurrently with and as a condition to the closing of the IPO, Comfort Systems acquired all of the outstanding capital stock of the Founding Companies. The acquisitions were accounted for using the purchase method of accounting with Comfort Systems being treated as the accounting acquirer.

The following table sets forth the consideration paid (a) in cash and (b) in shares of Common Stock to the common stockholders of each of the Founding Companies. For purposes of computing the estimated purchase price for accounting purposes, the value of the shares was determined using an estimated fair value of \$10.40 per share (or \$101.1 million), which represents a discount of twenty percent from the initial public offering price of \$13.00 due to restrictions on the sale and transferability of the shares issued. The total estimated purchase price of \$146.4 million for the acquisitions is based upon preliminary estimates and is subject to certain purchase price adjustments at and following closing. The table does not reflect the distributions totaling \$16.8 million as of March 31, 1997 constituting substantially all of the Founding Companies undistributed earnings previously taxed to their stockholders ("S Corporation Distributions").

	CASH	SHARES OF COMMON STOCK
	(DOLLARS	IN THOUSANDS)
Quality.....	\$ 10,082	2,207,158
Atlas.....	6,864	1,432,000
Tri-City.....	8,680	1,557,962
Lawrence.....	4,500	1,197,796
Accurate.....	3,145	564,537
Eastern.....	698	304,216
CSI/Bonneville.....	1,813	493,672
Tech.....	3,997	717,408
Seasonair.....	1,516	272,084
Western.....	2,022	362,939
Freeway.....	1,039	319,698
Standard.....	947	291,457
Total.....	\$ 45,303	9,720,927
	=====	=====



3. UNAUDITED PRO FORMA COMBINED BALANCE SHEET ADJUSTMENTS:

- (a) Records the S Corporation Distributions of \$16.8 million as of March 31, 1997, (including \$3.9 million recorded as a payable to affiliate at Quality) (See (b) below).
- (b) Records the debt obtained to fund the S Corporation Distributions.
- (c) Records the liability for the cash portion of the consideration paid to the stockholders of the Founding Companies in connection with the Mergers.
- (d) Records the purchase of the Founding Companies by Comfort System consisting of \$45.3 million in cash and 9,720,927 shares of Common Stock valued at \$10.40 per share (or \$101.1 million) for a total purchase price of \$146.4 million resulting in excess purchase price of \$139.8 million over the net assets acquired of \$6.6 million. See Note 2.
- (e) Records the cash proceeds of \$79.3 million from the issuance of shares of Comfort Systems Common Stock net of offering costs of \$10.5 million (includes the payment of deferred offering costs of \$4.9 of which \$2.9 million was incurred through March 31, 1997). Offering costs primarily consist of underwriting discounts and commissions, accounting fees, legal fees and printing expenses.
- (f) Records the cash portion of the consideration to be paid to the stockholders of the Founding Companies in connection with the Mergers.
- (g) Records the cash proceeds of \$11.9 million from the purchase of 915,000 shares of Comfort Systems Common Stock by the underwriters pursuant to an overallotment option net of offering costs of \$0.8 million. Offering costs primarily consist of underwriting discounts and commissions.

The following table summarizes unaudited pro forma combined balance sheet adjustments (in thousands):

	ADJUSTMENT				PRO FORMA ADJUSTMENTS
	(A)	(B)	(C)	(D)	
<b>ASSETS</b>					
Cash and cash equivalents.....	\$ (16,785)	\$ 11,025	\$ --	\$ --	\$ (5,760)
Total current assets.....	(16,785)	11,025	--	--	(5,760)
Goodwill, net.....	--	--	--	139,790	139,790
Total assets.....	\$ (16,785)	\$ 11,025	\$ --	\$ 139,790	\$ 134,030
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>					
Payable to shareholder/affiliate.....	\$ (3,875)	\$ --	\$ 45,303	\$ --	\$ 41,428
Total current liabilities.....	(3,875)	--	45,303	--	41,428
Long-term debt, net of current maturities.....	--	11,025	--	--	11,025
Total liabilities.....	(3,875)	11,025	45,303	--	52,453
Stockholders' equity:					
Common stock.....	--	--	--	(293)	(293)
Additional paid-in capital.....	(12,910)	--	(45,303)	147,042	88,829
Retained earnings.....	--	--	--	(8,160)	(8,160)
Treasury stock.....	--	--	--	1,201	1,201
Total stockholders' equity.....	(12,910)	--	(45,303)	139,790	81,577
Total liabilities and stockholders' equity.....	\$ (16,785)	\$ 11,025	\$ --	\$ 139,790	\$ 134,030
	(E)	(F)	(G)	POST MERGER ADJUSTMENTS	
<b>ASSETS</b>					
Cash and cash equivalents.....	\$ 68,813	\$ (45,303)	\$ 11,062	\$ 34,572	
Other.....	(2,866)	--	--	(2,866)	
Total current assets.....	65,947	(45,303)	11,062	31,706	
Total assets.....	\$ 65,947	\$ (45,303)	\$ 11,062	\$ 31,706	
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>					
Accounts payable and accrued expenses...	\$ (2,866)	\$ --	\$ --	\$ (2,866)	
Payable to shareholder/affiliate.....	--	(45,303)	--	(45,303)	
Total current liabilities.....	(2,866)	(45,303)	--	(48,169)	
Total liabilities.....	(2,866)	(45,303)	--	(48,169)	
Stockholders' equity:					

Common stock.....	61	--	9	70
Additional paid-in capital.....	68,752	--	11,053	79,805
Retained earnings.....	--	--	--	--
Treasury stock.....	--	--	--	--
	-----	-----	-----	-----
Total stockholders' equity.....	68,813	--	11,062	79,875
	-----	-----	-----	-----
Total liabilities and stockholders' equity.....	\$ 65,947	\$ (45,303)	\$ 11,062	\$ 31,706
	=====	=====	=====	=====

4. UNAUDITED PRO FORMA COMBINED STATEMENTS OF OPERATIONS ADJUSTMENTS:

YEAR ENDED DECEMBER 31, 1996

- (a) Reflects the reduction in salaries, bonuses and benefits from an aggregate total of \$9.0 million to \$2.4 million to the owners of the Founding Companies to which they have agreed prospectively. These reductions in salaries, bonuses and benefits are in accordance with the terms of the employment agreements. Such employment agreements are primarily for 5 years, contain restrictions related to competition and provide severance for termination of employment in certain circumstances.
- (b) Reflects the amortization of goodwill to be recorded as a result of these Mergers over a 40-year estimated life.
- (c) Reflects the interest expense on borrowings of \$12.5 million necessary to fund the S Corporation Distributions.
- (d) Reflects the incremental provision for federal and state income taxes relating to the other statements of operations adjustments and for income taxes on S Corporation income.

The following table summarizes unaudited pro forma combined statements of operations adjustments (in thousands):

	ADJUSTMENT				PRO FORMA ADJUSTMENTS
	(A)	(B)	(C)	(D)	
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	\$ (6,568)	\$ --	\$ --	\$ --	\$(6,568)
GOODWILL AMORTIZATION.....	--	3,495	--	--	3,495
INCOME (LOSS) FROM OPERATIONS.....	6,568	(3,495)	--	--	3,073
OTHER INCOME (EXPENSE):					
Interest expense.....	--	--	(935)	--	(935)
INCOME (LOSS) BEFORE INCOME TAXES....	6,568	(3,495)	(935)	--	2,138
PROVISION FOR INCOME TAXES.....	--	--	--	6,687	6,687
NET INCOME (LOSS).....	\$ 6,568	\$ (3,495)	\$ (935)	\$ (6,687)	\$(4,549)

THREE MONTHS ENDED MARCH 31, 1997

- (a) Reflects the reduction in salaries, bonuses and benefits from an aggregate total of \$1.0 million to \$0.6 million to the owners of the Founding Companies to which they have agreed prospectively. These reductions in salaries, bonuses and benefits are in accordance with the terms of the employment agreements. Such employment agreements are primarily for 5 years, contain restrictions related to competition and provide severance for termination of employment in certain circumstances.
- (b) Reflects the amortization of goodwill to be recorded as a result of these Mergers over a 40-year estimated life.
- (c) Reflects the interest expense on borrowings of \$11.0 million necessary to fund the S Corporation Distributions.
- (d) Reflects the incremental provision for federal and state income taxes relating to the other statements of operations adjustments and for income taxes on S Corporation income.
- (e) Reflects the reduction in compensation expense related to the non-recurring, non-cash compensation charge of \$11.6 million recorded by Comfort in the first quarter of 1997 related to Common Stock issued to management of and consultants to the Company offset by the increase in compensation expense related to the on-going salaries of the management of Comfort Systems of \$0.2 million in the first quarter of 1997. The issuances of Common Stock were made in contemplation of the Mergers and the IPO, and no future issuances of this nature are anticipated.

The following table summarizes unaudited pro forma combined statements of operations adjustments (in thousands):

	ADJUSTMENT					PRO FORMA ADJUSTMENTS
	(A)	(B)	(C)	(D)	(E)	
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	\$ (428)	\$ --	\$ --	\$ --	(11,341)	\$ (11,769)
GOODWILL AMORTIZATION.....	--	874	--	--	--	874
INCOME (LOSS) FROM OPERATIONS.....	428	(874)	--	--	11,341	10,895
OTHER INCOME (EXPENSE):						
Interest expense.....	--	--	(207)	--	--	(207)
INCOME (LOSS) BEFORE INCOME TAXES....	428	(874)	(207)	--	11,341	10,688
PROVISION FOR INCOME TAXES.....	--	--	--	492	--	492
NET INCOME (LOSS).....	\$ 428	\$ (874)	\$ (207)	\$ (492)	\$ 11,341	\$ 10,196

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Comfort Systems USA, Inc.:

We have audited the accompanying balance sheet of Comfort Systems USA, Inc. as of December 31, 1996. This financial statement is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statement referred to above presents fairly, in all material respects, the financial position of Comfort Systems USA, Inc. as of December 31, 1996, in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 25, 1997

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

	DECEMBER 31, 1996	MARCH 31, 1997
	-----	-----
ASSETS		
CASH AND CASH EQUIVALENTS.....	\$ 1	\$ 42
DEFERRED OFFERING COSTS.....	177	2,866
	-----	-----
Total assets.....	\$ 178	\$ 2,908
	=====	=====
LIABILITIES AND STOCKHOLDER'S EQUITY		
ACCRUED LIABILITIES AND AMOUNTS DUE TO STOCKHOLDER.....	\$ 177	\$ 2,866
STOCKHOLDER'S EQUITY:		
Preferred stock, \$.01 par, 5,000,000 authorized, none issued and outstanding.....	--	--
Common stock, \$.01 par, 52,969,912 shares authorized, 121,139 and 4,239,847 shares issued and outstanding, respectively.....	1	42
Additional paid in capital.....	--	11,556
Retained deficit.....	--	(11,556)
	-----	-----
Total stockholder's equity....	1	42
	-----	-----
Total liabilities and stockholder's equity.....	\$ 178	\$ 2,908
	=====	=====

Reflects a 121.1387-for-one stock split effective on March 19, 1997.  
The accompanying notes are an integral part of these financial statements.

COMFORT SYSTEMS USA, INC.  
STATEMENT OF OPERATIONS  
THREE MONTHS ENDED MARCH 31, 1997 (UNAUDITED)  
(IN THOUSANDS)

REVENUES.....	\$	--
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....		11,556
		-----
LOSS BEFORE INCOME TAXES.....		(11,556)
INCOME TAX BENEFIT.....		--
		-----
NET LOSS.....	\$	(11,556)
		=====

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

COMFORT SYSTEMS USA, INC.  
STATEMENT OF STOCKHOLDERS' EQUITY  
FOR THE PERIOD FROM INCEPTION (DECEMBER 12, 1996)  
THROUGH MARCH 31, 1997  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED DEFICIT	TOTAL STOCKHOLDERS' EQUITY
	SHARES	AMOUNT			
Initial Capitalization.....	121,139	\$ 1	\$ --	\$ --	\$ 1
BALANCE, December 31, 1996.....	121,139	1	--	--	1
Issuance of Management Shares (unaudited).....	4,118,708	41	11,556	--	11,597
Net loss (unaudited).....	--	--	--	(11,556)	(11,556)
BALANCE, March 31, 1997 (unaudited).....	4,239,847	\$ 42	\$ 11,556	\$(11,556)	\$ 42
	=====	=====	=====	=====	=====

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



COMFORT SYSTEMS USA, INC.  
STATEMENT OF CASH FLOWS  
THREE MONTHS ENDED MARCH 31, 1997 (UNAUDITED)  
(IN THOUSANDS)

CASH FLOWS FROM OPERATING ACTIVITIES:	
Net Loss.....	\$ (11,556)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities --	
Compensation expense related to issuance of management shares...	11,556
Changes in assets and liabilities --	
Increase in deferred offering costs.....	(2,689)
Increase in accrued liabilities and amounts due to stockholder.....	2,689
	-----
Net cash provided by operating activities.....	--
	-----
CASH FLOWS FROM FINANCING ACTIVITIES	
Issuance of stock.....	41
	-----
Net cash provided by financing activities.....	41
	-----
NET INCREASE IN CASH AND CASH EQUIVALENTS.....	
	41
CASH AND CASH EQUIVALENTS, beginning of period.....	1
	-----
CASH AND CASH EQUIVALENTS, end of period.....	\$ 42
	=====

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

1. BUSINESS AND ORGANIZATION:

Comfort Systems USA, Inc., a Delaware corporation, ("Comfort Systems" or the "Company") was founded in December 1996 to become a national provider of comprehensive HVAC installation services and maintenance, repair and replacement of HVAC systems, focusing primarily on the commercial and industrial markets. Comfort intends to acquire 12 U.S. businesses (the "Mergers"), complete an initial public offering (the "Offering") of its common stock and, subsequent to the Offering, continue to acquire through merger or purchase, similar companies to expand its national operations.

Comfort Systems has not conducted any operations, and all activities to date have related to the Offering and the Mergers. The Company's cash balances were generated from the initial capitalization of the Company (see Note 3). All other expenditures to date have been funded by the primary stockholder, Notre Capital Ventures II, L.L.C. ("Notre"), on behalf of the Company. Since there were no revenues, expenses or cash flows from Inception (December 12, 1996) through December 31, 1996, statements of operations and cash flows have been omitted for this period. Notre has committed to fund the organization expenses and offering costs. As of December 31, 1996 and March 31, 1997, costs of approximately \$177,000 and \$2,866,000 (unaudited), respectively have been incurred by Notre in connection with the Offering. Comfort Systems has treated these costs as deferred offering costs. There is no assurance that the pending Mergers discussed below will be completed or that Comfort Systems will be able to generate future operating revenues.

2. INTERIM FINANCIAL INFORMATION:

The interim financial statements as of March 31, 1997, and for the three months then ended are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim period is not necessarily indicative of the results for the entire fiscal year.

3. STOCKHOLDER'S EQUITY:

COMMON STOCK AND PREFERRED STOCK

Comfort Systems effected a 121.1387-for-one stock split on March 19, 1997 for each share of common stock of the Company ("Common Stock") then outstanding. In addition, the Company increased the number of authorized shares of Common Stock to 52,969,912 and authorized 5,000,000 shares of \$.01 par value preferred stock. The effects of the Common Stock split and the increase in the shares of authorized Common Stock have been retroactively reflected on the balance sheet and in the accompanying notes.

In connection with the organization and initial capitalization of Comfort Systems, the Company issued 121,139 shares of common stock at \$.01 per share to Notre. In January 1997, the Company issued 2,848,773 additional shares to Notre for \$.01 per share.

In January and February 1997, the Company issued a total of 1,269,935 shares of Common Stock to management and consultants to the Company at a price of \$.01 per share. As a result, the Company recorded a non-recurring, non-cash compensation charge of \$10.7 million (unaudited) in the first quarter of 1997, representing the difference between the amount paid for the shares and an estimated fair value of the shares on the date of sale.

RESTRICTED COMMON STOCK

In March 1997, the primary stockholder exchanged its 2,742,912 shares of Common Stock for an equal number of shares of restricted voting common stock ("Restricted Common Stock"). The holder of

Restricted Common Stock is entitled to elect one member of the Company's Board of Directors and to 0.55 of one vote for each share on all other matters on which they are entitled to vote. Holders of Restricted Common Stock are not entitled to vote on the election of any other directors.

Each share of Restricted 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 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 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 Common Stock into shares of Common Stock in the event 80% or more of the originally outstanding shares of Restricted Common Stock have been previously converted into shares of Common Stock.

#### LONG-TERM INCENTIVE PLAN

In March 1997, the Company's stockholders approved the Company's 1997 Long-Term Incentive Plan (the "Plan"), which provides for the granting or awarding of incentive or non-qualified stock options, stock appreciation rights, restricted or deferred stock, dividend equivalents and other incentive awards to directors, officers, key employees and consultants to the Company. The number of shares authorized and reserved for issuance under the Plan is the greater of 2,500,000 shares or 13% of the aggregate number of shares of Common Stock outstanding. The terms of the option awards will be established by the Compensation Committee of the Company's Board of Directors. The Company intends to file a registration statement on Form S-8 under the Securities Act registering the issuance of shares upon exercise of options granted under this Plan. The Company expects to grant non-qualified stock options to purchase a total of 675,000 shares of Common Stock to key employees of the Company at the initial public offering price upon consummation of the Offering. In addition, the Company expects to grant options to purchase a total of 1,271,953 shares of Common Stock to certain employees of the Founding Companies at the initial public offering price per share. These options will vest at the rate of 20% per year, commencing on the first anniversary of the IPO and will expire seven years from the date of grant or three months following termination of employment.

#### 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 nonemployees. The number of shares authorized and reserved for issuance under the Stock Plan is 250,000 shares. The Directors' Plan provides for the automatic grant of options to purchase 10,000 shares to each non-employee director serving at the commencement of the Offering.

Each non-employee director will be granted options to purchase an additional 10,000 shares at the time of the initial election. In addition, each director will be automatically granted options to purchase 5,000 shares at each annual meeting of the stockholders occurring more than two months after the date of the director's initial election. All options will be exercised at the fair market value at the date of grant and are immediately vested upon grant.

Options will be granted to each of two future and one current member of the board of directors to purchase 10,000 shares of Common Stock at the initial Offering price per share effective upon the consummation of this Offering. These options will expire the earlier of 10 years from the date of grant or one year after termination of service as a director.

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.

4. STOCK BASED COMPENSATION:

Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," allows entities to choose between a new fair value based method of accounting for employee stock options or similar equity instruments and the current intrinsic, value-based method of accounting prescribed by Accounting Principles Board Opinion No. 25 ("APB No. 25"). Entities electing to remain with the accounting in APB Opinion No. 25 must make pro forma disclosures of net income and earnings per share as if the fair value method of accounting had been applied. The Company will provide pro forma disclosure of net income and earnings per share, as applicable, in the notes to future consolidated financial statements.

5. EVENTS SUBSEQUENT TO THE DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

Wholly-owned subsidiaries of Comfort Systems have acquired by merger or share exchange 12 companies ("Founding Companies"). The companies are Accurate Air Systems, Inc., Atlas Comfort Services USA, Inc. and Subsidiary, Contract Service, Inc., Eastern Heating and Cooling, Inc., Freeway Heating and Air Conditioning, Inc., Quality Air Heating & Cooling, Inc., Seasonair, Inc., S.M. Lawrence Inc. and Related Company, Standard Heating and Air Conditioning Company, Tech Heating and Air Conditioning, Inc. and Related Company, Tri-City Mechanical, Inc. and Western Building Services, Inc. The aggregate consideration paid by Comfort Systems to acquire the Founding Companies was approximately \$45.3 million in cash and 9,720,927 shares of Common Stock.

On June 27, 1997, Comfort Systems completed the Offering, which involved the sale by Comfort Systems of 6,100,000 shares of Common Stock at a price to the public of \$13.00 per share. The net proceeds to Comfort Systems from the Offering (after deducting underwriting discounts and commissions and offering expenses) were approximately \$69.7 million. Of this amount, \$45.3 million was used to pay the cash portion of the purchase prices relating to the acquisitions for the Founding Companies. On July 9, 1997, Comfort Systems sold an additional 915,000 shares of Common Stock at \$13.00 per share (which represents net proceeds to the Company of \$11.1 million after underwriting discounts and commissions) pursuant to an overallotment option granted by Comfort Systems to the underwriters in connection with the Offering. See "Risk Factors" included elsewhere herein.

The Company has obtained a revolving line of credit of \$75.0 million. The facility is intended to be used for acquisitions, capital expenditures, refinancing of debt not paid out of the proceeds of the Offering and for general corporate purposes. The credit facility requires the Company to comply with various loan covenants including (i) maintenance of certain financial ratios, (ii) restrictions on additional indebtedness, and (iii) restrictions on liens, guarantees, advances and dividends. The line of credit is subject to customary drawing conditions. As of July 28, 1997, borrowings under the line of credit were \$17.3 million which was used to repay existing indebtedness of the Founding Companies.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Quality Air Heating & Cooling, Inc.:

We have audited the accompanying balance sheets of Quality Air Heating & Cooling, Inc., as of March 31, 1995 and 1996, and December 31, 1996, and the related statements of operations, shareholders' equity and cash flows for the years ended March 31, 1995 and 1996, the nine months ended December 31, 1996, and the year ended December 31, 1996. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Quality Air Heating & Cooling, Inc., as of March 31, 1995 and 1996, and December 31, 1996, and the results of their operations and their cash flows for the years ended March 31, 1995 and 1996, the nine months ended December 31, 1996 and the year ended December 31, 1996, in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

QUALITY AIR HEATING & COOLING, INC.  
BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	MARCH 31,		DECEMBER 31,	MARCH 31,
	1995	1996	1996	1997
	(UNAUDITED)			
<b>ASSETS</b>				
<b>CURRENT ASSETS:</b>				
Cash and cash equivalents.....	\$ 1,669	\$ 4,191	\$ 2,651	\$ 3,778
Accounts receivable --				
Trade, net of allowance of				
\$87, \$80, \$80 and \$80,				
respectively.....	4,510	4,188	5,260	5,896
Retainage.....	457	464	453	536
Other receivables.....	14	12	5	6
Inventories.....	445	480	541	601
Costs and estimated earnings in				
excess of billings on				
uncompleted contracts.....	1,192	964	1,312	595
Prepaid expenses and other				
current assets.....	92	63	17	50
Federal income tax deposit.....	506	654	691	692
	-----	-----	-----	-----
Total current				
assets.....	8,885	11,016	10,930	12,154
PROPERTY AND EQUIPMENT, net.....	771	708	758	774
	-----	-----	-----	-----
Total assets.....	\$ 9,656	\$ 11,724	\$ 11,688	\$ 12,928
	=====	=====	=====	=====
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>				
<b>CURRENT LIABILITIES:</b>				
Current maturities of long-term				
debt.....	\$ 470	\$ 613	\$ 675	\$ 695
Accounts payable and accrued				
expenses.....	2,786	2,734	2,178	2,654
Dividends payable to				
shareholder.....	1,538	3,314	1,519	3,875
Billings in excess of costs and				
estimated earnings on				
uncompleted contracts.....	897	604	1,254	988
Unearned revenue.....	335	362	372	391
	-----	-----	-----	-----
Total current				
liabilities.....	6,026	7,627	5,998	8,603
LONG-TERM DEBT, net of current				
maturities.....	2,444	1,392	646	362
<b>COMMITMENTS AND CONTINGENCIES</b>				
<b>SHAREHOLDERS' EQUITY:</b>				
Common stock, no par value;				
250,000 shares authorized and				
issued, 183,993 shares				
outstanding.....	22	22	22	22
Additional paid-in capital.....	6	6	6	6
Retained earnings.....	2,056	3,575	5,914	4,833
Treasury stock, 66,007 shares,				
at cost.....	(898)	(898)	(898)	(898)
	-----	-----	-----	-----
Total shareholders'				
equity.....	1,186	2,705	5,044	3,963
	-----	-----	-----	-----
Total liabilities and				
shareholders'				
equity.....	\$ 9,656	\$ 11,724	\$ 11,688	\$ 12,928
	=====	=====	=====	=====

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

QUALITY AIR HEATING & COOLING, INC.  
 STATEMENTS OF OPERATIONS  
 (IN THOUSANDS)

	YEARS ENDED MARCH 31,		NINE MONTHS ENDED DECEMBER 31, 1996	YEAR ENDED DECEMBER 31, 1996	THREE MONTHS ENDED MARCH 31,	
	----- 1995	----- 1996			----- 1996	----- 1997
					(UNAUDITED)	
REVENUES.....	\$ 24,434	\$ 32,594	\$ 23,282	\$ 29,597	\$ 6,315	\$ 8,766
COST OF SERVICES.....	15,634	20,850	14,176	18,467	4,291	5,372
Gross profit.....	8,800	11,744	9,106	11,130	2,024	3,394
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	6,646	6,791	5,032	6,640	1,608	2,094
Income from operations.....	2,154	4,953	4,074	4,490	416	1,300
OTHER INCOME (EXPENSE):						
Interest expense.....	(36)	(218)	(101)	(154)	(53)	(29)
Other.....	53	98	60	97	37	4
NET INCOME.....	<u>\$ 2,171</u>	<u>\$ 4,833</u>	<u>\$ 4,033</u>	<u>\$ 4,433</u>	<u>\$ 400</u>	<u>\$ 1,275</u>

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

QUALITY AIR HEATING & COOLING, INC.  
 STATEMENTS OF SHAREHOLDERS' EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	TREASURY STOCK	TOTAL SHAREHOLDERS' EQUITY
	SHARES	AMOUNT				
BALANCE, March 31, 1994.....	250,000	\$ 22	\$ 6	\$ 3,636	\$--	\$ 3,664
Purchase of treasury stock.....	--	--	--	--	(898)	(898)
Distributions to shareholders.....	--	--	--	(3,751)	--	(3,751)
Net income.....	--	--	--	2,171	--	2,171
BALANCE, March 31, 1995.....	250,000	22	6	2,056	(898)	1,186
Distributions to shareholders.....	--	--	--	(3,314)	--	(3,314)
Net income.....	--	--	--	4,833	--	4,833
BALANCE, March 31, 1996.....	250,000	22	6	3,575	(898)	2,705
Distributions to shareholders.....	--	--	--	(1,694)	--	(1,694)
Net income.....	--	--	--	4,033	--	4,033
BALANCE, December 31, 1996.....	250,000	22	6	5,914	(898)	5,044
Distribution to shareholders (unaudited).....	--	--	--	(2,356)	--	(2,356)
Net income (unaudited).....	--	--	--	1,275	--	1,275
BALANCE, March 31, 1997 (unaudited).....	250,000	\$ 22	\$ 6	\$ 4,833	\$ (898)	\$ 3,963

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



QUALITY AIR HEATING & COOLING, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEARS ENDED MARCH 31		NINE MONTHS ENDED	YEAR ENDED	THREE MONTHS ENDED MARCH 31,	
	-----	-----	-----	-----	-----	-----
	1995	1996	DECEMBER 31, 1996	DECEMBER 31, 1996	1996	1997
						(UNAUDITED)
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>						
Net income.....	\$ 2,171	\$ 4,833	\$ 4,033	\$ 4,433	\$ 400	\$ 1,275
Adjustments to reconcile net income to net cash provided by (used in) operating activities --.....						
Depreciation and amortization...	359	371	242	370	121	127
Loss (gain) on sale of property and equipment.....	7	--	25	25	3	(1)
Changes in operating assets and liabilities --.....						
(Increase) decrease in --.....						
Accounts receivable.....	(1,334)	317	(1,054)	335	1,389	(720)
Inventories.....	(6)	(35)	(61)	(76)	(15)	(60)
Costs and estimated earnings in excess of billings on uncompleted contracts.....	(804)	228	(348)	(253)	95	717
Prepaid expenses and other current assets.....	(15)	29	46	(3)	(49)	(33)
Federal income tax deposit.....	50	(148)	(37)	(185)	(148)	(1)
Increase (decrease) in --.....						
Accounts payable and accrued expenses.....	470	(52)	(556)	(481)	74	476
Billings in excess of costs and estimated earnings on uncompleted contracts.....	477	(293)	650	269	(381)	(266)
Unearned revenue.....	(15)	27	10	26	17	19
	-----	-----	-----	-----	-----	-----
Net cash provided by operating activities.....	1,360	5,277	2,950	4,460	1,506	1,533
	-----	-----	-----	-----	-----	-----
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>						
Proceeds from sale of property and equipment.....	21	--	14	14	4	3
Additions of property and equipment.....	(467)	(308)	(331)	(455)	(123)	(145)
	-----	-----	-----	-----	-----	-----
Net cash used in investing activities.....	(446)	(308)	(317)	(441)	(119)	(142)
	-----	-----	-----	-----	-----	-----
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>						
Borrowings of long-term debt.....	3,000	--	--	--	--	--
Payments of long-term debt.....	(226)	(909)	(684)	(903)	(219)	(264)
Distributions to shareholders.....	(3,088)	(1,538)	(3,489)	(3,488)	--	--
Purchase of treasury stock.....	(898)	--	--	--	--	--
	-----	-----	-----	-----	-----	-----
Net cash used in financing activities.....	(1,212)	(2,447)	(4,173)	(4,391)	(219)	(264)
	-----	-----	-----	-----	-----	-----
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....</b>	<b>(298)</b>	<b>2,522</b>	<b>(1,540)</b>	<b>(372)</b>	<b>1,168</b>	<b>1,127</b>
<b>CASH AND CASH EQUIVALENTS, beginning of period.....</b>	<b>1,967</b>	<b>1,669</b>	<b>4,191</b>	<b>3,023</b>	<b>3,023</b>	<b>2,651</b>
	-----	-----	-----	-----	-----	-----
<b>CASH AND CASH EQUIVALENTS, end of period.....</b>	<b>\$ 1,669</b>	<b>\$ 4,191</b>	<b>\$ 2,651</b>	<b>\$ 2,651</b>	<b>\$ 4,191</b>	<b>\$ 3,778</b>
	=====	=====	=====	=====	=====	=====
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>						
Cash paid for --						
Interest.....	\$ 44	\$ 201	\$ 107	\$ 152	\$ 45	\$ 25

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

QUALITY AIR HEATING & COOLING, INC.  
NOTES TO FINANCIAL STATEMENTS

1. BUSINESS AND ORGANIZATION:

Quality Air Heating & Cooling, Inc., a Michigan corporation, (the "Company") focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems primarily for mid-sized to large commercial facilities. Quality primarily operates throughout western Michigan.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems"), pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

INTERIM FINANCIAL INFORMATION

The interim financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

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 (FIFO) 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 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. 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.

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. 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 income and their effects are recognized in the period in which the revisions are determined.

QUALITY AIR HEATING & COOLING, INC.  
 NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The balances billed but not paid by customers pursuant to retainage provisions in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

WARRANTY COSTS

The Company 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 upon completion of installation or service.

INCOME TAXES

The Company has elected S Corporation status as defined by the Internal Revenue Code, whereby the Company is not subject to taxation for federal purposes. Under S Corporation status, the shareholders report their share of the Company's taxable earnings or losses in their personal tax returns. The Company will terminate its S Corporation status concurrently with the effective date of this Offering. Included in current assets are deposits to prepay certain of the shareholders' federal income taxes.

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 and 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.

NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	MARCH 31,		DECEMBER 31, 1996
		1995	1996	
Transportation equipment.....	5	\$ 1,449	\$ 1,554	\$1,725
Machinery and equipment.....	7	480	453	465
Computer and telephone equipment....	5-7	80	87	90
Leasehold improvements.....	5	838	834	859
Furniture and fixtures.....	7	435	414	459
		-----	-----	-----
Less -- Accumulated depreciation and amortization.....		(2,511)	(2,634)	(2,840)
		-----	-----	-----
Property and equipment, net.....		\$ 771	\$ 708	\$ 758
		=====	=====	=====

QUALITY AIR HEATING & COOLING, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS (IN THOUSANDS):

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

	MARCH 31,		DECEMBER 31,
	----- 1995	1996	----- 1996
Balance at beginning of year.....	\$ 70	\$ 87	\$ 80
Additions to costs and expenses.....	142	35	2
Deductions for uncollectible receivables written off and recoveries.....	(125)	(42)	(2)
	----- \$ 87	----- \$ 80	----- \$ 80
	=====	=====	=====

Accounts payable and accrued expenses consist of the following:

	MARCH 31,		DECEMBER 31,
	----- 1995	1996	----- 1996
Accounts payable, trade.....	\$ 1,353	\$ 1,145	\$ 921
Accrued compensation and benefits....	540	693	426
Other accrued expenses.....	893	896	831
	----- \$ 2,786	----- \$ 2,734	----- \$2,178
	=====	=====	=====

Installation contracts in progress are as follows:

	MARCH 31,		DECEMBER 31,
	----- 1995	1996	----- 1996
Costs incurred on contracts in progress.....	\$ 5,240	\$ 7,697	\$ 7,231
Estimated earnings, net of losses....	1,556	2,588	2,433
	----- 6,796	----- 10,285	----- 9,664
Less -- Billings to date.....	6,501	9,925	9,606
	----- \$ 295	----- \$ 360	----- \$ 58
	=====	=====	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 1,192	\$ 964	\$ 1,312
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(897)	(604)	(1,254)
	----- \$ 295	----- \$ 360	----- \$ 58
	=====	=====	=====

5. LONG-TERM DEBT:

Long-term debt consists of a note payable to a bank. The debt is secured by certain equipment, accounts receivable, inventory, a \$1,000,000 life insurance policy on the president and the personal guaranty of the president limited to 50 percent of the outstanding balance of the loan. The note is payable in monthly installments of \$63,000 including interest at the prime lending rate less .25 percent (8 percent at December 31, 1996). The Company has restrictive and various financial covenants with which the Company was in compliance at December 31, 1996.

QUALITY AIR HEATING & COOLING, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The maturities of long-term debt as of December 31, 1996, are as follows (in thousands):

Year ending December 31,	
1997.....	\$ 675
1998.....	646
	-----
	\$ 1,321
	=====

The Company has a \$2,000,000 line of credit with a bank. The line of credit expires August 1, 1997, and bears interest at one-half percent below the prime lending rate. The line of credit is secured by accounts receivable, inventory, a \$1,000,000 life insurance policy, and machinery and equipment. There was no balance outstanding under this line of credit at March 31, 1995 and 1996, and December 31, 1996.

6. LEASES:

The Company leases a facility from a company which is owned by one of the Company's shareholders. The lease expires on April 30, 2005. Quality has an option to renew the lease for one additional three-year term on the same terms. The rent paid under this related-party lease was approximately \$221,000 for each of the years ended March 31, 1995 and 1996, and December 31, 1996. The Company also leases a facility from a third party, which expires on June 30, 1998. The rent paid under this lease was approximately \$20,000 for each of the years ended March 31, 1995 and 1996, and December 31, 1996. The Company has guaranteed the payment of two series of public bonds issued in 1985 and 1990, respectively, by the Michigan Strategic Fund on behalf of two real property development entities owned by a shareholder, the proceeds of which were used to fund the construction of the Company's leased warehouse facility and a second adjacent warehouse. As of March 1997, approximately \$1.6 million of the bond debt remained outstanding.

Future minimum lease payments under these non-cancellable operating leases are as follows (in thousands):

Year ending December 31,	
1997.....	\$ 241
1998.....	231
1999.....	221
2000.....	221
2001.....	221
Thereafter.....	718
	-----
	\$ 1,853
	=====

7. RELATED-PARTY TRANSACTIONS:

The Company paid management fees to an entity owned by its majority shareholder through December 31, 1995. Total management fees paid amounted to \$260,000 and \$190,000 for the years ended March 31, 1995 and 1996, respectively.

8. EMPLOYEE BENEFIT PLAN:

The Company has a defined contribution profit sharing plan. The plan provides for the Company to match one-half of the first 4 percent contributed by each employee. Total contributions by the Company under the plan were approximately \$104,000, \$110,000 and \$125,000 for the years ending March 31, 1995 and 1996, and December 31, 1996, respectively. The Company may also make discretionary contributions. The Company made discretionary contributions of \$200,000 and \$300,000 for the years ended March 31,

1995 and 1996, and had accrued approximately \$169,000 at December 31, 1996, for contributions to be funded in 1997.

#### 9. FINANCIAL INSTRUMENTS

The Company's financial instruments consist of cash and cash equivalents, a line of credit, notes payable and debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

#### 10. COMMITMENTS AND CONTINGENCIES:

##### LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal actions will have a material adverse effect on the Company's financial position or results of operations.

##### INSURANCE

The Company carries a broad range of insurance coverage, including business auto liability, general liability and an umbrella policy. The Company has not incurred significant claims or losses on any of these insurance policies.

The Company is self-insured for medical claims up to \$30,000 per year per covered individual. Additionally, the Company is part of the state's workers' compensation plan and is responsible for claims up to \$275,000 per accident with a maximum aggregate exposure for twenty-four months of \$648,000. Claims in excess of these amounts are covered by a stop-loss policy. Under the state's policy, the Company has a \$300,000 letter of credit which expires December 31, 1997. The Company has recorded reserves for its portion of self-insured claims based on estimated claims incurred through March 31, 1995 and 1996 and December 31, 1996.

##### ROYALTY AGREEMENT

The Company is obligated to pay royalties ranging from 1 percent to 4.5 percent based on the level of service revenues through December 1, 2001, for management systems support. Royalties paid under this agreement were approximately \$157,000, \$159,000 and \$165,000 for the years ended March 31, 1995 and 1996 and December 31, 1996.

#### 11. SHAREHOLDERS' EQUITY:

On February 15, 1995, the Company acquired 66,007 shares of common stock from its majority shareholder for approximately \$898,000.

#### 12. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

As of March 31, 1997, the Company declared and accrued distributions of \$2,356,000 to its shareholders. In connection with the merger, the Company will make additional cash distributions of approximately \$4,833,000 prior to the merger which represents the Company's estimated S Corporation accumulated adjustment account. Had these transactions been recorded at March 31, 1997, the effect on the accompanying unaudited balance sheet would be a decrease in assets of \$3,478,000, an increase in liabilities of \$1,355,000 and a decrease in shareholders' equity of \$4,833,000.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Atlas Comfort Services USA, Inc.:

We have audited the accompanying consolidated balance sheets of Atlas Comfort Services USA, Inc. (a Texas corporation) and its subsidiary (the Company) as of June 30, 1995 and 1996 and December 31, 1996, and the related consolidated statements of operations, shareholders' equity and cash flows for the years ended June 30, 1994, 1995 and 1996 and the six months ended December 31, 1996. 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 generally accepted auditing standards. 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 Atlas Comfort Services USA, Inc., and its subsidiary as of June 30, 1995 and 1996, and December 31, 1996, and the consolidated results of their operations and their cash flows for the three years ended June 30, 1994, 1995 and 1996 and for the six months ended December 31, 1996, in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

ATLAS COMFORT SERVICES USA, INC. AND SUBSIDIARY  
CONSOLIDATED BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	JUNE 30,		DECEMBER 31,	MARCH 31,
	1995	1996	1996	1997
	(UNAUDITED)			
<b>ASSETS</b>				
<b>CURRENT ASSETS:</b>				
Cash and cash equivalents.....	\$ 427	\$ 391	\$ 101	\$ 356
Accounts receivable --				
Trade, net of allowance of				
\$60, \$60, \$100 and \$100,				
respectively.....	2,920	3,953	2,604	3,226
Retainage.....	904	1,327	1,208	1,280
Officers, employees and				
other receivables.....	114	172	159	158
Inventories.....	1,685	2,000	1,770	1,676
Costs and estimated earnings in				
excess of billings on				
uncompleted contracts.....	1,050	681	676	314
Current deferred income taxes...	155	164	145	145
Prepaid expenses and other				
current assets.....	40	27	82	56
	-----	-----	-----	-----
Total current				
assets.....	7,295	8,715	6,745	7,211
PROPERTY AND EQUIPMENT, net.....	231	484	499	598
<b>OTHER ASSETS:</b>				
Goodwill, net.....	24	23	22	22
Deferred income tax.....	167	105	88	88
	-----	-----	-----	-----
Total assets.....	\$ 7,717	\$ 9,327	\$7,354	\$ 7,919
	=====	=====	=====	=====
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>				
<b>CURRENT LIABILITIES:</b>				
Line of credit.....	\$ 500	\$ 600	\$--	\$ 200
Current maturities of notes				
payable to affiliates.....	200	102	107	107
Current obligations under				
capital leases.....	32	92	101	140
Current maturities of long-term				
debt.....	9	348	356	353
Accounts payable and accrued				
expenses.....	3,522	3,295	2,246	2,101
Income tax payable.....	363	390	752	936
Billings in excess of costs and				
estimated earnings on				
uncompleted contracts.....	1,115	1,947	523	570
	-----	-----	-----	-----
Total current				
liabilities.....	5,741	6,774	4,085	4,407
NOTES PAYABLE TO AFFILIATES, net of				
current portion.....	1,271	149	98	75
OBLIGATIONS UNDER CAPITAL LEASES, net				
of current portion.....	44	133	121	209
LONG-TERM DEBT, net of current				
portion.....	21	1,225	1,058	965
<b>COMMITMENTS AND CONTINGENCIES</b>				
<b>SHAREHOLDERS' EQUITY:</b>				
Common stock, no par value;				
5,000 shares authorized,				
1,000 issued and				
outstanding.....	1	1	1	1
Retained earnings.....	639	1,045	1,991	2,262
	-----	-----	-----	-----
Total shareholders'				
equity.....	640	1,046	1,992	2,263
	-----	-----	-----	-----
Total liabilities and				
shareholders'				
equity.....	\$ 7,717	\$ 9,327	\$7,354	\$ 7,919
	=====	=====	=====	=====

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



ATLAS COMFORT SERVICES USA, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(IN THOUSANDS)

	YEAR ENDED JUNE 30,			SIX MONTHS ENDED DECEMBER 31,	THREE MONTHS ENDED MARCH 31,	
	1994	1995	1996	1996	1996	1997
	(UNAUDITED)					
REVENUES.....	\$ 21,848	\$ 22,444	\$ 29,174	\$ 15,545	\$ 6,207	\$ 6,115
COST OF SERVICES.....	19,657	19,635	25,449	12,508	5,456	4,866
Gross profit.....	2,191	2,809	3,725	3,037	751	1,249
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	2,086	2,166	2,843	1,432	631	753
Income from operations.....	105	643	882	1,605	120	496
OTHER INCOME (EXPENSE):						
Interest expense.....	(156)	(168)	(185)	(107)	(51)	(54)
Other.....	2	28	(11)	78	--	17
Income (loss) before income taxes, extraordinary item, and cumulative effect of a change in accounting principle.....	(49)	503	686	1,576	69	459
Provision for income taxes (benefit).....	(2)	199	280	630	28	188
Income (loss) before extraordinary item and cumulative effect of a change in accounting principle.....	(47)	304	406	946	41	271
Extraordinary item -- gain on extinguishment of debt, net of deferred taxes of \$167,000 (Note 5).....	273	--	--	--	--	--
Income before cumulative effect of a change in accounting principle.....	226	304	406	946	41	271
Cumulative effect on prior years of a change in accounting for income taxes (Note 7).....	141	--	--	--	--	--
NET INCOME.....	\$ 367	\$ 304	\$ 406	\$ 946	\$ 41	\$ 271

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

ATLAS COMFORT SERVICES USA, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
(IN THOUSANDS, EXCEPT FOR SHARE INFORMATION)

	COMMON STOCK		RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
	SHARES	AMOUNT		
BALANCE, December 31, 1993.....	1,000	\$ 1	\$ (32)	\$ (31)
Net income.....	--	--	367	367
BALANCE, June 30, 1994.....	1,000	1	335	336
Net income.....	--	--	304	304
BALANCE, June 30, 1995.....	1,000	1	639	640
Net income.....	--	--	406	406
BALANCE, June 30, 1996.....	1,000	1	1,045	1,046
Net income.....	--	--	946	946
BALANCE, December 31, 1996.....	1,000	1	1,991	1,992
Net income (unaudited).....	--	--	271	271
BALANCE, March 31, 1997 (unaudited).....	1,000	\$ 1	\$ 2,262	\$ 2,263
	=====	=====	=====	=====

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

ATLAS COMFORT SERVICES USA, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEAR ENDED JUNE 30,			SIX MONTHS ENDED DECEMBER 31,	THREE MONTHS ENDED MARCH 31,	
	1994	1995	1996	1996	1996	1997
	(UNAUDITED)					
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>						
Net income.....	\$ 367	\$ 304	\$ 406	\$ 946	\$ 41	\$ 271
Adjustments to reconcile net income to net cash provided by (used in) operating activities --						
Depreciation and amortization.....	104	124	92	84	27	33
Cumulative effect of a change in accounting principle.....	(141)	--	--	--	--	--
Extraordinary gain on extinguishment of debt....	(440)	--	--	--	--	--
Deferred income tax provision.....	167	(196)	54	36	--	--
Changes in operating assets and liabilities --						
(Increase) decrease in --						
Accounts receivable.....	(1,672)	148	(1,514)	1,481	816	(693)
Inventories.....	(264)	(554)	(315)	230	(460)	94
Costs and estimated earnings in excess of billings on uncompleted contracts....	(145)	(266)	369	5	317	362
Prepaid expenses and other current assets.....	121	(14)	13	(55)	124	26
Increase (decrease) in --						
Accounts payable and accrued expenses.....	1,320	(417)	(227)	(1,049)	(135)	(146)
Income tax payable.....	--	363	27	362	(259)	184
Billings in excess of costs and estimated earnings on uncompleted contracts....	585	437	834	(1,424)	(445)	47
Net cash provided by (used in) operating activities.....	2	(71)	(261)	616	26	178
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>						
Additions to property and equipment.....	(139)	(67)	(121)	(50)	(96)	(131)
Net cash used in investing activities.....	(139)	(67)	(121)	(50)	(96)	(131)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>						
Net borrowings on line of credit.....	400	100	100	(600)	240	200
Principal payments on notes payable to affiliates.....	(38)	(261)	(1,219)	(50)	(23)	(23)
Borrowings on notes payable to affiliates.....	1,202	100	--	3	--	--
Principal payments on long-term debt.....	(1,067)	(14)	(150)	(176)	(29)	(95)
Borrowings on long-term debt....	41	--	1,689	15	315	19
Additions to (principal payments on) capital lease obligations.....	(29)	(37)	(74)	(48)	(9)	107
Net cash provided by (used in) financing activities.....	509	(112)	346	(856)	494	208
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....</b>	<b>372</b>	<b>(250)</b>	<b>(36)</b>	<b>(290)</b>	<b>424</b>	<b>255</b>
CASH AND CASH EQUIVALENTS, beginning of period.....	305	677	427	391	--	101
CASH AND CASH EQUIVALENTS, end of period.....	<u>\$ 677</u>	<u>\$ 427</u>	<u>\$ 391</u>	<u>\$ 101</u>	<u>\$ 424</u>	<u>\$ 356</u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>						
Cash paid for --						
Income Taxes.....	\$ --	\$ 30	\$ 200	\$ 224	\$ 200	\$ --

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

ATLAS COMFORT SERVICES USA, INC. AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. BUSINESS AND ORGANIZATION:

Atlas Comfort Services USA, Inc., a Texas corporation, and its subsidiary (the "Company") is a leading provider of HVAC installation services for apartment complexes, condominiums and hotels in the United States and also provides maintenance, repair and replacement of HVAC systems. Atlas primarily operates in the southwest, northeast, and the mid-Atlantic regions of the United States.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems"), pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

BASIS OF PRESENTATION

The consolidated financial statements include the accounts and results of operations of the Company and its subsidiary which are under common control and management of two individuals. All significant intercompany transactions and balances have been eliminated in combination.

INTERIM FINANCIAL INFORMATION

The interim consolidated financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the consolidated interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories 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 (FIFO) 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 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. 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 statements of operations.

#### 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. 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 income and are recognized in the period in which the revisions are determined.

The balances billed but not paid by customers pursuant to retainage provisions in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

#### WARRANTY COSTS

The Company warrants labor for the first year after installation on new air conditioning and heating units. The Company generally warrants labor for 30 days after servicing of existing air conditioning and heating units. A reserve for warranty costs is recorded upon completion of installation or service.

#### INCOME TAXES

The Company follows the liability method of accounting for income taxes in accordance with Statement of Financial Accounting Standards (SFAS) No. 109. Under this method, deferred income taxes are recorded based upon the differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the underlying assets or liabilities are recovered or settled.

#### 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 and 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.

#### GOODWILL

Goodwill, in the amount of \$33,000, represents the excess of cost over the fair value of net assets acquired and is amortized using the straight-line method over 40 years. The Company assesses the recoverability of its goodwill whenever adverse events occur and believes that no material impairment exists.

#### NEW ACCOUNTING PRONOUNCEMENTS

Effective July 1, 1996, the Company adopted SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment, and intangible or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	JUNE 30,		DECEMBER 31,
		1995	1996	1996
Transportation equipment.....	5	\$ 741	\$ 987	\$1,043
Machinery and equipment.....	5	116	140	137
Leasehold improvements.....	3	28	28	28
Furniture and fixtures.....	5	266	286	212
Less -- Accumulated depreciation and amortization.....		(920)	(957)	(921)
Property and equipment, net.....		\$ 231	\$ 484	\$ 499

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS (IN THOUSANDS):

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

	JUNE 30,		DECEMBER 31,
	1995	1996	1996
Balance at beginning of year.....	\$ 60	\$ 60	\$ 60
Additions to costs and expenses.....	75	77	42
Deductions for uncollectible receivables written off and recoveries.....	(75)	(77)	(2)
	\$ 60	\$ 60	\$ 100

Accounts payable and accrued expenses consist of the following:

	JUNE 30,		DECEMBER 31,
	1995	1996	1996
Accounts payable, trade.....	\$ 2,935	\$ 2,409	\$1,582
Accrued compensation and benefits....	197	231	163
Accrued warranty expense.....	250	300	310
Other accrued expenses.....	140	355	191
	\$ 3,522	\$ 3,295	\$2,246

Installation contracts in progress are as follows:

	JUNE 30,		DECEMBER 31,
	1995	1996	1996
Costs incurred on contracts in progress.....	\$ 11,884	\$ 12,526	\$ 12,643
Estimated earnings, net of losses....	2,666	2,589	2,582
	14,550	15,115	15,225
Less -- Billings to date.....	14,615	16,381	15,072
	\$ (65)	\$ (1,266)	\$ 153
Costs and estimated earnings in excess of billings on uncompleted contracts.....	1,050	681	676
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(1,115)	(1,947)	(523)
	\$ (65)	\$ (1,266)	\$ 153

5. DEBT:

LINE OF CREDIT

The Company has a \$700,000 revolving line-of-credit facility with a bank at the prime lending rate plus 1 percent with interest payable monthly. This credit facility is secured by the Company's cash, accounts receivable, inventory, and unpledged property and equipment. The credit facility is guaranteed by two of the Company's officers and is also secured by investment accounts of certain affiliates. The credit facility had an outstanding balance of \$500,000, \$600,000, and \$0 at June 30, 1995 and 1996 and December 31, 1996, respectively, and matures in January 1998. The Company paid approximately \$8,000, \$33,000 and \$35,000 of interest relating to the revolving credit line for the years ended June 30, 1994, 1995 and 1996 and \$18,500 for the six months ended December 31, 1996.

NOTES PAYABLE TO FINANCIAL INSTITUTIONS

Long-term debt is summarized as follows:

	JUNE 30,		DECEMBER 31,
	1995	1996	1996
(IN THOUSANDS)			
Note payable to a financial institution with interest at prime plus 1%, payable in monthly installments of \$26,667 plus interest through January 1999, when the entire balance of unpaid principal and accrued interest shall be due and payable.....	\$ --	\$ 1,467	\$1,306
Vehicle notes with interest at rates ranging from 7.9% to 9.4%, payable in monthly installments through March 2001.....	30	106	108
	30	1,573	1,414
Less -- Current maturities.....	9	348	356
	\$ 21	\$ 1,225	\$1,058

The note payable to a financial institution is secured by cash, accounts receivable, inventory, property and equipment, and the personal guarantee of the two shareholders. In addition, investment accounts of the shareholders and of certain affiliates of the shareholders are pledged as collateral for the note. The Company paid interest of \$3,000, \$3,000 and \$73,500 for the years ended June 30, 1994, 1995 and 1996, respectively, and \$73,000 for the six months ended December 31, 1996.

ATLAS COMFORT SERVICES USA, INC. AND SUBSIDIARY  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

In September 1993, the Company and a bank reached a settlement agreement in which the bank released the Company from its total obligation of approximately \$1,500,000 related to a revolving line of credit, installment notes, equipment notes and related accrued interest, for a lump sum payment of \$1,100,000. The payment was funded by the proceeds from the notes payable to affiliates mentioned below. This early extinguishment of debt generated a gain aggregating \$440,000. The Company paid approximately \$77,000 in interest during the year ended June 30, 1994 related to these extinguished notes.

NOTES PAYABLE TO AFFILIATES

Notes payable to affiliates are summarized as follows:

	JUNE 30,		DECEMBER 31,
	1995	1996	1996
	-----		
	(IN THOUSANDS)		
Note payable to a related party in monthly installments of \$5,500 including interest at 10% through March 1998, collateralized by stock of the Company.....	\$ 159	\$ 105	\$ 78
Unsecured note payable to an affiliate in monthly installments of \$2,500 including interest at 6% through September 1996.....	326	--	--
Notes payable to Company officers in monthly installments of \$4,812 including interest at 10% through June 1999.....	186	146	127
Notes payable to Company officers with interest due monthly at the prime rate through September 1996, secured by accounts receivable, certain property and equipment, and intangible assets.....	700	--	--
Unsecured note payable to Company officers with interest and any unpaid principal balance due August 8, 1995, at the rate of 9%.....	100	--	--
	-----	-----	-----
	1,471	251	205
Less -- Current maturities.....	200	102	107
	-----	-----	-----
	\$ 1,271	\$ 149	\$ 98
	=====	=====	=====

The Company paid interest of \$116,400, \$112,600 and \$68,000 related to notes payable to affiliates for the years ended June 30, 1994, 1995 and 1996, respectively, and \$12,600 for the six months ended December 31, 1996.

The aggregate maturities of notes payable to financial institutions and affiliates are as follows (in thousands):

Year ending December 31,	
1997.....	\$ 463
1998.....	424
1999.....	718
2000.....	13
2001 and thereafter.....	1
	-----
	\$ 1,619
	=====



6. LEASES:

The Company leases vehicles and warehouse facilities under capital and operating leases expiring through October, 2000. Total rent expense related to operating leases amounted to \$95,000, \$143,000 and \$180,000 for the years ended June 30, 1994, 1995 and 1996, respectively, and \$60,000 for the six months ended December 31, 1996.

Future minimum lease payments for capital and noncancelable operating leases are as follows (in thousands):

	CAPITAL LEASES	NONCANCELABLE OPERATING LEASES
	-----	-----
Year ended December 31,		
1997.....	\$ 117	\$ 142
1998.....	98	23
1999.....	44	--
2000.....	6	--
	-----	-----
Total minimum lease payments....	265	165
Amounts representing interest...	43	
	-----	
Present value of net minimum lease payments.....	222	
Less -- Current portion.....	101	
	-----	
Long-term obligation.....	\$ 121	
	=====	

7. INCOME TAXES (IN THOUSANDS):

Federal and state income taxes are as follows:

	YEAR ENDED JUNE 30,			SIX MONTHS ENDED DECEMBER 31,
	-----	-----	-----	-----
	1994	1995	1996	1996
	-----	-----	-----	-----
Federal --				
Current.....	\$ (2)	\$ 331	\$ 193	\$ 504
Deferred.....	141	(164)	43	28
State --				
Current.....	--	64	34	90
Deferred.....	26	(32)	10	8
	-----	-----	-----	-----
	\$ 165	\$ 199	\$ 280	\$ 630
	=====	=====	=====	=====

ATLAS COMFORT SERVICES USA, INC. AND SUBSIDIARY  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Actual income tax expense differs from income tax expense computed by applying the U.S. federal statutory corporate rate of 34 percent to income (loss) before income taxes as follows:

	YEAR ENDED JUNE 30,			SIX MONTHS ENDED DECEMBER 31,
	1994	1995	1996	1996
Provision at the statutory rate.....	\$ (16)	\$ 171	\$ 233	\$ 536
Increase resulting from --				
Permanent differences, mainly meals and entertainment.....	164	7	19	29
State income tax, net of benefit for federal deduction.....	17	21	28	65
	<u>\$ 165</u>	<u>\$ 199</u>	<u>\$ 280</u>	<u>\$ 630</u>

Deferred income tax provisions result from temporary differences in the recognition of income and expenses for financial reporting purposes and for tax purposes. The tax effects of these temporary differences, representing deferred tax assets and liabilities, result principally from the following:

	JUNE 30,		DECEMBER 31,
	1995	1996	1996
Accounting for long-term contracts...	\$ 159	\$ 74	\$ (11)
Warranty reserves.....	100	123	127
Inventory.....	32	38	40
Allowance for doubtful accounts.....	36	30	51
Other accrued expenses not deducted for tax purposes.....	25	62	90
Bases differences on property and equipment and capital lease accounting.....	(30)	(58)	(64)
Net deferred tax assets.....	<u>\$ 322</u>	<u>\$ 269</u>	<u>\$ 233</u>

The net deferred tax assets and liabilities are comprised of the following:

	JUNE 30,		DECEMBER 31,
	1995	1996	1996
Deferred tax assets --			
Current.....	\$ 209	\$ 240	\$ 293
Long-term.....	221	171	149
Total.....	<u>430</u>	<u>411</u>	<u>442</u>
Deferred tax liabilities --			
Current.....	(54)	(76)	(148)
Long-term.....	(54)	(66)	(61)
Total.....	<u>(108)</u>	<u>(142)</u>	<u>(209)</u>
Net deferred income tax assets.....	<u>\$ 322</u>	<u>\$ 269</u>	<u>\$ 233</u>

The Company adopted the provisions of SFAS No. 109 in fiscal year 1994 resulting in a cumulative effect of a change in accounting principle of \$141,000.

8. RELATED-PARTY TRANSACTIONS:

Two shareholders lease to the Company the main office facility. Total payments made under this lease agreement amounted to \$90,000 for each of the years ended June 30, 1994, 1995 and 1996, respectively, and \$45,000 for the six months ended December 31, 1996. The Company is in the process of entering into

an agreement with these shareholders to lease land on which a new facility will be built. This lease agreement is anticipated to have a twenty year term.

9. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal action will have a material adverse effect on the Company's financial position or consolidated results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

10. EMPLOYEE BENEFIT PLAN

The Company sponsors a Profit Sharing and Savings Plan (the "Plan") which covers substantially all employees. The employees who participate in the Plan may contribute 1 percent to 20 percent of their base compensation, and the Company may make discretionary matching contributions. The Company did not make any contributions for the years ended December 31, 1994 and 1995. The Company made \$18,248 in contributions for the year ended June 30, 1996 and \$12,667 for the six months ended December 31, 1996.

11. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, notes receivable, notes payable, a line of credit and long-term debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

12. SIGNIFICANT CUSTOMERS AND VENDORS:

Significant customers are those that account for greater than ten percent of the Company's revenues. For the year ended June 30, 1996 and the six months ended December 31, 1996, one customer, a publicly traded Real Estate Investment Trust, accounted for 14% and 20% of the Company's revenues, respectively. Receivables outstanding from this customer represented 13% and 12% of the Company's trade and retainage receivables as of June 30, 1996 and December 31, 1996, respectively. In addition, one of the Company's shareholders has less than 1% ownership in this customer.

During the years ended June 30, 1994, 1995 and 1996 and the six months ended December 31, 1996, two vendors accounted for 12% and 11%; 29% and 17%; 20% and 17%; and 15% and 12% of the Company's purchases, respectively.

13. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems providing for the merger of the Company with the subsidiary of Comfort Systems.

Concurrently with the merger, the Company will enter into agreements with the shareholders to lease land and buildings used in the Company's operations for negotiated amounts and terms.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Tri-City Mechanical, Inc.:

We have audited the accompanying balance sheets of Tri-City Mechanical, Inc. as of December 31, 1995 and 1996, and the related statements of operations, shareholders' equity and cash flows for each of the three years in the period ended December 31, 1996. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Tri-City Mechanical, Inc. as of December 31, 1995 and 1996, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1996 in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

TRI-CITY MECHANICAL, INC.  
BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	DECEMBER 31,		MARCH 31
	1995	1996	1997
			(UNAUDITED)
<b>ASSETS</b>			
<b>CURRENT ASSETS:</b>			
Cash and cash equivalents.....	\$ 2,551	\$1,958	\$2,665
Restricted cash.....	383	325	328
Investments.....	--	493	500
Accounts Receivable --			
Trade, net of allowance of			
\$130, \$30 and \$30,			
respectively.....	4,495	3,734	3,774
Retainage.....	831	756	728
Other receivables.....	2	11	66
Inventories.....	1,183	762	218
Costs and estimated earnings in			
excess of billings on			
uncompleted contracts.....	306	288	380
Prepaid expenses and other			
current assets.....	1	12	2
	9,752	8,339	8,661
PROPERTY AND EQUIPMENT, net.....	508	656	643
	\$ 10,260	\$8,995	\$9,304
	\$ 10,260	\$8,995	\$9,304
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>CURRENT LIABILITIES:</b>			
Accounts payable and accrued			
expenses.....	\$ 2,683	\$2,179	\$2,408
Billings in excess of costs and			
estimated earnings on			
uncompleted contracts.....	2,207	667	435
	4,890	2,846	2,843
<b>COMMITMENTS AND CONTINGENCIES</b>			
<b>SHAREHOLDERS' EQUITY:</b>			
Common stock, \$10 par 2,500			
shares authorized, 2,500			
issued and outstanding.....	25	25	25
Additional paid-in capital.....	105	105	105
Retained earnings.....	5,240	6,019	6,331
	5,370	6,149	6,461
	\$ 10,260	\$8,995	\$9,304
	\$ 10,260	\$8,995	\$9,304

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

TRI-CITY MECHANICAL, INC.  
STATEMENTS OF OPERATIONS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,			THREE MONTHS ENDED MARCH 31,	
	1994	1995	1996	1996	1997
				(UNAUDITED)	
REVENUES.....	\$ 16,883	\$ 25,030	\$ 24,237	\$ 6,482	\$ 6,791
COST OF SERVICES.....	14,271	19,298	18,561	5,082	5,946
Gross profit.....	2,612	5,732	5,676	1,400	845
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	2,219	3,193	3,903	1,026	567
Income from operations.....	393	2,539	1,773	374	278
OTHER INCOME (EXPENSE):					
Interest expense.....	(2)	(1)	--	--	--
Interest income.....	50	132	152	43	25
Other.....	24	81	89	18	9
NET INCOME.....	\$ 465	\$ 2,751	\$ 2,014	\$ 435	\$ 312

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

TRI-CITY MECHANICAL, INC.  
 STATEMENTS OF SHAREHOLDERS' EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
	SHARES	AMOUNT			
BALANCE, December 31, 1993.....	2,500	\$ 25	\$ 105	\$ 2,577	\$ 2,707
Distributions to shareholders...	--	--	--	(338)	(338)
Net income.....	--	--	--	465	465
BALANCE, December 31, 1994.....	2,500	25	105	2,704	2,834
Distributions to shareholders...	--	--	--	(215)	(215)
Net income.....	--	--	--	2,751	2,751
BALANCE, December 31, 1995.....	2,500	25	105	5,240	5,370
Distributions to shareholders...	--	--	--	(1,235)	(1,235)
Net income.....	--	--	--	2,014	2,014
BALANCE, December 31, 1996.....	2,500	25	105	6,019	6,149
Net income (unaudited).....	--	--	--	312	312
BALANCE, March 31, 1997 (unaudited).....	2,500	\$ 25	\$ 105	\$ 6,331	\$ 6,461

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

TRI-CITY MECHANICAL, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,			THREE MONTHS ENDED MARCH 31,	
	1994	1995	1996	1996	1997
	(UNAUDITED)				
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>					
Net income.....	\$ 465	\$ 2,751	\$ 2,014	\$ 435	\$ 312
Adjustments to reconcile net income to net cash provided by (used in) operating activities --					
Depreciation.....	131	134	102	36	26
Deferred income taxes.....	(218)	--	--	--	--
Loss (gain) on sale of property and equipment.....	--	1	(10)	--	--
Changes in operating assets and liabilities --					
(Increase) decrease in --					
Restricted cash.....	(73)	(75)	58	(22)	(3)
Accounts receivable.....	(231)	(1,306)	827	1,048	(67)
Inventories.....	(329)	(801)	421	1,037	544
Costs in excess of billings and estimated earnings on uncompleted contracts.....	17	(90)	18	(146)	(92)
Prepaid expenses and other current assets.....	(14)	28	(11)	(10)	10
Increase (decrease) in --					
Accounts payable and accrued expenses.....	864	519	(504)	(393)	229
Billings in excess of costs and estimated earnings on uncompleted contracts.....	1,360	508	(1,540)	(1,234)	(232)
Net cash provided by operating activities.....	1,972	1,669	1,375	751	727
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>					
Proceeds from sale of property and equipment.....	--	18	22	--	--
Additions of property and equipment.....	(311)	(157)	(262)	(6)	(13)
Purchase of investment.....	--	--	(493)	--	(7)
Net cash used in investing activities.....	(311)	(139)	(733)	(6)	(20)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>					
Decrease in payable to shareholders.....	(210)	--	--	--	--
Borrowings on line of credit.....	19	1	--	--	--
Payments on line of credit.....	(17)	(15)	--	--	--
Distributions to shareholders.....	(338)	(215)	(1,235)	--	--
Net cash used in financing activities.....	(546)	(229)	(1,235)	--	--
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	1,115	1,301	(593)	745	707
CASH AND CASH EQUIVALENTS, beginning of period.....	135	1,250	2,551	2,551	1,958
CASH AND CASH EQUIVALENTS, end of period.....	\$ 1,250	\$ 2,551	\$ 1,958	\$ 3,296	\$ 2,665
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>					
Cash paid for --					
Interest.....	\$ 2	\$ 1	\$ --	\$ --	\$ --

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



TRI-CITY MECHANICAL, INC.  
NOTES TO FINANCIAL STATEMENTS

1. BUSINESS AND ORGANIZATION:

Tri-City Mechanical, Inc., an Arizona corporation, (the "Company") focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems primarily for large commercial and industrial facilities, as well as process piping for industrial facilities. Tri-City primarily operates in Arizona, California and Nevada.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems") pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

INTERIM FINANCIAL INFORMATION

The interim financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

RESTRICTED CASH

The Company also maintains restricted cash which consists of certificates of deposit. These certificates of deposit are held in a joint checking account between the contractors and Tri-City for the retainage balance due from contractors at the completion of the job.

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories 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 (FIFO) method.

INVESTMENTS

The Company has adopted Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities," which requires that investments in debt securities and marketable equity securities be designated as trading, held-to-maturity or available-for-sale. At December 31, 1996, investments have been categorized as held-to-maturity, are stated at cost, and are classified in the balance sheet as current assets. Investments at December 31, 1996 consist of U.S. Treasury Bills.

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 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. 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.

#### 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. 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 income and their effects are recognized in the period in which the revisions are determined.

The balances billed but not paid by customers pursuant to retainage provisions in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

#### WARRANTY COSTS

The Company 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 upon completion of installation or service.

#### INCOME TAXES

The Company has elected S Corporation status as defined by the Internal Revenue Code, whereby the Company is not subject to taxation for federal purposes. Under S Corporation status, the shareholders report their share of the Company's taxable earnings or losses in their personal tax returns. The Company will terminate its S Corporation status concurrently with the effective date of the Offering.

#### 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 and 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.

#### NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset is compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

TRI-CITY MECHANICAL, INC.  
 NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	DECEMBER 31,	
		1995	1996
Transportation equipment.....	5	\$ 521	\$ 623
Machinery and equipment.....	10	639	680
Computer and telephone equipment....	5	121	157
Leasehold improvements.....	5	48	48
Furniture and fixtures.....	6	54	54
		-----	-----
		1,383	1,562
Less -- Accumulated depreciation....		(875)	(906)
		-----	-----
Property and equipment, net.....		\$ 508	\$ 656
		=====	=====

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

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

	DECEMBER 31,		
	1994	1995	1996
Balance at beginning of year.....	\$ 100	\$ 130	\$ 130
Additions to costs and expenses.....	184	1	48
Deductions for uncollectible receivables written off and recoveries.....	(154)	(1)	(148)
	-----	-----	-----
	\$ 130	\$ 130	\$ 30
	=====	=====	=====

Accounts payable and accrued expenses consist of the following (in thousands):

	DECEMBER 31,	
	1995	1996
Accounts payable, trade.....	\$ 2,178	\$ 1,749
Accrued compensation and benefits.....	181	97
Warranty reserve.....	301	278
Other accrued expenses.....	23	55
	-----	-----
	\$ 2,683	\$ 2,179
	=====	=====

TRI-CITY MECHANICAL, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

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

	DECEMBER 31,	
	1995	1996
Costs incurred on contracts in progress.....	\$ 14,659	\$ 8,615
Estimated earnings, net of losses....	3,865	2,471
	-----	-----
	18,524	11,086
Less -- Billings to date.....	20,425	11,465
	-----	-----
	\$ (1,901)	\$ (379)
	=====	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 306	\$ 288
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(2,207)	(667)
	-----	-----
	\$ (1,901)	\$ (379)
	=====	=====

5. LONG-TERM DEBT:

The Company has a \$1.0 million line of credit with a financial services company. The line of credit expires October 31, 1997, and bears interest at 9 percent per annum. The line of credit is secured by a lien on accounts receivable. There was no balance outstanding under this line of credit at December 31, 1995 or 1996.

6. LEASES:

The Company leases facilities from a company which is wholly owned by one of the shareholders. The lease expires June 30, 1998. The rent paid under this related-party lease was approximately \$109,000 for the year ended 1996. The lease requires the Company to pay taxes, maintenance, insurance and certain other operating costs of the leased property. The lease contains renewal and termination provisions.

The Company leases vehicles for certain key members of management. The leases expire October 1, 1999. The lease payments under these vehicle leases were approximately \$6,000, \$15,000 and \$16,000 for the years ended December 31, 1994, 1995 and 1996, respectively.

Future minimum lease payments for operating leases are as follows (in thousands):

Year ending December 31 --	
1997.....	\$ 142
1998.....	65
1999.....	3
	-----
	\$ 210
	=====

7. EMPLOYEE BENEFIT PLANS:

The Company has adopted a 401(k) plan. The plan provides for the Company to match 20 percent of the first 6 percent contributed by each employee. Total contributions by the Company under this plan were approximately \$13,000, \$22,000 and \$24,000 during 1994, 1995 and 1996, respectively. Amounts due to this plan were approximately \$ --, \$ -- and \$4,000 for the years ended December 31, 1994, 1995 and 1996, respectively.

8. RELATED-PARTY TRANSACTIONS:

The Company provides accounting services and building maintenance at no cost to Nothum Properties & SMAC companies which are wholly owned by the shareholders. The estimated value of the services provided during the years ended December 31, 1994, 1995 and 1996 was \$25,000, \$28,000 and \$30,000, respectively.

9. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal actions will have a material adverse effect on the Company's financial position or results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

10. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, investments, and a line of credit. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

11. SALES TO SIGNIFICANT CUSTOMER:

For the years ended December 31, 1994, 1995 and 1996, a customer accounted for approximately 17, 11 and 11 percent, respectively, of the Company's sales.

12. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

In connection with the merger the Company will make a cash distribution of approximately \$6,331,000 prior to the merger which represents the Company's estimated S Corporation accumulated adjustment account. Had these transactions been recorded at March 31, 1997, the effect on the accompanying unaudited balance sheet would be a decrease in assets of \$2,365,000, an increase in liabilities of \$3,966,000 and a decrease in shareholders' equity of \$6,331,000.

Concurrently with the merger, the Company will enter into agreements with the shareholders to lease land and buildings used in the Company's operations for a negotiated amount and term.

Tri-City has a verbal commitment with a limited liability corporation owned by Mr. Nothum, Jr. and his father to construct new office, operations and warehouse facilities. The Company believes that the rent for its current and future property does not and will not exceed fair market value.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To S. M. Lawrence Inc.:

We have audited the accompanying combined balance sheets of S. M. Lawrence Inc. and related company as of October 31, 1995 and 1996, and the related combined statements of operations, shareholders' equity and cash flows for the three years ended October 31, 1996. These combined financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined 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 combined financial statements referred to above present fairly, in all material respects, the financial position of S. M. Lawrence Inc. and related company as of October 31, 1995 and 1996, and the results of their operations and their cash flows for the three years ended October 31, 1996 in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

S. M. LAWRENCE INC. AND RELATED COMPANY  
COMBINED BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	OCTOBER 31,		APRIL 30,
	1995	1996	1997
			(UNAUDITED)
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents.....	\$ 680	\$ 327	\$ --
Accounts receivable --			
Trade.....	1,457	2,493	1,748
Retainage.....	454	896	1,249
Other receivables.....	1	1	--
Note receivable from shareholder...	50	75	76
Inventories.....	215	253	277
Costs and estimated earnings in excess of billings on uncompleted contracts.....	66	358	539
Prepaid expenses and other current assets.....	39	61	204
	-----	-----	-----
Total current assets.....	2,962	4,464	4,093
PROPERTY AND EQUIPMENT, net.....	459	644	721
OTHER NONCURRENT ASSETS.....	138	132	184
	-----	-----	-----
Total assets.....	\$ 3,559	\$ 5,240	\$ 4,998
	=====	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES:			
Line of credit.....	\$ 10	\$ --	\$ --
Note payable to affiliate.....	--	--	--
Accounts payable and accrued expenses.....	1,153	2,737	1,127
Income tax payable.....	--	--	368
Billings in excess of costs and estimated earnings on uncompleted contracts.....	299	344	790
	-----	-----	-----
Total current liabilities.....	1,462	3,081	2,285
COMMITMENTS AND CONTINGENCIES			
SHAREHOLDERS' EQUITY:			
Common stock, no par value, 3,000 shares authorized, 1,480 shares issued and outstanding.....	161	161	161
Treasury stock, at cost.....	(15)	(15)	(15)
Retained earnings.....	1,951	2,013	2,567
	-----	-----	-----
Total shareholders' equity.....	2,097	2,159	2,713
	-----	-----	-----
Total liabilities and shareholders' equity.....	\$ 3,559	\$ 5,240	\$ 4,998
	=====	=====	=====

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

S.M. LAWRENCE INC. AND RELATED COMPANY  
 COMBINED STATEMENTS OF OPERATIONS  
 (IN THOUSANDS)

	YEARS ENDED OCTOBER 31,			SIX MONTHS ENDED APRIL 30,	
	1994	1995	1996	1996	1997
	-----				
	(UNAUDITED)				
REVENUES.....	\$ 12,758	\$ 12,568	\$ 17,163	\$ 6,736	\$ 8,563
COST OF SERVICES.....	9,797	9,142	12,211	4,958	6,139
	-----				
Gross profit.....	2,961	3,426	4,952	1,778	2,424
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	2,849	3,477	4,885	1,976	1,630
	-----				
Income (loss) from operations.....	112	(51)	67	(198)	794
OTHER INCOME (EXPENSE):					
Interest income, net.....	32	55	47	--	(3)
Other.....	(41)	34	8	16	133
	-----				
INCOME BEFORE INCOME TAXES.....	103	38	122	(182)	924
PROVISION FOR INCOME TAXES.....	50	30	60	(73)	370
	-----				
NET INCOME.....	\$ 53	\$ 8	\$ 62	\$ (109)	\$ 554
	=====				

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



S.M. LAWRENCE INC. AND RELATED COMPANY  
 COMBINED STATEMENTS OF SHAREHOLDERS' EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		RETAINED EARNINGS	TREASURY STOCK	TOTAL SHAREHOLDERS' EQUITY
	SHARES	AMOUNT			
BALANCE, October 31, 1993.....	1,480	\$ 161	\$ 1,890	\$ (15)	\$ 2,036
Net income.....	--	--	53	--	53
BALANCE, October 31, 1994.....	1,480	161	1,943	(15)	2,089
Net income.....	--	--	8	--	8
BALANCE, October 31, 1995.....	1,480	161	1,951	(15)	2,097
Net income.....	--	--	62	--	62
BALANCE, October 31, 1996.....	1,480	161	2,013	(15)	2,159
Net income (unaudited).....	--	--	554	--	554
BALANCE, April 30, 1997 (unaudited).....	1,480	\$ 161	\$ 2,567	\$ (15)	\$ 2,713

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

S.M. LAWRENCE INC. AND RELATED COMPANY  
 COMBINED STATEMENTS OF CASH FLOWS  
 (IN THOUSANDS)

CASH FLOWS FROM OPERATING ACTIVITIES:	YEARS ENDED OCTOBER 31,			SIX MONTHS ENDED APRIL 30,	
	1994	1995	1996	1996	1997
	(UNAUDITED)				
Net income (loss).....	\$ 53	\$ 8	\$ 62	\$ (109)	\$ 554
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities --					
Depreciation and amortization...	263	121	200	86	109
Gain on sale of property and equipment.....	--	--	--	(1)	(120)
Changes in operating assets and liabilities					
(Increase) decrease in --					
Accounts receivable.....	262	203	(1,502)	(479)	393
Inventories.....	(18)	(26)	(38)	32	(24)
Costs and estimated earnings in excess of billings on uncompleted contracts.....	42	26	(292)	(77)	(181)
Prepaid expenses and other assets.....	46	(13)	3	(92)	(143)
Increase (decrease) in --.....					
Accounts payable and accrued expenses.....	(156)	143	1,584	469	(1,242)
Billings in excess of costs on uncompleted contracts.....	33	(171)	45	204	446
Net cash provided by (used in) operating activities.....	525	291	62	33	(208)
CASH FLOWS FROM INVESTING ACTIVITIES:					
Additions to cash surrender value of insurance.....	(38)	(45)	(19)	15	(52)
Purchases to property and equipment, net.....	(74)	(380)	(386)	(163)	(67)
Net cash used in investing activities.....	(112)	(425)	(405)	(148)	(119)
CASH FLOWS FROM FINANCING ACTIVITIES:					
Payments on note receivable from shareholder.....	--	(2)	(10)	(25)	--
Proceeds received on note from shareholder.....	--	12	--	--	--
Payments on note payable to shareholder.....	(181)	--	--	--	--
Net cash provided by (used in) financing activities.....	(181)	10	(10)	(25)	--
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	232	(124)	(353)	(140)	(327)
CASH AND CASH EQUIVALENTS, beginning of period.....	572	804	680	730	327
CASH AND CASH EQUIVALENTS, end of period.....	\$ 804	\$ 680	\$ 327	\$ 590	\$ --
	=====	=====	=====	=====	=====
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:					
Cash paid for --					
Interest.....	\$ 14	\$ --	\$ 5	\$ --	\$ 3
Income taxes.....	--	16	14	--	--

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

1. BUSINESS AND ORGANIZATION:

S.M. Lawrence Inc., a Tennessee corporation (the "Company") focuses on providing "design and build" installation services and process piping primarily for industrial facilities and maintenance, repair and replacement of commercial and industrial HVAC systems. S.M. Lawrence primarily operates in Tennessee and the immediately surrounding states.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems") pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

BASIS OF PRESENTATION

The financial statements include the accounts and results of operations of S.M. Lawrence Inc. and Lawrence Services, Inc. which are under common control and management of two individuals. All significant intercompany transactions and balances have been eliminated in combination.

INTERIM FINANCIAL INFORMATION

The interim combined financial statements as of January 31, 1997, and for the three months ended January 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the combined interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories 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 (FIFO) method.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost, and depreciation is computed using an accelerated method of depreciation. Leasehold improvements are capitalized and amortized over the lesser of the 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. 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 statements of operations.

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-

S.M. LAWRENCE INC. AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

completion method measured by the percentage of costs incurred to total estimated costs for each contract. 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 income and their effects are recognized in the period in which the revisions are determined.

The balances billed but not paid by customers pursuant to retainage provisions in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

#### WARRANTY COSTS

The Company warrants labor and parts for one year after installation of new air conditioning and heating systems. A reserve for warranty costs is recorded upon completion of installation or service.

#### INCOME TAXES

The Company follows the liability method of accounting for income taxes in accordance with Statement of Financial Accounting Standards (SFAS) No. 109. Under this method, deferred income taxes are recorded based upon the differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the underlying assets or liabilities are recovered or settled.

#### 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 and 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.

#### NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment, and intangible or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

S.M. LAWRENCE INC. AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	OCTOBER 31,	
		1995	1996
Transportation equipment.....	5	\$ 774	\$ 907
Machinery and equipment.....	7	648	677
Furniture and fixtures.....	5	145	210
Leasehold improvements.....	32	122	231
Construction in process.....		81	--
		-----	-----
		1,770	2,025
Less -- Accumulated depreciation and amortization.....		(1,311)	(1,381)
		-----	-----
Property and equipment, net.....		\$ 459	\$ 644
		=====	=====

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

Accounts payable and accrued expenses consist of the following (in thousands):

	OCTOBER 31,	
	1995	1996
Accounts payable, trade.....	\$ 620	\$ 1,560
Accrued compensation and benefits....	466	1,091
Other accrued expenses.....	67	86
	-----	-----
	\$ 1,153	\$ 2,737
	=====	=====

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

	OCTOBER 31,	
	1995	1996
Costs incurred on contracts in progress.....	\$ 13,475	\$ 15,503
Estimated earnings, net of losses....	4,193	5,641
	-----	-----
	17,668	21,144
Less -- Billings to date.....	17,901	21,130
	-----	-----
	\$ (233)	\$ 14
	=====	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 66	\$ 358
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(299)	(344)
	-----	-----
	\$ (233)	\$ 14
	=====	=====

5. LINE OF CREDIT:

The Company had an unsecured bank line of credit at October 31, 1995 and 1996, with an outstanding balance of \$0 for all years. The available balance was \$800,000 for 1995 and \$850,000 for 1996. The line of credit is secured by guarantees and is payable upon demand. Interest is payable on the line of credit at prime plus 1 percent.

S.M. LAWRENCE INC. AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

6. LEASES:

The Company leases facilities from a company which is owned by one of the shareholders. The lease is for a one-year period and is renewed annually. For each year ended October 31, 1994, 1995 and 1996, the rent expense under this related-party lease was \$110,400.

7. INCOME TAXES:

Federal and state income taxes are as follows (in thousands):

	OCTOBER 31,		
	1994	1995	1996
Federal --			
Current.....	\$ 25	\$ 24	\$ 54
Deferred.....	17	1	(3)
State --			
Current.....	5	4	10
Deferred.....	3	1	(1)
	-----	-----	-----
	\$ 50	\$ 30	\$ 60
	===	===	===

Actual income tax expense differs from income tax expense computed by applying the U.S. federal statutory corporate tax rate of 34 percent to income before income taxes for 1994 and 1995 and 35 percent for 1996 as follows (in thousands):

	OCTOBER 31,		
	1994	1995	1996
Provision at the statutory rate.....	\$ 35	\$ 13	\$ 39
Increase resulting from --			
State income tax, net of benefits for federal deduction.....	5	3	6
Other.....	10	14	15
	-----	-----	-----
	\$ 50	\$ 30	\$ 60
	===	===	===

Deferred income tax provisions result from temporary differences in the recognition of income and expenses for financial reporting purposes and for tax purposes. The tax effects of these temporary differences representing deferred tax assets and liabilities result principally from the following (in thousands):

	OCTOBER 31,	
	1995	1996
Accruals and reserves not deductible until paid.....	\$ (1)	\$ 2
Net deferred income tax assets (liabilities).....	\$ (1)	\$ 2
	=====	=====

S.M. LAWRENCE INC. AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

The net deferred tax assets and liabilities are comprised of the following (in thousands):

	OCTOBER 31,	
	1995	1996
Deferred tax assets --		
Current.....	\$ --	\$ 2
Total.....	--	2
Deferred tax liabilities --		
Current.....	(1)	--
Total.....	(1)	--
Net deferred income tax assets (liabilities).....	\$ (1)	\$ 2
	=====	=====

8. RELATED-PARTY TRANSACTIONS:

The Company loans one of the shareholders money annually. In 1994, the shareholder signed a promissory note for \$44,695 to be paid on demand, accruing interest at eight percent. The entire balance remained outstanding at year-end 1994. The entire note was repaid during fiscal year 1995. In fiscal year 1995, the shareholder signed a promissory note for \$50,435 to be paid on demand, accruing interest at eight percent. The entire amount remained outstanding at year-end 1995. The entire note was repaid during fiscal year 1996. In 1996, the shareholder signed a promissory note for \$75,435 to be paid on demand, accruing interest at eight percent. The entire balance remained outstanding at year-end 1996.

The Company entered into a non-compete agreement with a former major shareholder on November 1, 1991 for \$542,562. Under this agreement, the former shareholder agreed not to compete with the Company for a period of 36 months beginning with November 1, 1991. The principal to be paid was recorded as an asset and was fully amortized over 36 months. The last payment of \$180,854 was made during fiscal 1994.

In September 1995, the Company entered into an agreement to purchase equipment from a related party. The terms of the agreement included a \$2,776 cash down payment and a note payable due in one year for \$11,852. Payments on the note were \$1,975 and \$9,877 during 1995 and 1996, respectively.

9. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal actions will have a material adverse effect on the Company's financial position or results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

The Company has adopted a partially self-funded medical plan. Under this plan, the Company pays up to \$20,000 per year per employee. The Company's insurance copay pays the remaining amount. For the years ended December 31, 1994, 1995, and 1996 the Company contributed \$102,647, \$82,866 and \$143,788, respectively. For claims incurred but not yet reported the Company accrued \$25,000 for the years ended December 31, 1995 and 1996.

10. EMPLOYEE BENEFIT PLANS:

The Company has adopted a 401(k) retirement plan which provides for 100 percent matching contribution by the Company, up to a maximum liability of 5 percent of each participating employee's annual compensation. The Company has the right to make additional discretionary contributions. Total contributions by the Company under this plan to provide contributions and pay expenses were \$57,434, \$141,105 and \$368,377 during 1994, 1995, and 1996, respectively. Amounts due to this plan were approximately \$117,508 and \$397,000 for the years ended December 31, 1995 and 1996, respectively.

11. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, notes receivable, investments, notes payable and a line of credit. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

12. SALES TO SIGNIFICANT CUSTOMER:

During 1996, one customer accounted for approximately 19 percent of the Company's sales.

13. SUBSEQUENT EVENT:

In December 1996, the Company entered into an agreement to purchase a one-third interest in an investment. The investment is a partnership and will own an aircraft, available for use by any of the partners. The Company's cost for this investment was \$100,000. In connection with the agreement, the Company signed a note payable to the partnership on December 31, 1996 for \$100,000 with interest of 7 percent. This note was fully paid in 1997.

14. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

Concurrently with the merger, the Company will enter into agreements with the shareholders to lease land and buildings used in the Company's operations for a negotiated amount and term.



REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Accurate Air Systems, Inc.:

We have audited the accompanying balance sheets of Accurate Air Systems, Inc. as of June 30, 1995, December 31, 1995 and 1996, and the related statements of operations, shareholder's equity and cash flows for each of the years ended June 30, 1994 and 1995, for the six months ended December 31, 1995, and for the year ended December 31, 1996. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Accurate Air Systems, Inc., as of June 30, 1995, December 31, 1995 and 1996, and the results of their operations and their cash flows for the years ended June 30, 1994 and 1995, for the six months ended December 31, 1995, and for the year ended December 31, 1996 in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

ACCURATE AIR SYSTEMS, INC.  
BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	JUNE 30, 1995	DECEMBER 31, 1995	DECEMBER 31, 1996	MARCH 31, 1997
	-----	-----	-----	-----
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents.....	\$ 50	\$ 33	\$ 79	\$ 104
Accounts receivable --				
Trade, net of allowance of \$70, \$70, \$33 and \$28, respectively.....	1,385	1,671	1,778	2,035
Retainage.....	550	321	725	267
Other receivables.....	8	16	18	85
Inventories.....	122	129	104	141
Costs and estimated earnings in excess of billings on uncompleted contracts.....	275	212	231	228
Prepaid expenses and other current assets.....	181	81	--	--
	-----	-----	-----	-----
Total current assets.....	2,571	2,463	2,935	2,860
PROPERTY AND EQUIPMENT, net.....	804	1,014	925	932
DEFERRED TAX ASSET.....	14	--	--	--
	-----	-----	-----	-----
Total assets.....	<u>\$3,389</u>	<u>\$3,477</u>	<u>\$3,860</u>	<u>\$3,792</u>
LIABILITIES AND SHAREHOLDER'S EQUITY				
CURRENT LIABILITIES:				
Current maturities of long-term debt.....	\$ 88	\$ 109	\$ 42	\$ 16
Accounts payable and accrued expenses.....	1,707	1,355	1,236	1,197
Line of credit.....	374	600	500	700
Note payable -- shareholder.....	--	--	630	630
Billings in excess of costs and estimated earnings on uncompleted contracts.....	229	206	312	97
	-----	-----	-----	-----
Total current liabilities.....	2,398	2,270	2,720	2,640
LONG-TERM DEBT, net of current maturities.....	56	175	133	149
COMMITMENTS AND CONTINGENCIES				
SHAREHOLDER'S EQUITY:				
Common stock \$1 par, 250,000 shares authorized, 1,000 shares issued and outstanding.....	1	1	1	1
Retained earnings.....	934	1,031	1,006	1,002
	-----	-----	-----	-----
Total shareholder's equity.....	935	1,032	1,007	1,003
	-----	-----	-----	-----
Total liabilities and shareholder's equity.....	<u>\$3,389</u>	<u>\$3,477</u>	<u>\$3,860</u>	<u>\$3,792</u>

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

ACCURATE AIR SYSTEMS, INC.  
STATEMENTS OF OPERATIONS  
(IN THOUSANDS)

	YEARS ENDED JUNE 30,		SIX MONTHS ENDED DECEMBER 31,	YEAR ENDED DECEMBER 31,	THREE MONTHS ENDED MARCH 31,	
	1994	1995	1995	1996	1996	1997
	(UNAUDITED)					
REVENUES.....	\$9,763	\$ 12,171	\$5,585	\$ 16,806	\$ 3,161	\$ 2,642
COSTS OF SERVICES.....	7,204	8,998	4,312	13,270	2,450	2,095
Gross profit.....	2,559	3,173	1,273	3,536	711	547
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	2,681	2,960	1,131	3,037	684	526
Income (Loss) from operations.....	(122)	213	142	499	27	21
OTHER INCOME/(EXPENSE):						
Interest expense.....	(21)	(48)	(41)	(80)	(20)	(32)
Other.....	(9)	(9)	(4)	14	23	7
INCOME (LOSS) BEFORE INCOME TAXES....	(152)	156	97	433	30	(4)
PROVISION (BENEFIT) FOR INCOME TAXES.....	(54)	60	--	--	--	--
NET INCOME (LOSS).....	\$ (98)	\$ 96	\$ 97	\$ 433	\$ 30	\$ (4)
	=====	=====	=====	=====	=====	=====

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

ACCURATE AIR SYSTEMS, INC.  
 STATEMENTS OF SHAREHOLDER'S EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		RETAINED EARNINGS	TOTAL SHAREHOLDER'S EQUITY
	SHARES	AMOUNT		
BALANCE, June 30, 1993.....	1,000	\$ 1	\$ 941	\$ 942
Net loss.....	--	--	(98)	(98)
BALANCE, June 30, 1994.....	1,000	1	843	844
Distribution to shareholder....	--	--	(5)	(5)
Net income.....	--	--	96	96
BALANCE, June 30, 1995.....	1,000	1	934	935
Net income.....	--	--	97	97
BALANCE, December 31, 1995.....	1,000	1	1,031	1,032
Distributions to shareholder....	--	--	(458)	(458)
Net income.....	--	--	433	433
BALANCE, December 31, 1996.....	1,000	\$ 1	\$1,006	\$ 1,007
Net loss (unaudited).....	--	--	(4)	(4)
BALANCE, March 31, 1997 (unaudited).....	<u>1,000</u>	<u>\$ 1</u>	<u>\$1,002</u>	<u>\$ 1,003</u>

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

ACCURATE AIR SYSTEMS, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEAR ENDED JUNE 30,		SIX MONTHS ENDED	YEAR ENDED	THREE MONTHS ENDED	
	----- 1994	1995	DECEMBER 31, 1995	DECEMBER 31, 1996	----- 1996	MARCH 31, 1997 -----
	(UNAUDITED)					
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>						
Net income (loss).....	\$ (98)	\$ 96	\$ 97	\$ 433	\$ 30	\$ (4)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities --						
Depreciation and amortization...	128	124	85	186	31	36
Deferred income tax provision...	(150)	(70)	81	--	--	--
Changes in operating assets and liabilities --						
(Increase) decrease in --						
Accounts receivable.....	127	(395)	(66)	(513)	(458)	134
Costs and estimated earnings in excess of billings on uncompleted contracts.....	(90)	(58)	63	(19)	(60)	3
Prepaid expenses and other current assets.....	(1)	(44)	31	81	78	--
Inventories.....	(22)	(16)	(7)	25	(9)	(37)
Increase (decrease) in --						
Accounts payable and accrued expenses.....	365	419	(350)	(119)	176	(39)
Billings in excess of costs and estimated earnings on uncompleted contracts.....	64	119	(22)	106	71	(215)
Net cash provided by (used in) operating activities.....	----- 323	----- 175	----- (88)	----- 180	----- (141)	----- (122)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>						
Sales (purchase) of property and equipment.....	(100)	(347)	(295)	(97)	16	(43)
Net cash provided by (used in) investing activities.....	(100)	(347)	(295)	(97)	16	(43)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>						
Borrowings of long-term debt.....	--	183	192	--	--	--
Payments of long-term debt.....	(186)	(39)	(52)	(109)	(29)	(10)
Borrowings of short-term debt.....	--	--	--	630	--	--
Borrowings on line of credit.....	50	--	226	--	160	200
Payments on line of credit.....	--	(76)	--	(100)	--	--
Distributions to shareholder.....	--	(5)	--	(458)	--	--
Net cash provided by (used in) financing activities.....	(136)	63	366	(37)	131	190
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	87	(109)	(17)	46	6	25
CASH AND CASH EQUIVALENTS, beginning of period.....	72	159	50	33	33	79
CASH AND CASH EQUIVALENTS, end of period.....	=====	=====	=====	=====	=====	=====
	\$ 159	\$ 50	\$ 33	\$ 79	\$ 39	\$ 104
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>						
Cash paid for --						
Interest.....	\$ 21	\$ 48	\$ 41	\$ 79	\$ 8	\$ 33
Income taxes.....	53	34	--	--	--	--

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

ACCURATE AIR SYSTEMS, INC.  
NOTES TO FINANCIAL STATEMENTS

1. BUSINESS AND ORGANIZATION:

Accurate Air Systems, Inc., a Texas corporation, (the "Company") focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial facilities. Accurate primarily operates in Texas and Oklahoma.

The Company and its shareholder intend to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems") pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

CHANGE IN FISCAL YEAR END

Effective July 1, 1995, the Company changed its fiscal year end from June 30 to December 31. The statements of operations, shareholder's equity and cash flows for the six months ended December 31, 1995 are presented in the accompanying financial statements. The results of operations for the six month period are not necessarily indicative of the results for a full year period.

INTERIM FINANCIAL INFORMATION

The interim financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories held for use in the ordinary course of business and are stated at the lower of cost or market using the weighted-average 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 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. 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.

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. 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 income and their effects are recognized in the period in which the revisions are determined.

The balances billed but not paid by customers pursuant to retainage provisions in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

#### WARRANTY COSTS

The Company warrants labor for the first year after installation on new air conditioning and heating systems. The Company generally warrants labor for 90 days after the servicing of existing air conditioning and heating systems. A reserve for warranty costs is recorded upon completion of installation or service.

#### INCOME TAXES

Effective July 1, 1995, the Company elected S Corporation status as defined by the Internal Revenue Code whereby the Company is not subject to taxation for federal purposes. Under S Corporation status, each shareholder reports his share of the Company's taxable earnings or losses in his personal federal and state tax returns. The balance in the deferred tax liability account at July 1, 1995 was credited to income during the six month period ended December 31, 1995.

Prior to July 1, 1995, the Company followed the liability method of accounting for income taxes in accordance with Statement of Financial Accounting Standards (SFAS) No. 109. Under this method, deferred income taxes were recorded based upon differences between the financial reporting and tax bases of assets and liabilities and were measured using the enacted tax rates and laws that would have been in effect when the underlying assets or liabilities were recovered or settled.

#### 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 and 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.

#### NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment, and intangible or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

ACCURATE AIR SYSTEMS, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	JUNE 30, 1995	DECEMBER 31,	
			1995	1996
Land.....	--	\$ 200	\$ 200	\$ 200
Buildings.....	31.5	205	213	213
Transportation equipment.....	5	414	336	241
Machinery and equipment.....	5 - 7	262	477	510
Leasehold improvements.....	15 - 18	57	60	61
Furniture and fixtures.....	5 - 7	74	122	133
		-----	-----	-----
Less -- Accumulated depreciation and amortization.....		(408)	(394)	(433)
		-----	-----	-----
Property and equipment, net.....		\$ 804	\$ 1,014	\$ 925
		=====	=====	=====

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS (IN THOUSANDS):

Activity in the Company's allowance for doubtful accounts consist of the following:

	JUNE 30, 1995	DECEMBER 31,	
		1995	1996
Balance at beginning of year.....	\$ 57	\$ 70	\$ 70
Additions to costs and expenses.....	19	--	--
Deductions for uncollectible receivables written off and recoveries.....	(6)	--	(37)
	-----	-----	-----
	\$ 70	\$ 70	\$ 33
	===	===	=====

Accounts payable and accrued expenses consist of the following:

	JUNE 30, 1995	DECEMBER 31,	
		1995	1996
Accounts payable, trade.....	\$ 537	\$ 871	\$ 685
Accrued compensation and benefits....	509	179	288
Other accrued expenses.....	575	243	190
Warranty reserve.....	86	62	73
	-----	-----	-----
	\$1,707	\$ 1,355	\$ 1,236
	=====	=====	=====

Installation contracts in progress are as follows:

	JUNE 30, 1995	DECEMBER 31,	
		1995	1996
Costs incurred on contracts in progress.....	\$4,113	\$ 2,468	\$ 5,514
Estimated earnings, net of losses....	1,428	726	1,760
Less -- Billings to date.....	5,495	3,188	7,355
	-----	-----	-----
	\$ 46	\$ 6	\$ (81)
	=====	=====	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 275	\$ 212	\$ 231
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(229)	(206)	(312)
	-----	-----	-----
	\$ 46	\$ 6	\$ (81)
	=====	=====	=====



5. SHORT-TERM DEBT:

On October 15, 1996, the Company executed a renewal and extension of its revolving line of credit with its bank. The new agreement provides for maximum borrowings of up to \$900,000 with interest payable monthly on the amount outstanding at the rate of prime plus one percent, not to exceed 18 percent. The agreement provides that the Company may borrow up to 70 percent of its accounts receivable that are less than sixty days past due. The revolving line of credit is secured by accounts receivable and the personal guaranty of the sole shareholder, and requires the Company to maintain certain minimum tangible net worth and cash flow ratios. Balances outstanding relating to the line are approximately \$374,000, \$600,000, and \$500,000 as of June 30, 1995, and December 31, 1995 and 1996, respectively. The Company was in compliance with all covenants at each applicable year end.

On December 27, 1996, the Company borrowed \$630,000 from the Company's shareholder. Interest is payable monthly at a rate of 9 percent on the outstanding balance. The note matures on June 30, 1997. The entire balance was outstanding as of December 31, 1996.

6. LONG-TERM DEBT:

	JUNE 30, 1995	DECEMBER 31, ----- 1995      1996 -----	
(IN THOUSANDS)			
Note payable, secured by real estate, payable in twenty-four installments of \$2,540 including interest at 9.50% per annum with the final payment due January 28, 1997.....	\$ 44	\$ 31	\$ --
Notes payable, secured by transportation and operating equipment, monthly installments of various amounts, including interest at rates ranging from 9.00% to 9.75% per annum until 1997.....	100	69	21
Note payable, secured by operating equipment, payable in thirty-five installments of \$3,177 including interest at a rate of prime plus one percent. A final payment of \$128,696 due on August 1, 1998.....	--	184	154
	-----	-----	-----
	144	284	175
Less -- Current maturities.....	88	109	42
	-----	-----	-----
	\$ 56	\$ 175	\$ 133
	=====	=====	=====

The aggregate maturities of long-term debt as of December 31, 1996, are as follows (in thousands):

1997.....	\$ 42
1998.....	133
	-----
	\$ 175
	=====

7. LEASES:

The Company leases facilities from a company which is partially owned by the shareholder. The lease expires in April 1999. The rent paid under this related-party lease was approximately \$15,000, \$60,000, \$30,000 and \$60,000 for the years ended June 30, 1994 and 1995, the six months ended December 31, 1995 and the year ended December 31, 1996 respectively. The Company also leased a facility from a third party, which expired on December 31, 1996. The rent paid under this lease was approximately \$12,000, \$12,000, \$6,000 and \$13,200 for the years ended June 30, 1994 and 1995, the six months ended December 31, 1995, and the year ended December 31, 1996, respectively. The leases require the Company to pay taxes, maintenance, insurance and certain other operating costs of the leased properties.

ACCURATE AIR SYSTEMS, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The Company also leases vehicles for operations which expire in 1998. The payments under these vehicle leases were approximately \$--, \$1,400, \$26,000 and \$94,000 for the years ended June 30, 1994 and 1995, the six months ended December 31, 1995 and the year ended December 31, 1996, respectively.

Future minimum lease payments for operating leases are as follows (in thousands):

	DECEMBER 31, 1996
Year Ended	-----
1997.....	\$ 197
1998.....	60
1999.....	15
	-----
	\$ 272
	=====

8. INCOME TAXES (IN THOUSANDS):

Federal and state income taxes are as follows:

	YEAR ENDED JUNE 30,	
	1994	1995
Federal --		
Current.....	\$ (37)	\$ 111
Deferred.....	(9)	(60)
State --		
Current.....	(7)	20
Deferred.....	(1)	(11)
	-----	-----
	\$ (54)	\$ 60
	=====	=====

Actual income tax expense differs from income tax expense computed by applying the U.S. federal statutory corporate tax rate of 34 percent to income before income taxes as follows:

	YEAR ENDED JUNE 30,	
	1994	1995
Provision at the statutory rate.....	\$ (52)	\$ 53
Increase (decrease) resulting from --		
State income tax, net of benefit for federal deduction.....	(2)	6
Other.....	--	1
	-----	-----
	\$ (54)	\$ 60
	=====	=====

ACCURATE AIR SYSTEMS, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

Deferred income tax provisions result from temporary differences in the recognition of income and expenses for financial reporting purposes and for tax purposes. The tax effects of these temporary differences representing deferred tax assets and liabilities result principally from the following:

	JUNE 30, 1995
Depreciation and amortization.....	\$ 14
Accruals and reserves not deductible until paid.....	121
State taxes.....	(4)
Cash to accrual adjustments.....	(50)
	-----
Net deferred income tax assets.....	\$ 81
	=====

The net deferred tax assets and liabilities are comprised of the following:

	JUNE 30, 1995
Deferred tax assets --	
Current.....	\$ 114
Long-term.....	14
	-----
Total.....	128
	-----
Deferred tax liabilities --	
Current.....	47
Long-term.....	--
	-----
Total.....	47
	-----
Net deferred income tax assets.....	\$ 81
	=====

9. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal actions will have a material adverse effect on the Company's financial position or results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

Effective January 1, 1995, the Company became self-insured for medical claims up to \$30,000 per year per covered individual per event. Claims in excess of these amounts are covered by a stop-loss policy. The Company has recorded reserves for self-insured claims based on estimated claims incurred through June 30, 1995, six months ended December 31, 1995 and the year ended December 31, 1996.

10. EMPLOYEE BENEFIT PLANS:

The Company has adopted a 401(k) plan which provides for 10 percent matching contributions by the Company, up to a maximum of 6 percent of each participating employee's annual compensation. The Company has the right to make additional discretionary contributions. Employees become 100 percent vested in the employer's contribution after 7 years of service. Total contributions by the Company under

ACCURATE AIR SYSTEMS, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

this plan to provide contributions and pay expenses were approximately \$118,000, \$131,000, \$12,000 and \$199,000 during the years ended June 30, 1994 and 1995, the six months ended December 31, 1995 and the year ended December 31, 1996, respectively. Amounts due to this plan were approximately \$109,000, \$-- and \$173,000 for the year ended June 30, 1995, the six months ended December 31, 1995 and the year ended December 31, 1996, respectively.

The Company also adopted a discretionary profit-sharing plan under which the Company may contribute up to 25 percent of a participant's compensation, up to a maximum contribution of \$30,000. Employees become 100 percent vested in the employer's contributions after 7 years of service. The Company's contributions and administrative expenses were approximately \$5,000, \$8,000, \$-- and \$--, for the years ended June 30, 1994 and 1995, and six months ended December 31, 1995 and the year ended December 31, 1996, respectively.

11. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, notes payable, a line of credit, and debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

12. CAPITAL STOCK:

In addition to the 250,000 authorized shares of \$1 par value voting common stock, the Company has the following classes of authorized capital stock. None of these three classes have been issued.

	SHARES AUTHORIZED	PAR VALUE
	-----	-----
Nonvoting Common.....	250,000	\$ 1
Voting Preferred.....	250,000	\$ 1
Nonvoting Preferred.....	250,000	\$ 1

13. SALES TO SIGNIFICANT CUSTOMERS:

For the years ended June 30, 1994 and 1995, the six months ended December 31, 1995, and year ended December 31, 1996 one customer accounted for approximately 12, 25, 13, and 0 percent, respectively, of the Company's revenue.

14. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholder entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

In connection with the merger, the Company will dividend certain assets to the shareholder, consisting of land, buildings, and automobiles, with a total carrying value of approximately \$370,000 as of March 31, 1997. Had this adjustment been recorded at March 31, 1997, the effect on the accompanying unaudited balance sheet would be a decrease in shareholder's equity of \$370,000.

Concurrently with the merger, the Company will enter into new agreements with a company partially owned by the shareholder to lease land and buildings owned by such party used in the Company's operations for a negotiated amount and term.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Eastern Heating and Cooling, Inc.:

We have audited the accompanying balance sheet of Eastern Heating and Cooling, Inc., as of December 31, 1996, and the related statements of operations, shareholder's equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Eastern Heating and Cooling, Inc., as of December 31, 1996, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

EASTERN HEATING AND COOLING, INC.  
BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	DECEMBER 31, 1996	MARCH 31, 1997
	-----	-----
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents.....	\$ 83	\$ 131
Accounts receivable --		
Trade, net of allowance of		
\$25 and \$25,		
respectively.....	1,214	813
Retainage.....	43	83
Other receivables.....	13	27
Inventories.....	100	97
Costs and estimated earnings in		
excess of billings on		
uncompleted contracts.....	66	48
	-----	-----
Total current		
assets.....	1,519	1,199
PROPERTY AND EQUIPMENT, net.....	604	607
OTHER NONCURRENT ASSETS.....	144	174
	-----	-----
Total assets.....	\$2,267	\$1,980
	=====	=====
LIABILITIES AND SHAREHOLDER'S EQUITY		
CURRENT LIABILITIES:		
Current maturities of long-term		
debt.....	\$ 302	\$ 302
Accounts payable and accrued		
expenses.....	826	759
Line of credit.....	140	305
Billings in excess of costs and		
estimated earnings on		
uncompleted contracts.....	102	53
	-----	-----
Total current		
liabilities.....	1,370	1,419
LONG-TERM DEBT, net of current		
maturities.....	431	353
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDER'S EQUITY:		
Common stock, no par value, 200		
shares authorized, 100 shares		
issued and outstanding.....	50	50
Retained earnings.....	416	158
	-----	-----
Total shareholder's		
equity.....	466	208
	-----	-----
Total liabilities and		
shareholder's		
equity.....	\$2,267	\$1,980
	=====	=====

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

EASTERN HEATING AND COOLING, INC.  
 STATEMENTS OF OPERATIONS  
 (IN THOUSANDS)

	YEAR ENDED DECEMBER 31, 1996	THREE MONTHS ENDED MARCH 31,	
		1996	1997
		(UNAUDITED)	
REVENUES.....	\$ 7,944	\$ 1,525	\$ 1,284
COST OF SERVICES.....	5,276	973	805
Gross profit.....	2,668	552	479
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	2,237	532	582
Income (loss) from operations...	431	20	(103)
OTHER INCOME (EXPENSE):			
Interest expense.....	(87)	(19)	(20)
Other.....	40	--	--
NET INCOME (LOSS).....	\$ 384	\$ 1	\$ (123)

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

EASTERN HEATING AND COOLING, INC.  
 STATEMENTS OF SHAREHOLDER'S EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		RETAINED EARNINGS	TOTAL SHAREHOLDER'S EQUITY
	SHARES	AMOUNT		
BALANCE, December 31, 1995.....	100	\$ 50	\$ 356	\$ 406
Distributions to shareholder....	--	--	(324)	(324)
Net income.....	--	--	384	384
BALANCE, December 31, 1996.....	100	\$ 50	\$ 416	\$ 466
Distributions to shareholder (unaudited).....	--	--	(135)	(135)
Net loss (unaudited).....	--	--	(123)	(123)
BALANCE, March 31, 1997 (unaudited).....	100	\$ 50	\$ 158	\$ 208
	=====	=====	=====	=====

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



EASTERN HEATING AND COOLING, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

CASH FLOWS FROM OPERATING ACTIVITIES:	YEAR ENDED	THREE MONTHS ENDED	
	DECEMBER 31, 1996	MARCH 31,	
	-----	-----	-----
		1996	1997
		-----	
		(UNAUDITED)	
Net income (loss).....	\$ 384	\$ 1	\$ (123)
Adjustments to reconcile net income to net cash provided by operating activities --			
Depreciation and amortization....	144	31	40
Gain on sale of property and equipment.....	(31)	--	--
Changes in operating assets and liabilities --			
(Increase) decrease in --			
Accounts receivable.....	(434)	(119)	347
Inventories.....	4	(1)	2
Costs and estimated earnings in excess of billings on uncompleted contracts....	123	(60)	19
Other noncurrent assets....	80	3	(32)
Increase (decrease) in --			
Accounts payable and accrued expenses.....	246	114	(67)
Billings in excess of costs and estimated earnings on uncompleted contracts....	10	36	(48)
	-----	-----	-----
Net cash provided by operating activities.....	526	5	138
	-----	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sale of property and equipment.....	38	--	--
Additions of property and equipment.....	(262)	(3)	(42)
	-----	-----	-----
Net cash used in investing activities.....	(224)	(3)	(42)
	-----	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:			
Borrowings of long-term debt.....	208	--	--
Payments of long-term debt.....	(280)	(69)	(78)
Borrowings on line of credit.....	140	181	165
Distributions to shareholder.....	(325)	(80)	(135)
	-----	-----	-----
Net cash provided by (used in) financing activities.....	(257)	32	(48)
	-----	-----	-----
NET INCREASE IN CASH AND CASH EQUIVALENTS.....	45	34	48
CASH AND CASH EQUIVALENTS, beginning of period.....	38	38	83
	-----	-----	-----
CASH AND CASH EQUIVALENTS, end of period.....	\$ 83	\$ 72	\$ 131
	=====	=====	=====
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid for --			
Interest.....	\$ 52	\$ 19	\$ 20

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

1. BUSINESS AND ORGANIZATION:

Eastern Heating and Cooling, Inc., a New York corporation, (the "Company") focuses on providing "design and build" installation and maintenance, repair and replacement of HVAC systems for commercial and industrial facilities. Eastern also offers continuous monitoring and control systems for commercial facilities. Eastern primarily operates in the area within a 75 mile radius of Albany, New York.

The Company and its shareholder intends to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems") pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

INTERIM FINANCIAL INFORMATION

The interim financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

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 (FIFO) 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 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. 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.

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. 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 income and their effects are recognized in the period in which the revisions are determined.

EASTERN HEATING AND COOLING, INC.  
 NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The balances billed but not paid by customers pursuant to retainage provision in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

WARRANTY COSTS

The Company 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 upon completion of installation or service.

INCOME TAXES

The Company has elected S Corporation status as defined by the Internal Revenue Code, whereby the Company is not subject to taxation for federal purposes. Under S Corporation status, the shareholder reports his share of the Company's taxable earnings or losses in his personal tax returns. The Company will terminate its S Corporation status concurrently with the effective date of this Offering.

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 and 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.

NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment, and intangible or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	DECEMBER 31, 1996
	-----	-----
Transportation equipment.....	7	\$ 957
Machinery and equipment.....	10	54
Computer and telephone equipment....	3-5	6
Leasehold improvements.....	20	36
Furniture and fixtures.....	7-10	126
		-----
		1,179
Less -- Accumulated depreciation and amortization.....		(575)
		-----
Property and equipment, net.....		\$ 604
		=====

EASTERN HEATING AND COOLING, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

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

	DECEMBER 31, 1996
Balance at beginning of year.....	\$ 16
Additions to costs and expenses.....	25
Deductions for uncollectible receivables written off and recoveries.....	(16)
	\$ 25
	=====

Accounts payable and accrued expenses consist of the following (in thousands):

	DECEMBER 31, 1996
Accounts payable, trade.....	\$ 611
Accrued compensation and benefits....	120
Other accrued expenses.....	95
	\$ 826
	=====

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

	DECEMBER 31, 1996
Costs incurred on contracts in progress.....	\$ 749
Estimated earnings, net of losses....	235
	984
Less -- Billings to date.....	1,020
	\$ (36)
	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 66
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(102)
	\$ (36)
	=====

5. LONG-TERM DEBT:

Long-term debt consists of the following:

The Company has a term note payable to a financial institution with an outstanding balance of approximately \$133,000 at December 31, 1996. The term note matures in April 1999, and bears interest at prime plus 2 percent (10.25 percent at December 31, 1996) which is payable along with principal of \$4,583 monthly. The note is secured by substantially all assets of the Company and is guaranteed by the Company's shareholder.

The Company has various installment notes with several financial institutions which are secured by transportation equipment. The terms of the notes range from 48 months to 60 months with monthly payments of principal and interest of approximately \$12,300. The notes bear interest at rates ranging from 6.5 percent to 10.5 percent and mature from 1997 to 2001.

The Company has a note payable to its former owner with an outstanding balance of \$288,444 at December 31, 1996. The note payable was calculated using an implied interest rate of 9 percent. The note

EASTERN HEATING AND COOLING, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

payable is due in installments of \$159,385 on January 1, 1997 and \$168,948 on January 1, 1998, including interest.

The aggregate maturities of long-term debt as of December 31, 1996, are as follows (in thousands):

Year ending December 31 --	
1997.....	\$ 302
1998.....	296
1999.....	85
2000.....	42
2001.....	8
	-----
	\$ 733
	=====

6. LINE OF CREDIT:

The Company has a \$500,000 line of credit with a financial services company. The line of credit is due on demand and bears interest at prime plus 1 percent per annum (9.25 percent at December 31, 1996). The line of credit is secured by substantially all assets of the Company. The balance outstanding under this line of credit at December 31, 1996 was \$140,000.

7. LEASES:

The Company leases a facility from a company which is 50 percent owned by the Company's shareholder. The lease expires in December 1999. The rent paid under this related-party lease was approximately \$50,000 for the year ended December 31, 1996.

Additionally, the Company rents other facilities from non-related parties. Future minimum lease payments under non-cancellable operating leases are as follows (in thousands):

Year Ended December 31 --	
1997.....	\$ 55
1998.....	55
1999.....	50
	-----
	\$ 160
	=====

8. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal actions will have a material adverse effect on the Company's financial position or results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

9. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, investments, notes payable, a line of credit, and debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

10. SALES TO SIGNIFICANT CUSTOMER:

During 1996, one customer accounted for approximately 12 percent of the Company's sales.

11. SUBSEQUENT EVENT:

Effective January 2, 1997, an affiliate of the Company acquired the business and certain operating assets of RECC, Inc., a New York corporation. This affiliate agreed to pay \$10,000 over a period of one year.

12. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholder entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

As of March 31, 1997, the Company distributed \$135,000 from the accumulated adjustment account. In connection with the merger, the Company will make additional cash distributions of approximately \$158,000 prior to the merger which represents the Company's estimated S Corporation accumulated adjustment account. Had these transactions been recorded at March 31, 1997, the effect on the accompanying unaudited balance sheet would be an increase in liabilities of \$158,000 and a decrease in shareholder's equity of \$158,000.

Concurrently with the merger, the Company will enter into agreements with the shareholders to lease land and buildings used in the Company's operations for a negotiated amount and term.

Eastern intends to enter into a 10-year lease with 60 Loudonville Road Associates for a new building and terminate the existing lease. Eastern has agreed to install the HVAC systems in the new building at a price which the Company believes to be at a fair market value. The Company's annual rental in the new building will be at fair market value, as determined by appraisal.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Contract Service, Inc.:

We have audited the accompanying balance sheets of Contract Service, Inc., as of December 31, 1995 and 1996, and the related statements of operations, shareholders' equity and cash flows for the three years ended December 31, 1996. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Contract Service, Inc., as of December 31, 1995 and 1996, and the results of their operations and their cash flows for the three years ended December 31, 1996 in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

CONTRACT SERVICE, INC.  
BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	DECEMBER 31,		MARCH 31,
	1995	1996	1997
	(UNAUDITED)		
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents.....	\$ 116	\$ 207	\$ 103
Accounts receivable --			
Trade, net of allowance of			
\$11, \$22 and \$21,			
respectively.....	651	680	681
Retainage.....	10	26	41
Inventories.....	306	362	491
Costs and estimated earnings in			
excess of billings on uncompletedX			
contracts.....	104	110	129
Prepaid expenses and other current			
assets.....	11	4	4
	1,198	1,389	1,449
PROPERTY AND EQUIPMENT, net.....	549	642	690
OTHER NONCURRENT ASSETS.....	14	16	15
	\$ 1,761	\$ 2,047	\$ 2,154
	=====	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES:			
Current maturities of long-term			
debt.....	\$ 100	\$ 100	\$ 101
Accounts payable and accrued			
expenses.....	576	691	657
Billings in excess of costs and			
estimated earnings on uncompleted			
contracts.....	149	136	218
	825	927	976
LONG-TERM DEBT, net of current			
maturities.....	263	429	434
COMMITMENTS AND CONTINGENCIES			
SHAREHOLDERS' EQUITY:			
Common stock, \$1 par value, 20,000			
shares authorized, 8,946 shares			
issued and outstanding.....	9	9	9
Retained earnings.....	664	682	735
	673	691	744
	\$ 1,761	\$ 2,047	\$ 2,154
	=====	=====	=====

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



CONTRACT SERVICE, INC.  
STATEMENTS OF OPERATIONS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,			THREE MONTHS ENDED MARCH 31,	
	1994	1995	1996	1996	1997
	----- (UNAUDITED) -----				
REVENUES.....	\$ 6,502	\$ 6,361	\$ 7,842	\$ 1,369	\$ 1,562
COST OF SERVICES.....	4,393	4,413	5,201	926	1,045
Gross profit.....	2,109	1,948	2,641	443	517
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	1,228	1,500	1,660	368	458
Income from operations...	881	448	981	75	59
OTHER INCOME (EXPENSE):					
Interest expense.....	(5)	(9)	(29)	(9)	(15)
Other.....	29	38	51	13	9
NET INCOME.....	\$ 905	\$ 477	\$ 1,003	\$ 79	\$ 53
	=====	=====	=====	=====	=====

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

CONTRACT SERVICE, INC.  
 STATEMENTS OF SHAREHOLDERS' EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
	SHARES	AMOUNT		
BALANCE, December 31, 1993.....	8,946	\$ 9	\$ 660	\$ 669
Distributions to shareholders...	--	--	(911)	(911)
Net income.....	--	--	905	905
BALANCE, December 31, 1994.....	8,946	9	654	663
Distributions to shareholders...	--	--	(467)	(467)
Net income.....	--	--	477	477
BALANCE, December 31, 1995.....	8,946	9	664	673
Distributions to shareholders...	--	--	(985)	(985)
Net income.....	--	--	1,003	1,003
BALANCE, December 31, 1996.....	8,946	9	682	691
Net income (unaudited).....	--	--	53	53
BALANCE, March 31, 1997 (unaudited).....	8,946	\$ 9	\$ 735	\$ 744

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

CONTRACT SERVICE, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,			THREE MONTHS ENDED MARCH 31,	
	1994	1995	1996	1996	1997
	(UNAUDITED)				
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>					
Net income.....	\$ 905	\$ 477	\$ 1,003	\$ 79	\$ 53
Adjustments to reconcile net income to net cash provided by (used in) operating activities --					
Depreciation.....	97	120	138	28	33
Gain (loss) on sale of property and equipment.....	8	(5)	--	--	--
Changes in operating assets and liabilities --					
(Increase) decrease in --					
Accounts receivable.....	(219)	(96)	(45)	177	(16)
Inventories.....	20	(49)	(57)	(54)	(129)
Costs and estimated earnings in excess of billings on uncompleted contracts.....	(44)	35	(6)	8	(19)
Prepaid expenses and other current assets.....	(9)	(2)	7	2	--
Other noncurrent assets.....	(8)	5	(2)	(11)	1
Increase (decrease) in --					
Accounts payable and accrued expenses.....	(27)	(3)	115	(32)	(34)
Billings in excess of costs and estimated earnings on uncompleted contracts.....	12	17	(13)	(28)	82
Net cash provided by (used in) operating activities.....	735	499	1,140	169	(29)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>					
Proceeds from sale of property and equipment.....	--	6	--	1	--
Additions of property and equipment.....	(138)	(199)	(230)	(107)	(81)
Net cash used in investing activities.....	(138)	(193)	(230)	(106)	(81)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>					
Borrowings of long-term debt.....	102	201	166	--	6
Distributions to shareholders.....	(911)	(467)	(985)	--	--
Collections of advances to officers and shareholders.....	86	--	--	--	--
Net cash provided by (used in) financing activities.....	(723)	(266)	(819)	--	6
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....</b>	<b>(126)</b>	<b>40</b>	<b>91</b>	<b>63</b>	<b>(104)</b>
CASH AND CASH EQUIVALENTS, beginning of period.....	202	76	116	116	207
CASH AND CASH EQUIVALENTS, end of period.....	\$ 76	\$ 116	\$ 207	\$ 179	\$ 103
=====					
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>					
Cash paid for --					
Interest.....	\$ 6	\$ 30	\$ 41	\$ 9	\$ 15

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

CONTRACT SERVICE, INC.  
NOTES TO FINANCIAL STATEMENTS

1. BUSINESS AND ORGANIZATION:

Contract Service, Inc., a Utah corporation, (the "Company") focuses on providing comprehensive maintenance, repair and replacement of HVAC systems for commercial and residential facilities primarily in Utah.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems"), pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

INTERIM FINANCIAL INFORMATION

The interim financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories 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 (FIFO) 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.

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. 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.

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. 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 income and are recognized in the period in which the revisions are determined.

CONTRACT SERVICE, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The balances billed but not paid by customers pursuant to retainage provisions in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

WARRANTY COSTS

The Company warrants labor for the first year after installation of new air conditioning and heating units. The Company generally warrants labor for 30 days after the servicing of existing air conditioning and heating units. A reserve for warranty costs is recorded upon completion of installation or service.

INCOME TAXES

The Company has elected S Corporation status as defined by the Internal Revenue Code, whereby the Company is not subject to taxation for federal purposes. Under S Corporation status, the shareholders report their share of the Company's taxable earnings or losses in their personal tax returns. The Company will terminate its S Corporation status concurrently with the effective date of the Offering.

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 and 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.

NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment, and intangible or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	DECEMBER 31, 1995	DECEMBER 31, 1996
	-----	-----	-----
Transportation equipment.....	5-10	\$ 690	\$ 907
Machinery and equipment.....	5-30	126	127
Furniture and fixtures.....	5-20	178	189
		-----	-----
Less -- Accumulated depreciation.....		(445)	(581)
		-----	-----
Property and equipment, net.....		\$ 549	\$ 642
		=====	=====

CONTRACT SERVICE, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

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

	DECEMBER 31,	
	----- 1995	1996 -----
Balance at beginning of year.....	\$ 11	\$ 11
Additions to costs and expenses.....	18	26
Deductions for uncollectible receivables written off and recoveries.....	(18)	(15)
	----- \$ 11	----- \$ 22
	=====	=====

Accounts payable and accrued expenses consist of the following (in thousands):

	DECEMBER 31,	
	----- 1995	1996 -----
Accounts payable, trade.....	\$ 242	\$ 256
Accrued compensation.....	219	312
Other accrued expenses.....	115	123
	----- \$ 576	----- \$ 691
	=====	=====

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

	DECEMBER 31,	
	----- 1995	1996 -----
Costs incurred on contracts in progress.....	\$ 1,998	\$ 2,534
Estimated earnings, net of losses....	741	978
	----- 2,739	----- 3,512
Less -- Billings to date.....	2,784	3,538
	----- \$ (45)	----- \$ (26)
	=====	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 104	\$ 110
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(149)	(136)
	----- \$ (45)	----- \$ (26)
	=====	=====

5. LONG-TERM DEBT:

Long-term debt consists of ten unsecured promissory notes to the Company's shareholders of which two are demand notes. All notes, except the demand notes, are due 10 years from the date of the note. The notes bear an interest rate of 10 percent. Monthly interest payments are made to the shareholders with the principal due at the date of maturity.

CONTRACT SERVICE, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The aggregate maturities of long-term debt are as follows (in thousands):

Year ending December 31,	
1997.....	\$ 100
1998.....	--
1999.....	--
2000.....	--
2001.....	--
Thereafter.....	429
	-----
	\$ 529
	=====

6. LEASES:

The Company leases its facilities from a company owned by its two shareholders. The lease is currently on a month-to-month basis. The rent paid under this related-party lease was approximately \$66,000, \$106,000 and \$120,000 for the years ended December 31, 1994, 1995 and 1996, respectively.

Future minimum lease payments for operating leases are as follows (in thousands):

Year ending December 31,	
1997.....	\$ 120
1998.....	120
1999.....	120
2000.....	120
2001.....	120
	-----
	\$ 600
	=====

7. RELATED-PARTY TRANSACTIONS:

At December 31, 1994, 1995 and 1996, the Company held notes payable to the shareholders in the amount of \$162,000, \$363,000 and \$529,000, respectively. (See Note 5.) The notes bear interest at 10 percent. Interest paid during the years ended December 31, 1994, 1995 and 1996 related to these loans was \$6,000, \$29,000 and \$41,000, respectively.

8. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal action will have a material adverse effect on the Company's financial position or results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

9. EMPLOYEE BENEFIT PLAN:

Beginning January 1, 1994, the Company adopted a 401(k) plan. The plan allows employees to contribute a portion of their gross wages into the plan as a salary deferral and requires the Company to match 25 percent of the employee contribution up to 5 percent of employee's gross wages. The Company's matching contributions for the years ended December 31, 1995 and 1996 were \$17,000 and \$19,000 respectively.

The Company has also adopted a cafeteria plan pursuant to Section 125 of the Internal Revenue Code that covers all employees from 90 days after the commencement of employment. Under this plan, the employees may reduce their compensation to fund medical, dental and dependent care/day care benefits. The funds withheld are used to pay actual claims or medical insurance, based on the employees' elections.

10. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, and debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

11. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

In connection with the merger, the Company will make a cash distribution of approximately \$735,000 prior to the merger which represents the Company's estimated S Corporation accumulated adjustment account. Had these transactions been recorded at March 31, 1997, the effect on the accompanying unaudited balance sheet would be a decrease in assets of \$97,000 and an increase in liabilities of \$832,000 and a decrease in shareholders' equity of \$735,000.



REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Tech Heating and Air Conditioning, Inc.:

We have audited the accompanying combined balance sheets of Tech Heating and Air Conditioning, Inc., and related company as of December 31, 1995 and 1996, and the related combined statements of operations, shareholders' equity and cash flows for the years then ended. These combined financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined 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 combined financial statements referred to above present fairly, in all material respects, the combined financial position of Tech Heating and Air Conditioning, Inc., and related company as of December 31, 1995 and 1996, and the combined results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

TECH HEATING AND AIR CONDITIONING, INC.,  
AND RELATED COMPANY  
COMBINED BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	DECEMBER 31,		MARCH 31,
	1995	1996	1997
			(UNAUDITED)
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents.....	\$ 313	\$ 611	\$ 249
Accounts receivable --			
Trade, net of allowance of			
\$45, \$40 and \$45,			
respectively.....	1,244	1,723	1,216
Retainage.....	92	48	--
Other receivables.....	--	7	20
Inventories.....	67	208	193
Prepaid expenses and other current			
assets.....	7	33	20
	-----	-----	-----
Total current assets.....	1,723	2,630	1,698
PROPERTY AND EQUIPMENT, net.....	368	500	484
	-----	-----	-----
Total assets.....	\$ 2,091	\$ 3,130	\$ 2,182
	=====	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES:			
Current maturities of long-term			
debt.....	\$ --	\$ 62	\$ 69
Accounts payable and accrued			
expenses.....	1,048	757	701
Line of credit.....	88	190	900
	-----	-----	-----
Total current			
liabilities.....	1,136	1,009	1,670
LONG-TERM DEBT, net of current			
maturities.....	48	60	32
COMMITMENTS AND CONTINGENCIES			
SHAREHOLDERS' EQUITY:			
Common stock, no par value, 1,000			
shares authorized, 500 shares			
issued.....	1	1	1
Treasury stock.....	(3)	(3)	(3)
Retained earnings.....	909	2,063	482
	-----	-----	-----
Total shareholders'			
equity.....	907	2,061	480
	-----	-----	-----
Total liabilities and			
shareholders' equity.....	\$ 2,091	\$ 3,130	\$ 2,182
	=====	=====	=====

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

TECH HEATING AND AIR CONDITIONING, INC.,  
AND RELATED COMPANY  
COMBINED STATEMENTS OF OPERATIONS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,		THREE MONTHS ENDED MARCH 31,	
	1995	1996	1996	1997
			(UNAUDITED)	
REVENUES.....	\$ 6,960	\$ 7,537	\$ 1,075	\$ 1,656
COST OF SERVICES.....	4,212	3,996	639	1,034
Gross profit.....	2,748	3,541	436	622
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	1,800	1,861	390	565
Income from operations.....	948	1,680	46	57
OTHER INCOME (EXPENSE):				
Interest expense.....	(12)	(18)	(3)	(10)
Other.....	20	31	6	11
NET INCOME.....	\$ 956	\$ 1,693	\$ 49	\$ 58
	=====	=====	=====	=====

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

TECH HEATING AND AIR CONDITIONING, INC.,  
AND RELATED COMPANY  
COMBINED STATEMENTS OF SHAREHOLDERS' EQUITY  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		TREASURY STOCK	RETAINED EARNINGS	TOTAL SHAREHOLDERS' EQUITY
	SHARES	AMOUNT			
BALANCE, December 31, 1994.....	500	\$ 1	\$ (3)	\$ 575	\$ 573
Distributions to shareholders.....	--	--	--	(622)	(622)
Net income.....	--	--	--	956	956
BALANCE, December 31, 1995.....	500	1	(3)	909	907
Distributions to shareholders.....	--	--	--	(539)	(539)
Net income.....	--	--	--	1,693	1,693
BALANCE, December 31, 1996.....	500	1	(3)	2,063	2,061
Distributions to shareholders (unaudited).....	--	--	--	(1,639)	(1,639)
Net income (unaudited).....	--	--	--	58	58
BALANCE, March 31, 1997 (unaudited)....	500	\$ 1	\$ (3)	\$ 482	\$ 480

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

TECH HEATING AND AIR CONDITIONING, INC.,  
AND RELATED COMPANY  
COMBINED STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,		THREE MONTHS ENDED MARCH 31,	
	1995	1996	1996	1997
	(UNAUDITED)			
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>				
Net income.....	\$ 956	\$ 1,693	\$ 49	\$ 58
Adjustments to reconcile net income to net cash provided by (used in) operating activities --				
Depreciation.....	89	142	31	38
Changes in operating assets and liabilities --				
(Increase) decrease in --				
Accounts receivable.....	581	(442)	(48)	542
Inventories.....	(42)	(141)	1	15
Prepaid expenses and other current assets.....	7	(26)	(6)	13
Increase (decrease) in --				
Accounts payable and accrued expenses.....	(513)	(291)	(312)	(56)
Net cash provided by (used in) operating activities.....	1,078	935	(285)	610
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>				
Additions of property and equipment.....	(127)	(274)	(59)	(22)
Net cash used in investing activities.....	(127)	(274)	(59)	(22)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>				
Borrowings on line of credit.....	76	102	18	710
Borrowings on long-term debt.....	--	205	203	--
Payments on long-term debt.....	(100)	(131)	--	(21)
Distributions to shareholders.....	(622)	(539)	(15)	(1,639)
Net cash provided by (used in) financing activities.....	(646)	(363)	206	(950)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....</b>	<b>305</b>	<b>298</b>	<b>(138)</b>	<b>(362)</b>
CASH AND CASH EQUIVALENTS, beginning of period.....	8	313	313	611
CASH AND CASH EQUIVALENTS, end of period.....	\$ 313	\$ 611	\$ 175	\$ 249
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>				
Cash paid for --				
Interest.....	\$ 12	\$ 18	\$ 3	\$ 8

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

TECH HEATING AND AIR CONDITIONING, INC.  
AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS

1. BUSINESS AND ORGANIZATION:

Tech Heating and Air Conditioning, Inc., an Ohio corporation, and related company (collectively, the "Company") focuses on providing "design and build" installation and services, maintenance, repair and replacement of HVAC systems for commercial and industrial facilities. Tech also offers continuous monitoring and control services for commercial facilities. The Company's customers are primarily in the greater Cleveland, Ohio area.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems, USA, Inc. ("Comfort Systems") pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

BASIS OF PRESENTATION

The combined financial statements include the accounts and results of operations of Tech Heating and Air Conditioning, Inc., and its related company, Tech Mechanical which are under common control and management of two individuals. All significant intercompany transactions and balances have been eliminated in combination.

INTERIM FINANCIAL INFORMATION

The interim combined financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the combined interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories 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 (FIFO) 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.

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. 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 combined statements of operations.

TECH HEATING AND AIR CONDITIONING, INC.  
AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

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. 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 income and their effects are recognized in the period in which the revisions are determined.

The balances billed but not paid by customers pursuant to retainage provisions in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

WARRANTY COSTS

The Company warrants labor for the first year after installation of new air conditioning and heating systems. The Company generally warrants labor for 30 days after the servicing of existing air conditioning and heating systems. A reserve for warranty costs is recorded upon completion of installation or service.

INCOME TAXES

The Company has elected S Corporation status as defined by the Internal Revenue Code, whereby the Company is not subject to taxation for federal purposes. Under S Corporation status, the shareholders report their share of the Company's taxable earnings or losses in their personal tax returns. The Company will terminate its S Corporation status concurrently with the effective date of the Offering.

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 and 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.

NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or combined results of operations of the Company.

TECH HEATING AND AIR CONDITIONING, INC.  
AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	DECEMBER 31,	
		1995	1996
Transportation equipment.....	5	\$ 462	\$ 553
Machinery and equipment.....	7	61	159
Computer and telephone equipment.....	5	107	190
Furniture and fixtures.....	5-7	145	128
		-----	-----
Less -- Accumulated depreciation.....		(407)	(530)
		-----	-----
Property and equipment, net.....		\$ 368	\$ 500
		=====	=====

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

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

	DECEMBER 31,	
	1995	1996
Balance at beginning of year.....	\$ 25	\$ 45
Additions to costs and expenses.....	20	--
Deductions for uncollectible receivables written off and recoveries.....	--	(5)
	---	---
	\$ 45	\$ 40
	===	===

Accounts payable and accrued expenses consist of the following (in thousands):

	DECEMBER 31,	
	1995	1996
Accounts payable, trade.....	\$ 428	\$ 388
Accrued compensation and benefits.....	337	226
Other accrued expenses.....	283	143
	-----	-----
	\$ 1,048	\$ 757
	=====	=====

At December 31, 1995 and 1996 billings to customers generally equalled work performed which resulted in no costs and estimated earnings in excess of billings or billings in excess of costs and estimated earnings on uncompleted contracts.



TECH HEATING AND AIR CONDITIONING, INC.  
AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

5. LONG-TERM DEBT AND NOTES PAYABLE:

Long-term debt consists of installment notes payable for transportation equipment. The debt is secured by the related transportation equipment. The terms of the notes range from 24 months to 36 months with monthly payments of principal and interest of approximately \$8,000. The notes bear interest at rates ranging from 7.5 percent to 9.95 percent.

The aggregate maturities of long-term debt as of December 31, 1996, are as follows (in thousands):

Year ending December 31 --		
1997.....	\$	252
1998.....		55
1999.....		5
		-----
	\$	312
		=====

The Company has a \$1,500,000 line of credit with a financial services company. The line of credit expires in July 1997 and bears interest at prime plus .25 percent per annum (8.5 percent at December 31, 1996). The line of credit is secured by a lien on accounts receivable and inventory and is guaranteed by the shareholders. There was \$190,000 outstanding under this line of credit at December 31, 1996.

6. LEASES:

The Company leases facilities from a company which is partially owned by one of the shareholders. The lease expires in April of 2000. The rent paid under this related-party lease was approximately \$84,000 for the year ended December 31, 1996. The lease requires the Company to pay taxes, maintenance, insurance and certain other operating costs of the leased property. The lease contains renewal provisions.

The Company leases a vehicle for a key member of management. The lease payments under this vehicle lease totaled approximately \$6,700 for the year ended December 31, 1996.

Future minimum lease payments for operating leases are as follows (in thousands):

Year ending December 31		
1997.....	\$	100
1998.....		91
1999.....		86
2000.....		28
		-----
	\$	305
		=====

7. EMPLOYEE BENEFIT PLANS:

The Company has adopted a retirement plan which qualifies under Section 401(k) of the Internal Revenue Code. The Company has the right to make discretionary contributions. Total contributions by the Company under this plan were approximately \$18,000 and \$12,000 for 1995 and 1996, respectively.

8. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents and debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

TECH HEATING AND AIR CONDITIONING, INC.  
AND RELATED COMPANY  
NOTES TO COMBINED FINANCIAL STATEMENTS -- (CONTINUED)

9. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal actions will have a material adverse effect on the Company's financial position or combined results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

10. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

As of March 31, 1997, the Company distributed \$1,639,000 from the accumulated adjustment account and increased borrowings on the line of credit of \$900,000 with the remainder paid from cash on hand. In connection with the merger, the Company will make additional cash distributions of approximately \$482,000 prior to the merger which represents the Company's estimated S Corporation accumulated adjustment account. Had these transactions been recorded at March 31, 1997, the effect on the accompanying unaudited balance sheet would have been a decrease in assets of \$149,000, an increase in liabilities of \$333,000 and a decrease in shareholders' equity of \$482,000.

Concurrently with the merger, the Company will enter into agreements with the shareholders to lease land and buildings used in the Company's operations for a negotiated amount and term.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Seasonair, Inc.:

We have audited the accompanying balance sheet of Seasonair, Inc. as of December 31, 1996, and the related statements of operations, shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Seasonair, Inc., as of December 31, 1996, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

SEASONAIR, INC.  
BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE INFORMATION)

	DECEMBER 31, 1996	MARCH 31, 1997
	-----	-----
		(UNAUDITED)
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents.....	\$ 69	\$ 221
Accounts receivable --		
Trade, net of allowance of \$		
-- and \$9, respectively....	961	869
Retainage.....	17	44
Other receivables.....	--	40
Inventories.....	190	187
Costs on uncompleted contracts in		
excess of billings.....	75	89
Deferred tax asset.....	104	104
Prepaid expenses and other current		
assets.....	96	49
	-----	-----
Total current assets.....	1,512	1,603
PROPERTY AND EQUIPMENT, net.....	63	61
OTHER NONCURRENT ASSETS.....	83	110
	-----	-----
Total assets.....	\$1,658	\$1,774
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Line of credit.....	\$--	\$ 65
Current maturities of long-term		
debt.....	34	26
Accounts payable and accrued		
expenses.....	810	866
Billings in excess of costs and		
estimated earnings on uncompleted		
contracts.....	156	134
	-----	-----
Total current		
liabilities.....	1,000	1,091
LONG-TERM DEBT, net of current		
maturities.....	76	77
DEFERRED TAX LIABILITY.....	17	17
COMMITMENTS AND CONTINGENCIES.....		
SHAREHOLDERS' EQUITY:		
Common stock, no par value,		
2,000,000 shares authorized,		
1,244,000 shares issued and		
outstanding.....	78	78
Additional paid-in capital.....	1	1
Retained earnings.....	721	745
Treasury stock.....	(235)	(235)
	-----	-----
Total shareholders'		
equity.....	565	589
	-----	-----
Total liabilities and		
shareholders'		
equity.....	\$1,658	\$1,774
	=====	=====

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

SEASONAIR, INC.  
STATEMENTS OF OPERATIONS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31, 1996	THREE MONTHS ENDED MARCH 31,	
		1996	1997
		----- (UNAUDITED) -----	
REVENUES.....	\$ 6,737	\$ 1,128	\$ 1,831
COST OF SERVICES.....	4,006	586	1,165
	-----	-----	-----
Gross profit.....	2,731	542	666
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	2,597	604	644
	-----	-----	-----
Income (loss) from operations.....	134	(62)	22
OTHER INCOME (EXPENSE):			
Interest expense.....	(21)	(5)	(3)
Other.....	82	6	28
	-----	-----	-----
INCOME BEFORE INCOME TAXES.....	195	(61)	47
PROVISION FOR INCOME TAXES.....	69	--	23
	-----	-----	-----
NET INCOME (LOSS).....	\$ 126	\$ (61)	\$ 24
	=====	=====	=====

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

SEASONAIR, INC.  
 STATEMENTS OF SHAREHOLDERS' EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	TREASURY STOCK	TOTAL SHAREHOLDERS' EQUITY
	SHARES	AMOUNT				
BALANCE, December 31, 1995.....	1,214,724	\$ 78	\$ 1	\$ 632	\$ (269)	\$ 442
Sales of treasury stock.....	29,503	--	--	--	34	34
Distributions to shareholders...	--	--	--	(37)	--	(37)
Net income.....	--	--	--	126	--	126
	-----	-----	--	-----	-----	-----
BALANCE, December 31, 1996.....	1,244,227	78	1	721	(235)	565
Purchase of treasury stock.....	(266)	--	--	--	--	--
Net income (unaudited).....	--	--	--	24	--	24
	-----	-----	--	-----	-----	-----
BALANCE, March 31, 1997 (unaudited).....	<u>1,243,961</u>	<u>\$ 78</u>	<u>\$ 1</u>	<u>\$ 745</u>	<u>\$ (235)</u>	<u>\$ 589</u>

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

SEASONAIR, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31, 1996	THREE MONTHS ENDED MARCH 31,	
		1996	1997
		----- (UNAUDITED) -----	
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income (loss).....	\$ 126	\$ (61)	\$ 24
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities			
Depreciation.....	(54)	5	5
Gain on sale of property and equipment.....	(4)	--	--
Changes in operating assets and liabilities -- (Increase) decrease in --			
Accounts receivable.....	49	282	25
Inventories.....	(35)	(6)	3
Prepaid expenses and other current assets.....	(171)	(37)	47
Costs of uncompleted contracts in excess of billings.....	58	(65)	(14)
Other noncurrent assets....	(71)	--	(27)
Increase (decrease) in --			
Accounts payable and accrued expenses.....	(74)	(76)	56
Billings in excess of costs on uncompleted contracts.....	(23)	12	(22)
Deferred tax liability.....	30	--	--
	-----	-----	-----
Net cash provided by (used in) operating activities.....	(169)	54	97
	-----	-----	-----
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Proceeds from sale of property and equipment.....	71	(8)	(3)
	-----	-----	-----
Net cash provided by (used in) investing activities.....	71	(8)	(3)
	-----	-----	-----
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Borrowings on line of credit....	--	--	65
Payments of long-term debt.....	(105)	(82)	(7)
Distributions to shareholders...	(37)	--	--
Cash received for sale of treasury shares.....	34	(1)	--
	-----	-----	-----
Net cash provided by (used in) financing activities.....	(108)	(83)	58
	-----	-----	-----
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....</b>	<b>(206)</b>	<b>(37)</b>	<b>152</b>
<b>CASH AND CASH EQUIVALENTS, beginning of period.....</b>	<b>275</b>	<b>275</b>	<b>69</b>
	-----	-----	-----
<b>CASH AND CASH EQUIVALENTS, end of period.....</b>	<b>\$ 69</b>	<b>\$ 238</b>	<b>\$ 221</b>
	=====	=====	=====
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>			
Cash paid for --			
Interest.....	\$ 22	\$ 3	\$ 5
Income taxes.....	163	30	40

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

1. BUSINESS AND ORGANIZATION:

Seasonair, Inc., a Maryland corporation, (the "Company") focuses on providing installation services and maintenance, repair and replacement of HVAC systems for light commercial facilities. Seasonair primarily operates in Maryland, the District of Columbia and Virginia.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems, USA, Inc. ("Comfort Systems") pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

INTERIM FINANCIAL INFORMATION

The interim financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

CASH AND CASH EQUIVALENTS

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

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories held for use in the ordinary course of business and are stated at the lower of cost or market using the weighted-average method.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost, and depreciation is computed using an accelerated method over the estimated useful lives of the assets. Leasehold improvements are capitalized and amortized over the lesser of the 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. 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.

REVENUE RECOGNITION

The Company recognizes revenue when services are performed except when work is being performed under a construction contract. Revenue from construction contracts is recognized on the completed-contract method. This method is used because the typical contract is completed within a twelve-month period, and the Company's current financial position and results of operations do not vary significantly from those which would result from use of the percentage-of-completion method. A contract is considered complete when all costs except insignificant items have been incurred, and the installation is operating according to specifications or has been accepted by the customer.



SEASONAIR, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The balances billed but not paid by customers pursuant to retainage provision in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

Contract costs include all direct equipment, material, labor, and subcontract costs. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined.

WARRANTY COSTS

The Company 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 upon completion of installation or service.

INCOME TAXES

The Company follows the liability method of accounting for income taxes in accordance with Statement of Financial Accounting Standards (SFAS) No. 109 "Accounting for Income Taxes". Under this method, deferred income taxes are recorded based upon differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the underlying assets or liabilities are recovered or settled.

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 and 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.

NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment and intangible or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	DECEMBER 31, 1996
	-----	-----
Transportation equipment.....	5	\$ 17
Machinery and equipment.....	5	208
Leasehold improvements.....	39	15
Furniture and fixtures.....	7	16
		-----
		256
Less -- Accumulated depreciation and amortization.....		(193)
		-----
Property and equipment, net.....		\$ 63
		=====

SEASONAIR, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

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

	DECEMBER 31, 1996
Balance at beginning of year.....	\$ --
Additions to costs and expenses.....	5
Deductions for uncollectible receivables written off and recoveries.....	(5)
	\$ --
	===

Accounts payable and accrued expenses consist of the following (in thousands):

	DECEMBER 31, 1996
Accounts payable, trade.....	\$ 353
Accrued compensation and benefits....	321
Warranty reserve.....	37
Other.....	99
	\$ 810
	=====

5. LONG-TERM DEBT:

Long-term debt consists of two notes payable to officers and an installment note payable for transportation equipment, which is secured by the related transportation equipment. The terms of the notes range from 51 months to 80 months with monthly payments of principal and interest of approximately \$3,598. The notes bear interest at rates ranging from 10 percent to 12.7 percent.

The aggregate maturities of long-term debt as of December 31, 1996, are as follows (in thousands):

Year ending December 31 --	
1997.....	\$ 34
1998.....	37
1999.....	38
2000.....	1
	\$ 110
	=====

The Company has a \$150,000 line of credit with a financial services company. The line of credit expires August 5, 1997, and bears interest at prime plus one percent per annum. There was no balance outstanding under this line of credit at December 31, 1996.

6. LEASES:

The Company leases facilities from a partnership which is partially owned by one of the shareholders. The lease expires in October, 2006. The rent paid under this lease was approximately \$62,640 for the year ended December 31, 1996. The lease requires the Company to pay taxes, maintenance, insurance and certain other operating costs of the leased property.

The Company leases vehicles for operations. The payments under these vehicle leases were approximately \$189,000 for the year ended December 31, 1996.

SEASONAIR, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

Future minimum lease payments for operating leases are as follows (in thousands):

Year ending December 31 --	
1997.....	\$ 241
1998.....	202
1999.....	158
2000.....	105
2001.....	65
	-----
	\$ 771
	=====

7. INCOME TAXES:

Federal and state income taxes for the year ended December 31, 1996, are as follows (in thousands):

Federal --	
Current.....	\$ 50
Deferred.....	7
State --	
Current.....	11
Deferred.....	1
	---
	\$ 69
	===

Actual income tax expense for the year ended December 31, 1996, differs from income tax expense computed by applying the U.S. federal statutory corporate tax rate of 35% to income before income taxes as follows (in thousands):

Provision at the statutory rate.....	\$ 68
Increase (decrease) resulting from --	
State income tax, net of benefits for federal deduction.....	8
Other.....	(7)
	---
	\$ 69
	===

Deferred income tax provisions result from temporary differences in the recognition of income and expenses for financial reporting purposes and for tax purposes. The tax effects of these temporary differences representing deferred tax assets and liabilities as of December 31, 1996, result principally from the following (in thousands):

Depreciation and amortization.....	\$ (18)
Accruals and reserves not deductible until paid.....	110
State taxes.....	(5)
	-----
Net deferred income tax asset.....	\$ 87
	=====

SEASONAIR, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The net deferred tax assets and liabilities at December 31, 1996, are comprised of the following (in thousands):

Deferred tax assets --	
Current.....	\$ 104
Long-term.....	--
	-----
Total.....	104
	-----
Deferred tax liabilities --	
Current.....	--
Long-term.....	17
	-----
Total.....	17
	-----
Net deferred income tax asset.....	\$ 87
	=====

8. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal action will have a material adverse effect on the Company's financial position or results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

9. EMPLOYEE BENEFIT PLAN:

The Company has a 401(k) profit-sharing plan which provides for the Company to match employee contributions up to a maximum of \$260 per person per year as well as an employee stock ownership plan. Total contributions for both plans by the Company under the plan were approximately \$80,000 for purchase of treasury stock for the employee stock ownership plan, and \$5,000 for the 401(k) plan for the year ended December 31, 1996.

10. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, notes receivable, investments, notes payable, and debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

11. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the exchange of shares by the Company with the subsidiary of Comfort Systems. A total of 70,197 shares will be exchanged for cash and distributed to the employee stock ownership plan.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Western Building Services, Inc.:

We have audited the accompanying balance sheets of Western Building Services, Inc. as of December 31, 1995 and 1996, and the related statements of operations, shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Western Building Services, Inc. as of December 31, 1995 and 1996, and the results of their operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Houston, Texas  
March 7, 1997

WESTERN BUILDING SERVICES, INC.  
BALANCE SHEETS  
(IN THOUSANDS, EXCEPT FOR SHARE INFORMATION)

	DECEMBER 31,		MARCH 31,
	1995	1996	1997
			(UNAUDITED)
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents.....	\$ --	\$ 177	\$ 34
Accounts receivable --			
Trade.....	726	661	513
Retainage on uncompleted contracts.....	78	183	128
Other receivables.....	133	3	6
Inventories.....	71	86	86
Costs and estimated earnings in excess of billings on uncompleted contracts.....	65	26	91
Prepaid expenses and other current assets.....	31	30	9
	1,104	1,166	867
PROPERTY AND EQUIPMENT, net.....	150	191	189
OTHER NONCURRENT ASSETS.....	22	129	174
	\$ 1,276	\$ 1,486	\$ 1,230
	\$ 1,276	\$ 1,486	\$ 1,230
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES:			
Line of credit.....	\$ 231	\$ --	\$ --
Notes payable.....	--	6	--
Current maturities of long-term debt.....	86	73	78
Current portion of capital leases.....	17	21	19
Accounts payable and accrued expenses.....	732	556	437
Billings in excess of costs and estimated earnings on uncompleted contracts.....	76	151	21
	1,142	807	555
LONG-TERM DEBT, net of current maturities.....	179	261	241
COMMITMENTS AND CONTINGENCIES			
SHAREHOLDERS' EQUITY:			
Common Stock, \$.10 par value, 4,000,000 shares authorized, 2,600 and 2,700 shares issued and outstanding.....	1	1	1
Additional paid-in capital.....	61	62	62
Retained earnings (deficit).....	(107)	355	371
	(45)	418	434
Total liabilities and shareholders' equity.....	\$ 1,276	\$ 1,486	\$ 1,230
	\$ 1,276	\$ 1,486	\$ 1,230

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

WESTERN BUILDING SERVICES, INC.  
 STATEMENTS OF OPERATIONS  
 (IN THOUSANDS)

	YEAR ENDED DECEMBER 31,		THREE MONTHS ENDED MARCH 31,	
	1995	1996	1996	1997
----- (UNAUDITED) -----				
REVENUES.....	\$ 4,112	\$ 6,494	\$ 1,185	\$ 1,072
COST OF SERVICES.....	3,408	4,662	857	812
	-----	-----	-----	-----
Gross profit.....	704	1,832	328	260
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.....	855	1,088	232	231
	-----	-----	-----	-----
Income (loss) from operations..	(151)	744	96	29
OTHER INCOME (EXPENSE):				
Interest expense.....	(35)	(51)	(11)	(11)
Other.....	6	(21)	(1)	(2)
	-----	-----	-----	-----
NET INCOME (LOSS).....	\$ (180)	\$ 672	\$ 84	\$ 16
	=====	=====	=====	=====

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

WESTERN BUILDING SERVICES, INC.  
 STATEMENTS OF SHAREHOLDERS' EQUITY  
 (IN THOUSANDS, EXCEPT SHARE INFORMATION)

	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS (DEFICIT)	TOTAL SHAREHOLDERS' EQUITY (DEFICIT)
	SHARES	AMOUNT			
BALANCE, December 31, 1994.....	2,600	\$ 1	\$ 61	\$ 73	\$ 135
Net loss.....	--	--	--	(180)	(180)
BALANCE, December 31, 1995.....	2,600	1	61	(107)	(45)
Distributions to shareholders...	--	--	--	(210)	(210)
Net income.....	--	--	--	672	672
Common stock issuance.....	100	--	1	--	1
BALANCE, December 31, 1996.....	2,700	1	62	355	418
Net income (unaudited).....	--	--	--	16	16
BALANCE, March 31, 1997 (unaudited).....	2,700	\$ 1	\$ 62	\$ 371	\$ 434

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



WESTERN BUILDING SERVICES, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

	YEAR ENDED DECEMBER 31,		THREE MONTHS ENDED MARCH 31,	
	1995	1996	1996	1997
	-----	-----	-----	-----
	(UNAUDITED)			
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>				
Net income (loss).....	\$(180)	\$ 672	\$ 84	\$ 16
Adjustments to reconcile net income to net cash provided by (used in) operating activities --.....				
Depreciation and amortization...	51	51	9	25
Changes in operating assets and liabilities --.....				
(Increase) decrease in --.....				
Accounts receivable.....	(179)	91	23	200
Inventories.....	(35)	(15)	--	--
Costs and estimated earnings in excess of billings on uncompleted contracts.....	(5)	39	65	(65)
Prepaid expenses and other current assets.....	5	1	(19)	21
Other noncurrent assets....	(15)	(106)	(90)	(56)
Increase (decrease) in --.....				
Accounts payable and accrued expenses.....	186	(177)	(22)	(119)
Billings in excess of costs and estimated earnings on uncompleted contracts.....	17	74	(50)	(130)
	-----	-----	-----	-----
Net cash provided by (used in) operating activities.....	(155)	630	--	(108)
	-----	-----	-----	-----
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>				
Proceeds from sale of property and equipment.....	--	20	--	--
Additions of property and equipment.....	(40)	(113)	(20)	(12)
	-----	-----	-----	-----
Net cash used in investing activities.....	(40)	(93)	(20)	(12)
	-----	-----	-----	-----
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>				
Proceeds from sale of common stock.....	--	1	--	--
Borrowings of long-term debt.....	206	175	20	--
Payments of long-term debt.....	(259)	(96)	--	(23)
Net borrowings in line of credit...	230	(230)	--	--
Distributions to shareholders.....	--	(210)	--	--
	-----	-----	-----	-----
Net cash provided by (used in) financing activities.....	177	(360)	20	(23)
	-----	-----	-----	-----
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....</b>	<b>(18)</b>	<b>177</b>	<b>--</b>	<b>(143)</b>
CASH AND CASH EQUIVALENTS, beginning of period.....	18	--	--	177
	-----	-----	-----	-----
CASH AND CASH EQUIVALENTS, end of period.....	\$ --	\$ 177	\$--	\$ 34
	=====	=====	=====	=====
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>				
Cash paid for --				
Interest.....	\$ 35	\$ 51	\$ 11	\$ 11

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

1. BUSINESS AND ORGANIZATION:

Western Building Services, Inc., a Colorado corporation, (the "Company") focuses on providing "design and build" installation services and maintenance, repair and replacement of HVAC systems for commercial facilities. Western also offers continuous monitoring and control services for commercial facilities. The Company primarily operates in Colorado.

The Company and its shareholders intend to enter into a definitive agreement with Comfort Systems USA, Inc. ("Comfort Systems"), pursuant to which all outstanding shares of the Company's common stock will be exchanged for cash and shares of Comfort Systems common stock concurrently with the consummation of the initial public offering (the "Offering") of the common stock of Comfort Systems.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

INTERIM FINANCIAL INFORMATION

The interim financial statements as of March 31, 1997, and for the three months ended March 31, 1996 and 1997, are unaudited, and certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been omitted. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year.

CASH AND CASH EQUIVALENTS

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

INVENTORIES

Inventories consist of duct materials, air conditioning equipment, refrigeration supplies and accessories 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 (FIFO) 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 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. 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.

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. 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

WESTERN BUILDING SERVICES, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

settlements may result in revisions to costs and income and are recognized in the period in which the revisions are determined.

The balances billed but not paid by customers pursuant to retainage provision in construction contracts will be 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 will be billed and collected in the upcoming fiscal year.

Revenues of approximately \$783,000 and \$2,291,000 with gross profits of \$339,000 and \$874,000 were recognized by the Company in 1995 and 1996, respectively, for energy conversions and new installations related to an incentive program developed by the Public Service Company of Colorado (PSC). The Demand Side Management program provided incentives for PSC customers to convert from electric heat to gas/steam heat in order to reduce peak demand for electricity. This program ended November 1996.

#### WARRANTY COSTS

The Company warrants labor for the first year after installation on new air conditioning and heating units. The Company generally warrants labor for 30 days after servicing of existing air conditioning and heating units. A reserve for warranty costs is recorded upon completion of installation or service.

#### INCOME TAXES

The Company has elected S Corporation status as defined by the Internal Revenue Code, whereby the Company is not subject to taxation for federal purposes. Under S Corporation status, the shareholders report their share of the Company's taxable earnings or losses in their personal tax returns. The Company will terminate its S Corporation status concurrently with the effective date of this Offering.

#### 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 and 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.

#### NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1996, the Company adopted Statement of Financial Accounting Standard (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." Accordingly, in the event that facts and circumstances indicate that property and equipment, and intangible or other assets may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if a write-down to market value is necessary. Adoption of this standard did not have a material effect on the financial position or results of operations of the Company.

WESTERN BUILDING SERVICES, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

3. PROPERTY AND EQUIPMENT:

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

	ESTIMATED USEFUL LIVES IN YEARS	DECEMBER 31,	
		1995	1996
Transportation equipment.....	5	\$ 47	\$ 47
Machinery and equipment.....	6-7	133	68
Computer and telephone equipment.....	5	120	145
Leasehold improvements.....	3	21	71
Furniture and fixtures.....	7	28	20
		-----	-----
		349	351
Less -- Accumulated depreciation and amortization.....		(199)	(160)
		-----	-----
Property and equipment, net.....		\$ 150	\$ 191
		=====	=====

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS:

Other noncurrent assets consist of the following (in thousands):

	DECEMBER 31,	
	1995	1996
Covenant not to compete.....	\$ --	\$ 75
Life insurance surrender value.....	14	27
Other noncurrent assets.....	8	27
	-----	-----
	\$ 22	\$ 129
	=====	=====

At December 31, 1996, the Company acquired the contract rights of a competitor for \$75,000 through a covenant not to compete agreement. This agreement will be amortized over its three year term which expires at December 31, 1999.

Accounts payable and accrued expenses consist of the following (in thousands):

	DECEMBER 31,	
	1995	1996
Accounts payable, trade.....	\$ 403	\$ 249
Accrued compensation and benefits....	108	86
Accrued warranty expense.....	82	82
Other accrued expenses.....	139	139
	-----	-----
	\$ 732	\$ 556
	=====	=====

WESTERN BUILDING SERVICES, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

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

	DECEMBER 31,	
	1995	1996
Costs incurred on contracts in progress.....	\$ 335	\$ 530
Estimated earnings, net of losses....	206	160
	-----	-----
	541	690
Less -- Billings to date.....	552	815
	-----	-----
	\$ (11)	\$ (125)
	=====	=====
Costs and estimated earnings in excess of billings on uncompleted contracts.....	\$ 65	\$ 26
Billings in excess of costs and estimated earnings on uncompleted contracts.....	(76)	(151)
	-----	-----
	\$ (11)	\$ (125)
	=====	=====

5. LONG-TERM DEBT:

Long-term debt consists of installment notes payable for transportation equipment. The debt is secured by the related transportation equipment. The terms of the notes range from 36 months to 48 months with monthly payments of principal and interest of approximately \$8,600. The notes bear interest at rates ranging from 9 percent to 13 percent.

Long-term debt also consists of term loans and capital leases. The term loans were issued in the amounts of \$175,000 and \$200,000 in 1996 and 1995, respectively. The \$175,000 term loan is secured by equipment, inventory, accounts receivable and all contract rights. The \$200,000 term loan is secured by all inventory and equipment and bears interest at prime plus 2 percent per annum. These term loans are also guaranteed by the Company president.

The capital leases relate to computer equipment and printers. The terms of the leases range from 12 to 36 months. The interest rates on these leases range from 10 to 12 percent.

The aggregate maturities of long-term debt as of December 31, 1996, are as follows (in thousands):

Year ending December 31	
1997.....	\$ 85
1998.....	89
1999.....	98
2000.....	89
	-----
	\$ 361
	=====

The Company has a \$300,000 line of credit with a financial institution. The line of credit expires September 28, 1997, and bears interest at prime plus 2 percent per annum. The line of credit is secured by accounts receivable and inventory and is guaranteed by the Company president. There was no balance outstanding under this line of credit at December 31, 1996.

6. LEASES:

The Company leases its facility from a third party, which expires in 1999. The rent paid under this lease was approximately \$43,000 and \$66,500 for the years ended December 31, 1995 and 1996. The lease requires the Company to pay taxes, maintenance, insurance and certain other operating costs of the leased property. The lease contains renewal provisions.

WESTERN BUILDING SERVICES, INC.  
NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

The Company leases vehicles for operating purposes. The lease payments under these vehicle leases totaled approximately \$47,000 and \$71,000 for the years ended December 31, 1995 and 1996, respectively.

Future minimum lease payments for operating leases are as follows (in thousands):

Year ending December 31	
1997.....	\$ 144
1998.....	132
1999.....	19
	-----
	\$ 295
	=====

7. EMPLOYEE BENEFIT PLANS:

The Company has adopted a 401(k) plan which allows the Company to make discretionary contributions and discretionary profit sharing contributions. No contributions were made by the Company under this plan in 1995 and 1996. However, expenses of \$2,733 and \$3,903 were incurred by the Company during 1995 and 1996, respectively.

8. FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash and cash equivalents, investments, notes payable, a line of credit, and debt. The Company believes that the carrying value of these instruments on the accompanying balance sheet approximates their fair value.

9. RELATED-PARTY TRANSACTIONS:

At December 31, 1995, the Company had a receivable of \$109,500 due from the president and vice president. At December 31, 1996, this balance was \$173,500. The Company offset this balance with the dividends payable of \$210,315 at December 31, 1996, resulting in a remaining dividend payable of \$36,875 to two shareholders and one director.

10. COMMITMENTS AND CONTINGENCIES:

LITIGATION

The Company is involved in legal actions arising in the ordinary course of business. Management does not believe the outcome of such legal actions will have a material adverse effect on the Company's financial position or results of operations.

INSURANCE

The Company carries a broad range of insurance coverage, including general and business auto liability, commercial property, workers' compensation and a general umbrella policy. The Company has not incurred significant claims or losses on any of its insurance policies.

11. EVENT SUBSEQUENT TO DATE OF AUDITORS' REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS (UNAUDITED):

In March 1997, the Company and its shareholders entered into a definitive agreement with a wholly-owned subsidiary of Comfort Systems, providing for the merger of the Company with the subsidiary of Comfort Systems.

In connection with the merger, the Company will make a cash distribution of approximately \$371,000 prior to the merger which represents the Company's estimated S Corporation accumulated adjustment account. Had these transactions been recorded at March 31, 1997, the effect on the accompanying unaudited balance sheet would be a decrease in assets of \$41,000 and an increase in liabilities of \$333,000 and a decrease in shareholders' equity of \$371,000.

NO PERSON HAS BEEN AUTHORIZED IN CONNECTION WITH THE OFFERING MADE HEREBY TO GIVE ANY INFORMATION OR TO MAKE ANY REPRESENTATION NOT CONTAINED IN THIS PROSPECTUS AND, IF GIVEN OR MADE, SUCH INFORMATION OR REPRESENTATION MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY THE COMPANY OR ANY UNDERWRITER. THIS PROSPECTUS DOES NOT CONSTITUTE AN OFFER TO SELL OR A SOLICITATION OF ANY OFFER TO BUY ANY OF THE SECURITIES OFFERED HEREBY TO ANY PERSON OR BY ANYONE IN ANY JURISDICTION IN WHICH IT IS UNLAWFUL TO MAKE SUCH OFFER OR SOLICITATION. NEITHER THE DELIVERY OF THIS PROSPECTUS NOR ANY SALE MADE HEREUNDER SHALL, UNDER ANY CIRCUMSTANCES, CREATE ANY IMPLICATION THAT THE INFORMATION CONTAINED HEREIN IS CORRECT AS OF ANY DATE SUBSEQUENT TO THE DATE HEREOF.

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8,000,000 SHARES

[LOGO]  
COMFORT SYSTEMS USA, INC.  
COMMON STOCK

-----  
PROSPECTUS  
-----

, 1997

=====

PART II  
INFORMATION NOT REQUIRED IN PROSPECTUS

ITEM 13. OTHER EXPENSES OF ISSUANCE AND DISTRIBUTION.

The following table sets forth the costs and expenses payable by the Company in connection with the registration of the securities being registered. In connection with future acquisitions, additional printing, legal, accounting and miscellaneous expenses are expected to be incurred with respect to the issuance and distribution of the securities being registered hereby. All amounts are estimates except for the fees payable to the SEC.

	AMOUNT TO BE PAID
SEC registration fee.....	\$ 43,182
Printing expenses.....	\$ 10,000
Legal fees and expenses.....	\$ 20,000
Accounting fees and expenses.....	\$ 20,000
Transfer Agent's and Registrar's fees...	\$ 1,000
Miscellaneous.....	\$ 5,818
	-----
TOTAL.....	\$ 100,000
	=====

ITEM 14. INDEMNIFICATION OF OFFICERS AND DIRECTORS.

The Company's Certificate of Incorporation, as amended, and Bylaws incorporate substantially the provisions of the Delaware General Corporation Law ("DGCL") providing for indemnification of directors and officers of the Company against expenses, judgments, fines, settlements and other amounts actually and reasonably incurred in connection with any proceeding arising by reason of the fact that such person is or was an officer or director of the Company or is or was serving at the request of the Company as a director, officer or employee of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise.

As permitted by Section 102 of the DGCL, the Company's Certificate of Incorporation, as amended, contains provisions eliminating a director's personal liability for monetary damages to the Company and its stockholders arising from a breach of a director's fiduciary duty except for liability (a) for any breach of the director's duty of loyalty to the Company or its stockholders, (b) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (c) under Section 174 of the DGCL, or (d) for any transaction from which the director derived an improper personal benefit.

Section 145 of the DGCL provides generally that a person sued as a director, officer, employee or agent of a corporation may be indemnified by the corporation for reasonable expenses, including attorneys' fees, if in the case of other than derivative suits such person has acted in good faith and in a manner such person reasonably believed to be in or not opposed to the best interests of the corporation (and, in the case of a criminal proceeding, had no reasonable cause to believe that such person's conduct was unlawful). In the case of a derivative suit, an officer, employee or agent of the corporation which is not protected by the Certificate of Incorporation may be indemnified by the corporation for reasonable expenses, including attorneys' fees, if such person has acted in good faith and in a manner such person reasonably believed to be in or not opposed to the best interests of the corporation, except that no indemnification shall be made in the case of a derivative suit in respect of any claim as to which an officer, employee or agent has been adjudged to be liable to the corporation unless that person is fairly and reasonably entitled to indemnity for proper expenses. Indemnification is mandatory in the case of a director, officer, employee, or agent who is successful on the merits in defense of a suit against such person.

The Company has entered into Indemnity Agreements with its directors and certain key officers pursuant to which the Company generally is obligated to indemnify its directors and such officers to the full extent permitted by the DGCL as described above.



The Company has purchased liability insurance policies covering directors and officers in certain circumstances.

ITEM 15. RECENT SALES OF UNREGISTERED SECURITIES.

On December 12, 1996, Comfort Systems issued and sold 1,000 shares of Common Stock to Notre for a consideration of \$1,000. This sale was exempt from registration under Section 4(2) of the Securities Act, no public offering being involved.

On January 6, 1997, Comfort Systems issued and sold shares of Common Stock to the following parties in the amounts and for the consideration indicated. These sales were exempt from registration under Section 4(2) of the Securities Act: Notre -- 23,516.623 shares for a consideration of \$28,699.12; Fred M. Ferreira -- 3957.7359 shares for a consideration of \$4,794.35; J. Gordon Beittenmiller -- 825.5 shares for a consideration of \$1,000.00; Reagan S. Busbee -- 825.5 shares for a consideration of \$1,000.00; S. Craig Lemmon -- 825.5 shares for a consideration of \$1,000.00; Milburn E. Honeycutt -- 412.75 shares for a consideration of \$500.00; Brian J. Vensel -- 412.75 shares for a consideration of \$500.00; Emmett E. Moore -- 412.75 shares for a consideration of \$500.00; John W. Bouloubasis -- 412.75 shares for a consideration of \$500.00; Stephen R. Baur -- 330.2 shares for a consideration of \$400.00; Shellie LePori -- 206.375 shares for a consideration of \$250.00; Constance Drew -- 288.925 shares for a consideration of \$350.00; John Mercandante, Jr. -- 82.55 shares for a consideration of \$100.00; Larry Martin -- 82.55 shares for a consideration of \$100.00; Norton Family Trust -- 61.9125 shares for a consideration of \$75.00; Larry E. Jacobs -- 61.9125 shares for a consideration of \$75.00; Richard T. Howell -- 41.275 shares for a consideration of \$50.00; Rod Crosby -- 41.275 shares for a consideration of \$50.00; Jennifer Summerford -- 24.765 shares for a consideration of \$30.00; Infoscope Partners, Inc. -- 8.255 shares for a consideration of \$10.00; Melinda Malik -- 4.1275 shares for a consideration of \$5.00; and Steven T. Zellers -- 16.51 shares for a consideration of \$20.00.

On February 25, 1997, Comfort Systems issued and sold shares of Common Stock to the following parties in the amounts and for the consideration indicated. These sales were exempt from registration under Section 4(2) of the Securities Act, no public offering being involved: William George, III -- 619.125 shares for a consideration of \$750.00; J. Gordon Beittenmiller -- 132.08 shares for a consideration of \$160.00; Reagan S. Busbee -- 132.08 shares for a consideration of \$160.00; S. Craig Lemmon -- 132.08 shares for a consideration of \$160.00; Milburn E. Honeycutt -- 66.04 shares for a consideration of \$80.00; and Brian J. Vensel -- 66.04 shares for a consideration of \$80.00.

Effective March 20, 1997, Comfort Systems effected a 121.1387 to 1 stock split on outstanding shares of Common Stock as of March 19, 1997.

Effective March 20, 1997, Comfort Systems issued and sold 2,742,912 shares of Restricted Voting Common Stock to Notre in exchange for 2,742,912 shares of Common Stock. This sale was exempt from registration under Section 4(2) of the Securities Act, no public offering being involved.

On July 2, 1997, the Company issued 9,720,927 shares of its Common Stock in connection with the Mergers of the Founding Companies. Each of these transactions was completed without registration under the Securities Act in reliance upon the exemption provided by Section 4(2) of the Securities Act.

ITEM 16. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a) EXHIBITS

The exhibits listed below are filed as exhibits to this registration statement and are filed manually herewith or incorporated by reference to the statements or reports indicated below:

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

EXHIBIT NUMBER	DESCRIPTION OF EXHIBITS	EXHIBIT NUMBER	FILE NUMBER
2.1	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Accurate Acquisition Corp., Accurate Air Systems, Inc. and the Stockholder named therein	2.1	333-24021
2.2	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Atlas Air Acquisition I Corp., Atlas Comfort Services USA, Inc. and the Stockholders named therein	2.2	333-24021
2.3	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Contract Acquisition Corp., Contract Service, Inc. and the Stockholders named therein	2.3	333-24021
2.4	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Eastern Acquisition Corp., Eastern II Acquisition Corp., Eastern Heating & Cooling, Inc., Eastern Refrigeration Co., Inc. and the Stockholder named therein	2.4	333-24021
2.5	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Freeway Acquisition Corp., Freeway Heating & Air Conditioning, Inc. and the Stockholders named therein	2.5	333-24021
2.6	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Quality Acquisition Corp., Quality Air Heating & Cooling, Inc. and the Stockholders named therein	2.6	333-24021
2.7	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., S. M. Lawrence Acquisition Corp., S. M. Lawrence II Acquisition Corp., S. M. Lawrence Company, Inc., Lawrence Service, Inc. and the Stockholders named therein	2.7	333-24021
2.8	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Seasonair, Inc. and the Stockholders named therein	2.8	333-24021
2.9	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Standard Acquisition Corp., Standard Heating & Air Conditioning Company and the Stockholders named therein	2.9	333-24021
2.10	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Tech I Acquisition Corp., Tech II Acquisition Corp., Tech Heating and Air Conditioning, Inc., Tech Mechanical, Inc. and the Stockholder named therein	2.10	333-24021
2.11	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Tri-City Acquisition Corp., Tri-City Mechanical, Inc. and the Stockholders named therein	2.11	333-24021
2.12	-- Agreement and Plan of Organization, dated as of March 18, 1997, by and among Comfort Systems USA, Inc., Western Building Acquisition Corp., Western Building Services, Inc. and the Stockholders named therein	2.12	333-24021
3.1	-- Second Amended and Restated Certificate of Incorporation of Comfort Systems USA, Inc.	3.1	333-24021

3.2	--	Bylaws of Comfort Systems USA, Inc., as amended	3.2	333-24021
4.1	--	Form of certificate evidencing ownership of Common Stock of Comfort Systems USA, Inc.	4.1	333-24021
5.1	--	Opinion of Bracewell & Patterson, L.L.P.	Filed herewith	
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 Comfort Systems USA, Inc. and Fred M. Ferreira.	10.3	333-24021
10.4	--	Form of Employment Agreement between Comfort Systems USA, Inc. and J. Gordon Beittenmiller.	10.4	333-24021
10.5	--	Form of Employment Agreement between Comfort Systems USA, Inc. and William George, III.	10.5	333-24021
10.6	--	Form of Employment Agreement between Comfort Systems USA, Inc. and Reagan S. Busbee.	10.6	333-24021
10.7	--	Form of Employment Agreement between Comfort Systems USA, Inc., Accurate Air Systems, Inc. and Thomas J. Beaty.	10.7	333-24021
10.8	--	Form of Employment Agreement between Comfort Systems USA, Inc., Atlas Comfort Services USA, Inc. and Brian S. Atlas.	10.8	333-24021
10.9	--	Form of Employment Agreement between Comfort Systems USA, Inc., Contract Service, Inc. and John C. Phillips.	10.9	333-24021
10.10	--	Form of Employment Agreement between Comfort Systems USA, Inc., Eastern Heating & Cooling, Inc. and Alfred J. Giardenelli, Jr.	10.10	333-24021
10.11	--	Form of Employment Agreement between Comfort Systems USA, Inc., Quality Air Heating & Cooling, Inc. and Robert J. Powers.	10.11	333-24021
10.12	--	Form of Employment Agreement between Comfort Systems USA, Inc., S. M. Lawrence Company, Inc. and Samuel M. Lawrence III.	10.12	333-24021
10.13	--	Form of Employment Agreement between Comfort Systems USA, Inc., Tech Heating and Air Conditioning, Inc. and Robert R. Cook.	10.13	333-24021
10.14	--	Form of Employment Agreement between Comfort Systems USA, Inc., Tri-City Mechanical, Inc. and Michael Nothum, Jr.	10.14	333-24021
10.15	--	Form of Employment Agreement between Comfort Systems USA, Inc., Western Building Services, Inc. and Charles W. Klapperich.	10.15	333-24021
10.16	--	Form of Agreement among certain stockholders	10.16	333-24021
10.17	--	Lease between M & B Interests, Inc. and Atlas Air Conditioning Company, Inc. dated October 1, 1994.	Filed herewith	
10.18	--	Lease between Thomas J. and Bonnie J. Beaty and Accurate Air Systems, Inc. dated July 1, 1997.	Filed herewith	
10.19	--	Amended and Restated Agreement of Lease between Thomas J. and Bonnie J. Beaty and Accurate Air Systems, Inc. dated July 1, 1997.	Filed herewith	
10.20	--	Lease between Nothum Development, L.L.C. and Tri-City Mechanical, Inc. dated July 1, 1997.	Filed herewith	
10.21	--	Lease between Samuel Matthews Lawrence, Jr. and S.M. Lawrence Company, Incorporated dated November 1, 1996.	Filed herewith	
10.22	--	Lease between K and P Warehouse #1 and Quality Trane Heating and Cooling, Inc. (n/k/a/ Quality Air Heating and Cooling, Inc.) dated April 1, 1986, together with amendments thereto.	Filed herewith	
10.23	--	Lease between J&J Investments and Contract Service, Inc. dated March 1, 1997.	Filed herewith	
10.24	--	Lease by Tech Heating and Air Conditioning, Inc. dated April 2, 1995 as amended by Amendment between Cook Properties, Inc. and Tech Heating and Air Conditioning, Inc. on March 13, 1997.	Filed herewith	
10.25	--	Credit Agreement among the Company and its subsidiaries, Bank One, Texas, N.A., as agent and the banks listed therein dated July 2, 1997.	Filed herewith	

10.26	--	Form of Indemnity Agreement entered into by the Company with each of the following persons: Fred M. Ferreira, J. Gordon Beittenmiller, Reagan S. Busbee, William George, III, Steven S. Harter, Robert J. Powers, Michael Nothum, Jr., Robert R. Cook, Brian S. Atlas, Thomas J. Beaty, John C. Phillips, Samuel M. Lawrence III, Alfred J. Giardenelli, Jr., Charles W. Klapperich, Larry Martin and John Mercadante, Jr. on June 27, 1997.	Filed herewith
10.27	--	Indemnity Agreement between the Company and Notre Capital Ventures II, L.L.C.	Filed herewith
21.1	--	List of subsidiaries of Comfort Systems USA, Inc.	21.1 333-24021
23.1	--	Consent of Arthur Andersen LLP	Filed herewith
23.2	--	Consent of Bracewell & Patterson, L.L.P. (contained in Exhibit 5.1).	Filed herewith
23.3	--	Consent of Fred M. Ferreira to be named as a director.	23.3 333-24021
23.4	--	Consent of J. Gordon Beittenmiller to be named as a director.	23.4 333-24021
23.5	--	Consent of Brian S. Atlas to be named as a director.	23.5 333-24021
23.6	--	Consent of Thomas J. Beaty to be named as a director.	23.6 333-24021
23.7	--	Consent of Robert R. Cook to be named as a director.	23.7 333-24021
23.8	--	Consent of Alfred J. Giardenelli, Jr. to be named as a director.	23.8 333-24021
23.9	--	Consent of Charles W. Klapperich to be named as a director.	23.9 333-24021
23.10	--	Consent of Samuel M. Lawrence III to be named as a director.	23.10 333-24021
23.11	--	Consent of Michael Nothum, Jr. to be named as a director.	23.11 333-24021
23.12	--	Consent of John C. Phillips to be named as a director.	23.12 333-24021
23.13	--	Consent of Robert J. Powers to be named as a director.	23.13 333-24021
23.14	--	Consent of Steven S. Harter to be named as a director.	23.14 333-24021
23.15	--	Consent of Larry Martin to be named as a director.	23.15 333-24021
23.16	--	Consent of John Mercadante, Jr. to be named as a director.	23.16 333-24021
24.1	--	Power of Attorney (included herein on Signature Page)	Filed herewith
27.1	--	Financial Data Schedule	Filed herewith

(b) FINANCIAL STATEMENT SCHEDULES

All schedules for which provision is made in the applicable accounting regulation of the SEC are not required under the related instructions, are inapplicable, or the information is included in the consolidated financial statements, and therefore have been omitted.

ITEM 17. UNDERTAKINGS.

(a) Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers and controlling persons of the Company pursuant to the provisions described in Item 14, or otherwise, the Company has been advised that in the opinion of the SEC such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than payment by the Company of expenses incurred or paid by a director, officer or controlling person of the Company in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the Company will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Securities Act and will be governed by the final adjudication of such issue.

(b) The undersigned registrant hereby undertakes:

(1) To file, during any period in which offers or sales are being made, a post-effective amendment to this registration statement:

(i) To include any prospectus required by Section 10(a)(3) of the Securities Act of 1933;

(ii) To reflect in the prospectus any facts or events arising after the effective date of the registration statement (or the most recent post-effective amendment thereof) which, individually or in the aggregate, represents a fundamental change in the information set forth in the registration statement. Notwithstanding the foregoing, any increase or decrease in volume of securities offered (if the total dollar value of securities offered would not exceed that which was registered) and any deviation from the low or high and of the estimated maximum offering range may be reflected in the form of prospectus filed with the Commission pursuant to Rule 424(b), if, in the aggregate, the changes in volume and price represent no more than 20 percent change in the maximum aggregate offering price set forth in the "Calculation of Registration Fee" table in the effective registration statement.

(iii) To include any material information with respect to the plan of distribution not previously disclosed in the registration statement or any material change in the registration statement.

(2) That, for the purpose of determining any liability under the Securities Act of 1933, each such post-effective amendment shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at the time shall be deemed to be the initial bona fide offering thereof.

(3) To remove from registration by means of a post-effective amendment any of the securities being registered which remain unsold at the termination of the offering.

SIGNATURES

PURSUANT TO THE REQUIREMENTS OF THE SECURITIES ACT OF 1933, COMFORT SYSTEMS USA, INC. HAS DULY CAUSED THIS REGISTRATION STATEMENT TO BE SIGNED ON ITS BEHALF BY THE UNDERSIGNED, THEREUNTO DULY AUTHORIZED, IN THE CITY OF HOUSTON, STATE OF TEXAS, ON JULY 31, 1997.

COMFORT SYSTEMS USA, INC.  
By /s/ FRED M. FERREIRA  
FRED M. FERREIRA  
CHIEF EXECUTIVE OFFICER

POWER OF ATTORNEY

Each person whose signature appears below on this Registration Statement hereby constitutes and appoints Fred M. Ferreira, J. Gordon Beittenmiller and William George, III, each with full power to act without the other, his or her true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities (until revoked in writing) to sign any and all amendments (including post-effective amendments and amendments thereto) to this Registration Statement, and to file the name, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorney-in-fact and agent full power and authority to do and perform each and every act and thing he or she might do or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agent, or his substitute, may lawfully do or cause to be done by virtue hereof.

PURSUANT TO THE REQUIREMENTS OF THE SECURITIES ACT OF 1933, THIS REGISTRATION STATEMENT OR AMENDMENT THERETO HAS BEEN SIGNED BELOW BY THE FOLLOWING PERSONS IN THE INDICATED CAPACITIES ON JULY 31, 1997.

SIGNATURE	TITLE
/s/ FRED M. FERREIRA FRED M. FERREIRA	Chairman of the Board, Chief Executive Officer and President
/s/ J. GORDON BEITTENMILLER J. GORDON BEITTENMILLER	Senior Vice President, Chief Financial Officer and Director (PRINCIPAL ACCOUNTING OFFICER)
/s/ STEVEN S. HARTER STEVEN S. HARTER	Director
/s/ MICHAEL NOTHUM, JR. MICHAEL NOTHUM, JR.	Director
_____ BRIAN S. ATLAS	Director
/s/ THOMAS J. BEATY THOMAS J. BEATY	Director

SIGNATURES -- (CONTINUED)

/s/ROBERT R. COOK                      Director  
ROBERT R. COOK

/s/ALFRED J. GIARDENELLI              Director  
ALFRED J. GIARDENELLI

/s/CHARLES W. KLAPPERICH              Director  
CHARLES W. KLAPPERICH

/s/SAMUEL M. LAWRENCE III              Director  
SAMUEL M. LAWRENCE III

/s/ JOHN C. PHILLIPS                    Director  
JOHN C. PHILLIPS

/s/ROBERT J. POWERS                   Director  
ROBERT J. POWERS

\_\_\_\_\_  
LARRY MARTIN                           Director

\_\_\_\_\_  
JOHN MERCADANTE, JR.                   Director

July 31, 1997

Comfort Systems USA, Inc.  
4801 Woodway Drive, Suite 300E  
Houston, Texas 77056

Gentlemen:

We have acted as counsel to Comfort Systems USA, Inc., a Delaware corporation (the "Company"), in connection with the preparation of its Registration Statement on Form S-1 (the "Registration Statement"), filed by the Company under the Securities Act of 1933, as amended (the "Securities Act"), with respect to the offering and sale by the Company of up to 8,000,000 shares of its common stock, par value \$.01 per share (the "Common Stock").

We have examined originals or copies of (i) the Amended and Restated Certificate of Incorporation of the Company; (ii) the Bylaws of the Company, as amended; (iii) certain resolutions of the Board of Directors of the Company; and (iv) such other documents and records as we have deemed necessary and relevant for purposes hereof. We have relied upon certificates of public officials and officers of the Company as to all matters of fact relating to this opinion and have made such investigations of law as we have deemed necessary and relevant as a basis hereof. We have not independently verified any factual matter relating to this opinion.

We have assumed the genuineness of all signatures, the authenticity of all documents, certificates and records submitted to us as copies, and the conformity to original documents, certificates and records of all documents, certificates and records submitted to us as copies.

Based upon the foregoing, and subject to the limitations and assumptions set forth herein, and having due regard for such legal considerations as we deem relevant, we are of the opinion that:

1. The Company is a corporation duly incorporated, validly existing and in good standing under the laws of the State of Delaware.

Comfort Systems USA, Inc.  
July 31, 1997  
Page 2

2. The Common Stock is duly authorized, and when issued and delivered by the Company against payment therefor as described in the Registration Statement pursuant to Board authorization of the transactions contemplated by the Registration Statement, such shares will be duly and validly issued, fully paid and nonassessable.

The foregoing opinion is based on and is limited to the laws of the General Corporation Law of the State of Delaware, and we render no opinion with respect to any other law.

We hereby consent to the filing of this opinion with the Securities and Exchange Commission as Exhibit 5.1 to the Registration Statement and to the reference to this firm as having passed on the validity of the issuance of the Common Stock under the caption "Legal Matters" in the prospectus contained in the Registration Statement. By giving such consent, we do not admit that we are included within the category of persons whose consent is required under Section 7 of the Securities Act or the rules and regulations issued thereunder.

Very truly yours,

/s/ BRACEWELL & PATTERSON, L.L.P.  
Bracewell & Patterson, L.L.P.



STANDARD COMMERCIAL LEASE AGREEMENT  
(EXISTING BUILDING) #1

## LEASE AGREEMENT

THIS LEASE AGREEMENT, made and entered into by and between M & B INTERESTS, INC. hereinafter referred to as "Landlord", and ATLAS AIR CONDITIONING COMPANY, INC. hereinafter referred to as "Tenant";

## WITNESSETH:

1. PREMISES AND TERM. Landlord hereby leases unto Tenant and Tenant hereby leases from Landlord, subject to the terms of this Lease, approximately 12,500 square feet of space (the "Premises") in Building 4125 SOUTHERLAND ROAD (the "Building") of HOUSTON, TEXAS 77092 (the "Project"), constructed upon that tract of land (the "Site") described more particularly in Exhibit "A" annexed hereto, such Premises being outlined in red on Exhibit A.

TO HAVE AND TO HOLD the same for a term commencing on OCTOBER 1, 1994 and ending SEPTEMBER 30, 1997 months thereafter. Tenant acknowledges that it has inspected and accepts the premises, and specifically the buildings and improvements comprising the same, in their present condition as suitable for the purpose for which the premises are leased. Taking of possession by Tenant shall be deemed conclusively to establish that said buildings and other improvements are in good and satisfactory condition as of when possession was taken. Tenant further acknowledges that no representations as to the repair of the premises, nor promises to alter, remodel or improve the premises have been made by Landlord, unless such are expressly set forth in this lease. If this lease is executed before the premises become vacant or otherwise available and ready for occupancy, or if any present tenant or occupant of the premises holds over, and Landlord cannot acquire possession of the premises prior to the date above recited as the commencement date of this lease, Landlord shall not be deemed to be in default hereunder, and Tenant agrees to accept possession of the premises at such time as Landlord is able to tender the same, which date shall thenceforth be deemed the "commencement date"; and Landlord hereby waives payment of rent covering any period prior to the tendering of possession to Tenant hereunder. After the commencement date Tenant shall, upon demand, execute and deliver to Landlord a letter of acceptance of delivery of the premises.

## 2. BASE RENT AND SECURITY DEPOSIT.

A. Tenant agrees to pay to Landlord rent for the premises in advance, without demand, deduction or set off, for the entire term hereof at the rate of SEVEN THOUSAND FIVE HUNDRED AND 00/00 Dollars (\$7,500.00) per month. One such monthly installment shall be due and payable on the date hereof and a like monthly installment shall be due and payable on or before the first day of each calendar month at the commencement or end of the lease period shall be prorated.

B. In addition, Tenant agrees to deposit with Landlord on the date hereof the sum of \$-0- Dollars (\$-0-), which sum shall be held by Landlord, without obligation for interest, as security for the performance of Tenant's covenants and obligations under this lease, it being expressly understood and agreed that such deposit is not an advance rental deposit or a measure of Landlord's damages in case of Tenant's default. Upon the occurrence of any event of default by Tenant, Landlord may, from time to time, without prejudice to any other remedy provided herein or provided by law, use such fund to the extent necessary to make good any arrears of rent or other payments due Landlord hereunder, and any other damage, injury, expense or liability caused by such event of default; and Tenant shall pay to Landlord on demand the amount so applied in order to restore the security deposit to its original amount. Although the security deposit shall be deemed the property of Landlord, any remaining balance of such deposit shall be returned by Landlord to Tenant at such time after termination of this lease that all of Tenant's obligations under this lease have been fulfilled.

## 3. ADDITIONAL RENT.

A. The rental payment under Paragraph 2A of the Lease is based, in part, on estimated operating expenses for the calendar year in which the lease commences of \$-0- per square foot. In the event that the operating expenses, as hereinafter defined, for any calendar year during the term of this lease (including without limitation the calendar year in which the lease commences) exceed \$\_\_\_\_\_ per square foot, the tenant agrees to pay, upon demand, to the Landlord as additional rent, a pro rated share of such expenses for the entire building and/or project. Tenant's pro rata share, as used in this lease shall mean a fraction, the numerator of which is the total number of square feet in the demised premises and the denominator of which is the total number of square feet in the building and/or project.

Landlord may within 150 days after close of each calendar year give Tenant an invoice to include in reasonable detail, all computation of additional rent. Tenant will cause payment of said invoice within thirty (30) days of receipt. An equitable adjustment shall be made for Tenant's share of excess operating expenses in the last partial calendar year of the term of this lease computed upon the previous year's figures. Such payment shall be due from Tenant thirty (30) days prior to the expiration of the lease term. Tenant shall have the right at Landlord's convenience to review Landlord's books relevant to the additional rental.

B. The term "Operating Expenses" as used in this Lease includes all generally accepted expenses incurred by Landlord with respect to the maintenance and operation of the building and/or project of which the premises are a part, including, but not limited to, maintenance and repair costs, water, sewer, gas, heat, light, power, telephone and other utilities, security, trash and snow removal, landscaping, wages and benefits payable to employees of Landlord, whose duties are connected with the operation and maintenance of the building and/or project, amounts to be paid to contractors for subcontractors for the work or

service performed in connection with the operation and maintenance of the building and/or project, all services, supplies, repairs, replacements or other expenses for maintaining and operating the building and/or project including common area and parking area. The term "Operating Expenses" includes all taxes and assessments and governmental charges whether federal, state, county or municipal, and whether they be by taxing districts or authorities presently taxing the leased premises or by others, subsequently created or otherwise, and by any other taxes and assessments attributable to the building and its operation excluding, however, federal and state taxes on income. In connection with the taxes there may be the expense of employing a tax consulting firm to attempt to assure a fair tax burden on the building and grounds within applicable taxing jurisdiction. The term "Operating Expenses" also includes all insurance premiums Landlord is required to pay or deems necessary to pay for public liability insurance and fire and extended insurance coverage, with respect to the building and/or project of which the premises are part. The term "Operating Expenses" does not include any capital improvement to the building and/or project of which the premises are part, nor shall it include any repairs, restoration or other work, occasioned by fire, windstorm or other casualty, income and franchise taxes of the Landlord, expenses incurred in leasing to or procuring of tenants, leasing commissions, advertising expenses, expenses of the renovating of space for new tenants, interest or principal payments on any mortgage or indebtedness of Landlord, nor depreciation allowance or expense.

4. USE. The demised premises shall be used only for the purpose of receiving, storing, shipping and selling (other than retail) products, materials and merchandise made and/or distributed by Tenant and for such other lawful purposes as may be incidental thereto. Outside storage, including without limitation, trucks and other vehicles, is prohibited without Landlord's prior written consent. Tenant shall at its own cost and expense obtain any and licenses and permits necessary for any such use. Tenant shall comply with all governmental laws, ordinances and regulations applicable to the use of the premises, and shall promptly comply with all governmental orders and directives for the correction, prevention and abatement of nuisances, in or upon, or connected with, the premises, all at Tenant's sole expense. Tenant shall not permit any objectionable or unpleasant odors, smoke, dust, gas, noise or vibrations to emanate from the premises, nor take any other action which would constitute a nuisance or would disturb or endanger any other tenants of the building in which the premises are situated or unreasonably interfere with their use of their respective premises. Without Landlord's prior written consent, Tenant shall not receive, store or otherwise handle any product, material or merchandise which is explosive or highly inflammable. Tenant will not permit the premises to be used for any purpose or in any manner (including without limitation any method of storage) which would render the insurance thereon void or the insurance risk more hazardous or cause the State Board of insurance or other insurance authority to disallow any sprinkler credits.

5. TAXES. Landlord agrees to pay before they become delinquent all taxes, assessments and governmental charges of any kind and nature whatsoever lawfully levied or assessed against the building and the ground, parking areas, driveways, and alleys around the building.

6. LANDLORD'S REPAIRS. Landlord shall at his expense maintain only the roof, foundation and the structural soundness of the exterior walls of the building in good repair, reasonable wear and tear excepted. Tenant shall repair and pay for any damage caused by the negligence of Tenant, or Tenant's employees, agents or invitees, or caused by Tenant's default hereunder. The term "walls" as used herein shall not include windows, glass or plate glass, doors, special store fronts or office entries. Tenant shall immediately give Landlord written notice of defect or need for repairs, after which Landlord shall have reasonable opportunity to repair same or cure such defect. Landlord's liability with respect to any defects, repairs or maintenance for which Landlord is responsible under any of the provisions of this lease shall be limited to the cost of such repairs or maintenance or the curing of such defect.

#### 7. TENANT'S REPAIRS.

A. Tenant shall at its own cost and expense keep and maintain all parts of the premises (except those for which Landlord is expressly responsible under the terms of this lease) in good condition, promptly making all necessary repairs and replacements, including but not limited to, windows, glass and plate glass, doors, any special office entry, interior wells and finish work, floors and floor covering, downspouts, gutters, heating and air conditioning systems, dock boards, truck doors, dock bumpers, paving, plumbing work and fixtures, termite and pest extermination, regular removal of trash and debris, including rail spur areas, keeping the parking areas, driveways, alleys and the whole of the premises in a clean and sanitary condition, and maintaining any spur tracks serving the premises (Tenant agrees to sign a joint maintenance agreement with the railroad company servicing the premises, if requested by the railroad company), Tenant shall not be obligated to repair any damage caused by fire, tornado or other casualty covered by the insurance to be maintained by Landlord pursuant to subparagraph 13 (A) below, except the Tenant shall be obligated to repair all wind damage to glass except with respect to tornado or hurricane damage.

B. Tenant shall not damage any demising wall or disturb the integrity and support provided by any demising wall and shall, at its sole cost and expense, promptly repair any damage or injury to any demising wall caused by Tenant or its employees, agents or invitees.

C. In the event the premises constitute a portion of a multiple occupancy building, Tenant and its employees, customers and licensees shall have the exclusive right to use the parking areas, if any, as may be designated by Landlord in writing, subject to such reasonable rules and regulations as Landlord may from time to time prescribe and subject to rights of ingress and egress of other tenants, Landlord shall not be responsible for enforcing Tenant's exclusive parking rights against any third parties. Further, in multiple occupancy buildings, Landlord reserves the right to perform the paving and landscape maintenance, exterior painting and common sewage line plumbing

which are otherwise Tenant's obligations under subparagraph A above, and Tenant shall, in lieu of the obligations set forth under subparagraph A above and with respect to such items, be liable for its proportionate share (as defined in subparagraph 3 (B) (above) of the cost and expense of the care for the grounds around the building, including but not limited to, the mowing of grass, care of shrubs, general landscaping, maintenance of parking areas, driveways and alleys, exterior repainting and common sewage line plumbings provided that if Tenant or any other particular tenant of the building can be clearly identified as being responsible for obstructions or stoppage of the common sanitary sewage line, then Tenant, if Tenant is responsible, or such other responsible tenant, shall pay the entire cost thereof, upon demand, as additional rent, Tenant shall pay when due its share, determined as aforesaid, of such costs and expenses along with the other tenants of the building to Landlord upon demand, as additional rent, for the amount of its share as aforesaid of such costs and expenses in the event Landlord elects to perform or cause to be performed such work.

D. In the event the premises constitute a portion of a multiple occupancy building, Landlord shall have the right to coordinate any repairs and other maintenance of any rail tracks serving or to serve the building, and if Tenant uses such rail tracks, Tenant shall reimburse Landlord from time to time upon demand, as additional rent, for a share of the costs of such repairs and maintenance and any other sums specified in any agreement to which Landlord is a party respecting such tracks, such share to be a fraction, the numerator of which is the space contained in the premises, and the denominator of which is the entire space occupied by rail users in the building.

E. Tenant shall, at his own cost and expense, enter into a regularly scheduled preventive maintenance service contract with a maintenance contractor for servicing all hot water, heating and air conditioning systems and equipment within the premises. The maintenance contractor and the contract must be approved by Landlord. The service contract must include all services suggested by the equipment manufacturer within the operations/maintenance manual and must become effective (and a copy thereof delivered to Landlord) within thirty (30) days of the date Tenant takes possession of the premises.

8. ALTERATIONS. Tenant shall not make any alterations, additions or improvements to the premises (including but not limited to roof and wall penetrations) without the prior written consent of Landlord. Tenant may, without the consent of Landlord, but at its own cost and expense and in a good workmanlike manner erect such shelves, bins, machinery and trade fixtures as it may deem advisable, without altering the basic character of the building or improvements and without overloading or damaging such building or improvements, and in each case complying with all applicable governmental laws, ordinances, regulations and other requirements. All alterations, additions, improvements and partitions erected by Tenant shall be and remain the property of Tenant during the term of this lease and Tenant shall, unless Landlord otherwise elects as hereinafter provided, remove all alterations, additions, improvements and partitions erected by Tenant and restore the premises to their original condition by the date of termination of this lease and Tenant shall, unless however, that if Landlord so elects prior to termination of this lease or upon earlier vacating of the premises, such alterations, additions, improvements and partitions shall become the property of Landlord as of the date of termination of this lease or upon earlier vacating of the premises and shall be delivered up to the Landlord with the premises. All shelves, bins, machinery and trade fixtures installed by Tenant may be removed by Tenant prior to the termination of this lease if Tenant so elects, and shall be removed by the date of termination of this lease or upon earlier vacating of the premises if required by Landlord; upon any such removal Tenant shall restore the premises to their original condition. All such removals and restoration shall be accomplished in a good workmanlike manner so as not to damage the primary structure or structural qualities of the buildings and other improvements situated on the premises.

9. SIGNS. Tenant shall have the right to install signs upon the premises only when first approved in writing by Landlord and subject to any applicable governmental laws, ordinances, regulations and other requirements, Tenant shall remove all such signs by the termination of this lease. Such installations and removals shall be made in such manner as to avoid injury or defacement of the building and other improvements, and Tenant shall repair any injury or defacement, including without limitation discoloration, caused by such installation and/or removal.

10. INSPECTION. Landlord and Landlord's agents and representatives shall have the right to enter and inspect the premises at any reasonable time during business hours, for the purpose of ascertaining the condition of the premises or in order to make such repairs as may be required or permitted to be made by Landlord under the terms of this lease. During the period that is six (6) months prior to the end of the term hereof, Landlord and Landlord's agents and representatives shall have the right to enter the premises at any reasonable time during business hours for the purpose of showing the premises and shall have the right to erect on the premises a suitable sign indicating the premises are available. Tenant shall give written notice to Landlord at least thirty (30) days prior to vacating the premises and shall arrange to meet with Landlord for a joint inspection of the premises prior to vacating. In the event of Tenant's failure to give such notice or arrange such joint inspection, Landlord's inspection at or after Tenant's vacating the premises shall be conclusively deemed correct for purposes of determining Tenant's responsibility for repairs and restoration.

11. UTILITIES. Landlord agrees to provide at its cost water, electricity and telephone service connections into the premises, but Tenant shall pay for all water, gas, heat, light, water, telephone, sewer, sprinkler charges and other utilities and services used on or from the premises, together with any taxes, penalties, surcharges or the like pertaining thereto and any maintenance charges for utilities and shall furnish all electric light bulbs and tubes. If any such services are not separately metered to Tenant, Tenant shall pay a reasonable proportion as determined by Landlord of all charges jointly metered with other premises. Landlord shall in no event be liable for any interruption or failure of utility services on the premises.

12. ASSIGNMENT AND SUBLETTING. Tenant shall not have the right to assign this lease or to sublet the whole or any part of the premises without the prior written consent of Landlord. Notwithstanding any permitted assignment of subletting, Tenant shall at all times remain directly, primarily and fully responsible and liable for the payment of the rent herein specified and for compliance with all of its other obligations under the terms, provisions and covenants of this lease. Upon the occurrence of an "event of default" as hereinafter defined, if the premises or any part thereof are then assigned or sublet, Landlord, in addition to any other remedies herein provided, or provided by law, may at its option collect directly from such assignee its subtenant all rents becoming due to Tenant under such assignment or sublease and apply such rent against any sums due to Landlord from Tenant hereunder, and no such collection shall be construed to constitute a novation or a release of Tenant from the further performance of Tenant's obligations hereunder.

13. FIRE AND CASUALTY DAMAGE.

A. Landlord agrees to maintain standard fire and extended coverage insurance covering the building of which the premises are a part in an amount not less than 80% (or such greater percentage as may be necessary to comply with the provisions of any co-insurance clauses of the policy) of the "replacement cost" thereof as such terms is defined in the Replacement Cost Endorsement to be attached thereto, insuring against the perils of Fire, Lighting and Extended Coverage, such coverages and endorsements to be as defined, provided and limited in the standard bureau forms prescribed by the insurance regulatory authority for the State in which the premises are situated for use by insurance companies admitted in such state for the writing of such insurance on risks located within such state. Subject to the provisions of subparagraphs 13 (C), 13 (D) and 13 (E) below, such insurance shall be for the sole benefit of Landlord and under its sole control.

B. If the buildings situated upon the premises should be damaged or destroyed by fire, tornado or other casualty, Tenant shall give immediate written notice thereof to Landlord.

C. If the buildings situated upon the premises should be totally destroyed by fire, tornado or other casualty, or if they should be so damaged thereby that rebuilding or repairs cannot in Landlord's estimation be completed within two hundred (200) days after the date upon which Landlord is notified by Tenant of such damage, this lease shall terminate and the rent shall be abated during the unexpired portion of this lease, effective upon the date of the occurrence of such damage.

D. If the buildings situated upon the premises should be damaged by any peril covered by the insurance to be provided by Landlord under subparagraph 13 (A) above, but only to such extent that rebuilding or repairs can in Landlord's estimation be completed within two hundred (200) days after the date upon which Landlord is notified by Tenant of such damage, this lease shall not terminate, and Landlord shall at its sole cost and expense thereupon proceed with reasonable diligence to rebuild and repair such buildings to substantially the condition in which they existed prior to such damage, except that Landlord shall not be required to rebuild, repair or replace any part of the partitions, fixtures, additions and other improvements which may have been placed in, on or about the premises by Tenant. If the premises are untenable in whole or in part following such damage, the rent payable hereunder during the period in which they are untenable shall be reduced to such extent as may be fair and reasonable under all of the circumstances. In the event that Landlord should fail to complete such repairs and rebuilding within two hundred (200) days after the date upon which Landlord is notified by Tenant of such damage, Tenant may at its option terminate this lease by delivering written notice of termination to Landlord as Tenant's exclusive remedy, whereupon all rights and obligations hereunder shall cease and terminate.

E. Notwithstanding anything herein to the contrary, in the event the holder of any indebtedness secured by a mortgage of deed of trust covering premises requires that the insurance proceeds be applied to such indebtedness, then Landlord shall have the right to terminate this lease by delivering written notice of termination to Tenant within fifteen (15) days after such requirement is made by any such holder, whereupon all rights and obligations hereunder shall cease and terminate.

F. Each of Landlord and Tenant hereby releases the other from any loss or damage to property caused by fire or any other perils insured through or under them by way of subrogation or otherwise for any loss or damage to property caused by fire or any other perils insured in policies of insurance covering such property, even if such loss or damage shall have been caused by the fault or negligence of the other party, or anyone for whom such party may be responsible; provided, however, that this release shall be applicable and in force and effect only with respect to loss or damage occurring during such times as the releasor's policies shall contain a clause or endorsement to the effect that any such release shall not adversely affect or impair said policies or prejudice the right of the releasor to recover thereunder and then only to the extent of the insurance proceeds payable under such policies. Each of the Landlord and Tenant agrees that it will request its insurance carriers to include in its policies such a clause or endorsement. If extra cost shall be charged therefor, each party shall advise the other thereof and of the amount of the extra cost, and the other party, at its election, may pay the same, but shall not be obligated to do so.

14. LIABILITY. Landlord shall not be liable to Tenant or Tenant's employees, agents, patrons or visitors, or to any other person whomsoever, for any injury to person or damage to property on or about the premises, resulting from and/or caused in part or whole by the negligence or misconduct of Tenant, its agents, servants or employees, or of any other person entering upon the premises, or caused by the buildings and improvements located on the premises becoming out of repair, or caused by leakage of gas, oil, water or steam or by electricity emanating from the premises, or due to any cause whatsoever, and

Tenant hereby covenants and agrees that it will at all times indemnify and hold safe and harmless the property, the Landlord (including without limitation the trustee and beneficiaries if Landlord is a trust), Landlord's agents and employees from any loss, liability, claims, suits, costs, expenses, including without limitation attorney's fees and damages, both real and alleged, arising out of any such damage or injury; except injury to persons or damage to property the sole cause of which is the negligence of Landlord or the failure of Landlord to repair any part of the premises which Landlord is obligated to repair and maintain hereunder within a reasonable time after the receipt of written notice from Tenant of needed repairs. Tenant shall procure and maintain throughout the term of this lease a policy or policies of insurance, at its sole cost and expense, insuring both Landlord and Tenant against all claims, demands or actions arising out of or in connection with: (I) the premises; (II) the condition of the premises; (III) Tenant's operations in and maintenance and use of the premises; and (IV) Tenant's liability assumed under this lease, the limits of such policy or policies to be in the amount of not less than \$300,000 per occurrence in respect of injury to persons (including death), and in the amount of not less than \$50,000 per occurrence in respect of property damage or destruction, including loss of use thereof. All such policies shall be procured by Tenant from responsible insurance companies satisfactory to Landlord. Certified copies of such policies, together with receipt evidencing payment of premium therefor, shall be delivered to Landlord prior to the commencement date of this lease. Not less than fifteen (15) days prior to the expiration date of any such policies, certified copies of the renewals thereof (bearing notations evidencing the payment of renewal premiums) shall be delivered to Landlord. Such policies shall further provide the not less than thirty (30) days written notice shall be given to Landlord before such policy may be cancelled or changed to reduce insurance provided thereby.

#### 15. CONDEMNATION.

A. If the whole or any substantial part of the premises should be taken for any public or quasi-public use under governmental law, ordinance or regulation, or by right of eminent domain, or by private purchase in lieu thereof and the taking would prevent or materially interfere with the use of the premises for the purpose for which they are being used, this lease shall terminate and the rent shall be abated during the unexpired portion of this lease, effective when the physical taking of said premises shall occur.

B. If part of the premises shall be taken for any public or quasi-public use under any governmental law, ordinance or regulation, or by right of eminent domain, or by private purchase in lieu thereof, and this lease is not terminated as provided in the subparagraph above, this lease shall not terminate by the rent payable hereunder during the unexpired portion of this lease shall be reduced to such extent as may be fair and reasonable under all of the circumstances.

C. In the event of any such taking or private purchase in lieu thereof, Landlord and Tenant shall each be entitled to receive and retain such separate awards and/or portion of lump sum awards as may be allocated to their respective interests in any condemnation proceedings.

16. HOLDING OVER. Tenant will, at the termination of this lease by lapse of time or otherwise, yield up immediate possession to Landlord. If Landlord agrees in writing that Tenant may hold over after the expiration or termination of this lease, unless the parties hereto otherwise agree in writing on the terms of such holding over, the hold over tenancy shall be subject to termination by Landlord at any time upon not less than five (5) days advance written notice, or by Tenant at any time upon not less than thirty (30) days advance written notice, and all of the other terms and provisions of this lease shall be applicable during that period, except that Tenant shall pay Landlord from time to time upon demand, as rental for the period of any hold over, an amount equal to one and one-half (1 1/2) the rent in effect on the termination date, computed on a daily basis for each day of the hold over period. No holding over by Tenant, whether with or without consent of Landlord, shall operate to extend this lease except as otherwise expressly provided. The preceding provisions of this paragraph 16 shall not be constructed as Landlord's consent for Tenant to hold over.

17. QUIET ENJOYMENT. Landlord covenants that it now has, or will acquire before Tenant takes possession of the premises, good title to the premises, free and clear of all liens and encumbrances, excepting only the lien for current taxes not yet due, such mortgage or mortgages as are permitted by the terms of this lease, zoning ordinances and other conditions of record. In the event this lease is a sublease, then Tenant agrees to take the premises subject to the provisions of the prior leases. Landlord represents and warrants that it has full right and authority to enter into this lease and that Tenant, upon paying the rental herein set forth and performing its other covenants and agreements herein set forth, shall peaceably and quietly have, hold and enjoy the premises for the term hereof without hindrance or molestation from Landlord, subject to the terms and provisions of this lease.

18. EVENTS OF DEFAULT. The following events shall be deemed to be events of default by Tenant under this lease:

(a) Tenant shall fail to pay any installment of the rent herein reserved when due, or any payment with respect to taxes hereunder when due, or any other payment or reimbursement to Landlord required herein when due, and such failure shall continue for a period of five (5) days from the date such payment was due.

(b) Tenant shall become insolvent, or shall make a transfer in fraud of creditors, or shall make an assignment for the benefit of creditors.

(c) Tenant shall file a petition under any section or chapter of the National Bankruptcy Act as amended, or under any similar law or statute of the United States or any State thereof; or Tenant shall be adjudged bankrupt or insolvent in proceedings filed against Tenant thereunder.

(d) A receiver or trustee shall be appointed for all or substantially all of the assets of Tenant.

(e) Tenant shall desert or vacate any substantial portion of premises.

(f) Tenant shall fail to comply with any term, provision or covenant of this lease (other than the foregoing in this Paragraph 18), and shall not cure such failure within twenty (20) days after written notice thereof to Tenant.

19. REMEDIES. Upon the occurrence of any of such events of default described in Paragraph 18 hereof, Landlord shall have the option to pursue any one or more of the following remedies without any notice or demand whatsoever:

(a) Terminate this lease, in which event Tenant shall immediately surrender the premises to Landlord, and if Tenant fails so to do, Landlord may, without prejudice to any other remedy which it may have for possession or arrearages in rent, enter upon and take possession of the premises and expel or remove Tenant and any other person who may be occupying such premises or any part thereof, by force if necessary, without being liable for prosecution or any claim of damages therefor; and Tenant agrees to pay to Landlord on demand the amount of all loss and damage which Landlord may suffer by reason of such termination, whether through inability to relet the premises on satisfactory terms or otherwise.

(b) Enter upon and take possession of the premises and expel or remove Tenant and any other person who may be occupying such premises or any part thereof, by force if necessary, without being liable for prosecution or any claim for damages therefor, and relet the premises and receive the rent therefor; and Tenant agrees to pay to the Landlord on demand any deficiency that may arise by reason of such reletting. In the event Landlord is successful in reletting the premises at a rental in excess of that agreed to be paid by the Tenant pursuant to the terms of this lease, Landlord and Tenant each mutually agree that Tenant shall not be entitled, under any circumstances, to such excess rental, and Tenant does hereby specifically waive any claim to such excess rental.

(c) Enter upon the premises, by force if necessary, without being liable for prosecution or any claim for damages therefor, and do whatever Tenant is obligated to do under the terms of this lease; and Tenant agrees to reimburse Landlord on demand for any expenses which Landlord may incur in this effecting compliance with Tenant's obligations under this lease, and Tenant further agrees that Landlord shall not be liable for any damages resulting to the Tenant from such action, whether caused by the negligence of Landlord or otherwise.

In the event Tenant fails to pay any installment of rent hereunder as and when such installment is due, to help defray the additional cost to Landlord for processing such late payments Tenant shall pay to Landlord on demand a late charge in an amount equal to five percent (5%) of such installment; and the failure to pay such amount within ten (10) days after demand therefor shall be an event of default hereunder. The provision for such late charge shall be in addition to all of Landlord's other rights and remedies hereunder or at law and shall not be construed as a liquidated damages or as limiting Landlord's remedies in any manner.

Pursuit of any of the foregoing remedies shall not preclude pursuit of any of the other remedies herein provided or any other remedies provided by law, nor shall pursuit of any remedy herein provided constitute a forfeiture or waiver of any rent due to Landlord hereunder or of any damages accruing to Landlord by reason of the violation of any of the terms, provisions and covenants herein contained. No act or thing done by the Landlord or its agents during the term hereby granted shall be deemed a termination of this lease or an acceptance of the surrender of the premises, and no agreement to terminate this lease or accept a surrender of said premises shall be valid unless in writing signed by Landlord. No waiver by Landlord of any violation or breach of any of the terms, provisions and covenants herein contained. Landlord's acceptance of the payment of rental or other payments hereunder after the occurrence of an event of default shall not be construed as a waiver of such default, unless Landlord so notifies Tenant in writing. Forbearance by Landlord to enforce one or more of the remedies herein provided upon an event of default shall not be deemed or construed to constitute a waiver of such default or of Landlord's right to enforce any such remedies with respect to such default or any subsequent default. If, on account of any breach of default by Tenant in Tenant's obligations under the terms and conditions of this lease, it shall become necessary or appropriate for Landlord to employ or consult with an attorney concerning or to enforce or defend any of Landlord's rights or remedies hereunder, Tenant agrees to pay any reasonable attorney's fees so incurred.

20. LANDLORD'S LIEN. In addition to any statutory lien for rent in Landlord's favor, Landlord shall have and Tenant hereby grants to Landlord a continuing security interest for all rentals and other sums of money becoming due hereunder from Tenant, upon all goods, wares, equipment, fixtures, furniture, inventory, accounts, contract rights, chattel paper and other personal property of Tenant situated on the premises, and such property shall not be removed therefrom without the consent of Landlord until all arrearages in rent as well as any and all other sums of money then due to Landlord hereunder shall first have been paid and discharged. In the event of a default under this lease, Landlord shall have, in addition to any other remedies provided herein or by law, all rights and remedies under the Uniform Commercial Code, including without limitation the right to sell the property described in this Paragraph 20 at public or private sale upon five (5) days notice to Tenant. Tenant hereby agrees to execute such financing statements and other instruments necessary or desirable in Landlord's discretion to perfect the security interest hereby created. Any statutory lien for rent is not hereby waived, the express contractual lien herein granted being in addition and supplementary thereto.

21. MORTGAGES. Tenant accepts this lease subject and subordinate to any mortgage(s) and/or deed(s) of trust now or at any time hereafter constituting a

lien or charge upon the premises or the improvements situated thereon, provided, however, that if the mortgagee, trustee, or holder of any such mortgage or deed of trust elects to have Tenant's interest in this lease superior to any such instruments, releases or other documents which may be desired by any mortgagee for the purpose of subjecting and subordinating this lease to the lien of any such mortgage.

22. LANDLORD'S DEFAULT. In the event Landlord should become in default in any payments due on any such mortgage described in Paragraph 21 hereof or in the payment of taxes or any other items which might become a lien upon the premises and which Tenant is not obligated to pay under the terms and provisions of this lease, Tenant is authorized and empowered after giving Landlord five (5) days prior written notice of such default and Landlord's failure to cure such default, to pay any such items for and on behalf of Landlord, and the amount of any item so paid by Tenant for or on behalf of Landlord, together with any interest or penalty required to be paid in connection therewith, shall be payable on demand by Landlord to Tenant; provided, however, that Tenant shall not be authorized and empowered to make any payment under the terms of this Paragraph 22 unless the item paid shall be superior to Tenant's interest hereunder. In the event Tenant pays any mortgage debt in full, in accordance with this paragraph, it shall, at its election, be entitled to the mortgage security by assignment or subrogation.

23. MECHANIC'S LIENS. Tenant shall have no authority, express or implied, to create or place any lien or encumbrance of any kind or nature whatsoever upon, or in any manner to bind, the interest of Landlord in the premises or to charge the rentals payable hereunder for any claim in favor of any person dealing with Tenant, including those who may furnish materials or perform labor for any construction or repairs, and each such claim shall affect and each such lien shall attach to, if at all, only the leasehold interest granted to Tenant by this instrument. Tenant covenants and agrees that it will pay or cause to be paid all sums legally due and payable by it on account of any labor performed or materials furnished in connection with any work performed on the premises on which any lien is or can be validly and legally asserted against its leasehold interest in the premises or the improvements thereon and that it will save and hold Landlord harmless from any and all loss, cost or expense based on or arising out of asserted claims or liens against the leasehold estate or against the right, title and interest of the Landlord in the premises or under the terms of this lease.

24. NOTICES. Each provision of this instrument or of any applicable governmental laws, ordinances, regulations and other requirements with reference to the sending, mailing or delivery of any notice or the making of any payment by Landlord to Tenant or with reference to the sending, mailing delivery of any notice or the making of any payment by Tenant to Landlord shall be deemed to be complied with when and if the following steps are taken:

(a) All rent and other payments required to be made by Tenant to Landlord hereunder shall be payable to Landlord at the address hereinbelow set forth or at such other address as Landlord may specify from time to time by written notice delivered in accordance herewith Tenant's obligation to pay rent and any other amounts to Landlord under the terms of this lease shall not be deemed satisfied until such rent and other amounts have been actually received by Landlord.

(b) All payments required to be made by Landlord to Tenant hereunder shall be payable to Tenant at the address hereinbelow set forth, or at such other address within the continental United States as Tenant may specify from time to time by written notice delivered in accordance herewith.

(c) Any notice or document required or permitted to be delivered hereunder shall be deemed to be delivered whether actually received or not when deposited in the United States Mail, postage prepaid, Certified or Registered Mail, addressed to the parties hereto at the respective addresses set out below, or at such other address as they have theretofore specified by written notice delivered in accordance herewith:

LANDLORD:

TENANT:

M & B INTERESTS, INC.  
4125 SOUTHERLAND  
HOUSTON, TEXAS 77092

ATLAS AIR CONDITIONING COMPANY, INC.  
4125 SOUTHERLAND ROAD  
HOUSTON, TEXAS 77092

If and when included within the term "Landlord", as used in this instrument, there are more than one person, firm or corporation, all shall jointly arrange among themselves for their joint execution of such a notice specifying some individual at some specific address for the receipt of notices and payments to Landlord; if and when included within the term "Tenant", as used in this instrument, there are more than one person, firm or corporation, all shall jointly arrange among themselves for their joint execution of such a notice specifying some individual at some specific address within the continental United States for the receipt of notices and payments to Tenant. All parties included within the terms "Landlord" and "Tenant", respectively, shall be bound by notices given in accordance with the provisions of this paragraph to the same effect as if each had received such notice.

25. MISCELLANEOUS.

A. Words of any gender used in this lease shall be held and construed to include any other gender, and words in the singular number shall be held to include the plural, unless the context otherwise requires.

B. The terms, provisions and covenants and conditions contained in this lease shall apply to, inure to the benefit of, and be binding upon, the parties hereto and upon their respective heirs, legal representatives, successors and permitted assigns, except as otherwise herein expressly provided. Landlord shall have the right to assign any of its rights and obligations under this lease. Each party agrees to furnish to the other, promptly upon demand, a corporate

resolution, proof of due authorization by partners, or other appropriate documentation evidencing the due authorization of such party to enter into this lease.

C. The captions inserted in this lease are for convenience only and in no way define, limit or otherwise describe the scope or intent of this lease, or any provision hereof, or in any way affect the interpretation of this lease.

D. Tenant agrees from time to time within ten (10) days after request of Landlord, to deliver to Landlord, or Landlord's designee, an estoppel certificate stating that this lease is in full force and effect, the date to which rent has been paid, the unexpired term of this lease and such other matters pertaining to this lease as may be requested by Landlord. It is understood and agreed that Tenant's obligation to furnish such estoppel certificates in a timely fashion is a material inducement for Landlord's execution of this lease.

E. This lease may not be altered, changed or amended except by an instrument in writing signed by both parties hereto.

F. All obligations of Tenant hereunder not fully performed as of the expiration or earlier termination of the term of this lease shall survive the expiration or earlier termination of the term hereof, including without limitation all payment obligations with respect to taxes and insurance and all obligations concerning the condition of the premises. Upon the expiration or earlier termination of the term hereof, and prior to Tenant vacating the premises, Tenant shall pay to Landlord any amount reasonably estimated by Landlord as necessary to put the premises, including without limitation all heating and air conditioning systems and equipment therein, in good condition and repair. Tenant shall also, prior to vacating the premises, pay to Landlord the amount, as estimated by Landlord, of Tenant's obligation hereunder for real estate taxes and insurance premiums for the year in which the lease expires or terminates. All such amounts shall be used and held by Landlord for payment of such obligations of Tenant hereunder, with Tenant being liable for any additional costs therefor upon demand by Landlord, or with any excess to be returned to Tenant after all such obligations have been determined and satisfied, as the case may be. Any security deposit held by Landlord shall be credited against the amount payable by Tenant under this Paragraph 25 (F).

G. If any clause or provision of this lease is illegal, invalid or unenforceable under present or future laws effective during the term of this lease, then and in the event, it is the intention of the parties hereto that the remainder of this lease shall not be affected thereby, and it is also the intention of the parties to this lease that in lieu of each clause or provision of this lease that is illegal, invalid or unenforceable, there be added as a part of this lease contract a clause or provision as similar in terms to such illegal, invalid or unenforceable clause or provision as may be possible and be legal, valid and enforceable.

H. Because the premises are on the open market and are presently being shown, this lease shall be treated as an offer with the premises being subject to prior lease and such offer subject to withdrawal or non-acceptance by Landlord or to other use of the premises without notice, and this lease shall not be valid or binding unless and until accepted by Landlord in writing and a fully executed copy delivered to both parties hereto.

I. All references in this lease to "the date hereof" or similar references shall be deemed to refer to the last date, in point of time, on which all parties hereto have executed this lease.

26. ADDITIONAL PROVISIONS.

EXECUTED BY LANDLORD, this 1st day of OCTOBER 1994

Attest/Witness  
/s/ CHARLES I. HITT  
Title:

M & B INTERESTS, INC.  
By /s/ MICHAEL ATLAS  
Title: President

EXECUTED BY TENANT, this 1st day of OCTOBER 1994

Attest/Witness  
/s/ CHARLES I. HITT  
Title:

ATLAS AIR CONDITIONING CO.  
By: /s/ CLIFFORD STEAKLEY  
Title: Treasurer



AGREEMENT OF LEASE

BETWEEN

THOMAS J. AND BONNIE J. BEATY

LANDLORD

AND

ACCURATE AIR SYSTEMS, INC.

TENANT

=====

DATED: JULY 1, 1997

=====

PREMISES

8508 Rannie Road  
Houston, Texas 77080

AGREEMENT OF LEASE, made as of the 1st day of July, 1997, among THOMAS J. BEATY and BONNIE J. BEATY, collectively as Landlord, and ACCURATE AIR SYSTEMS, INC., a Texas corporation, having an address at 4801 Woodway Drive, Suite 300E, Houston, Texas 77056, as Tenant.

W I T N E S S E T H:

WHEREAS, the Landlord is the owner of certain premises known as and by the street address of 8508 Rannie Road, Houston, Texas (as more particularly described on Schedule "A", annexed hereto and made a part hereof) together with all buildings and other improvements thereon, and all fixtures, materials, equipment, apparatus, furniture, furnishings and other property, real and personal installed or used on the above described property or the improvements thereon; and

WHEREAS, the Landlord desires to rent the aforementioned premises to the Tenant and the Tenant desires to rent the aforementioned premises from the Landlord.

NOW, THEREFORE, in consideration of the mutual promises and covenants herein contained and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereto, for themselves, as well as their respective legal representatives, heirs, successors and assigns, hereby agree as follows:

ARTICLE 1

GLOSSARY

For the purposes of this Lease, the following terms shall have the meanings indicated below:

"ADA" shall have the meaning set forth in Section 9.1 hereof.

"ADDITIONAL RENT" shall have the meaning set forth in Section 2.2 hereof.

"ALTERATION" or "ALTERATIONS" shall mean any and all alterations, decorations, installations, repairs, improvements, additions, replacements or other physical changes of any nature whatsoever in or about the Premises at any time, now or hereafter.

"APPLICABLE RATE" shall mean the lesser of (x) three percentage points above the then current Base Rate, or (y) the maximum rate permitted by applicable law.

"BANKRUPTCY CODE" shall mean 11 U.S.C. Section 101 ET SEQ., or any statute, federal or state, of similar nature and purpose, now or hereafter.

"BASE RATE" shall mean the rate of interest publicly announced from time to time by Bank One, Texas, N.A., or its successor, as its "base rate" (or such other term as may be used by Bank One, Texas, N.A., from time to time, for the rate presently referred to as its "base rate").

"BUILDING SYSTEMS" shall mean the mechanical, electrical, sanitary, heating, air conditioning, ventilating, elevator, plumbing, life-safety and other service or support systems of any nature whatsoever located at or on the Premises, but shall not include installations made by Tenant or fixtures or appliances (regardless of whether or not such fixtures or appliances are owned by the Tenant or the Landlord).

"BUILDING INSURANCE" shall have the meaning set forth in Section 11.2 hereof.

"BUSINESS DAYS" shall mean all days, excluding Saturdays, Sundays and all days observed as holidays by the State of Texas or the federal government.

"COMMENCEMENT DATE" is July 1, 1997.

"DEFICIENCY" shall have the meaning set forth in Section 18.2(A)(2) hereof.

"EVENT OF DEFAULT" shall have the meaning set forth in Section 17.1 hereof.

"EXPIRATION DATE" shall mean the Fixed Expiration Date or such other date on which the Term ends pursuant to any of the terms, conditions or covenants of this Lease or pursuant to law.

"FIXED EXPIRATION DATE" is June 30, 2002.

"FIXED RENT" shall mean \$46,700.04 per annum (\$3,891.67 per month) for the first Lease Year (as such term is hereinafter defined) to be adjusted thereafter on each anniversary date from and after the Commencement Date in accordance with the provisions of Article 8 of this Lease.

"GOVERNMENT AUTHORITY" or "GOVERNMENT AUTHORITIES" shall mean the United States of America, the State of Texas, the county of Harris, the Municipality of Houston, and/or any political subdivision thereof and any agency, department, commission, board, bureau or instrumentality of any of the foregoing, now existing or hereafter created, having jurisdiction over the Premises or any portion thereof.

"HAZARDOUS MATERIALS" shall have the meaning set forth in Section 9.2(A) hereof.

"INCREASE NOTICE" shall have the meaning set forth in Section 8.3 hereof.

"INDEMNITEES" shall mean Landlord, his agents and contractors (and the partners, shareholders, officers, directors and employees of any of the Landlord's agents or contractors).

"INITIAL TERM" shall mean five (5) years.

"LANDLORD", on the date as of which this Lease is made, shall mean Thomas J. and Bonnie J. Beaty, but thereafter, "Landlord" shall mean any fee owner of the Premises.

"LEASE YEAR" shall mean each twelve (12) month period commencing on each anniversary date from and after the Commencement Date.

"MORTGAGE(S)" shall mean any trust indenture or mortgage which may now or hereafter affect the Premises and all extensions, supplements, amendments, modifications, consolidations,

refinancings and replacements thereof or thereto, substitutions therefor, and advances made thereunder.

"MORTGAGEE(S)" shall mean any trustee or mortgagee or holder of a Mortgage.

"NOTICE(S)" shall have the meaning set forth in Section 27.1(A) hereof.

"OPTION" or "OPTIONS" shall have the meaning set forth in Section 31.1 hereof.

"OPTION PERIOD" or "OPTION PERIODS" shall have the meaning set forth in Section 31.1 hereof.

"PARTIES" shall have the meaning set forth in Section 34.2 hereof.

"PERMITTED USE" shall mean general, executive and administrative offices, parking and related facilities in connection with Tenant's business as a air conditioning systems business and uses related thereto including the evolution of the Tenant's business consistent with the evolution of the air conditioning systems industry in general.

"PERSON(S) OR PERSON(S)" shall mean any natural person or persons, a partnership, a corporation and any other form of business or legal association or entity.

"PERSONS WITHIN TENANT'S CONTROL" shall mean and include Tenant, all of Tenant's respective shareholders, directors, officers, agents, contractors, sub-contractors, servants, employees, licensees and invitees as well as any of the heirs, successors, representatives and assigns of any of the foregoing.

"PREMISES" shall mean all that certain plot, piece and parcel of land, known as and by the street address of 8508 Rannie Road, Houston, Texas 77080 (as more particularly described on Schedule "A", annexed hereto and made a part hereof) together with all buildings and other improvements thereon and hereafter placed thereon, and all fixtures, materials, equipment, apparatus, furniture, furnishings and other property, real and personal, now or hereafter installed or used on the above described property or the improvements thereon.

"PRICE INDEX" shall have the meaning set forth in Section 8.1(ii) hereof.

"RENTAL" shall mean and be deemed to include Fixed Rent, Additional Rent and any other sums payable, now or hereafter, by Tenant hereunder.

"REQUIREMENTS" shall mean (i) all present and future laws, rules, ordinances, regulations, statutes, requirements, codes and executive orders, extraordinary as well as ordinary, retroactive and prospective, of all Governmental Authorities, now existing or hereafter created, which affect, directly or indirectly, the Premises and/or the maintenance, use, operation or occupation of the Premises, (ii) all requirements, obligations and conditions of all instruments of record on the date of this Lease, and (iii) all requirements, obligations and conditions imposed by any fire rating agency or by the carrier of Landlord's hazard insurance policy for the Premises.

"TAXES" shall have the meaning set forth in Section 3.1 hereof.

"TENANT", on the date as of which this Lease is made, shall mean the Tenant named in this Lease, but thereafter "Tenant" shall mean only the tenant under this Lease at the time in question; provided, however, that the Tenant named in this Lease and any and all successor tenant(s) hereunder shall not be released and relieved from any liability hereunder in the event of any assignment of this Lease or a sublet, in whole or in part, of the Premises.

"TENANT'S PROPERTY" shall mean Tenant's movable fixtures and movable partitions, telephone and other equipment, furniture, furnishings and other movable items of personal property owned by the Tenant.

"TERM", on the date as of which this Lease is made shall mean five (5) years, but thereafter shall be deemed to include any Option Period for which the Tenant exercises its Option pursuant to the provisions of Article 31 hereof.

"TERMINATION NOTICE PERIOD" shall have the meaning set forth in Section 27.1 hereof.

"UNAVOIDABLE DELAYS" shall have the meaning set forth in Article 25 hereof.

## ARTICLE 2

### DEMISE; PREMISES; TERM; RENT

SECTION 2.1. Landlord hereby leases to Tenant and Tenant hereby hires from Landlord the Premises for the Term to commence on the Commencement Date and to end on the Fixed Expiration Date, unless earlier terminated as provided herein.

SECTION 2.2. Commencing upon the Commencement Date, Tenant shall pay to Landlord, in lawful money of the United States of America, without notice or demand, by good and sufficient check at the office of Landlord or at such other place as Landlord may designate from time to time, the following:

(A) the Fixed Rent, as such term is defined in Article 1 hereof, which shall be payable in equal monthly installments in advance on the first day of each and every calendar month during the Term, and

(B) additional rent ("ADDITIONAL RENT") consisting of all other sums of money as shall become due from and be payable by Tenant hereunder (for default in the payment of which Landlord shall have the same remedies as for a default in the payment of Fixed Rent).

SECTION 2.3. If the Commencement Date is other than the first day of a calendar month, or the Fixed Expiration Date is other than the last day of a calendar month, Fixed Rent for such month shall be prorated on a per diem basis.

SECTION 2.4. Tenant shall pay the Fixed Rent and Additional Rent when due without notice, demand (except as provided herein) and without abatement, deduction, counterclaim, setoff or defense of any nature.

ARTICLE 3

REAL ESTATE TAXES; MORTGAGE(S)

SECTION 3.1. The Tenant represents, warrants, covenants and agrees that it shall, within five (5) days of written demand by the Landlord to the Tenant, pay to the Landlord, as Additional Rent, any and all Taxes (as hereinafter defined) of any nature whatsoever assessed or imposed against the Premises for each and every Lease Year during the Term of this Lease. The Landlord hereby agrees that any demand given by the Landlord to the Tenant pursuant to the provisions of this Section 3.1 shall include an accurate copy of the invoice, statement, bill or similar document issued by the relevant Governmental Authority or Governmental Authorities, as the case may be, with respect to the Taxes for which payment is demanded. For purposes of this Section 3.1, "TAXES" shall include, without limitation, any and all taxes assessed against the Premises, all personal property taxes, all ad valorem taxes, all license fees, all rent taxes, all levies, all penalties and any and all other taxes assessed against the Premises by any Governmental Authority, now or hereafter.

SECTION 3.2. The Tenant represents, warrants and covenants and agrees that it shall, within five (5) days of written demand by the Landlord to the Tenant, pay to the Landlord, as Additional Rent, any and all amounts which may be due and owing under and pursuant to the terms and conditions of any Mortgage or Mortgages, as the case may be, encumbering the Premises, now or hereafter, during the Term of this Lease including, but not limited to, any extensions, supplements, amendments, modifications, consolidations, refinancings and replacements of any such Mortgage or Mortgages provided that:

(A) the principal balance of any Mortgage subsequent to any extension, supplement, amendment, modification, consolidation, refinancing or replacement shall not exceed the outstanding principal balance of the Mortgage which is to be extended, supplemented, amended, modified, consolidated, refinanced or replaced at the time of such extension, supplement, amendment, modification, consolidation, refinancing or replacement, as the case may be; and

(B) the amount of the monthly payments of principal and interest payable pursuant to the terms and conditions of any Mortgage subsequent to any extension, supplement, amendment, modification, consolidation, refinancing or replacement shall not exceed the amount of the monthly payments with respect to the Mortgage which is to be extended, supplemented, amended, modified, consolidated, refinanced or replaced at the time of such extension, supplement, amendment, modification, consolidation, refinancing or replacement, as the case may be; and

(C) the terms of any extended, supplemented, amended, modified, consolidated, refinanced or replaced Mortgage shall be no more financially onerous than the provisions of such Mortgage prior to such extension, supplement, amendment, modification, consolidation, refinancing or replacement, as the case may be; and

(D) the term of any Mortgage extended, supplemented, amended, modified, consolidated, refinanced or replaced shall be no less than the term of such Mortgage prior to such

extension, supplementation, amendment, modification, consolidation, refinancing or replacement, as the case may be.

Notwithstanding anything contained herein to the contrary, the provisions of this Section 3.2 shall not apply with respect to any amounts which may be due and owing under and pursuant to the terms and conditions of any Mortgage securing additional indebtedness (above and beyond any Mortgage or Mortgages existing as of the date hereof) which first becomes a recorded lien on the Premises subsequent to the date of this Lease and which is executed and delivered by the Landlord without the consent of the Tenant. The Landlord hereby agrees that any demand given by the Landlord to the Tenant for payment of Additional Rent pursuant to the provisions of this Section 3.2 shall include, only to the extent provided to the Landlord by the Mortgagee, an accurate copy of the invoice, statement, bill or similar document issued by such Mortgagee or Mortgagees, as the case may be, with respect to any amount for which payment of Additional Rent is demanded by the Landlord under and pursuant to the provisions of this Section 3.2.

#### ARTICLE 4

##### UTILITIES

SECTION 4.1. The Tenant represents, warrants, covenants and agrees that it shall, within five (5) days of written demand by the Landlord to the Tenant, pay to the Landlord, as Additional Rent, any and all charges incurred by the Landlord for any and all utilities supplied to the Premises including, without limitation, telephone, electricity, water, heating oil and/or natural gas. The Landlord hereby agrees that any demand given by the Landlord to the Tenant pursuant to the provisions of this Section 4.1 shall include an accurate copy of the invoice, statement, bill or similar document issued by the public utility or any private company providing such utility, as the case may be, with respect to any utility for which payment is demanded.

SECTION 4.2. Landlord shall not be liable in any way to Tenant for any interruption or failure of or defect in the supply or character of any utility furnished to the Premises, now or hereafter, or for any loss, damage or expense Tenant may sustain if either the quantity or character of any utility is changed or is no longer suitable for Tenant's requirements, whether by reason of any requirement, act or omission of the public utility serving the Premises or for any other reason whatsoever. Notwithstanding the provisions of this Section 4.2, the Landlord shall be responsible for any and all actual damages suffered by the Tenant as a result of any interruption of utility service caused solely by the Landlord's failure to remit (prior to the expiration of any applicable grace period) to the appropriate public utility or private company providing such utility, as the case may be, any amount which has been paid by the Tenant to the Landlord pursuant to the provisions of Section 4.1 hereof.

SECTION 4.3. Tenant shall at all times comply with the rules, regulations, terms and conditions applicable to service, equipment, wiring, as well as any and all requirements of the public utility supplying electricity to the Premises. Tenant shall not, without Landlord's prior written consent in each instance (which consent may be withheld by the Landlord in its reasonable discretion), connect any fixtures, machinery, appliances or equipment to the Premises electric distribution system or make any alteration or addition to Tenant's machinery, appliances or equipment, or the electric system of the Premises, if the effect thereof would be to increase the electrical load in the Premises. Should Landlord grant such consent, all additional risers or

other equipment required therefor shall be provided by Landlord and the cost thereof shall be deemed Additional Rent due hereunder and shall be forthwith paid by Tenant within five (5) days of Landlord's written demand.

SECTION 4.4. If any Taxes are imposed upon Landlord with respect to any utility furnished as a service to Tenant by any Governmental Authority, Tenant agrees that such Taxes shall be reimbursed by Tenant to Landlord within five (5) days of written demand. The Landlord hereby agrees that any demand given by the Landlord to the Tenant pursuant to the provisions of this Section 4.4 shall include an accurate copy of the invoice, statement, bill or similar document issued by the relevant Governmental Authority or Governmental Authorities, as the case may be, with respect to the Taxes for which payment is demanded.

#### ARTICLE 5

##### USE AND OCCUPANCY

SECTION 5.1. Tenant shall use and occupy the Premises for the Permitted Use and for no other purpose of any nature whatsoever.

#### ARTICLE 6

##### ALTERATIONS

##### SECTION 6.1.

(A) (1) Prior to making any Alterations, Tenant shall (i) submit to Landlord detailed plans and specifications for approval by the Landlord (including layout, architectural, electrical, mechanical and structural drawings) and that comply with all Requirements for each proposed Alteration, and Tenant shall not commence any such Alteration without first obtaining Landlord's approval of such plans and specifications, (ii) at Tenant's expense, obtain all permits, approvals and certificates required by any Governmental Authorities, and (iii) furnish to Landlord duplicate original policies or certificates thereof for worker's compensation insurance (covering all persons to be employed by Tenant, and Tenant's contractors and subcontractors, in connection with such Alteration) and commercial general liability insurance (including premises operation, bodily injury, personal injury, death, independent contractors, products and completed operations, broad form contractual liability and broad form property damage coverages) in such form, with such companies, for such periods and in such amounts as Landlord may reasonably approve, naming Landlord and its agents and any Mortgagee, as additional insureds. Upon completion of such Alteration, Tenant, at Tenant's expense, shall obtain certificates of final approval of such Alterations required by any Governmental Authority and shall furnish Landlord with copies thereof, together with the "as-built" plans and specifications for such Alterations. All Alterations shall be made and performed in accordance with the plans and specifications therefor as approved by Landlord and otherwise in accordance with all Requirements. All materials and equipment to be incorporated in the Premises as a result of any Alterations shall be first quality and no such materials or equipment shall be subject to any lien, encumbrance, chattel mortgage, title retention or security agreement.

(2) Landlord reserves the right to disapprove any plans and specifications, in whole or in part, to reserve approval of items shown thereon pending its review and approval of other plans and specifications, and to condition its approval upon Tenant making revisions to the plans and specifications or supplying additional information. Tenant agrees that any review or approval by Landlord of any plans and/or specifications with respect to any Alteration is solely for Landlord's benefit, and without any representation or warranty whatsoever to Tenant or any other Person with respect to the adequacy, correctness or sufficiency thereof or with respect to Requirements or otherwise.

(B) All Alterations shall become a part of the Premises and shall be Landlord's property from and after the installation thereof and may not be removed or changed without Landlord's prior written consent. Notwithstanding the foregoing, Landlord, upon notice given at least thirty (30) days prior to the Expiration Date or upon such shorter notice as is reasonable under the circumstances upon the earlier expiration of the Term, may require Tenant to remove any specified Alterations and to repair and restore in a good and workmanlike manner any damage to the Premises caused by such removal all at Tenant's sole cost and expense. All Tenant's Property shall remain the property of Tenant and, on or before the Expiration Date or earlier end of the Term, may be removed from the Premises by Tenant at Tenant's sole cost and expense; provided, however, that Tenant shall repair and restore in a good and workmanlike manner any damage to the Premises caused by such removal. The provisions of this Section 6.1(B) shall survive the expiration or earlier termination of this Lease.

(C) (1) Any and all Alterations shall be performed, at Tenant's sole cost and expense, by contractors, subcontractors or mechanics previously approved in writing by Landlord. Prior to making an Alteration, at Tenant's request, Landlord shall furnish Tenant with a list of contractors who may perform Alterations to the Premises on behalf of Tenant.

(2) Notwithstanding the terms and conditions of Section 6.1(C)(1) hereof, with respect to any Alteration affecting any Building Systems, (i) Tenant shall only employ Landlord's designated contractor, and (ii) the Alteration shall, at Tenant's expense, be designed by Landlord's engineer.

(D) (1) Any mechanic's lien filed against the Premises for work claimed to have been done for, or materials claimed to have been furnished to, Tenant shall be canceled or discharged by Tenant, at Tenant's expense, within twenty (20) days after such lien shall be filed, by payment or filing of the bond required by law, and Tenant shall indemnify and hold Landlord harmless from and against any and all costs, expenses, claims, losses or damages resulting therefrom by reason thereof.

(2) If Tenant shall fail to discharge such mechanic's lien within the aforesaid period, then, in addition to any other right or remedy of Landlord, Landlord may, but shall not be obligated to, discharge the same either by paying the amount claimed to be due or by procuring the discharge of such lien by deposit in court or bonding, and in any such event, Landlord shall be entitled, if Landlord so elects, to compel the prosecution of an action for the foreclosure of such mechanics lien by the lienor and to pay the amount of the judgment, if any, in favor of the lienor, with interest, costs and allowances.



(3) Any amount paid by Landlord for any of the aforesaid charges and for all expenses of Landlord (including, but not limited to, attorneys' fees and disbursements) incurred in defending any such action, discharging said lien or in procuring the discharge of said lien, with interest on all such amounts at the maximum legal rate of interest then chargeable to Tenant from the date of payment, shall be repaid by Tenant within ten (10) days after written demand therefor, and all amounts so repayable, together with such interest, shall be considered Additional Rent.

SECTION 6.2. Landlord, at Tenant's expense, and upon the request of Tenant, shall join in any applications for any permits, approvals or certificates required to be obtained by Tenant in connection with any permitted Alteration (provided that the provisions of the applicable Requirements shall require that Landlord join in such application) and shall otherwise cooperate with Tenant in connection therewith; provided, however, that Landlord shall not be obligated to incur any cost or expense or liability in connection therewith.

SECTION 6.3. Tenant shall furnish to Landlord copies of records of all Alterations and of the cost thereof within fifteen (15) days after the completion of such Alterations.

SECTION 6.4. Tenant shall not, at any time prior to or during the Term, directly or indirectly, employ, or permit the employment of, any contractor, mechanic or laborer in the Premises, whether in connection with any Alteration or otherwise, if such employment would interfere or cause any conflict with other contractors, mechanics or laborers engaged in the construction, maintenance or operation of the Premises by Landlord, Tenant or others, or of any other property owned by Landlord. In the event of any such interference or conflict, Tenant, upon demand of Landlord, shall cause all contractors, mechanics or laborers causing such interference or conflict to leave the Premises immediately.

## ARTICLE 7

### REPAIRS; REPLACEMENTS; MAINTENANCE

SECTION 7.1. Tenant, at Tenant's sole cost and expense, shall take good care of the Premises and the fixtures, equipment and appurtenances therein and make all repairs and replacements thereto, both structural and non-structural, of any nature whatsoever as and when needed to preserve them in good working order and condition, except for (a) reasonable wear and tear and (b) obsolescence. If Tenant shall fail, after five (5) days notice (or such shorter period as may be required because of an emergency), to proceed with due diligence to make repairs required to be made by Tenant, the same may be made by Landlord, at the expense of Tenant, and the expenses thereof incurred by Landlord, with interest thereon at the Applicable Rate, shall be paid to Landlord, as Additional Rent, within ten (10) days after rendition of a bill or statement therefor. Tenant shall give Landlord prompt notice of any defective condition in any Building Systems located in, servicing or passing through the Premises.

ARTICLE 8

INCREASES IN FIXED RENT

SECTION 8.1. For purposes of the Lease:

(i) "BUREAU" shall mean the Federal Bureau of Labor Statistics or any successor agency that shall issue the indices or data referred to in subparagraph (ii) below.

(ii) "PRICE INDEX" shall mean the Consumer Price Index for All Urban Consumers for the Houston, Texas geographic area, 1982-1984=100, issued from time to time by the Bureau or any other successor measure hereafter employed by the Bureau in lieu of such price index that measures the cost of living for such geographic area, failing such successor, the most nearly comparable index (reflecting changes in costs of housing including rental housing, energy and services), published by a Governmental Authority, appropriately adjusted. Furthermore, if hereafter the Price Index is converted to a different standard reference base or a substantial change is made in the terms or number of items contained therein, the Price Index shall be adjusted (with the use of such conversion factor, formula or table as is published by the Bureau, or if it shall not publish same, the conversion factor published by Prentice Hall, Inc., or, failing such publication, by any other nationally recognized publisher of similar statistical information) to the figure that would have resulted if not for such conversion or change.

(iii) "APPLICABLE PRICE INDEX" for a Lease Year shall mean the Price Index issued for August of the year in which such Lease Year commences.

SECTION 8.2. (A) Tenant shall pay to Landlord Fixed Rent in the amount set forth in Article 1 of this Lease for the first Lease Year.

(B) For each Lease Year subsequent to the first Lease Year (and for each and every Lease Year thereafter during the Term hereof), the Tenant shall pay to the Landlord, as Fixed Rent, an amount equal to the greater of:

(i) an amount equal to the sum of (x) the percentage by which the Applicable Price Index for such Lease Year exceeds the Applicable Price Index for the immediately preceding Lease Year, multiplied by the Fixed Rent payable for such immediately preceding Lease Year and (y) such Fixed Rent payable for the immediately preceding Lease Year (e.g., if the Base Index is 200, the Applicable Price Index for the second Lease Year is 203, the Applicable Price Index for the third Lease Year is 215, and the Fixed Rent payable for the second Lease Year is \$50,000.00, then the Applicable Price Index for the third Lease Year exceeds the Applicable Price Index for the second Year by 5.91% (i.e., the difference between 203 and 215), and the Fixed Rent derived from the aforesaid calculation shall be \$52,955.75 (5.91% of \$50,000.00, \$2,955.00, plus \$50,000.00); or

(ii) an amount equal to the Fixed Rent for the immediately preceding Lease Year.

The Landlord and the Tenant hereby acknowledge that it is the mutual intention of the parties that for each and every Lease Year subsequent to the first Lease Year during the Term hereof,

the Fixed Rent payable by the Tenant to the Landlord hereunder shall never be decreased from the prior Lease Year.

SECTION 8.3. Upon notice by the Landlord to the Tenant of an increase in the Fixed Rent pursuant to the provisions of this Article 8 ("INCREASE NOTICE"), the Tenant shall pay the Fixed Rent as set forth in the Increase Notice.

## ARTICLE 9

### REQUIREMENTS OF LAW

SECTION 9.1. Tenant shall not do, and shall not permit any act or thing in or upon the Premises which will invalidate or be in conflict with the certificate of occupancy for the Premises or violate any Requirements. Tenant shall, at Tenant's sole cost and expense, immediately take all action, including but not limited to, making any required Alterations necessary to comply with all Requirements [including, but not limited to, the Americans With Disabilities Act of 1990 (the "ADA"), as modified and supplemented from time to time] which shall or may impose any violation, order or duty upon Landlord or Tenant arising from, or in connection with, the Premises, Tenant's occupancy, use or manner of use of the Premises (including, without limitation, any occupancy, use or manner of use that constitutes a "place of public accommodation" under the ADA), or any installations in the Premises, or required by reason of a breach of any of Tenant's covenants or agreements under this Lease, whether or not such Requirements shall now be in effect or hereafter enacted or issued, and whether or not any work required shall be ordinary or extraordinary or foreseen or unforeseen as of the date hereof.

SECTION 9.2. Tenant covenants and agrees that Tenant shall, at Tenant's sole cost and expense, comply at all times with all Requirements governing the use, generation, storage, treatment and/or disposal of any Hazardous Materials (as defined below), the presence of which results from or in connection with the act or omission of Tenant or Persons Within Tenant's Control or the breach of this Lease by Tenant or Persons Within Tenant's Control. The term "HAZARDOUS MATERIALS" shall mean any biologically or chemically active or other toxic or hazardous wastes, pollutants or substances, including, without limitation, asbestos, PCBs, petroleum products and by-products, substances defined or listed as "hazardous substances" or "toxic substances" or similarly identified in or pursuant to the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. ss. 9601 ET SEQ., and as hazardous wastes under the Resource Conservation and Recovery Act, 42 U.S.C. ss. 6010, ET SEQ., any chemical substance or mixture regulated under the Toxic Substance Control Act of 1976, as amended, 15 U.S.C. 2601, ET SEQ., any "toxic pollutant" under the Clean Water Act, 33 U.S.C. ss. 466 ET SEQ., as amended, any hazardous air pollutant under the Clean Air Act, 42 U.S.C. ss. 7401 ET SEQ., hazardous materials identified in or pursuant to the Hazardous Materials Transportation Act, 49 U.S.C. ss. 1802, ET SEQ., and any hazardous or toxic substances or pollutant regulated under any other Requirements including, without limitation, ECRA (as such term is hereinafter defined). Tenant agrees to execute, from time to time, at Landlord's request, affidavits, representations and the like concerning Tenant's best knowledge and belief regarding the presence of Hazardous Materials in, on, under or about the Premises. Tenant shall indemnify and hold harmless all Indemnitees from and against any loss, claim, cost, damage, liability or expense (including attorneys' fees and disbursements) arising by reason of any clean up, removal, remediation, detoxification action or any other activity required or recommended of any Indemnitees by any

Governmental Authority by reason of the presence in, on, under or about the Premises of any Hazardous Materials, as a result of or in connection with the act or omission of Tenant or Persons Within Tenant's Control or the breach of this Lease by Tenant or Persons Within Tenant's Control. The foregoing covenants and indemnity shall survive the expiration or any termination of this Lease.

SECTION 9.3. If Tenant shall receive notice of any violation of, or defaults under, any Requirements, liens or other encumbrances applicable to the Premises, Tenant shall give immediate written notice thereof to Landlord.

SECTION 9.4. If any governmental license or permit shall be required for the proper and lawful conduct of Tenant's business and if the failure to secure such license or permit would, in any way, affect Landlord or the Premises, then Tenant, at Tenant's expense, shall promptly procure and thereafter maintain, submit for inspection by Landlord, and at all times comply with the terms and conditions of, each such license or permit.

#### ARTICLE 10

##### SUBORDINATION

SECTION 10.1. This Lease shall at all times, now and hereafter, be subject and subordinate to each and every Mortgage, whether made prior to or after the execution of this Lease, and to all extensions, supplements, amendments, modifications, consolidations and replacements thereof or thereto, substitutions therefor, and advances made thereunder; provided, that Tenant has received from the holder of any Mortgage an agreement that Tenant will not be disturbed in its possession of the Premises, or have its rights under this Lease modified or terminated other than pursuant to the terms of this Lease. This clause shall be self-operative and no further agreement of subordination shall be required to make the interest of any Mortgagee superior to the interest of Tenant hereunder. In confirmation of such subordination, Tenant shall promptly execute and deliver, at its own cost and expense, any document, in recordable form if requested, that Landlord or any Mortgagee may request to evidence such subordination; and if Tenant fails to execute, acknowledge or deliver any such document within five (5) days after request therefor, Tenant hereby irrevocably constitutes and appoints Landlord as Tenant's attorney-in-fact, coupled with an interest, to execute, acknowledge and deliver any such document for and on behalf of Tenant. Tenant shall not do anything that would constitute a default under any Mortgage, or omit to do anything that Tenant is obligated to do under the terms of this Lease so as to cause Landlord to be in default thereunder.

SECTION 10.2. If, at any time prior to the expiration of the Term, any Mortgagee comes into possession of the Premises, by receiver or otherwise, Tenant agrees, at the election and upon demand of any owner of the Premises, or of any Mortgagee in possession of the Premises, to attorn, from time to time, to any such owner or Mortgagee or any person acquiring the interest of Landlord as a result of any such termination or as a result of a foreclosure of the Mortgage or the granting of a deed in lieu of foreclosure, upon the then executory terms and conditions of this Lease (except as provided below), for the remainder of the Term, provided that such owner or Mortgagee, as the case may be, or receiver caused to be appointed by any of the foregoing,

is then entitled to possession of the Premises. Any such attornment shall be made upon the condition that no such owner or Mortgagee shall be:

(1) liable for any act or omission of any prior landlord (including, without limitation, the then defaulting landlord); or

(2) subject to any defense or offsets (except as expressly set forth in this Lease) which Tenant may have against any prior landlord (including, without limitation, the then defaulting landlord); or

(3) bound by any payment of Rental which Tenant might have paid for more than the current month to any prior landlord (including, without limitation, the then defaulting landlord); or

(4) bound by any obligation to make any payment to Tenant which was required to be made prior to the time such owner or Mortgagee succeeded to any prior landlord's interest; or

(5) bound by any obligation to perform any work or to make improvements to the Premises except for (i) repairs to the Premises or any part thereof as a result of damage by fire or other casualty pursuant to Article 12, but only to the extent that such repairs can be reasonably made from the net proceeds of any insurance actually made available to such owner or Mortgagee and (ii) repairs to the Premises as a result of a partial condemnation pursuant to Article 13, but only to the extent that such repairs can be reasonably made from the net proceeds of any award made available to such owner or Mortgagee. Tenant, upon demand of any such owner or Mortgagee, shall execute, from time to time, agreements in confirmation of the foregoing provisions of this Section 10.2, satisfactory to any such owner or Mortgagee, and acknowledging such attornment and setting forth the terms and conditions of its tenancy. Nothing contained in this Section 10.2 shall be construed to impair any right otherwise exercisable by any such owner or Mortgagee.

SECTION 10.3. If requested by any Mortgagee or Landlord, Tenant shall promptly execute and deliver, at Tenant's own cost and expense, any document in accordance with the terms of this Article 10, in recordable form, to evidence such subordination.

SECTION 10.4. At any time and from time to time upon not less than ten (10) days' prior notice to Tenant or Landlord given by the other, or to Tenant given by a Mortgagee, Tenant or Landlord, as the case may be, shall, without charge, execute, acknowledge and deliver a statement in writing addressed to such party as Tenant, Landlord or Mortgagee, as the case may be, may designate, in form satisfactory to Tenant, Landlord or Mortgagee, as the case may be, certifying all or any of the following: (i) that this Lease is unmodified and in full force and effect (or if there have been modifications, that this Lease is in full force and effect as modified and stating the modifications); (ii) the date that the Term commenced and the date(s) that Fixed Rent and Additional Rent became payable hereunder and the dates to which they have been paid; (iii) whether or not, to the best knowledge of the signer of such certificate, Landlord is in default in performance of any of the terms of this Lease and, if so, specifying each such event of default of which the signer may have knowledge; (iv) whether or not, to the best knowledge of the signer of such certificate, Tenant has accepted possession of the Premises; (v) whether Tenant has made

any claim against Landlord under this Lease and, if so, the nature thereof and the dollar amount, if any, of such claim; (vi) either that Tenant does not know of any default in the performance of any provision of this Lease or specifying the details of any default of which Tenant may have knowledge and stating what action Tenant is taking or proposes to take with respect thereto; (vii) that, to the best knowledge of Tenant, there are no proceedings pending or threatened against Tenant before or by any court or administrative agency which, if adversely decided, would materially or adversely affect the financial condition or operations of Tenant or, if any such proceedings are pending or threatened to the best knowledge of Tenant, specifying and describing the same; and (viii) such further information with respect to the Lease or the Premises as Landlord may reasonably request or Mortgagee may require; it being intended that any such statement delivered pursuant hereto may be relied upon by any prospective purchaser of the Premises or any part thereof or of the interest of Landlord in any part thereof, by any Mortgagee or prospective Mortgagee or by any prospective assignee of any Mortgage or by any assignee of Tenant.

The failure of either Tenant or Landlord to execute, acknowledge and deliver a statement in accordance with the provisions of this Section 10.4 within said ten (10) day period shall constitute an acknowledgment by Tenant or Landlord, as the case may be, which may be relied on by any person or entity of any nature whatsoever who would be entitled to rely upon any such statement, that such statement as submitted by Landlord or Tenant, as the case may be, is true and correct.

SECTION 10.5. As long as any Mortgage exists, Tenant shall not seek to terminate this Lease by reason of any act or omission of Landlord until Tenant has given not less than thirty (30) days prior written notice of such act or omission to all Mortgagees, and if any such Mortgagee notifies Tenant within thirty (30) days following receipt of such notice of its intention to remedy such act or omission, until a reasonable period of time shall have elapsed following the giving of such notice, during which period such Mortgagee shall have the right, but not the obligation, to remedy such act or omission.

#### ARTICLE 11

##### INSURANCE; PROPERTY LOSS OR DAMAGE; REIMBURSEMENT

###### SECTION 11.1.

(A) Neither Landlord nor Landlord's agents shall be liable for any injury or damage to persons or property, or interruption of Tenant's business, resulting from fire or other casualty; nor shall Landlord or Landlord's agents be liable for any such damage caused by Persons other than the Landlord or the Landlord's agents or by construction of any private, public or quasi-public work; nor shall Landlord be liable for any latent defect in the Premises.

(B) Tenant shall give written notice to Landlord, immediately after Tenant learns thereof, of any accident, emergency, occurrence for which Landlord might be liable, fire or other casualty and all damages to or defects in the Premises for the repair of which Landlord might be responsible or which constitutes Landlord's property. Such notice shall be given by telecopy or personal delivery to the address(es) of Landlord in effect for notice.

SECTION 11.2. Tenant shall not do or permit to be done any act or thing in or upon the Premises which will invalidate or be in conflict with the terms of the State of Texas standard form of fire insurance with extended coverage, or with rental, liability, boiler, sprinkler, water damage, war risk or other insurance policies covering the Premises and the fixtures and property therein (hereinafter referred to as "BUILDING INSURANCE"); and Tenant, at Tenant's own expense, shall comply with all rules, orders, regulations and requirements of all insurance boards, and shall not do or permit anything to be done in or upon the Premises or bring or keep anything therein or use the Premises in a manner which increases the rate of premium for any of the Building Insurance or any property or equipment located therein over the rate in effect at the commencement of the Term of this Lease.

SECTION 11.3.

(A) If, by reason of any failure of Tenant to comply with the provisions of this Lease, the rate of premium for Building Insurance or other insurance on the property and equipment of Landlord shall be higher than it otherwise would be, Tenant shall reimburse Landlord for that part of the insurance premiums thereafter paid by Landlord which shall have been charged because of such failure by Tenant. Tenant shall make said reimbursement on the first day of the month following such payment by Landlord.

(B) In any action or proceeding wherein Landlord and Tenant are parties, a schedule of any insurance rate for the Premises issued by any insurance board establishing insurance premium rates for the Premises shall be prima facie evidence of the facts therein stated and of the several items and charges in the insurance premium rates then applicable to the Premises.

SECTION 11.4.

(A) Tenant shall, at Tenant's own cost and expense, obtain, maintain and keep in full force and effect during the Term, for the benefit of Landlord, any Mortgagees and Tenant, commercial general liability insurance (including premises operation, bodily injury, personal injury, death, independent contractors, products and completed operations, broad form contractual liability and broad form property damage coverages) in a combined single limit amount of not less than Five Million and 00/100 (\$5,000,000.00) Dollars, against all claims, demands or actions with respect to damage, injury or death made by or on behalf of any person or entity, arising from or relating to the conduct and operation of Tenant's business in, on or about the Premises (which shall include Tenant's signs, if any), or arising from or related to any act or omission of Tenant or of Persons Within Tenant's Control. If Tenant shall install or maintain one or more pressure vessels to serve Tenant's operations at the Premises, Tenant shall, at Tenant's own cost and expense, obtain, maintain and keep in full force and effect, for the benefit of Landlord, any Mortgagees and Tenant, appropriate boiler or other insurance coverage therefor in an amount not less than Three Million and 00/100 (\$3,000,000.00) Dollars (it being understood and agreed, however, that the foregoing shall not be deemed a consent by Landlord to the installation and/or maintenance of any such pressure vessels in the Premises, which installation and/or maintenance shall at all times be subject to the prior written consent of Landlord). Whenever, in Landlord's reasonable judgment, good business practice and changing conditions indicate a need for additional amounts or different types of insurance coverage, Tenant shall, within ten (10) days after Landlord's request, obtain such insurance coverage, at Tenant's expense.

(B) Tenant, at Tenant's sole cost and expense, shall maintain insurance protecting and indemnifying Tenant against any and all damage to or loss of any Alterations and leasehold improvements, including any made by Landlord to prepare the Premises for Tenant's occupancy, and Tenant's Property, and all claims and liabilities relating thereto.

(C) Landlord and any Mortgagees shall be named as insureds in said policies and shall be protected against all liability occasioned by an occurrence insured against. All said policies of insurance shall be: (i) written as "occurrence" policies; (ii) written as primary policy coverage and not contributing with or in excess of any coverage which Landlord may carry; and (iii) issued by reputable and independent insurance companies rated in Best's Insurance Guide, or any successor thereto (or if there be none, an organization having a national reputation) as having a general policyholder rating of "A+" and a financial rating of at least "13", and which are licensed to do business in the State of Texas. Tenant shall deliver to Landlord the policies of insurance or certificates thereof, together with evidence of payment of premiums thereon, and shall thereafter furnish to Landlord, at least thirty (30) days prior to the expiration of any such policies and any renewal thereof, a new policy or certificate in lieu thereof, with evidence of the payment of premiums thereon. Each of said policies shall also contain a provision whereby the insurer agrees not to cancel, fail to renew, diminish or materially modify said insurance policy(ies) without having given Landlord and any Mortgagees at least thirty (30) days prior written notice thereof.

(D) Tenant shall pay all premiums and charges for all of said policies, and, if Tenant shall fail to make any payment when due or carry any such policy, Landlord may, but shall not be obligated to, make such payment or carry such policy, and the amount paid by Landlord, with interest thereon (at the Applicable Rate), shall be repaid to Landlord by Tenant on demand, and all such amounts so repayable, together with such interest, shall be deemed to constitute Additional Rent hereunder. Payment by Landlord of any such premium, or the carrying by Landlord of any such policy, shall not be deemed to waive or release the default of Tenant with respect thereto.

#### SECTION 11.5.

(A) Tenant shall cause each insurance policy carried by Tenant and insuring the Premises and Tenant's Alterations, leasehold improvements, space equipment, furnishings, furniture, contents and fixtures against loss, damage or destruction by fire or other casualty, to be written in a manner so as to provide that the insurance company waives all rights of recovery by way of subrogation against Landlord or Tenant in connection with any loss or damage covered by any such policy. If the release of either Landlord or Tenant shall contravene any law with respect to exculpatory agreements, the liability of the party in question shall be deemed not released, but no action or rights shall be sought or enforced against such party unless and until all rights and remedies against the insurer are exhausted and such party shall be unable to collect such insurance proceeds.

(B) The waiver of subrogation referred to in Section 11.5(A) above shall extend to the agents and employees of each party, but-only if and to the extent that such waiver can be obtained without additional charge (unless such party shall pay such charge). Nothing contained in this Section 11.5 shall be deemed to relieve the Tenant from any duty imposed elsewhere in this Lease to repair, restore and rebuild the Premises, in whole or in part.



ARTICLE 12

DESTRUCTION BY FIRE OR OTHER CAUSE

SECTION 12.1. If the Premises or any part thereof shall be damaged by fire or other casualty, Tenant shall give immediate written notice thereof to Landlord. Landlord shall, subject to the provisions of Sections 12.2 and 12.3 below, proceed with reasonable diligence, after receipt of the net proceeds of insurance, to repair or cause to be repaired such damage at its expense, but in no event shall such repair or restoration be greater in scope than the quantity or quality of construction of the Premises as of the Commencement Date; and, if the Premises, or any part thereof, shall be rendered untenable by reason of such damage and such damage shall not be due to the fault of Tenant or Persons Within Tenant's Control, then the Fixed Rent hereunder, or an amount thereof apportioned according to the area of the Premises so rendered untenable (if less than the entire Premises shall be so rendered untenable), shall be abated for the period from the date of such damage to the date when the repair of such damage shall have been substantially completed. If Landlord or any Mortgagee shall be unable to collect the insurance proceeds (including rent insurance proceeds) applicable to such damage because of some action or inaction on the part of Tenant or Persons Within Tenant's Control, then the cost of repairing such damage shall be paid by Tenant and there shall be no abatement of Fixed Rent. Tenant covenants and agrees to cooperate with Landlord and any Mortgagee in their efforts to collect insurance proceeds (including rent insurance proceeds) payable to such parties. Landlord shall not be liable for any delay which may arise by reason of adjustment of insurance on the part of Landlord and/or Tenant, or any cause beyond the control of Landlord or contractors employed by Landlord.

It is expressly understood that if Landlord is prevented from substantially completing the repairs by reason of any acts of Tenant or Persons Within Tenant's Control, including, without limitation, by reason of the performance of any Alterations, or by reason of Tenant's failure or refusal to comply or to cause its architects, engineers, designers and contractors to comply with any of Tenant's obligations described or referred to in this Lease, then such work shall be deemed substantially completed on the date when the work would have been substantially completed but for such delay, and the expiration of the abatement of Tenant's obligations to pay Fixed Rent shall not be postponed by reason of such delay. Any additional costs to Landlord to complete any work occasioned by such delay shall be paid by Tenant to Landlord, as Additional Rent, within ten (10) days after demand therefor by Landlord.

SECTION 12.2. Landlord shall not be liable for any inconvenience or annoyance to Tenant or injury to the business of Tenant resulting in any way from damage from fire or other casualty or the repair thereof. Tenant understands that Landlord, in reliance upon Section 11.4 hereof, will not carry insurance of any kind on Tenant's furnishings, furniture, contents, fixtures, space equipment and leasehold improvements, and that Landlord shall not be obligated to repair any damage thereto or replace the same.

SECTION 12.3. (A) Notwithstanding anything to the contrary contained in Sections 12.1 and 12.2 above, in the event that:

(i) at least fifty (50%) percent of the rentable square feet of the Premises shall be damaged by a fire or other casualty so that substantial alteration or

reconstruction of the Premises shall, in Landlord's sole opinion, be required (whether or not the Premises shall have been damaged by such fire or other casualty and without regard to the structural integrity of the Premises); or

(ii) the Premises shall be totally or substantially damaged or shall be rendered wholly or substantially untenable; or

(iii) there shall be any damage to the Premises within the last two (2) years of the Term wherein the cost of repair exceeds an amount equal to three (3) monthly installments of Fixed Rent, then, as a result of any circumstances described in subparagraphs (i), (ii) or (iii) hereof, the Landlord may, in Landlord's sole and absolute discretion, terminate this Lease and the term and estate hereby granted, by notifying Tenant in writing of such termination within one hundred twenty (120) days after the date of such damage. In the event that such a notice of termination shall be given, then this Lease and the term and estate hereby granted shall expire as of the date of termination stated in said notice with the same effect as if that were the Fixed Expiration Date, and the Fixed Rent and Additional Rent hereunder shall be apportioned as of such date.

SECTION 12.4. Except as may be provided in Section 11.5, nothing herein contained shall relieve Tenant from any liability to Landlord or to Landlord's insurers in connection with any damage to the Premises by fire or other casualty if Tenant shall be legally liable in such respect.

#### ARTICLE 13

##### EMINENT DOMAIN

SECTION 13.1. If the whole of the Premises is acquired or condemned for any public or quasi-public use or purpose, this Lease and the Term shall end as of the date of the vesting of title with the same effect as if said date were the Fixed Expiration Date. If only a part of the Premises is so acquired or condemned then, (1) except as hereinafter provided in this Section 13.1, this Lease and the Term shall continue in effect but, if a part of the Premises is so acquired or condemned, from and after the date of the vesting of title, the Fixed Rent and Additional Rent, if any, shall be reduced in the proportion which the area of the part of the Premises so acquired or condemned bears to the total area of the Premises immediately prior to such acquisition or condemnation; (2) whether or not the Premises are affected thereby, Landlord, at Landlord's option, may give to Tenant, within sixty (60) days next following the date upon which Landlord receives notice of vesting of title, a thirty (30) day notice of termination of this Lease; and (3) if the part of the Premises so acquired or condemned contains more than seventy-five (75%) percent of the total area of the Premises immediately prior to such acquisition or condemnation, or if, by reason of such acquisition or condemnation, Tenant no longer has access to the Premises, Tenant, at Tenant's option, may give to Landlord, within thirty (30) days next following the date upon which Tenant receives notice of vesting of title, a thirty (30) day notice of termination of this Lease. If any such thirty (30) day notice of termination is given, by Landlord or Tenant, this Lease and the Term shall come to an end and expire upon the expiration of said thirty (30) days with the same effect as if the date of expiration of said thirty (30) days were the Fixed Expiration Date. In the event of any termination of this Lease and the Term pursuant to the provisions of this Section 13.1, the Fixed Rent or Additional Rent shall be apportioned as of

the date of sooner termination and any prepaid portion of the Fixed Rent for any period after such date shall be refunded by Landlord to Tenant.

SECTION 13.2. In the event of any such acquisition or condemnation of all or any part of the Premises, Landlord shall be entitled to receive the entire award for any such acquisition or condemnation. Tenant shall have no claim against Landlord or the condemning authority for the value of any unexpired portion of the Term and Tenant hereby expressly assigns to Landlord all of its right in and to any such award. Nothing contained in this Section 13.2 shall be deemed to prevent Tenant from making a separate claim in any condemnation proceedings for the value of any Tenant's Property included in such taking, and for any moving expenses, so long as Landlord's award is not reduced thereby.

#### ARTICLE 14

##### ASSIGNMENT; SUBLETTING; MORTGAGE; ETC.

SECTION 14.1. (A) The Tenant shall not (a) assign this Lease (whether by operation of law, transfers of interests in Tenant or otherwise); or (b) mortgage or encumber Tenant's interest in this Lease, in whole or in part; or (c) sublet, or permit the subletting of, the Premises or any part thereof. Notwithstanding the provisions of this Section 14.1, the use of the Premises by any Person affiliated (as such term is hereinafter defined) with the Tenant or under the common control (as such term is hereinafter defined) of Comfort Systems USA, Inc., as the case may be, shall not be deemed an assignment of this Lease or a sublet of the Premises; provided, however, that such use of the Premises as aforesaid shall not violate or be prohibited by any of the provisions of any Mortgage then encumbering the Premises, if any. For purposes of this Article 14, a Person shall be deemed to be an "AFFILIATE" of the Tenant or under the "COMMON CONTROL" of Comfort Systems USA, Inc. if such Person is a member of a "parent-subsidiary controlled group" [as such term is defined by Section 1563(a)(1) of the Internal Revenue Code of 1986, as amended] or a member of a "brother-sister controlled group" [as such term is defined by Section 1563(a)(2) of the Internal Revenue Code of 1986, as amended] of which either Comfort Systems USA, Inc. or the Tenant, as the case may be, is a member.

(B) Notwithstanding the provisions otherwise set forth in this Article 14, any reorganization, consolidation and/or restructuring of the Tenant in which the issued and outstanding stock of the Tenant remains under the common control (as such term is defined in Section 14.1 hereinabove) of Comfort Systems USA, Inc. shall not be deemed an assignment of this Lease or a sublet of the Premises; provided, however, that the same shall not violate or be prohibited by any of the provisions of any Mortgage then encumbering the Premises, if any.

SECTION 14.2. If Tenant's interest in this Lease shall be assigned in violation of the provisions of this Article 14, such assignment shall be invalid and of no force and effect against Landlord; provided, however, that Landlord may collect an amount equal to the then Fixed Rent plus any other item of Rental from the assignee as a fee for its use and occupancy. If the Premises or any part thereof are sublet to, or occupied by, or used by, any person other than Tenant, whether or not in violation of this Article 14, Landlord, after default by Tenant under this Lease, may collect any item of Rental or other sums paid by the subtenant, user or occupant as a fee for its use and occupancy, and shall apply the net amount collected to the Fixed Rent and the items of Rental reserved in this Lease. No such assignment, subletting, occupancy, or use,

nor any such collection or application of Rental or fee for use and occupancy, shall be deemed a waiver by Landlord of any term, covenant or condition of this Lease or the acceptance by Landlord of such assignee, subtenant, occupant or user as Tenant hereunder, nor shall the same, in any circumstances, relieve Tenant of any of its obligations under this Lease.

SECTION 14.3. Except as otherwise set forth in Section 14.1 hereof, for purposes of this Article 14, (i) any increase in the amount of issued and/or outstanding capital stock of any corporate tenant and/or the creation of one or more additional classes of capital stock of any corporate tenant, in a single transaction or a series of related or unrelated transactions, resulting in a change in the legal or beneficial ownership of such tenant so that the shareholders of such tenant existing immediately prior to such transaction or series of transactions shall no longer own a majority of the issued and outstanding capital stock of such tenant shall be deemed an assignment of this Lease and (ii) any Person or legal representative of Tenant, to whom Tenant's interest under this Lease passes by operation of law, or otherwise, shall be bound-by the provisions of this Article 14. Tenant agrees to furnish to Landlord on request at any time such information and assurances as Landlord may reasonably request that Tenant has not violated the provisions of this Article 14.

## ARTICLE 15

### ACCESS TO PREMISES

SECTION 15.1. Tenant shall permit Landlord, Landlord's agents and any public utilities servicing the Premises to erect, use and maintain, now and hereafter, concealed ducts, pipes and conduits in and through the Premises. Landlord or Landlord's agents shall have the right to enter the Premises at all reasonable times upon (except in case of emergency) reasonable prior notice, which notice may be oral, to examine the same, to show the same to prospective purchasers or Mortgagees and to make such repairs, alterations, improvements or additions (i) as Landlord may deem necessary or desirable to the Premises, or (ii) which Landlord may elect to perform at least ten (10) days after notice (except in an emergency when no notice shall be required) following Tenant's failure to make repairs or perform any work which Tenant is obligated to make or perform under this Lease, or (iii) for the purpose of complying with Requirements, and Landlord shall be allowed to take all material into and upon the Premises that may be required therefor without the same constituting an eviction or constructive eviction of Tenant in whole or in part and the Fixed Rent (and any other item of Rental) shall in no respect abate or be reduced by reason of said repairs, alterations, improvements or additions, wherever located, or while the same are being made, by reason of loss or interruption of business of Tenant, or otherwise. Landlord shall promptly repair any damage caused to the Premises by such work, alterations, improvements or additions.

SECTION 15.2. If Tenant is not present when for any reason entry into the Premises may be necessary or permissible, Landlord or Landlord's agents may enter the same without rendering Landlord or such agents liable therefor.

SECTION 15.3. Landlord also shall have the right at any time, without the same constituting an actual or constructive eviction and without incurring any liability to Tenant therefor, to change the arrangement or location of entrances or passageways, doors and doorways, and corridors, stairs, toilets or other parts of the Premises, provided any such change does not unreasonably

interfere with, or deprive Tenant of access to, the Premises; to put so-called "solar film" or other energy-saving installations on the inside and outside of the windows; and to change the name, number or designation by which the Premises is commonly known.

ARTICLE 16

CERTIFICATE OF OCCUPANCY

SECTION 16.1. Tenant shall not at any time, now or hereafter, use or occupy the Premises, directly or indirectly, in violation of the certificate of occupancy for the Premises and in the event that any Governmental Authority hereafter contends or declares by notice, violation, order or in any other manner whatsoever that the Premises are used for a purpose that is a violation of such certificate of occupancy, Tenant shall, upon three (3) Business Days' written notice from Landlord or any Government Authority, immediately discontinue such use of the Premises.

ARTICLE 17

DEFAULT

SECTION 17.1. Each of the following events shall be an "EVENT OF DEFAULT" under this Lease:

(A) if Tenant shall on any occasion default in the payment when due of any installment of Fixed Rent or Additional Rent or in the payment when due of any other item of Rental and such default shall continue for five (5) business days from and after the date when written notice has been received by Tenant; or

(B) if the Premises shall become vacant or abandoned; or

(C) if Tenant's interest in this Lease shall devolve upon or pass to any person, whether by operation of law or otherwise, except as specifically permitted by the provisions of Article 14 hereof; or

(D) (1) if Tenant shall not, or shall be unable to, or shall admit in writing Tenant's inability to, as to any obligation, pay Tenant's debts as they become due; or

(2) if Tenant shall commence or institute any case, proceeding or other action (a) seeking relief on Tenant's behalf as debtor, or to adjudicate it a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to Tenant or Tenant's debts under any existing or future law of any jurisdiction, domestic or foreign, relating to bankruptcy, insolvency, reorganization or relief of debtors, or (b) seeking appointment of a receiver, trustee, custodian or other similar official for it or for all or any substantial part of its property; or

(3) if Tenant shall make a general assignment for the benefit of creditors; or

(4) if any case, proceeding or other action shall be commenced or instituted against Tenant (a) seeking to have an order for relief entered against Tenant as debtor or to adjudicate Tenant a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to Tenant or Tenant's debts under any existing or future law of any jurisdiction, domestic or foreign, relating to bankruptcy, insolvency, reorganization or relief of debtors, or (b) seeking appointment of a receiver, trustee, custodian or other similar official for Tenant or for all or any substantial part of Tenant's property, which either (i) results in any such entry of an order for relief, adjudication of bankruptcy or insolvency or such an appointment or the issuance or entry of any other order having a similar effect or (ii) remains undismissed for a period of sixty (60) days; or

(5) if a trustee, receiver or other custodian shall be appointed for any substantial part of the assets of Tenant which appointment is not vacated or effectively stayed within thirty (30) days; or

(E) if Tenant shall default in the observance or performance of any other term, covenant or condition of this Lease on Tenant's part to be observed or performed including, without limitation, the terms and conditions of Article 27 hereof, and Tenant shall fail to remedy such default within ten (10) days after written notice by Landlord to Tenant of such default, or if such default is of such a nature that it cannot with due diligence be completely remedied within said period of ten (10) days and the continuation of which for the period required for cure will not subject Landlord to the risk of criminal liability or foreclosure of any Mortgage, if Tenant shall not, (i) within said ten (10) day period advise Landlord of Tenant's intention duly to institute all steps necessary to remedy such situation, (ii) duly institute within said ten (10) day period, and thereafter diligently and continuously prosecutes to completion all steps necessary to remedy the same and (iii) completes such remedy within such time after the date of the giving of said notice by Landlord as shall reasonably be necessary.

SECTION 17.2. If an Event of Default shall occur, Landlord may, at any time thereafter, at Landlord's option, give written notice to Tenant stating that this Lease and the Term shall expire and terminate on the date specified in such notice whereupon this Lease and the Term and all rights of Tenant under this Lease shall automatically expire and terminate as if the date specified in the notice given pursuant to this Section 17.2 were the Fixed Expiration Date and Tenant immediately shall quit and surrender the Premises, but Tenant shall remain liable for damages as provided herein or pursuant to law. Anything contained herein to the contrary notwithstanding, if such termination shall be stayed by order of any court having jurisdiction over any proceeding described in Section 17.1(D), or by federal or state statute, then, following the expiration of any such stay, or if the trustee appointed in any such proceeding, Tenant or Tenant as debtor-in-possession fails to assume Tenant's obligations under this Lease within the period prescribed therefor by law or within one hundred twenty (120) days after entry of the order for relief or as may be allowed by the court, or if said trustee, Tenant or Tenant as debtor-in-possession shall fail to provide adequate protection of Landlord's right, title and interest in and to the Premises or adequate assurance of the complete and continuous future performance of Tenant's obligations under this Lease, Landlord, to the extent permitted by law or by leave of the court having jurisdiction over such proceeding, shall have the right, at its election, to terminate this Lease on three (3) days' notice to Tenant, Tenant as debtor-in-possession or said trustee and upon the expiration of said three (3) day period this Lease shall cease and expire as aforesaid and

Tenant, Tenant as debtor-in-possession or said trustee shall immediately quit and surrender the Premises as aforesaid.

SECTION 17.3. If, at any time, (i) Tenant shall consist of two (2) or more Persons, or (ii) Tenant's obligations under this Lease shall have been guaranteed by any Person other than Tenant, or (iii) Tenant's interest in this Lease has been assigned, the word "Tenant" as used and referred to in this Lease, shall be deemed to mean any one or more of the persons primarily or secondarily liable for Tenant's obligations under this Lease. Any monies received by Landlord from or on behalf of Tenant during the pendency of any proceeding of the types referred to in Section 17.1(D) hereof shall be deemed paid as compensation for the use and occupancy of the Premises and the acceptance of any such compensation by Landlord shall not be deemed an acceptance of Rental or a waiver on the part of Landlord of any rights under Section 17.2 hereof.

## ARTICLE 18

### REMEDIES AND DAMAGES

#### SECTION 18.1.

(A) If any Event of Default shall occur, or this Lease and the Term shall expire and come to an end as provided in Article 17 hereof:

(1) Tenant shall quit and peacefully surrender the Premises to Landlord, and Landlord and its agents may immediately, or at any time after such Event of Default or after the date upon which this Lease and the Term shall expire and come to an end, re-enter the Premises or any part thereof, without notice, either by summary proceedings, or by any other applicable action or proceeding or otherwise (without being liable to indictment, prosecution or damages therefor), and may repossess the Premises and dispossess Tenant and any other persons from the Premises by summary proceedings or otherwise and remove any and all of their property and effects from the Premises (and Tenant shall remain liable for damages as provided herein or pursuant to law); and

(2) Landlord, at Landlord's option, may relet the whole or any part or parts of the Premises from time to time, either in the name of Landlord or otherwise, to such tenant or tenants, for such term or terms ending before, on or after the Fixed Expiration Date, at such rent or rentals and upon such other conditions, which may include concessions and free rent periods, as Landlord, in Landlord's sole discretion, may determine; provided, however, that Landlord shall have no obligation to relet the Premises or any part thereof and shall in no event be liable for refusal or failure to relet the Premises or any part thereof, or, in the event of any such reletting, for refusal or failure to collect any rent due upon any such reletting, and no such refusal or failure shall operate to relieve Tenant of any liability under this Lease or otherwise affect any such liability, and Landlord, at Landlord's option, may make such Alterations, in and to the Premises as Landlord, in Landlord's sole discretion, shall consider advisable or necessary in connection with any such reletting or proposed reletting, without relieving Tenant of any liability under this Lease or otherwise affecting any such liability.

(B) Tenant hereby waives the service of any notice of intention to re-enter or to institute legal proceedings to that end that may otherwise be required to be given under any

present or future law. Tenant, on its own behalf and on behalf of all persons claiming through or under Tenant, including all creditors of Tenant, does further hereby waive any and all rights that Tenant and all such persons might otherwise have under any present or future law to redeem the Premises, or to re-enter or repossess the Premises, or to restore the operation of this Lease, after (a) Tenant shall have been dispossessed by a judgment or by warrant of any court, or (b) any re-entry by Landlord, or (c) any expiration or termination of this Lease and the Term, whether such dispossession, re-entry, expiration or termination is by operation of law or pursuant to the provisions of this Lease. The words "re-entry", "re-enter" and "re-entered" as used in this Lease shall not be deemed to be restricted to their technical legal meanings. In the event of a breach or threatened breach by Tenant, or any persons claiming through or under Tenant, of any term, covenant or condition of this Lease, Landlord shall have the right to enjoin such breach and the right to invoke any other remedy allowed by law or in equity as if reentry, summary proceedings and other special remedies were not provided in this Lease for such breach. The right to invoke the remedies hereinbefore set forth are cumulative and shall not preclude Landlord from invoking any other remedy allowed at law or in equity.

SECTION 18.2.

(A) If this Lease and the Term shall expire and come to an end as provided in Article 17 hereof, or by or under any summary proceeding or any other action or proceeding, or if Landlord shall re-enter the Premises as provided in Section 18.1 hereof, or by or under any summary proceeding or any other action or proceeding, then, in any of said events:

(1) Tenant shall pay to Landlord all Fixed Rent, Additional Rent and other items of Rental payable under this Lease by Tenant to Landlord to the date upon which this Lease and the Term shall have expired and come to an end or to the date of re-entry upon the Premises by Landlord, as the case may be;

(2) Tenant also shall be liable for and shall pay to Landlord, as damages, any deficiency ("DEFICIENCY") between the Rental for the period which otherwise would have constituted the unexpired portion of the Term and the net amount, if any, of rents collected under any reletting effected pursuant to the provisions of Section 18.1(2) for any part of such period (after first deducting from the rents collected under any such reletting all of Landlord's expenses in connection with the termination of this Lease, Landlord's re-entry upon the Premises and such reletting including, but not limited to, all repossession costs, brokerage commissions, attorneys' fees and disbursements, alteration costs and other expenses of preparing the Premises for such reletting); any such Deficiency shall be paid in monthly installments by Tenant on the days specified in this Lease for payment of installments of Fixed Rent; Landlord shall be entitled to recover from Tenant each monthly Deficiency as the same shall arise, and no suit to collect the amount of the Deficiency for any month shall prejudice Landlord's right to collect the Deficiency for any subsequent month by a similar proceeding; and

(3) whether or not Landlord shall have collected any Deficiency as aforesaid, Landlord shall be entitled to recover from Tenant, and Tenant shall pay to Landlord, on demand, in lieu of any further Deficiency as and for liquidated and agreed final damages, a sum equal to the amount by which the unpaid Rental for the period which otherwise would have constituted the unexpired portion of the Term exceeds the then fair and reasonable rental value of the Premises for the same period; if, before presentation of proof of such liquidated damages



to any court, commission or tribunal, the Premises, or any part thereof, are relet by Landlord for the period which otherwise would have constituted the unexpired portion of the Term, or any part thereof, the amount of rent reserved upon such reletting shall be deemed, prima facie, to be the fair and reasonable rental value for the part or the whole of the Premises so relet during the term of the reletting.

(B) Tenant shall in no event be entitled to any rents collected or payable under any reletting, whether or not such rents exceed the Fixed Rent reserved in this Lease. Nothing contained in Article 17 hereof or this Article 18 shall be deemed to limit or preclude the recovery by Landlord from Tenant of the maximum amount allowed to be obtained as damages by any statute or rule of law, or of any sums or damages to which Landlord may be entitled in addition to the damages set forth in this Section 18.2.

#### ARTICLE 19

##### FEES AND EXPENSES

SECTION 19.1. If an Event of Default shall have occurred, Landlord may (1) perform the same for the account of Tenant, or (2) make any expenditure or incur any obligation for the payment of money in connection with any obligation owed to Landlord, including, but not limited to, reasonable attorneys fees and disbursements in instituting, prosecuting or defending any action or proceeding, and in either case the cost thereof with interest thereon at the Applicable Rate shall be deemed to be Additional Rent hereunder and shall be paid by Tenant to Landlord within ten (10) days after rendition of any bill or statement to Tenant therefor. In addition, Tenant shall pay Landlord any reasonable attorneys fees and disbursements incurred by Landlord in connection with any proceeding in which the value for the use and occupancy of the Premises by Tenant is being determined (whether or not any such proceeding results from a default by Tenant under this Lease).

SECTION 19.2. If Tenant shall fail to pay any installment of Fixed Rent, Additional Rent or any other item of Rental for a period longer than five (5) days after the same shall have become due, Tenant shall pay to Landlord, in addition to such installment of Fixed Rent, Additional Rent or other item of Rental, as the Case may be, as a late charge and as Additional Rent, a sum equal to interest at the Applicable Rate on the amount unpaid, computed from the date such payment was due, without regard to any such grace period, to and including the date of payment.

#### ARTICLE 20

##### NO REPRESENTATIONS BY LANDLORD

SECTION 20.1. LANDLORD AND LANDLORD'S AGENTS HAVE MADE NO REPRESENTATIONS, PROMISES OR WARRANTIES EXPRESS OR IMPLIED, INCLUDING WITHOUT LIMITATION, WARRANTIES OF SUITABILITY, HABITABILITY AND FITNESS FOR A PARTICULAR USE OR PURPOSE WITH RESPECT TO THE PREMISES EXCEPT AS HEREIN EXPRESSLY SET FORTH, AND NO RIGHTS, EASEMENTS OR LICENSES ARE ACQUIRED BY TENANT BY IMPLICATION OR OTHERWISE EXCEPT AS EXPRESSLY SET FORTH HEREIN. TENANT SHALL ACCEPT POSSESSION OF THE

PREMISES IN ITS "AS IS" CONDITION ON THE COMMENCEMENT DATE, AND LANDLORD SHALL HAVE NO OBLIGATION TO PERFORM ANY WORK OR MAKE ANY INSTALLATIONS IN ORDER TO PREPARE THE PREMISES FOR TENANT'S OCCUPANCY. THE TAKING OF OCCUPANCY OF THE WHOLE OR ANY PART OF THE PREMISES BY TENANT SHALL BE CONCLUSIVE EVIDENCE, AS AGAINST TENANT, THAT TENANT ACCEPTS POSSESSION OF THE SAME AND THAT THE PREMISES WERE IN GOOD AND SATISFACTORY CONDITION AT THE TIME SUCH OCCUPANCY WAS SO TAKEN. All references in this Lease to the consent or approval of Landlord shall be deemed to mean the written consent or approval executed by Landlord and no other consent or approval of Landlord shall be effective for any purpose whatsoever.

#### ARTICLE 21

##### END OF TERM

SECTION 21.1. Upon the expiration or other termination of this Lease, Tenant shall quit and surrender to Landlord the Premises, vacant, broom clean, in good order and condition, ordinary wear and tear excepted, and Tenant shall remove all of Tenant's Alterations as may be required pursuant to Article 6. Tenant shall also remove all of Tenant's Property and all other personal property and personal effects of all persons claiming through or under Tenant, and shall pay the cost of repairing all damage to the Premises occasioned by such removal. Any Tenant's Property or other personal property that remains in, on or at the Premises after the termination of this Lease shall be deemed to have been abandoned and either may be retained by Landlord as its property or may be disposed of in such manner as Landlord may see fit. If Tenant's Property or other personal property or any part thereof is sold, Landlord may receive and retain the proceeds of such sale as the property of Landlord. Any expense incurred by Landlord in removing or disposing of Tenant's Property or other personal property or Alterations required to be removed as provided in Article 6, as well as the cost of repairing all damage to the Premises caused by such removal, shall be reimbursed to Landlord by Tenant, as Additional Rent, on demand.

SECTION 21.2. If the Expiration Date falls on a day which is not a Business Day, then Tenant's obligations under Section 21.1 shall be performed on or prior to such Business Day.

SECTION 21.3. If the Premises are not surrendered upon the expiration or other termination of this Lease, Tenant hereby indemnifies Landlord against liability resulting from delay by Tenant in so surrendering the Premises, including any claims made by any succeeding tenant or prospective tenant founded upon such delay and agrees to be liable to Landlord for (i) any payment or rent concession which Landlord may be required to make to any tenant obtained by Landlord for all or any part of the Premises in order to induce such tenant not to terminate its lease by reason of the holding-over by Tenant and (ii) the loss of the benefit of the bargain if any such tenant shall terminate its lease by reason of the holding-over by Tenant.

SECTION 21.4. Tenant's obligations under this Article 21 shall survive the expiration or termination of this Lease.

ARTICLE 22

POSSESSION

SECTION 22.1. If Landlord shall be unable to deliver possession of the Premises on the Commencement Date for any reason whatsoever, Landlord shall not be subject to any liability therefor and the validity of this Lease shall not be impaired thereby nor the Expiration Date extended, but the Commencement Date shall be postponed until five (5) Business Days following notice from Landlord that the Premises are available for occupancy by Tenant. Tenant expressly waives any right to rescind this Lease under any present or future statute and further expressly waives the right to recover any damages that may result from Landlord's failure to deliver possession of the Premises on the Commencement Date.

ARTICLE 23

NO WAIVER

SECTION 23.1. No act or thing done by Landlord or Landlord's agents during the Term shall be deemed an acceptance of a surrender of the Premises, and no agreement to accept such surrender shall be valid unless in writing signed by Landlord. No employee of Landlord or of Landlord's agents shall have any power to accept the keys to the Premises prior to the termination of this Lease. The delivery of keys to any employee of Landlord or of Landlord's agents shall not operate as a termination of this Lease or a surrender of the Premises.

SECTION 23.2. The failure of Landlord to seek redress for violation of, or to insist upon the strict performance of, any covenant or condition of this Lease shall not prevent a subsequent act, which would have originally constituted a violation, from having all of the force and effect of an original violation. The receipt by Landlord of Fixed Rent, Additional Rent or any other item of Rental with knowledge of the breach of any covenant of this Lease shall not be deemed a waiver of such breach. No provision of this Lease shall be deemed to have been waived by Landlord, unless such waiver shall be in writing and shall be signed by Landlord. No payment by Tenant or receipt by Landlord of a lesser amount than the Rental then due and payable shall be deemed to be other than on account of the earliest item(s) of Rental, or as Landlord may elect to apply the same, nor shall any endorsement or statement on any check or any letter accompanying any check or payment be deemed an accord and satisfaction, and Landlord may accept such check or payment without prejudice to Landlord's right to recover the balance due of the Rental or to otherwise pursue any other remedy in this Lease provided. This Lease contains the entire agreement between the parties and all prior negotiations and agreements are merged herein. Any executory agreement hereafter made shall be ineffective to change, discharge or effect an abandonment of this Lease in whole or in part unless such executory agreement is in writing and signed by the party against whom enforcement of the change, discharge or abandonment is sought.

ARTICLE 24

WAIVER OF TRIAL BY JURY

SECTION 24.1. Tenant hereby waives trial by jury in any action or proceeding brought by or against the Tenant with respect to any matters whatsoever arising out of or in any way connected with this Lease, the relationship of Landlord and Tenant, Tenant's use or occupancy of the Premises, whether during or after the Term, or for the enforcement of any remedy under any statute, emergency or otherwise. If Landlord shall commence any summary proceeding against Tenant, Tenant will not interpose any counterclaim of whatever nature or description in any such proceeding, and will not seek to consolidate such proceeding with any other action which may have been or will be brought in any other court by Tenant or Landlord.

ARTICLE 25

INABILITY TO PERFORM

SECTION 25.1. This Lease and the obligation of Tenant to pay Rental hereunder and to perform all of the other covenants and agreements hereunder on the part of Tenant to be performed shall in no way be affected, impaired or excused because Landlord is unable to fulfill any of Landlord's obligations under this Lease, expressly or implicitly to be performed by Landlord, or because Landlord is unable to make or is delayed in making any repairs, or is unable to supply or is delayed in supplying any services, if Landlord is prevented from or delayed in so doing by reason of acts of God, casualty, strikes or labor troubles, accident, governmental preemption in connection with an emergency, Requirements, conditions of supply and demand which have been or are affected by war or other emergency, or any other cause whatsoever, whether similar or dissimilar to the foregoing, beyond Landlord's reasonable control ("UNAVOIDABLE DELAYS").

ARTICLE 26

NOTICES

SECTION 26.1.

(A) Except as otherwise expressly provided in this Lease, any bills, statements, consents, notices, demands, requests or other communications given or required to be given under this Lease ("NOTICE(S)") shall be in writing and shall be deemed sufficiently given or rendered if delivered by hand (against a signed receipt) or if deposited with a nationally recognized overnight courier and in either case addressed:

IF TO TENANT:

4801 Woodway Drive, Suite 300E  
Houston, Texas 77056

WITH A COPY TO:

Bracewell & Patterson, L.L.P.  
711 Louisiana St., Suite 2900  
Houston, Texas 77002  
Attn: Thomas W. Adkins

(a) at Tenant's address first set forth in this Lease or (b) at any place where Tenant or any agent or employee of Tenant may be found if given subsequent to Tenant's vacating, deserting, abandoning or surrendering the Premises, and

IF TO LANDLORD:

17402 Bending Cypress  
Cypress, Texas 77429

and any Mortgagee who may have requested the same, by Notice given in accordance with the provisions of this Article 26, at the address designated by such Mortgagee,

or to such other address(es) as either Landlord or Tenant may designate as its new address(es) for such purpose by notice given to the other in accordance with the provisions of this Article 26.

(B) Notices shall be deemed to have been rendered or given (a) on the date delivered, if delivered by hand, or (b) on the day after being deposited with a nationally recognized overnight courier as provided in Section 26.1(A) hereof.

#### ARTICLE 27

##### LANDLORD'S AGREEMENT ON WAIVER

SECTION 27.1. Landlord agrees that from time to time the Tenant shall mortgage and grant security interest in the inventory, equipment, accounts, general intangibles and other personal property of the Tenant (collectively, the "Pledged Property") to Bank One, Texas, N.A., as Agent for a group of lenders (in such capacity, the "Agent"), or to such other lender or lenders from time to time, which Pledged Property may now or hereafter be situated upon the Premises. For valuable consideration, the receipt of which is hereby acknowledged, by the Landlord, the Landlord hereby waives all landlords' liens, whether contractual, statutory, constitutional or otherwise that the Landlord now has or hereafter may obtain against the Pledged Property, and all of the liens, security interests, claims and other interests that the Landlord now has or hereafter may obtain against the Pledged Property. The Landlord agrees that the Agent may, at any time upon reasonable notice to the Landlord, enter and remove the Pledged Property from the Premises. This waiver binds the Landlord, its successors, and assigns.

ARTICLE 28

BROKER

SECTION 28.1. Landlord represents and warrants to Tenant that Landlord has not dealt with any broker or Person in connection with this Lease. Tenant represents and warrants to Landlord that Tenant has not dealt with any broker or Person in connection with this Lease. The execution and delivery of this Lease by Tenant shall be conclusive evidence that Tenant acknowledges that Landlord has relied upon the foregoing representation and warranty. Tenant shall indemnify and hold harmless Landlord from and against any and all claims for commission, fee or other compensation by any broker or Person who claims to have dealt with Tenant in connection with this Lease and for any and all costs incurred by Landlord in connection with such claims, including, without limitation, attorneys' fees and disbursements. The provisions of this Article 28 shall survive the expiration or earlier termination of this Lease.

ARTICLE 29

INDEMNITY

SECTION 29.1. Tenant shall not do or permit any act or thing to be done in, at or upon the Premises that may subject any Indemnitee to any liability or responsibility for injury, damage to persons or property or to any liability by reason of the existence or application of, compliance with or violation of any Requirement, but shall exercise such control over the Premises as to protect each Indemnitee fully against any such liability and responsibility. Tenant shall indemnify and save harmless the Indemnitees from and against (a) all claims of whatever nature against the Indemnitees arising from any act, omission or negligence of Tenant or Persons Within Tenant's Control, (b) all claims against the Indemnitees arising from any accident, injury or damage whatsoever caused to any person or to the property of any person and occurring in or about the Premises during the Term or during Tenant's occupancy of the Premises, unless and to the extent caused by the gross negligence of Landlord or its shareholders, officers and employees, (c) all claims against the Indemnitees arising from any accident, injury or damage occurring outside of the Premises but anywhere within or about the Premises, where such accident, injury or damage results or is claimed to have resulted from an act, omission or negligence of Tenant or Persons Within Tenant's Control, and (d) any breach, violation or non-performance of any covenant, condition or agreement contained in this Lease to be fulfilled, kept, observed and performed by Tenant. This indemnity and hold harmless agreement shall include indemnity from and against any and all liability, claims, fines, suits, demands, costs and expenses of any kind or nature (including, without limitation, attorneys' fees and disbursements) incurred in or in connection with any such claim or proceeding brought thereon, and the defense thereof.

SECTION 29.2. If any claim, action or proceeding is made or brought against any Indemnitee, against which claim, action or proceeding Tenant is obligated to indemnify such Indemnitee pursuant to the terms of this Lease, then, upon demand by the Indemnitee, Tenant, at its sole cost and expense, shall resist or defend such claim, action or proceeding in the Indemnitee's name, if necessary, by such attorneys as the Indemnitee may select, including, without limitation, attorneys for the Indemnitee's insurer. The provisions of this Article 29 shall survive the expiration or earlier termination of this Lease.

ARTICLE 30

ADJACENT EXCAVATION

SECTION 30.1. If an excavation shall be made upon land adjacent to the Premises, or shall be authorized to be made, Tenant shall, upon reasonable advance notice, afford to the person or entity causing or authorized to cause such excavation, a limited license to enter upon the Premises for the purpose of doing such work as said person or entity deems necessary to preserve the walls of any building located on the Premises from injury or damage and to support the same by proper foundations without any claim for eviction or constructive eviction, damages or indemnity against Landlord, or diminution or abatement of Rental.

ARTICLE 31

RENEWAL OPTIONS

SECTION 31.1. Provided that the Tenant is not in default with respect to any of its obligations to the Landlord under and pursuant to the terms and conditions of this Lease at the time each Option (as such term is hereinafter defined) is to be exercised, the Tenant shall have the option to renew this Lease for two (2) additional five (5) year periods [the option with respect to each additional five (5) year period is referred to herein as an "OPTION" and, collectively, all of the options granted herein are referred to as the "OPTIONS"] as follows:

OPTION PERIOD 1 shall commence on July 1, 2002 and shall continue up to and including June 30, 2007.

OPTION PERIOD 2 shall commence on July 1, 2007 and shall continue up to and including June 30, 2012.

(each of the aforementioned option periods is individually referred to herein as an "OPTION PERIOD" and, collectively, all of the aforementioned Option Periods are referred to herein as "OPTION PERIODS")

SECTION 31.2. Each Option granted to the Tenant pursuant to the provisions of Section 31.1 hereof shall be exercised by the Tenant giving written notice to the Landlord of the Tenant's intent to exercise the Option not less than one-hundred eighty (180) days prior to the expiration of the Initial Term or not less than one-hundred eighty (180) days prior to the expiration of the Option Period which is then in effect, as the case may be. Time is of the essence in the exercise of the Options and should Tenant fail to exercise any of said Options by timely notice, said Options shall lapse and be of no further force or effect.

SECTION 31.3. In the event that the Tenant exercises the Option with respect to any Option Period, the Landlord and the Tenant hereby agree that this Lease shall continue in full force and effect and remain unamended during the applicable Option Period AND specifically, without limitation, that the Fixed Rent payable by the Tenant to the Landlord during such Option Period shall be increased on each anniversary date from and after the Commencement Date in accordance with the provisions of Article 8 hereof.

ARTICLE 32

RENT REGULATION

SECTION 32.1. If at any time or times during the Term of this Lease, the Rental reserved in this Lease is not fully collectible by reason of any Requirement, Tenant shall enter into such agreements and take such other steps as Landlord may request and as may be legally permissible to permit Landlord to collect the maximum rents that may from time to time during the continuance of such legal rent restriction be legally permissible (and not in excess of the amounts reserved under this Lease). Upon the termination of such legal rent restriction (a) the Rental shall become and thereafter be payable hereunder in accordance with the amounts reserved in this Lease for the remainder of the Term, and (b) Tenant shall pay to Landlord, if legally permissible, an amount equal to (i) the items of Rental that would have been paid pursuant to this Lease but for such legal rent restriction less (ii) the rents paid by Tenant to Landlord during the period or periods such legal rent restriction was in effect. This provision shall survive the expiration or earlier termination of this Lease to the maximum enforceable extent.

ARTICLE 33

COVENANT OF QUIET ENJOYMENT

SECTION 33.1. Landlord covenants that, upon Tenant paying all Fixed Rent and Additional Rent and observing and performing all the terms, agreements, covenants, provisions and conditions of this Lease on Tenant's part to be observed and performed, Tenant may peaceably and quietly enjoy the Premises, subject nevertheless to the terms and conditions of this Lease; provided, however, that no eviction of Tenant by reason of the foreclosure of any Mortgage now or hereafter affecting the Premises shall be construed as a breach of this covenant nor shall any action by reason thereof be brought against Landlord, and provided further that this covenant shall bind and be enforceable against Landlord or any successor to Landlord's interest, subject to the terms hereof, only so long as Landlord or any successor to Landlord's interest, is in possession and is collecting rent from Tenant but not thereafter.

ARTICLE 34

MISCELLANEOUS

SECTION 34.1. This Lease is presented for signature by Tenant and it is understood that this Lease shall not constitute an offer by or be binding upon Landlord unless and until Landlord shall have executed and delivered a fully executed copy of this Lease to Tenant.

SECTION 34.2. The obligations of Landlord under this Lease shall not be binding upon Landlord named herein after the sale, conveyance, assignment or transfer by such Landlord (or upon any subsequent landlord after the sale, conveyance, assignment or transfer by such subsequent landlord) of its interest in the Premises, as the case may be, and in the event of any such sale, conveyance, assignment or transfer, Landlord shall be and hereby is entirely freed and relieved of all covenants and obligations of Landlord under this Lease thereafter arising, and the transferee shall be deemed to have assumed, subject to the remaining provisions of this Section 34.2, all obligations of the Landlord under this Lease arising after the effective date of the



transfer. No trustee, partner, principal, shareholder, director or officer of Landlord (collectively, the "PARTIES") shall have any direct or personal liability for the performance of Landlord's obligations under this Lease, and Tenant shall look solely to Landlord's interest in the Premises to enforce Landlord's obligations hereunder and shall not otherwise seek any damages against Landlord or any of the Parties whatsoever. Tenant shall not look to any other property or assets of Landlord or any property or assets of any of the Parties in seeking either to enforce Landlord's obligations under this Lease or to satisfy a judgment for Landlord's failure to perform such obligations.

SECTION 34.3. Notwithstanding anything contained in this Lease to the contrary, all amounts payable by Tenant to or on behalf of Landlord under this Lease, whether or not expressly denominated Fixed Rent, Additional Rent or Rental, shall constitute rent for the purposes of Section 502(b)(7) of the Bankruptcy Code.

SECTION 34.4. Neither this Lease nor any memorandum of this Lease shall be recorded without the prior written consent of the Landlord, which consent may be withheld by the Landlord in its sole and absolute discretion.

SECTION 34.5. Except as otherwise expressly stated in this Lease, any consent or approval required to be obtained from Landlord may be granted by Landlord in its sole and absolute discretion. In any instance in which Landlord agrees not to act unreasonably, Tenant hereby waives any claim for damages against or liability of Landlord that Tenant may have based upon any assertion that Landlord has unreasonably withheld or unreasonably delayed any consent or approval requested by Tenant, and Tenant agrees that its sole remedy shall be an action or proceeding to enforce any related provision or for specific performance, injunction or declaratory judgment. If with respect to any required consent or approval Landlord is required by the express provisions of this Lease not to unreasonably withhold or delay its consent or approval, and if it is determined in any such proceeding referred to in the preceding sentence that Landlord acted unreasonably, the requested consent or approval shall be deemed to have been granted; however, Landlord shall have no liability whatsoever to Tenant for its refusal or failure to give such consent or approval. Tenant's sole remedy for Landlord's unreasonably withholding or delaying consent or approval shall be as provided in this Section 34.5.

SECTION 34.6. Landlord shall have the right at any time, and from time to time, to amend unilaterally the provisions of this Lease if Landlord is advised by its counsel that all or any portion of the Rental paid by Tenant to Landlord hereunder is, or may be deemed to be, unrelated business taxable income within the meaning of the United States Internal Revenue Code or regulations issued thereunder, and Tenant agrees that it will execute all documents necessary to effect any such amendment, provided that no such amendment shall increase Tenant's payment obligations or other liability under this Lease nor reduce Landlord's obligations hereunder.

SECTION 34.7. If Tenant shall remain in possession of the Premises after the Expiration Date, without the execution by both Tenant and Landlord of a new lease, Tenant, at the election of Landlord, shall be deemed to be occupying the Premises as a Tenant from month-to-month, at a monthly rental equal to three (3x) times the Rental payable during the last month of the Term, subject to all the other conditions, provisions and obligations of this Lease insofar as the same are applicable to a month-to-month tenancy.

SECTION 34.8. This Lease shall be construed without regard to any presumption or other rule requiring construction against the party causing this Lease to be drafted. If any words or phrases in this Lease are stricken out or otherwise eliminated, whether or not any other words or phrases have been added, this Lease shall be construed as if the words or phrases so stricken out or otherwise eliminated were never included in this Lease and no implication or inference shall be drawn from the fact that such words or phrases were stricken out or otherwise eliminated.

SECTION 34.9. If any of the provisions of this Lease, or the application thereof to any person or circumstance, shall, to any extent, be invalid or unenforceable, the remainder of this Lease, or the application of such provisions to persons or circumstances other than those as to whom or which it is held invalid or unenforceable, shall not be affected thereby and shall remain valid and enforceable, and every provision of this Lease shall be valid and enforceable to the fullest extent permitted by law.

SECTION 34.10. Landlord shall have the right to erect any gate, chain or other obstruction or to close off any portion of the Premises to the public at any time to the extent necessary to prevent a dedication thereof for public use.

SECTION 34.11. Tenant hereby represents to Landlord that it is not entitled, directly or indirectly, to diplomatic or sovereign immunity and Tenant agrees that in all disputes arising directly or indirectly out of this Lease Tenant shall be subject to service of process in, and the jurisdiction of the courts of, the State of Texas. The provisions of this Section 34.11 shall survive the expiration of this Lease.

SECTION 34.12. This Lease contains the entire agreement between the parties and all prior negotiations and agreements are merged into this Lease. Except as provided in Section 34.6 this Lease may not be changed, abandoned or discharged, in whole or in part, nor may any of its provisions be waived except by a written agreement that (a) expressly refers to this Lease, (b) is executed by the party against whom enforcement of the change, abandonment, discharge or waiver is sought and (c) is permissible under the Mortgage(s).

SECTION 34.13. Any apportionment or prorations of Rental to be made under this Lease shall be computed on the basis of a three hundred sixty (360) day year, with twelve (12) months of thirty (30) days each.

SECTION 34.14. The laws of the State of Texas applicable to contracts made and to be performed wholly within the State of Texas shall govern and control the validity, interpretation, performance and enforcement of this Lease without regard to principles of conflicts of law.

SECTION 34.15. If Tenant is a corporation, each person executing this Lease on behalf of Tenant hereby covenants, represents and warrants that Tenant is a duly incorporated or duly qualified (if foreign) corporation and is authorized to do business in the State of Texas (a copy of evidence thereof to be supplied to Landlord upon request); and that each person executing this Lease on behalf of Tenant is an officer of Tenant and that he or she is duly authorized to execute, acknowledge and deliver this Lease to Landlord (a copy of a resolution to that effect to be supplied to Landlord upon request).

SECTION 34.16. The captions are inserted only as a matter of convenience and for reference and in no way define, limit or describe the scope of this Lease nor the intent of any provision thereof.

SECTION 34.17. The covenants, conditions and agreements contained in this Lease shall bind and inure to the benefit of Landlord and Tenant and their respective legal representatives, heirs, successors, and, except as otherwise provided in this Lease, their assigns.

SECTION 34.18. For the purposes of this Lease and all agreements supplemental to this Lease, unless the context otherwise requires:

(A) The words "herein", "hereof", "hereunder" and "hereby" and words of similar import shall be construed to refer to this Lease as a whole and not to any particular Article or Section unless expressly so stated.

(B) Tenant's obligations hereunder shall be construed in every instance as conditions as well as covenants, each separate and independent of any other terms of this Lease.

(C) Reference to Landlord as having "no liability" or being "without liability" shall mean that Tenant shall not be entitled to terminate this Lease, or to claim actual or constructive eviction, partial or total, or to receive any abatement or diminution of rent, or to be relieved in any manner of any of its other obligations hereunder, or to be compensated for loss or injury suffered or to enforce any other right or liability whatsoever against Landlord under or with respect to this Lease or with respect to Tenant's use or occupancy of the Premises.

(D) Reference to "termination of this Lease" or "expiration of this Lease" and words of like import includes expiration or sooner termination of this Lease and the Term and the estate hereby granted or cancellation of this Lease pursuant to any of the provisions of this Lease or by law. Upon the termination of this Lease, the Term and estate granted by this Lease shall end at noon on the date of termination as if such date were the Fixed Expiration Date, and neither party shall have any further obligation or liability to the other after such termination except (i) as shall be expressly provided for in this Lease, and (ii) for such obligations as by their nature under the circumstances can only be, or by the provisions of this Lease, may be, performed after such termination, and, in any event, unless expressly otherwise provided in this Lease, any liability for a payment (which shall be apportioned as of such termination) which shall have accrued to or with respect to any period ending at the time of termination shall survive the termination of this Lease.

(E) Words and phrases used in the singular shall be deemed to include the plural and vice versa, and nouns and pronouns used in any particular gender shall be deemed to include any other gender.

(F) The rule of "ejusdem generis" shall not be applicable to limit a general statement following or referable to an enumeration of specific matters to matters similar to the matters specifically mentioned.

IN WITNESS WHEREOF, Landlord and Tenant have duly executed this Lease as of the day and year first above written.

"LANDLORD":

THOMAS J. BEATY

By: \_\_\_\_\_

BONNIE J. BEATY

By: \_\_\_\_\_

"TENANT":

ACCURATE AIR SYSTEMS, INC.

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

AMENDED AND RESTATED AGREEMENT OF LEASE

BETWEEN

THOMAS J. AND BONNIE J. BEATY

LANDLORD

AND

ACCURATE AIR SYSTEMS, INC.

TENANT

=====

DATED: JULY 1, 1997

=====

PREMISES

8505 Rannie Road  
Houston, Texas 77080

AMENDED AND RESTATED AGREEMENT OF LEASE, made as of the 1st day of July, 1997, among THOMAS J. BEATY and BONNIE J. BEATY, collectively as Landlord, and ACCURATE AIR SYSTEMS, INC., a Texas corporation, having an address at 4801 Woodway Drive, Suite 300E, Houston, Texas 77056, as Tenant.

W I T N E S S E T H:

WHEREAS, Lessor and Lessee entered into that certain Lease Agreement (the "Original Lease Agreement") dated as of April 1, 1994, certain premises known as and by the street address of 8505 Rannie Road, Houston, Texas (as more particularly described on Schedule "A", annexed hereto and made a part hereof) together with all buildings and other improvements thereon, and all fixtures, materials, equipment, apparatus, furniture, furnishings and other property, real and personal installed or used on the above described property or the improvements thereon; and

WHEREAS, Lessee has requested that the Lessor amend the Original Lease Agreement in order to revise certain terms thereof and the Lessor has agreed to do so on the terms and conditions set forth herein; and

WHEREAS, the parties hereto have agreed to restate the Original Lease Agreement as amended in its entirety for clarity only, and this Amended and Restated Lease Agreement constitutes for all purposes an amendment to the Original Lease Agreement and not a new or substitute agreement; in the event of a conflict between this Lease and the Original Lease Agreement, this Lease shall control; and

WHEREAS, the terms and provisions of the Original Lease Agreement are incorporated herein by reference and made a part of this Lease to the same extent as though set forth in full herein.

NOW, THEREFORE, in consideration of the mutual promises and covenants herein contained and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereto, for themselves, as well as their respective legal representatives, heirs, successors and assigns, hereby agree as follows:

ARTICLE 1

GLOSSARY

For the purposes of this Lease, the following terms shall have the meanings indicated below:

"ADA" shall have the meaning set forth in Section 9.1 hereof.

"ADDITIONAL RENT" shall have the meaning set forth in Section 2.2 hereof.

"ALTERATION" or "ALTERATIONS" shall mean any and all alterations, decorations, installations, repairs, improvements, additions, replacements or other physical changes of any nature whatsoever in or about the Premises at any time, now or hereafter.

"APPLICABLE RATE" shall mean the lesser of (x) three percentage points above the then current Base Rate, or (y) the maximum rate permitted by applicable law.

"BANKRUPTCY CODE" shall mean 11 U.S.C. Section 101 ET SEQ., or any statute, federal or state, of similar nature and purpose, now or hereafter.

"BASE RATE" shall mean the rate of interest publicly announced from time to time by Bank One, Texas, N.A., or its successor, as its "base rate" (or such other term as may be used by Bank One, Texas, N.A., from time to time, for the rate presently referred to as its "base rate").

"BUILDING SYSTEMS" shall mean the mechanical, electrical, sanitary, heating, air conditioning, ventilating, elevator, plumbing, life-safety and other service or support systems of any nature whatsoever located at or on the Premises, but shall not include installations made by Tenant or fixtures or appliances (regardless of whether or not such fixtures or appliances are owned by the Tenant or the Landlord).

"BUILDING INSURANCE" shall have the meaning set forth in Section 11.2 hereof.

"BUSINESS DAYS" shall mean all days, excluding Saturdays, Sundays and all days observed as holidays by the State of Texas or the federal government.

"COMMENCEMENT DATE" is July 1, 1997.

"DEFICIENCY" shall have the meaning set forth in Section 18.2(A)(2) hereof.

"EVENT OF DEFAULT" shall have the meaning set forth in Section 17.1 hereof.

"EXPIRATION DATE" shall mean the Fixed Expiration Date or such other date on which the Term ends pursuant to any of the terms, conditions or covenants of this Lease or pursuant to law.

"FIXED EXPIRATION DATE" is June 30, 2002.

"FIXED RENT" shall mean \$38,000.04 per annum (\$3,166.67 per month) for the first Lease Year (as such term is hereinafter defined) to be adjusted thereafter on each anniversary date from and after the Commencement Date in accordance with the provisions of Article 8 of this Lease.

"GOVERNMENT AUTHORITY" or "GOVERNMENT AUTHORITIES" shall mean the United States of America, the State of Texas, the county of Harris, the Municipality of Houston, and/or any political subdivision thereof and any agency, department, commission, board, bureau or instrumentality of any of the foregoing, now existing or hereafter created, having jurisdiction over the Premises or any portion thereof.

"HAZARDOUS MATERIALS" shall have the meaning set forth in Section 9.2(A) hereof.

"INCREASE NOTICE" shall have the meaning set forth in Section 8.3 hereof. "INDEMNITEES" shall mean Landlord, his agents and contractors (and the partners, shareholders, officers, directors and employees of any of the Landlord's agents or contractors).

"INITIAL TERM" shall mean five (5) years.

"LANDLORD", on the date as of which this Lease is made, shall mean Thomas J. and Bonnie J. Beaty, but thereafter, "Landlord" shall mean any fee owner of the Premises.

"LEASE YEAR" shall mean each twelve (12) month period commencing on each anniversary date from and after the Commencement Date.

"MORTGAGE(S)" shall mean any trust indenture or mortgage which may now or hereafter affect the Premises and all extensions, supplements, amendments, modifications, consolidations, refinancings and replacements thereof or thereto, substitutions therefor, and advances made thereunder.

"MORTGAGEE(S)" shall mean any trustee or mortgagee or holder of a Mortgage.

"NOTICE(S)" shall have the meaning set forth in Section 27.1(A) hereof.

"OPTION" or "OPTIONS" shall have the meaning set forth in Section 31.1 hereof.

"OPTION PERIOD" or "OPTION PERIODS" shall have the meaning set forth in Section 31.1 hereof.

"PARTIES" shall have the meaning set forth in Section 34.2 hereof.

"PERMITTED USE" shall mean general, executive and administrative offices, parking and related facilities in connection with Tenant's business as a air conditioning systems business and uses related thereto including the evolution of the Tenant's business consistent with the evolution of the air conditioning systems industry in general.

"PERSON(S) OR PERSON(S)" shall mean any natural person or persons, a partnership, a corporation and any other form of business or legal association or entity.

"PERSONS WITHIN TENANT'S CONTROL" shall mean and include Tenant, all of Tenant's respective shareholders, directors, officers, agents, contractors, sub-contractors, servants, employees, licensees and invitees as well as any of the heirs, successors, representatives and assigns of any of the foregoing.

"PREMISES" shall mean all that certain plot, piece and parcel of land, known as and by the street address of 8505 Rannie Road, Houston, Texas 77080 (as more particularly described on Schedule "A", annexed hereto and made a part hereof) together with all buildings and other improvements thereon and hereafter placed thereon, and all fixtures, materials, equipment, apparatus, furniture, furnishings and other property, real and personal, now or hereafter installed or used on the above described property or the improvements thereon.

"PRICE INDEX" shall have the meaning set forth in Section 8.1(ii) hereof.

"RENTAL" shall mean and be deemed to include Fixed Rent, Additional Rent and any other sums payable, now or hereafter, by Tenant hereunder.

"REQUIREMENTS" shall mean (i) all present and future laws, rules, ordinances, regulations, statutes, requirements, codes and executive orders, extraordinary as well as ordinary, retroactive and prospective, of all Governmental Authorities, now existing or hereafter created, which affect, directly or indirectly, the Premises and/or the maintenance, use, operation or occupation of the Premises, (ii) all requirements, obligations and conditions of all instruments of record on the date of this Lease, and (iii) all requirements, obligations and conditions imposed by any fire rating agency or by the carrier of Landlord's hazard insurance policy for the Premises.

"TAXES" shall have the meaning set forth in Section 3.1 hereof.

"TENANT", on the date as of which this Lease is made, shall mean the Tenant named in this Lease, but thereafter "Tenant" shall mean only the tenant under this Lease at the time in question; provided, however, that the Tenant named in this Lease and any and all successor tenant(s) hereunder shall not be released and relieved from any liability hereunder in the event of any assignment of this Lease or a sublet, in whole or in part, of the Premises.

"TENANT'S PROPERTY" shall mean Tenant's movable fixtures and movable partitions, telephone and other equipment, furniture, furnishings and other movable items of personal property owned by the Tenant.

"TERM", on the date as of which this Lease is made shall mean five (5) years, but thereafter shall be deemed to include any Option Period for which the Tenant exercises its Option pursuant to the provisions of Article 31 hereof.

"TERMINATION NOTICE PERIOD" shall have the meaning set forth in Section 27.1 hereof.

"UNAVOIDABLE DELAYS" shall have the meaning set forth in Article 25 hereof.

## ARTICLE 2

### DEMISE; PREMISES; TERM; RENT

SECTION 2.1. Landlord hereby leases to Tenant and Tenant hereby hires from Landlord the Premises for the Term to commence on the Commencement Date and to end on the Fixed Expiration Date, unless earlier terminated as provided herein.

SECTION 2.2. Commencing upon the Commencement Date, Tenant shall pay to Landlord, in lawful money of the United States of America, without notice or demand, by good and sufficient check at the office of Landlord or at such other place as Landlord may designate from time to time, the following:

(A) the Fixed Rent, as such term is defined in Article 1 hereof, which shall be payable in equal monthly installments in advance on the first day of each and every calendar month during the Term, and

(B) additional rent ("ADDITIONAL RENT") consisting of all other sums of money as shall become due from and be payable by Tenant hereunder (for default in the payment of which Landlord shall have the same remedies as for a default in the payment of Fixed Rent).



SECTION 2.3. If the Commencement Date is other than the first day of a calendar month, or the Fixed Expiration Date is other than the last day of a calendar month, Fixed Rent for such month shall be prorated on a per diem basis.

SECTION 2.4. Tenant shall pay the Fixed Rent and Additional Rent when due without notice, demand (except as provided herein) and without abatement, deduction, counterclaim, setoff or defense of any nature.

### ARTICLE 3

#### REAL ESTATE TAXES; MORTGAGE(S)

SECTION 3.1. The Tenant represents, warrants, covenants and agrees that it shall, within five (5) days of written demand by the Landlord to the Tenant, pay to the Landlord, as Additional Rent, any and all Taxes (as hereinafter defined) of any nature whatsoever assessed or imposed against the Premises for each and every Lease Year during the Term of this Lease. The Landlord hereby agrees that any demand given by the Landlord to the Tenant pursuant to the provisions of this Section 3.1 shall include an accurate copy of the invoice, statement, bill or similar document issued by the relevant Governmental Authority or Governmental Authorities, as the case may be, with respect to the Taxes for which payment is demanded. For purposes of this Section 3.1, "TAXES" shall include, without limitation, any and all taxes assessed against the Premises, all personal property taxes, all ad valorem taxes, all license fees, all rent taxes, all levies, all penalties and any and all other taxes assessed against the Premises by any Governmental Authority, now or hereafter.

SECTION 3.2. The Tenant represents, warrants and covenants and agrees that it shall, within five (5) days of written demand by the Landlord to the Tenant, pay to the Landlord, as Additional Rent, any and all amounts which may be due and owing under and pursuant to the terms and conditions of any Mortgage or Mortgages, as the case may be, encumbering the Premises, now or hereafter, during the Term of this Lease including, but not limited to, any extensions, supplements, amendments, modifications, consolidations, refinancings and replacements of any such Mortgage or Mortgages provided that:

(A) the principal balance of any Mortgage subsequent to any extension, supplement, amendment, modification, consolidation, refinancing or replacement shall not exceed the outstanding principal balance of the Mortgage which is to be extended, supplemented, amended, modified, consolidated, refinanced or replaced at the time of such extension, supplement, amendment, modification, consolidation, refinancing or replacement, as the case may be; and

(B) the amount of the monthly payments of principal and interest payable pursuant to the terms and conditions of any Mortgage subsequent to any extension, supplement, amendment, modification, consolidation, refinancing or replacement shall not exceed the amount of the monthly payments with respect to the Mortgage which is to be extended, supplemented, amended, modified, consolidated, refinanced or replaced at the time of such extension, supplement, amendment, modification, consolidation, refinancing or replacement, as the case may be; and

(C) the terms of any extended, supplemented, amended, modified, consolidated, refinanced or replaced Mortgage shall be no more financially onerous than the provisions of such Mortgage prior to such extension, supplement, amendment, modification, consolidation, refinancing or replacement, as the case may be; and

(D) the term of any Mortgage extended, supplemented, amended, modified, consolidated, refinanced or replaced shall be no less than the term of such Mortgage prior to such extension, supplementation, amendment, modification, consolidation, refinancing or replacement, as the case may be.

Notwithstanding anything contained herein to the contrary, the provisions of this Section 3.2 shall not apply with respect to any amounts which may be due and owing under and pursuant to the terms and conditions of any Mortgage securing additional indebtedness (above and beyond any Mortgage or Mortgages existing as of the date hereof) which first becomes a recorded lien on the Premises subsequent to the date of this Lease and which is executed and delivered by the Landlord without the consent of the Tenant. The Landlord hereby agrees that any demand given by the Landlord to the Tenant for payment of Additional Rent pursuant to the provisions of this Section 3.2 shall include, only to the extent provided to the Landlord by the Mortgagee, an accurate copy of the invoice, statement, bill or similar document issued by such Mortgagee or Mortgagees, as the case may be, with respect to any amount for which payment of Additional Rent is demanded by the Landlord under and pursuant to the provisions of this Section 3.2.

#### ARTICLE 4

##### UTILITIES

SECTION 4.1. The Tenant represents, warrants, covenants and agrees that it shall, within five (5) days of written demand by the Landlord to the Tenant, pay to the Landlord, as Additional Rent, any and all charges incurred by the Landlord for any and all utilities supplied to the Premises including, without limitation, telephone, electricity, water, heating oil and/or natural gas. The Landlord hereby agrees that any demand given by the Landlord to the Tenant pursuant to the provisions of this Section 4.1 shall include an accurate copy of the invoice, statement, bill or similar document issued by the public utility or any private company providing such utility, as the case may be, with respect to any utility for which payment is demanded.

SECTION 4.2. Landlord shall not be liable in any way to Tenant for any interruption or failure of or defect in the supply or character of any utility furnished to the Premises, now or hereafter, or for any loss, damage or expense Tenant may sustain if either the quantity or character of any utility is changed or is no longer suitable for Tenant's requirements, whether by reason of any requirement, act or omission of the public utility serving the Premises or for any other reason whatsoever. Notwithstanding the provisions of this Section 4.2, the Landlord shall be responsible for any and all actual damages suffered by the Tenant as a result of any interruption of utility service caused solely by the Landlord's failure to remit (prior to the expiration of any applicable grace period) to the appropriate public utility or private company providing such utility, as the case may be, any amount which has been paid by the Tenant to the Landlord pursuant to the provisions of Section 4.1 hereof.

SECTION 4.3. Tenant shall at all times comply with the rules, regulations, terms and conditions applicable to service, equipment, wiring, as well as any and all requirements of the public utility supplying electricity to the Premises. Tenant shall not, without Landlord's prior written consent in each instance (which consent may be withheld by the Landlord in its reasonable discretion), connect any fixtures, machinery, appliances or equipment to the Premises electric distribution system or make any alteration or addition to Tenant's machinery, appliances or equipment, or the electric system of the Premises, if the effect thereof would be to increase the electrical load in the Premises. Should Landlord grant such consent, all additional risers or other equipment required therefor shall be provided by Landlord and the cost thereof shall be deemed Additional Rent due hereunder and shall be forthwith paid by Tenant within five (5) days of Landlord's written demand.

SECTION 4.4. If any Taxes are imposed upon Landlord with respect to any utility furnished as a service to Tenant by any Governmental Authority, Tenant agrees that such Taxes shall be reimbursed by Tenant to Landlord within five (5) days of written demand. The Landlord hereby agrees that any demand given by the Landlord to the Tenant pursuant to the provisions of this Section 4.4 shall include an accurate copy of the invoice, statement, bill or similar document issued by the relevant Governmental Authority or Governmental Authorities, as the case may be, with respect to the Taxes for which payment is demanded.

#### ARTICLE 5

##### USE AND OCCUPANCY

SECTION 5.1. Tenant shall use and occupy the Premises for the Permitted Use and for no other purpose of any nature whatsoever.

#### ARTICLE 6

##### ALTERATIONS

##### SECTION 6.1.

(A) (1) Prior to making any Alterations, Tenant shall (i) submit to Landlord detailed plans and specifications for approval by the Landlord (including layout, architectural, electrical, mechanical and structural drawings) and that comply with all Requirements for each proposed Alteration, and Tenant shall not commence any such Alteration without first obtaining Landlord's approval of such plans and specifications, (ii) at Tenant's expense, obtain all permits, approvals and certificates required by any Governmental Authorities, and (iii) furnish to Landlord duplicate original policies or certificates thereof for worker's compensation insurance (covering all persons to be employed by Tenant, and Tenant's contractors and subcontractors, in connection with such Alteration) and commercial general liability insurance (including premises operation, bodily injury, personal injury, death, independent contractors, products and completed operations, broad form contractual liability and broad form property damage coverages) in such form, with such companies, for such periods and in such amounts as Landlord may reasonably approve, naming Landlord and its agents and any Mortgagee, as additional insureds. Upon completion of such Alteration, Tenant, at Tenant's expense, shall obtain certificates of final approval of such Alterations required by any Governmental Authority and shall furnish Landlord with copies

thereof, together with the "as-built" plans and specifications for such Alterations. All Alterations shall be made and performed in accordance with the plans and specifications therefor as approved by Landlord and otherwise in accordance with all Requirements. All materials and equipment to be incorporated in the Premises as a result of any Alterations shall be first quality and no such materials or equipment shall be subject to any lien, encumbrance, chattel mortgage, title retention or security agreement.

(2) Landlord reserves the right to disapprove any plans and specifications, in whole or in part, to reserve approval of items shown thereon pending its review and approval of other plans and specifications, and to condition its approval upon Tenant making revisions to the plans and specifications or supplying additional information. Tenant agrees that any review or approval by Landlord of any plans and/or specifications with respect to any Alteration is solely for Landlord's benefit, and without any representation or warranty whatsoever to Tenant or any other Person with respect to the adequacy, correctness or sufficiency thereof or with respect to Requirements or otherwise.

(B) All Alterations shall become a part of the Premises and shall be Landlord's property from and after the installation thereof and may not be removed or changed without Landlord's prior written consent. Notwithstanding the foregoing, Landlord, upon notice given at least thirty (30) days prior to the Expiration Date or upon such shorter notice as is reasonable under the circumstances upon the earlier expiration of the Term, may require Tenant to remove any specified Alterations and to repair and restore in a good and workmanlike manner any damage to the Premises caused by such removal all at Tenant's sole cost and expense. All Tenant's Property shall remain the property of Tenant and, on or before the Expiration Date or earlier end of the Term, may be removed from the Premises by Tenant at Tenant's sole cost and expense; provided, however, that Tenant shall repair and restore in a good and workmanlike manner any damage to the Premises caused by such removal. The provisions of this Section 6.1(B) shall survive the expiration or earlier termination of this Lease.

(C) (1) Any and all Alterations shall be performed, at Tenant's sole cost and expense, by contractors, subcontractors or mechanics previously approved in writing by Landlord. Prior to making an Alteration, at Tenant's request, Landlord shall furnish Tenant with a list of contractors who may perform Alterations to the Premises on behalf of Tenant.

(2) Notwithstanding the terms and conditions of Section 6.1(C)(1) hereof, with respect to any Alteration affecting any Building Systems, (i) Tenant shall only employ Landlord's designated contractor, and (ii) the Alteration shall, at Tenant's expense, be designed by Landlord's engineer.

(D) (1) Any mechanic's lien filed against the Premises for work claimed to have been done for, or materials claimed to have been furnished to, Tenant shall be canceled or discharged by Tenant, at Tenant's expense, within twenty (20) days after such lien shall be filed, by payment or filing of the bond required by law, and Tenant shall indemnify and hold Landlord harmless from and against any and all costs, expenses, claims, losses or damages resulting therefrom by reason thereof.

(2) If Tenant shall fail to discharge such mechanic's lien within the aforesaid period, then, in addition to any other right or remedy of Landlord, Landlord may, but

shall not be obligated to, discharge the same either by paying the amount claimed to be due or by procuring the discharge of such lien by deposit in court or bonding, and in any such event, Landlord shall be entitled, if Landlord so elects, to compel the prosecution of an action for the foreclosure of such mechanics lien by the lienor and to pay the amount of the judgment, if any, in favor of the lienor, with interest, costs and allowances.

(3) Any amount paid by Landlord for any of the aforesaid charges and for all expenses of Landlord (including, but not limited to, attorneys' fees and disbursements) incurred in defending any such action, discharging said lien or in procuring the discharge of said lien, with interest on all such amounts at the maximum legal rate of interest then chargeable to Tenant from the date of payment, shall be repaid by Tenant within ten (10) days after written demand therefor, and all amounts so repayable, together with such interest, shall be considered Additional Rent.

SECTION 6.2. Landlord, at Tenant's expense, and upon the request of Tenant, shall join in any applications for any permits, approvals or certificates required to be obtained by Tenant in connection with any permitted Alteration (provided that the provisions of the applicable Requirements shall require that Landlord join in such application) and shall otherwise cooperate with Tenant in connection therewith; provided, however, that Landlord shall not be obligated to incur any cost or expense or liability in connection therewith.

SECTION 6.3. Tenant shall furnish to Landlord copies of records of all Alterations and of the cost thereof within fifteen (15) days after the completion of such Alterations.

SECTION 6.4. Tenant shall not, at any time prior to or during the Term, directly or indirectly, employ, or permit the employment of, any contractor, mechanic or laborer in the Premises, whether in connection with any Alteration or otherwise, if such employment would interfere or cause any conflict with other contractors, mechanics or laborers engaged in the construction, maintenance or operation of the Premises by Landlord, Tenant or others, or of any other property owned by Landlord. In the event of any such interference or conflict, Tenant, upon demand of Landlord, shall cause all contractors, mechanics or laborers causing such interference or conflict to leave the Premises immediately.

## ARTICLE 7

### REPAIRS; REPLACEMENTS; MAINTENANCE

SECTION 7.1. Tenant, at Tenant's sole cost and expense, shall take good care of the Premises and the fixtures, equipment and appurtenances therein and make all repairs and replacements thereto, both structural and non-structural, of any nature whatsoever as and when needed to preserve them in good working order and condition, except for (a) reasonable wear and tear and (b) obsolescence. If Tenant shall fail, after five (5) days notice (or such shorter period as may be required because of an emergency), to proceed with due diligence to make repairs required to be made by Tenant, the same may be made by Landlord, at the expense of Tenant, and the expenses thereof incurred by Landlord, with interest thereon at the Applicable Rate, shall be paid to Landlord, as Additional Rent, within ten (10) days after rendition of a bill or statement therefor. Tenant shall give Landlord prompt notice of any defective condition in any Building Systems located in, servicing or passing through the Premises.

ARTICLE 8

INCREASES IN FIXED RENT

SECTION 8.1. For purposes of the Lease:

(i) "BUREAU" shall mean the Federal Bureau of Labor Statistics or any successor agency that shall issue the indices or data referred to in subparagraph (ii) below.

(ii) "PRICE INDEX" shall mean the Consumer Price Index for All Urban Consumers for the Houston, Texas geographic area, 1982-1984=100, issued from time to time by the Bureau or any other successor measure hereafter employed by the Bureau in lieu of such price index that measures the cost of living for such geographic area, failing such successor, the most nearly comparable index (reflecting changes in costs of housing including rental housing, energy and services), published by a Governmental Authority, appropriately adjusted. Furthermore, if hereafter the Price Index is converted to a different standard reference base or a substantial change is made in the terms or number of items contained therein, the Price Index shall be adjusted (with the use of such conversion factor, formula or table as is published by the Bureau, or if it shall not publish same, the conversion factor published by Prentice Hall, Inc., or, failing such publication, by any other nationally recognized publisher of similar statistical information) to the figure that would have resulted if not for such conversion or change.

(iii) "APPLICABLE PRICE INDEX" for a Lease Year shall mean the Price Index issued for August of the year in which such Lease Year commences.

SECTION 8.2. (A) Tenant shall pay to Landlord Fixed Rent in the amount set forth in Article 1 of this Lease for the first Lease Year.

(B) For each Lease Year subsequent to the first Lease Year (and for each and every Lease Year thereafter during the Term hereof), the Tenant shall pay to the Landlord, as Fixed Rent, an amount equal to the greater of:

(i) an amount equal to the sum of (x) the percentage by which the Applicable Price Index for such Lease Year exceeds the Applicable Price Index for the immediately preceding Lease Year, multiplied by the Fixed Rent payable for such immediately preceding Lease Year and (y) such Fixed Rent payable for the immediately preceding Lease Year (e.g., if the Base Index is 200, the Applicable Price Index for the second Lease Year is 203, the Applicable Price Index for the third Lease Year is 215, and the Fixed Rent payable for the second Lease Year is \$50,000.00, then the Applicable Price Index for the third Lease Year exceeds the Applicable Price Index for the second Year by 5.91% (i.e., the difference between 203 and 215), and the Fixed Rent derived from the aforesaid calculation shall be \$52,955.75 (5.91% of \$50,000.00, \$2,955.00, plus \$50,000.00); or

(ii) an amount equal to the Fixed Rent for the immediately preceding Lease Year.

The Landlord and the Tenant hereby acknowledge that it is the mutual intention of the parties that for each and every Lease Year subsequent to the first Lease Year during the Term hereof,

the Fixed Rent payable by the Tenant to the Landlord hereunder shall never be decreased from the prior Lease Year.

SECTION 8.3. Upon notice by the Landlord to the Tenant of an increase in the Fixed Rent pursuant to the provisions of this Article 8 ("INCREASE NOTICE"), the Tenant shall pay the Fixed Rent as set forth in the Increase Notice.

## ARTICLE 9

### REQUIREMENTS OF LAW

SECTION 9.1. Tenant shall not do, and shall not permit any act or thing in or upon the Premises which will invalidate or be in conflict with the certificate of occupancy for the Premises or violate any Requirements. Tenant shall, at Tenant's sole cost and expense, immediately take all action, including but not limited to, making any required Alterations necessary to comply with all Requirements [including, but not limited to, the Americans With Disabilities Act of 1990 (the "ADA"), as modified and supplemented from time to time] which shall or may impose any violation, order or duty upon Landlord or Tenant arising from, or in connection with, the Premises, Tenant's occupancy, use or manner of use of the Premises (including, without limitation, any occupancy, use or manner of use that constitutes a "place of public accommodation" under the ADA), or any installations in the Premises, or required by reason of a breach of any of Tenant's covenants or agreements under this Lease, whether or not such Requirements shall now be in effect or hereafter enacted or issued, and whether or not any work required shall be ordinary or extraordinary or foreseen or unforeseen as of the date hereof.

SECTION 9.2. Tenant covenants and agrees that Tenant shall, at Tenant's sole cost and expense, comply at all times with all Requirements governing the use, generation, storage, treatment and/or disposal of any Hazardous Materials (as defined below), the presence of which results from or in connection with the act or omission of Tenant or Persons Within Tenant's Control or the breach of this Lease by Tenant or Persons Within Tenant's Control. The term "HAZARDOUS MATERIALS" shall mean any biologically or chemically active or other toxic or hazardous wastes, pollutants or substances, including, without limitation, asbestos, PCBs, petroleum products and by-products, substances defined or listed as "hazardous substances" or "toxic substances" or similarly identified in or pursuant to the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. ss. 9601 ET SEQ., and as hazardous wastes under the Resource Conservation and Recovery Act, 42 U.S.C. ss. 6010, ET SEQ., any chemical substance or mixture regulated under the Toxic Substance Control Act of 1976, as amended, 15 U.S.C. 2601, ET SEQ., any "toxic pollutant" under the Clean Water Act, 33 U.S.C. ss. 466 ET SEQ., as amended, any hazardous air pollutant under the Clean Air Act, 42 U.S.C. ss. 7401 ET SEQ., hazardous materials identified in or pursuant to the Hazardous Materials Transportation Act, 49 U.S.C. ss. 1802, ET SEQ., and any hazardous or toxic substances or pollutant regulated under any other Requirements including, without limitation, ECRA (as such term is hereinafter defined). Tenant agrees to execute, from time to time, at Landlord's request, affidavits, representations and the like concerning Tenant's best knowledge and belief regarding the presence of Hazardous Materials in, on, under or about the Premises. Tenant shall indemnify and hold harmless all Indemnitees from and against any loss, claim, cost, damage, liability or expense (including attorneys' fees and disbursements) arising by reason of any clean up, removal, remediation, detoxification action or any other activity required or recommended of any Indemnitees by any

Governmental Authority by reason of the presence in, on, under or about the Premises of any Hazardous Materials, as a result of or in connection with the act or omission of Tenant or Persons Within Tenant's Control or the breach of this Lease by Tenant or Persons Within Tenant's Control. The foregoing covenants and indemnity shall survive the expiration or any termination of this Lease.

SECTION 9.3. If Tenant shall receive notice of any violation of, or defaults under, any Requirements, liens or other encumbrances applicable to the Premises, Tenant shall give immediate written notice thereof to Landlord.

SECTION 9.4. If any governmental license or permit shall be required for the proper and lawful conduct of Tenant's business and if the failure to secure such license or permit would, in any way, affect Landlord or the Premises, then Tenant, at Tenant's expense, shall promptly procure and thereafter maintain, submit for inspection by Landlord, and at all times comply with the terms and conditions of, each such license or permit.

#### ARTICLE 10

##### SUBORDINATION

SECTION 10.1. This Lease shall at all times, now and hereafter, be subject and subordinate to each and every Mortgage, whether made prior to or after the execution of this Lease, and to all extensions, supplements, amendments, modifications, consolidations and replacements thereof or thereto, substitutions therefor, and advances made thereunder; provided, that Tenant has received from the holder of any Mortgage an agreement that Tenant will not be disturbed in its possession of the Premises, or have its rights under this Lease modified or terminated other than pursuant to the terms of this Lease. This clause shall be self-operative and no further agreement of subordination shall be required to make the interest of any Mortgagee superior to the interest of Tenant hereunder. In confirmation of such subordination, Tenant shall promptly execute and deliver, at its own cost and expense, any document, in recordable form if requested, that Landlord or any Mortgagee may request to evidence such subordination; and if Tenant fails to execute, acknowledge or deliver any such document within five (5) days after request therefor, Tenant hereby irrevocably constitutes and appoints Landlord as Tenant's attorney-in-fact, coupled with an interest, to execute, acknowledge and deliver any such document for and on behalf of Tenant. Tenant shall not do anything that would constitute a default under any Mortgage, or omit to do anything that Tenant is obligated to do under the terms of this Lease so as to cause Landlord to be in default thereunder.

SECTION 10.2. If, at any time prior to the expiration of the Term, any Mortgagee comes into possession of the Premises, by receiver or otherwise, Tenant agrees, at the election and upon demand of any owner of the Premises, or of any Mortgagee in possession of the Premises, to attorn, from time to time, to any such owner or Mortgagee or any person acquiring the interest of Landlord as a result of any such termination or as a result of a foreclosure of the Mortgage or the granting of a deed in lieu of foreclosure, upon the then executory terms and conditions of this Lease (except as provided below), for the remainder of the Term, provided that such owner or Mortgagee, as the case may be, or receiver caused to be appointed by any of the foregoing,



is then entitled to possession of the Premises. Any such attornment shall be made upon the condition that no such owner or Mortgagee shall be:

(1) liable for any act or omission of any prior landlord (including, without limitation, the then defaulting landlord); or

(2) subject to any defense or offsets (except as expressly set forth in this Lease) which Tenant may have against any prior landlord (including, without limitation, the then defaulting landlord); or

(3) bound by any payment of Rental which Tenant might have paid for more than the current month to any prior landlord (including, without limitation, the then defaulting landlord); or

(4) bound by any obligation to make any payment to Tenant which was required to be made prior to the time such owner or Mortgagee succeeded to any prior landlord's interest; or

(5) bound by any obligation to perform any work or to make improvements to the Premises except for (i) repairs to the Premises or any part thereof as a result of damage by fire or other casualty pursuant to Article 12, but only to the extent that such repairs can be reasonably made from the net proceeds of any insurance actually made available to such owner or Mortgagee and (ii) repairs to the Premises as a result of a partial condemnation pursuant to Article 13, but only to the extent that such repairs can be reasonably made from the net proceeds of any award made available to such owner or Mortgagee. Tenant, upon demand of any such owner or Mortgagee, shall execute, from time to time, agreements in confirmation of the foregoing provisions of this Section 10.2, satisfactory to any such owner or Mortgagee, and acknowledging such attornment and setting forth the terms and conditions of its tenancy. Nothing contained in this Section 10.2 shall be construed to impair any right otherwise exercisable by any such owner or Mortgagee.

SECTION 10.3. If requested by any Mortgagee or Landlord, Tenant shall promptly execute and deliver, at Tenant's own cost and expense, any document in accordance with the terms of this Article 10, in recordable form, to evidence such subordination.

SECTION 10.4. At any time and from time to time upon not less than ten (10) days' prior notice to Tenant or Landlord given by the other, or to Tenant given by a Mortgagee, Tenant or Landlord, as the case may be, shall, without charge, execute, acknowledge and deliver a statement in writing addressed to such party as Tenant, Landlord or Mortgagee, as the case may be, may designate, in form satisfactory to Tenant, Landlord or Mortgagee, as the case may be, certifying all or any of the following: (i) that this Lease is unmodified and in full force and effect (or if there have been modifications, that this Lease is in full force and effect as modified and stating the modifications); (ii) the date that the Term commenced and the date(s) that Fixed Rent and Additional Rent became payable hereunder and the dates to which they have been paid; (iii) whether or not, to the best knowledge of the signer of such certificate, Landlord is in default in performance of any of the terms of this Lease and, if so, specifying each such event of default of which the signer may have knowledge; (iv) whether or not, to the best knowledge of the signer of such certificate, Tenant has accepted possession of the Premises; (v) whether Tenant has made

any claim against Landlord under this Lease and, if so, the nature thereof and the dollar amount, if any, of such claim; (vi) either that Tenant does not know of any default in the performance of any provision of this Lease or specifying the details of any default of which Tenant may have knowledge and stating what action Tenant is taking or proposes to take with respect thereto; (vii) that, to the best knowledge of Tenant, there are no proceedings pending or threatened against Tenant before or by any court or administrative agency which, if adversely decided, would materially or adversely affect the financial condition or operations of Tenant or, if any such proceedings are pending or threatened to the best knowledge of Tenant, specifying and describing the same; and (viii) such further information with respect to the Lease or the Premises as Landlord may reasonably request or Mortgagee may require; it being intended that any such statement delivered pursuant hereto may be relied upon by any prospective purchaser of the Premises or any part thereof or of the interest of Landlord in any part thereof, by any Mortgagee or prospective Mortgagee or by any prospective assignee of any Mortgage or by any assignee of Tenant.

The failure of either Tenant or Landlord to execute, acknowledge and deliver a statement in accordance with the provisions of this Section 10.4 within said ten (10) day period shall constitute an acknowledgment by Tenant or Landlord, as the case may be, which may be relied on by any person or entity of any nature whatsoever who would be entitled to rely upon any such statement, that such statement as submitted by Landlord or Tenant, as the case may be, is true and correct.

SECTION 10.5. As long as any Mortgage exists, Tenant shall not seek to terminate this Lease by reason of any act or omission of Landlord until Tenant has given not less than thirty (30) days prior written notice of such act or omission to all Mortgagees, and if any such Mortgagee notifies Tenant within thirty (30) days following receipt of such notice of its intention to remedy such act or omission, until a reasonable period of time shall have elapsed following the giving of such notice, during which period such Mortgagee shall have the right, but not the obligation, to remedy such act or omission.

#### ARTICLE 11

##### INSURANCE; PROPERTY LOSS OR DAMAGE; REIMBURSEMENT

###### SECTION 11.1.

(A) Neither Landlord nor Landlord's agents shall be liable for any injury or damage to persons or property, or interruption of Tenant's business, resulting from fire or other casualty; nor shall Landlord or Landlord's agents be liable for any such damage caused by Persons other than the Landlord or the Landlord's agents or by construction of any private, public or quasi-public work; nor shall Landlord be liable for any latent defect in the Premises.

(B) Tenant shall give written notice to Landlord, immediately after Tenant learns thereof, of any accident, emergency, occurrence for which Landlord might be liable, fire or other casualty and all damages to or defects in the Premises for the repair of which Landlord might be responsible or which constitutes Landlord's property. Such notice shall be given by telecopy or personal delivery to the address(es) of Landlord in effect for notice.

SECTION 11.2. Tenant shall not do or permit to be done any act or thing in or upon the Premises which will invalidate or be in conflict with the terms of the State of Texas standard form of fire insurance with extended coverage, or with rental, liability, boiler, sprinkler, water damage, war risk or other insurance policies covering the Premises and the fixtures and property therein (hereinafter referred to as "BUILDING INSURANCE"); and Tenant, at Tenant's own expense, shall comply with all rules, orders, regulations and requirements of all insurance boards, and shall not do or permit anything to be done in or upon the Premises or bring or keep anything therein or use the Premises in a manner which increases the rate of premium for any of the Building Insurance or any property or equipment located therein over the rate in effect at the commencement of the Term of this Lease.

SECTION 11.3.

(A) If, by reason of any failure of Tenant to comply with the provisions of this Lease, the rate of premium for Building Insurance or other insurance on the property and equipment of Landlord shall be higher than it otherwise would be, Tenant shall reimburse Landlord for that part of the insurance premiums thereafter paid by Landlord which shall have been charged because of such failure by Tenant. Tenant shall make said reimbursement on the first day of the month following such payment by Landlord.

(B) In any action or proceeding wherein Landlord and Tenant are parties, a schedule of any insurance rate for the Premises issued by any insurance board establishing insurance premium rates for the Premises shall be prima facie evidence of the facts therein stated and of the several items and charges in the insurance premium rates then applicable to the Premises.

SECTION 11.4.

(A) Tenant shall, at Tenant's own cost and expense, obtain, maintain and keep in full force and effect during the Term, for the benefit of Landlord, any Mortgagees and Tenant, commercial general liability insurance (including premises operation, bodily injury, personal injury, death, independent contractors, products and completed operations, broad form contractual liability and broad form property damage coverages) in a combined single limit amount of not less than Five Million and 00/100 (\$5,000,000.00) Dollars, against all claims, demands or actions with respect to damage, injury or death made by or on behalf of any person or entity, arising from or relating to the conduct and operation of Tenant's business in, on or about the Premises (which shall include Tenant's signs, if any), or arising from or related to any act or omission of Tenant or of Persons Within Tenant's Control. If Tenant shall install or maintain one or more pressure vessels to serve Tenant's operations at the Premises, Tenant shall, at Tenant's own cost and expense, obtain, maintain and keep in full force and effect, for the benefit of Landlord, any Mortgagees and Tenant, appropriate boiler or other insurance coverage therefor in an amount not less than Three Million and 00/100 (\$3,000,000.00) Dollars (it being understood and agreed, however, that the foregoing shall not be deemed a consent by Landlord to the installation and/or maintenance of any such pressure vessels in the Premises, which installation and/or maintenance shall at all times be subject to the prior written consent of Landlord). Whenever, in Landlord's reasonable judgment, good business practice and changing conditions indicate a need for additional amounts or different types of insurance coverage, Tenant shall, within ten (10) days after Landlord's request, obtain such insurance coverage, at Tenant's expense.

(B) Tenant, at Tenant's sole cost and expense, shall maintain insurance protecting and indemnifying Tenant against any and all damage to or loss of any Alterations and leasehold improvements, including any made by Landlord to prepare the Premises for Tenant's occupancy, and Tenant's Property, and all claims and liabilities relating thereto.

(C) Landlord and any Mortgagees shall be named as insureds in said policies and shall be protected against all liability occasioned by an occurrence insured against. All said policies of insurance shall be: (i) written as "occurrence" policies; (ii) written as primary policy coverage and not contributing with or in excess of any coverage which Landlord may carry; and (iii) issued by reputable and independent insurance companies rated in Best's Insurance Guide, or any successor thereto (or if there be none, an organization having a national reputation) as having a general policyholder rating of "A+" and a financial rating of at least "13", and which are licensed to do business in the State of Texas. Tenant shall deliver to Landlord the policies of insurance or certificates thereof, together with evidence of payment of premiums thereon, and shall thereafter furnish to Landlord, at least thirty (30) days prior to the expiration of any such policies and any renewal thereof, a new policy or certificate in lieu thereof, with evidence of the payment of premiums thereon. Each of said policies shall also contain a provision whereby the insurer agrees not to cancel, fail to renew, diminish or materially modify said insurance policy(ies) without having given Landlord and any Mortgagees at least thirty (30) days prior written notice thereof.

(D) Tenant shall pay all premiums and charges for all of said policies, and, if Tenant shall fail to make any payment when due or carry any such policy, Landlord may, but shall not be obligated to, make such payment or carry such policy, and the amount paid by Landlord, with interest thereon (at the Applicable Rate), shall be repaid to Landlord by Tenant on demand, and all such amounts so repayable, together with such interest, shall be deemed to constitute Additional Rent hereunder. Payment by Landlord of any such premium, or the carrying by Landlord of any such policy, shall not be deemed to waive or release the default of Tenant with respect thereto.

#### SECTION 11.5.

(A) Tenant shall cause each insurance policy carried by Tenant and insuring the Premises and Tenant's Alterations, leasehold improvements, space equipment, furnishings, furniture, contents and fixtures against loss, damage or destruction by fire or other casualty, to be written in a manner so as to provide that the insurance company waives all rights of recovery by way of subrogation against Landlord or Tenant in connection with any loss or damage covered by any such policy. If the release of either Landlord or Tenant shall contravene any law with respect to exculpatory agreements, the liability of the party in question shall be deemed not released, but no action or rights shall be sought or enforced against such party unless and until all rights and remedies against the insurer are exhausted and such party shall be unable to collect such insurance proceeds.

(B) The waiver of subrogation referred to in Section 11.5(A) above shall extend to the agents and employees of each party, but-only if and to the extent that such waiver can be obtained without additional charge (unless such party shall pay such charge). Nothing contained in this Section 11.5 shall be deemed to relieve the Tenant from any duty imposed elsewhere in this Lease to repair, restore and rebuild the Premises, in whole or in part.

ARTICLE 12

DESTRUCTION BY FIRE OR OTHER CAUSE

SECTION 12.1. If the Premises or any part thereof shall be damaged by fire or other casualty, Tenant shall give immediate written notice thereof to Landlord. Landlord shall, subject to the provisions of Sections 12.2 and 12.3 below, proceed with reasonable diligence, after receipt of the net proceeds of insurance, to repair or cause to be repaired such damage at its expense, but in no event shall such repair or restoration be greater in scope than the quantity or quality of construction of the Premises as of the Commencement Date; and, if the Premises, or any part thereof, shall be rendered untenable by reason of such damage and such damage shall not be due to the fault of Tenant or Persons Within Tenant's Control, then the Fixed Rent hereunder, or an amount thereof apportioned according to the area of the Premises so rendered untenable (if less than the entire Premises shall be so rendered untenable), shall be abated for the period from the date of such damage to the date when the repair of such damage shall have been substantially completed. If Landlord or any Mortgagee shall be unable to collect the insurance proceeds (including rent insurance proceeds) applicable to such damage because of some action or inaction on the part of Tenant or Persons Within Tenant's Control, then the cost of repairing such damage shall be paid by Tenant and there shall be no abatement of Fixed Rent. Tenant covenants and agrees to cooperate with Landlord and any Mortgagee in their efforts to collect insurance proceeds (including rent insurance proceeds) payable to such parties. Landlord shall not be liable for any delay which may arise by reason of adjustment of insurance on the part of Landlord and/or Tenant, or any cause beyond the control of Landlord or contractors employed by Landlord.

It is expressly understood that if Landlord is prevented from substantially completing the repairs by reason of any acts of Tenant or Persons Within Tenant's Control, including, without limitation, by reason of the performance of any Alterations, or by reason of Tenant's failure or refusal to comply or to cause its architects, engineers, designers and contractors to comply with any of Tenant's obligations described or referred to in this Lease, then such work shall be deemed substantially completed on the date when the work would have been substantially completed but for such delay, and the expiration of the abatement of Tenant's obligations to pay Fixed Rent shall not be postponed by reason of such delay. Any additional costs to Landlord to complete any work occasioned by such delay shall be paid by Tenant to Landlord, as Additional Rent, within ten (10) days after demand therefor by Landlord.

SECTION 12.2. Landlord shall not be liable for any inconvenience or annoyance to Tenant or injury to the business of Tenant resulting in any way from damage from fire or other casualty or the repair thereof. Tenant understands that Landlord, in reliance upon Section 11.4 hereof, will not carry insurance of any kind on Tenant's furnishings, furniture, contents, fixtures, space equipment and leasehold improvements, and that Landlord shall not be obligated to repair any damage thereto or replace the same.

SECTION 12.3. (A) Notwithstanding anything to the contrary contained in Sections 12.1 and 12.2 above, in the event that:

(i) at least fifty (50%) percent of the rentable square feet of the Premises shall be damaged by a fire or other casualty so that substantial alteration or

reconstruction of the Premises shall, in Landlord's sole opinion, be required (whether or not the Premises shall have been damaged by such fire or other casualty and without regard to the structural integrity of the Premises); or

(ii) the Premises shall be totally or substantially damaged or shall be rendered wholly or substantially untenable; or

(iii) there shall be any damage to the Premises within the last two (2) years of the Term wherein the cost of repair exceeds an amount equal to three (3) monthly installments of Fixed Rent, then, as a result of any circumstances described in subparagraphs (i), (ii) or (iii) hereof, the Landlord may, in Landlord's sole and absolute discretion, terminate this Lease and the term and estate hereby granted, by notifying Tenant in writing of such termination within one hundred twenty (120) days after the date of such damage. In the event that such a notice of termination shall be given, then this Lease and the term and estate hereby granted shall expire as of the date of termination stated in said notice with the same effect as if that were the Fixed Expiration Date, and the Fixed Rent and Additional Rent hereunder shall be apportioned as of such date.

SECTION 12.4. Except as may be provided in Section 11.5, nothing herein contained shall relieve Tenant from any liability to Landlord or to Landlord's insurers in connection with any damage to the Premises by fire or other casualty if Tenant shall be legally liable in such respect.

#### ARTICLE 13

##### EMINENT DOMAIN

SECTION 13.1. If the whole of the Premises is acquired or condemned for any public or quasi-public use or purpose, this Lease and the Term shall end as of the date of the vesting of title with the same effect as if said date were the Fixed Expiration Date. If only a part of the Premises is so acquired or condemned then, (1) except as hereinafter provided in this Section 13.1, this Lease and the Term shall continue in effect but, if a part of the Premises is so acquired or condemned, from and after the date of the vesting of title, the Fixed Rent and Additional Rent, if any, shall be reduced in the proportion which the area of the part of the Premises so acquired or condemned bears to the total area of the Premises immediately prior to such acquisition or condemnation; (2) whether or not the Premises are affected thereby, Landlord, at Landlord's option, may give to Tenant, within sixty (60) days next following the date upon which Landlord receives notice of vesting of title, a thirty (30) day notice of termination of this Lease; and (3) if the part of the Premises so acquired or condemned contains more than seventy-five (75%) percent of the total area of the Premises immediately prior to such acquisition or condemnation, or if, by reason of such acquisition or condemnation, Tenant no longer has access to the Premises, Tenant, at Tenant's option, may give to Landlord, within thirty (30) days next following the date upon which Tenant receives notice of vesting of title, a thirty (30) day notice of termination of this Lease. If any such thirty (30) day notice of termination is given, by Landlord or Tenant, this Lease and the Term shall come to an end and expire upon the expiration of said thirty (30) days with the same effect as if the date of expiration of said thirty (30) days were the Fixed Expiration Date. In the event of any termination of this Lease and the Term pursuant to the provisions of this Section 13.1, the Fixed Rent or Additional Rent shall be apportioned as of

the date of sooner termination and any prepaid portion of the Fixed Rent for any period after such date shall be refunded by Landlord to Tenant.

SECTION 13.2. In the event of any such acquisition or condemnation of all or any part of the Premises, Landlord shall be entitled to receive the entire award for any such acquisition or condemnation. Tenant shall have no claim against Landlord or the condemning authority for the value of any unexpired portion of the Term and Tenant hereby expressly assigns to Landlord all of its right in and to any such award. Nothing contained in this Section 13.2 shall be deemed to prevent Tenant from making a separate claim in any condemnation proceedings for the value of any Tenant's Property included in such taking, and for any moving expenses, so long as Landlord's award is not reduced thereby.

#### ARTICLE 14

##### ASSIGNMENT; SUBLETTING; MORTGAGE; ETC.

SECTION 14.1. (A) The Tenant shall not (a) assign this Lease (whether by operation of law, transfers of interests in Tenant or otherwise); or (b) mortgage or encumber Tenant's interest in this Lease, in whole or in part; or (c) sublet, or permit the subletting of, the Premises or any part thereof. Notwithstanding the provisions of this Section 14.1, the use of the Premises by any Person affiliated (as such term is hereinafter defined) with the Tenant or under the common control (as such term is hereinafter defined) of Comfort Systems USA, Inc., as the case may be, shall not be deemed an assignment of this Lease or a sublet of the Premises; provided, however, that such use of the Premises as aforesaid shall not violate or be prohibited by any of the provisions of any Mortgage then encumbering the Premises, if any. For purposes of this Article 14, a Person shall be deemed to be an "AFFILIATE" of the Tenant or under the "COMMON CONTROL" of Comfort Systems USA, Inc. if such Person is a member of a "parent-subsidiary controlled group" [as such term is defined by Section 1563(a)(1) of the Internal Revenue Code of 1986, as amended] or a member of a "brother-sister controlled group" [as such term is defined by Section 1563(a)(2) of the Internal Revenue Code of 1986, as amended] of which either Comfort Systems USA, Inc. or the Tenant, as the case may be, is a member.

(B) Notwithstanding the provisions otherwise set forth in this Article 14, any reorganization, consolidation and/or restructuring of the Tenant in which the issued and outstanding stock of the Tenant remains under the common control (as such term is defined in Section 14.1 hereinabove) of Comfort Systems USA, Inc. shall not be deemed an assignment of this Lease or a sublet of the Premises; provided, however, that the same shall not violate or be prohibited by any of the provisions of any Mortgage then encumbering the Premises, if any.

SECTION 14.2. If Tenant's interest in this Lease shall be assigned in violation of the provisions of this Article 14, such assignment shall be invalid and of no force and effect against Landlord; provided, however, that Landlord may collect an amount equal to the then Fixed Rent plus any other item of Rental from the assignee as a fee for its use and occupancy. If the Premises or any part thereof are sublet to, or occupied by, or used by, any person other than Tenant, whether or not in violation of this Article 14, Landlord, after default by Tenant under this Lease, may collect any item of Rental or other sums paid by the subtenant, user or occupant as a fee for its use and occupancy, and shall apply the net amount collected to the Fixed Rent and the items of Rental reserved in this Lease. No such assignment, subletting, occupancy, or use,

nor any such collection or application of Rental or fee for use and occupancy, shall be deemed a waiver by Landlord of any term, covenant or condition of this Lease or the acceptance by Landlord of such assignee, subtenant, occupant or user as Tenant hereunder, nor shall the same, in any circumstances, relieve Tenant of any of its obligations under this Lease.

SECTION 14.3. Except as otherwise set forth in Section 14.1 hereof, for purposes of this Article 14, (i) any increase in the amount of issued and/or outstanding capital stock of any corporate tenant and/or the creation of one or more additional classes of capital stock of any corporate tenant, in a single transaction or a series of related or unrelated transactions, resulting in a change in the legal or beneficial ownership of such tenant so that the shareholders of such tenant existing immediately prior to such transaction or series of transactions shall no longer own a majority of the issued and outstanding capital stock of such tenant shall be deemed an assignment of this Lease and (ii) any Person or legal representative of Tenant, to whom Tenant's interest under this Lease passes by operation of law, or otherwise, shall be bound by the provisions of this Article 14. Tenant agrees to furnish to Landlord on request at any time such information and assurances as Landlord may reasonably request that Tenant has not violated the provisions of this Article 14.

## ARTICLE 15

### ACCESS TO PREMISES

SECTION 15.1. Tenant shall permit Landlord, Landlord's agents and any public utilities servicing the Premises to erect, use and maintain, now and hereafter, concealed ducts, pipes and conduits in and through the Premises. Landlord or Landlord's agents shall have the right to enter the Premises at all reasonable times upon (except in case of emergency) reasonable prior notice, which notice may be oral, to examine the same, to show the same to prospective purchasers or Mortgagees and to make such repairs, alterations, improvements or additions (i) as Landlord may deem necessary or desirable to the Premises, or (ii) which Landlord may elect to perform at least ten (10) days after notice (except in an emergency when no notice shall be required) following Tenant's failure to make repairs or perform any work which Tenant is obligated to make or perform under this Lease, or (iii) for the purpose of complying with Requirements, and Landlord shall be allowed to take all material into and upon the Premises that may be required therefor without the same constituting an eviction or constructive eviction of Tenant in whole or in part and the Fixed Rent (and any other item of Rental) shall in no respect abate or be reduced by reason of said repairs, alterations, improvements or additions, wherever located, or while the same are being made, by reason of loss or interruption of business of Tenant, or otherwise. Landlord shall promptly repair any damage caused to the Premises by such work, alterations, improvements or additions.

SECTION 15.2. If Tenant is not present when for any reason entry into the Premises may be necessary or permissible, Landlord or Landlord's agents may enter the same without rendering Landlord or such agents liable therefor.

SECTION 15.3. Landlord also shall have the right at any time, without the same constituting an actual or constructive eviction and without incurring any liability to Tenant therefor, to change the arrangement or location of entrances or passageways, doors and doorways, and corridors, stairs, toilets or other parts of the Premises, provided any such change does not unreasonably



interfere with, or deprive Tenant of access to, the Premises; to put so-called "solar film" or other energy-saving installations on the inside and outside of the windows; and to change the name, number or designation by which the Premises is commonly known.

ARTICLE 16

CERTIFICATE OF OCCUPANCY

SECTION 16.1. Tenant shall not at any time, now or hereafter, use or occupy the Premises, directly or indirectly, in violation of the certificate of occupancy for the Premises and in the event that any Governmental Authority hereafter contends or declares by notice, violation, order or in any other manner whatsoever that the Premises are used for a purpose that is a violation of such certificate of occupancy, Tenant shall, upon three (3) Business Days' written notice from Landlord or any Government Authority, immediately discontinue such use of the Premises.

ARTICLE 17

DEFAULT

SECTION 17.1. Each of the following events shall be an "EVENT OF DEFAULT" under this Lease:

(A) if Tenant shall on any occasion default in the payment when due of any installment of Fixed Rent or Additional Rent or in the payment when due of any other item of Rental and such default shall continue for five (5) business days from and after the date when written notice has been received by Tenant; or

(B) if the Premises shall become vacant or abandoned; or

(C) if Tenant's interest in this Lease shall devolve upon or pass to any person, whether by operation of law or otherwise, except as specifically permitted by the provisions of Article 14 hereof; or

(D) (1) if Tenant shall not, or shall be unable to, or shall admit in writing Tenant's inability to, as to any obligation, pay Tenant's debts as they become due; or

(2) if Tenant shall commence or institute any case, proceeding or other action (a) seeking relief on Tenant's behalf as debtor, or to adjudicate it a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to Tenant or Tenant's debts under any existing or future law of any jurisdiction, domestic or foreign, relating to bankruptcy, insolvency, reorganization or relief of debtors, or (b) seeking appointment of a receiver, trustee, custodian or other similar official for it or for all or any substantial part of its property; or

(3) if Tenant shall make a general assignment for the benefit of creditors; or

(4) if any case, proceeding or other action shall be commenced or instituted against Tenant (a) seeking to have an order for relief entered against Tenant as debtor or to adjudicate Tenant a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to Tenant or Tenant's debts under any existing or future law of any jurisdiction, domestic or foreign, relating to bankruptcy, insolvency, reorganization or relief of debtors, or (b) seeking appointment of a receiver, trustee, custodian or other similar official for Tenant or for all or any substantial part of Tenant's property, which either (i) results in any such entry of an order for relief, adjudication of bankruptcy or insolvency or such an appointment or the issuance or entry of any other order having a similar effect or (ii) remains undismissed for a period of sixty (60) days; or

(5) if a trustee, receiver or other custodian shall be appointed for any substantial part of the assets of Tenant which appointment is not vacated or effectively stayed within thirty (30) days; or

(E) if Tenant shall default in the observance or performance of any other term, covenant or condition of this Lease on Tenant's part to be observed or performed including, without limitation, the terms and conditions of Article 27 hereof, and Tenant shall fail to remedy such default within ten (10) days after written notice by Landlord to Tenant of such default, or if such default is of such a nature that it cannot with due diligence be completely remedied within said period of ten (10) days and the continuation of which for the period required for cure will not subject Landlord to the risk of criminal liability or foreclosure of any Mortgage, if Tenant shall not, (i) within said ten (10) day period advise Landlord of Tenant's intention duly to institute all steps necessary to remedy such situation, (ii) duly institute within said ten (10) day period, and thereafter diligently and continuously prosecutes to completion all steps necessary to remedy the same and (iii) completes such remedy within such time after the date of the giving of said notice by Landlord as shall reasonably be necessary.

SECTION 17.2. If an Event of Default shall occur, Landlord may, at any time thereafter, at Landlord's option, give written notice to Tenant stating that this Lease and the Term shall expire and terminate on the date specified in such notice whereupon this Lease and the Term and all rights of Tenant under this Lease shall automatically expire and terminate as if the date specified in the notice given pursuant to this Section 17.2 were the Fixed Expiration Date and Tenant immediately shall quit and surrender the Premises, but Tenant shall remain liable for damages as provided herein or pursuant to law. Anything contained herein to the contrary notwithstanding, if such termination shall be stayed by order of any court having jurisdiction over any proceeding described in Section 17.1(D), or by federal or state statute, then, following the expiration of any such stay, or if the trustee appointed in any such proceeding, Tenant or Tenant as debtor-in-possession fails to assume Tenant's obligations under this Lease within the period prescribed therefor by law or within one hundred twenty (120) days after entry of the order for relief or as may be allowed by the court, or if said trustee, Tenant or Tenant as debtor-in-possession shall fail to provide adequate protection of Landlord's right, title and interest in and to the Premises or adequate assurance of the complete and continuous future performance of Tenant's obligations under this Lease, Landlord, to the extent permitted by law or by leave of the court having jurisdiction over such proceeding, shall have the right, at its election, to terminate this Lease on three (3) days' notice to Tenant, Tenant as debtor-in-possession or said trustee and upon the expiration of said three (3) day period this Lease shall cease and expire as aforesaid and

Tenant, Tenant as debtor-in-possession or said trustee shall immediately quit and surrender the Premises as aforesaid.

SECTION 17.3. If, at any time, (i) Tenant shall consist of two (2) or more Persons, or (ii) Tenant's obligations under this Lease shall have been guaranteed by any Person other than Tenant, or (iii) Tenant's interest in this Lease has been assigned, the word "Tenant" as used and referred to in this Lease, shall be deemed to mean any one or more of the persons primarily or secondarily liable for Tenant's obligations under this Lease. Any monies received by Landlord from or on behalf of Tenant during the pendency of any proceeding of the types referred to in Section 17.1(D) hereof shall be deemed paid as compensation for the use and occupancy of the Premises and the acceptance of any such compensation by Landlord shall not be deemed an acceptance of Rental or a waiver on the part of Landlord of any rights under Section 17.2 hereof.

## ARTICLE 18

### REMEDIES AND DAMAGES

#### SECTION 18.1.

(A) If any Event of Default shall occur, or this Lease and the Term shall expire and come to an end as provided in Article 17 hereof:

(1) Tenant shall quit and peacefully surrender the Premises to Landlord, and Landlord and its agents may immediately, or at any time after such Event of Default or after the date upon which this Lease and the Term shall expire and come to an end, re-enter the Premises or any part thereof, without notice, either by summary proceedings, or by any other applicable action or proceeding or otherwise (without being liable to indictment, prosecution or damages therefor), and may repossess the Premises and dispossess Tenant and any other persons from the Premises by summary proceedings or otherwise and remove any and all of their property and effects from the Premises (and Tenant shall remain liable for damages as provided herein or pursuant to law); and

(2) Landlord, at Landlord's option, may relet the whole or any part or parts of the Premises from time to time, either in the name of Landlord or otherwise, to such tenant or tenants, for such term or terms ending before, on or after the Fixed Expiration Date, at such rent or rentals and upon such other conditions, which may include concessions and free rent periods, as Landlord, in Landlord's sole discretion, may determine; provided, however, that Landlord shall have no obligation to relet the Premises or any part thereof and shall in no event be liable for refusal or failure to relet the Premises or any part thereof, or, in the event of any such reletting, for refusal or failure to collect any rent due upon any such reletting, and no such refusal or failure shall operate to relieve Tenant of any liability under this Lease or otherwise affect any such liability, and Landlord, at Landlord's option, may make such Alterations, in and to the Premises as Landlord, in Landlord's sole discretion, shall consider advisable or necessary in connection with any such reletting or proposed reletting, without relieving Tenant of any liability under this Lease or otherwise affecting any such liability.

(B) Tenant hereby waives the service of any notice of intention to re-enter or to institute legal proceedings to that end that may otherwise be required to be given under any

present or future law. Tenant, on its own behalf and on behalf of all persons claiming through or under Tenant, including all creditors of Tenant, does further hereby waive any and all rights that Tenant and all such persons might otherwise have under any present or future law to redeem the Premises, or to re-enter or repossess the Premises, or to restore the operation of this Lease, after (a) Tenant shall have been dispossessed by a judgment or by warrant of any court, or (b) any re-entry by Landlord, or (c) any expiration or termination of this Lease and the Term, whether such dispossession, re-entry, expiration or termination is by operation of law or pursuant to the provisions of this Lease. The words "re-entry", "re-enter" and "re-entered" as used in this Lease shall not be deemed to be restricted to their technical legal meanings. In the event of a breach or threatened breach by Tenant, or any persons claiming through or under Tenant, of any term, covenant or condition of this Lease, Landlord shall have the right to enjoin such breach and the right to invoke any other remedy allowed by law or in equity as if reentry, summary proceedings and other special remedies were not provided in this Lease for such breach. The right to invoke the remedies hereinbefore set forth are cumulative and shall not preclude Landlord from invoking any other remedy allowed at law or in equity.

SECTION 18.2.

(A) If this Lease and the Term shall expire and come to an end as provided in Article 17 hereof, or by or under any summary proceeding or any other action or proceeding, or if Landlord shall re-enter the Premises as provided in Section 18.1 hereof, or by or under any summary proceeding or any other action or proceeding, then, in any of said events:

(1) Tenant shall pay to Landlord all Fixed Rent, Additional Rent and other items of Rental payable under this Lease by Tenant to Landlord to the date upon which this Lease and the Term shall have expired and come to an end or to the date of re-entry upon the Premises by Landlord, as the case may be;

(2) Tenant also shall be liable for and shall pay to Landlord, as damages, any deficiency ("DEFICIENCY") between the Rental for the period which otherwise would have constituted the unexpired portion of the Term and the net amount, if any, of rents collected under any reletting effected pursuant to the provisions of Section 18.1(2) for any part of such period (after first deducting from the rents collected under any such reletting all of Landlord's expenses in connection with the termination of this Lease, Landlord's re-entry upon the Premises and such reletting including, but not limited to, all repossession costs, brokerage commissions, attorneys' fees and disbursements, alteration costs and other expenses of preparing the Premises for such reletting); any such Deficiency shall be paid in monthly installments by Tenant on the days specified in this Lease for payment of installments of Fixed Rent; Landlord shall be entitled to recover from Tenant each monthly Deficiency as the same shall arise, and no suit to collect the amount of the Deficiency for any month shall prejudice Landlord's right to collect the Deficiency for any subsequent month by a similar proceeding; and

(3) whether or not Landlord shall have collected any Deficiency as aforesaid, Landlord shall be entitled to recover from Tenant, and Tenant shall pay to Landlord, on demand, in lieu of any further Deficiency as and for liquidated and agreed final damages, a sum equal to the amount by which the unpaid Rental for the period which otherwise would have constituted the unexpired portion of the Term exceeds the then fair and reasonable rental value of the Premises for the same period; if, before presentation of proof of such liquidated damages

to any court, commission or tribunal, the Premises, or any part thereof, are relet by Landlord for the period which otherwise would have constituted the unexpired portion of the Term, or any part thereof, the amount of rent reserved upon such reletting shall be deemed, prima facie, to be the fair and reasonable rental value for the part or the whole of the Premises so relet during the term of the reletting.

(B) Tenant shall in no event be entitled to any rents collected or payable under any reletting, whether or not such rents exceed the Fixed Rent reserved in this Lease. Nothing contained in Article 17 hereof or this Article 18 shall be deemed to limit or preclude the recovery by Landlord from Tenant of the maximum amount allowed to be obtained as damages by any statute or rule of law, or of any sums or damages to which Landlord may be entitled in addition to the damages set forth in this Section 18.2.

#### ARTICLE 19

##### FEES AND EXPENSES

SECTION 19.1. If an Event of Default shall have occurred, Landlord may (1) perform the same for the account of Tenant, or (2) make any expenditure or incur any obligation for the payment of money in connection with any obligation owed to Landlord, including, but not limited to, reasonable attorneys fees and disbursements in instituting, prosecuting or defending any action or proceeding, and in either case the cost thereof with interest thereon at the Applicable Rate shall be deemed to be Additional Rent hereunder and shall be paid by Tenant to Landlord within ten (10) days after rendition of any bill or statement to Tenant therefor. In addition, Tenant shall pay Landlord any reasonable attorneys fees and disbursements incurred by Landlord in connection with any proceeding in which the value for the use and occupancy of the Premises by Tenant is being determined (whether or not any such proceeding results from a default by Tenant under this Lease).

SECTION 19.2. If Tenant shall fail to pay any installment of Fixed Rent, Additional Rent or any other item of Rental for a period longer than five (5) days after the same shall have become due, Tenant shall pay to Landlord, in addition to such installment of Fixed Rent, Additional Rent or other item of Rental, as the Case may be, as a late charge and as Additional Rent, a sum equal to interest at the Applicable Rate on the amount unpaid, computed from the date such payment was due, without regard to any such grace period, to and including the date of payment.

#### ARTICLE 20

##### NO REPRESENTATIONS BY LANDLORD

SECTION 20.1. LANDLORD AND LANDLORD'S AGENTS HAVE MADE NO REPRESENTATIONS, PROMISES OR WARRANTIES EXPRESS OR IMPLIED, INCLUDING WITHOUT LIMITATION, WARRANTIES OF SUITABILITY, HABITABILITY AND FITNESS FOR A PARTICULAR USE OR PURPOSE WITH RESPECT TO THE PREMISES EXCEPT AS HEREIN EXPRESSLY SET FORTH, AND NO RIGHTS, EASEMENTS OR LICENSES ARE ACQUIRED BY TENANT BY IMPLICATION OR OTHERWISE EXCEPT AS EXPRESSLY SET FORTH HEREIN. TENANT SHALL ACCEPT POSSESSION OF THE

PREMISES IN ITS "AS IS" CONDITION ON THE COMMENCEMENT DATE, AND LANDLORD SHALL HAVE NO OBLIGATION TO PERFORM ANY WORK OR MAKE ANY INSTALLATIONS IN ORDER TO PREPARE THE PREMISES FOR TENANT'S OCCUPANCY. THE TAKING OF OCCUPANCY OF THE WHOLE OR ANY PART OF THE PREMISES BY TENANT SHALL BE CONCLUSIVE EVIDENCE, AS AGAINST TENANT, THAT TENANT ACCEPTS POSSESSION OF THE SAME AND THAT THE PREMISES WERE IN GOOD AND SATISFACTORY CONDITION AT THE TIME SUCH OCCUPANCY WAS SO TAKEN. All references in this Lease to the consent or approval of Landlord shall be deemed to mean the written consent or approval executed by Landlord and no other consent or approval of Landlord shall be effective for any purpose whatsoever.

ARTICLE 21

END OF TERM

SECTION 21.1. Upon the expiration or other termination of this Lease, Tenant shall quit and surrender to Landlord the Premises, vacant, broom clean, in good order and condition, ordinary wear and tear excepted, and Tenant shall remove all of Tenant's Alterations as may be required pursuant to Article 6. Tenant shall also remove all of Tenant's Property and all other personal property and personal effects of all persons claiming through or under Tenant, and shall pay the cost of repairing all damage to the Premises occasioned by such removal. Any Tenant's Property or other personal property that remains in, on or at the Premises after the termination of this Lease shall be deemed to have been abandoned and either may be retained by Landlord as its property or may be disposed of in such manner as Landlord may see fit. If Tenant's Property or other personal property or any part thereof is sold, Landlord may receive and retain the proceeds of such sale as the property of Landlord. Any expense incurred by Landlord in removing or disposing of Tenant's Property or other personal property or Alterations required to be removed as provided in Article 6, as well as the cost of repairing all damage to the Premises caused by such removal, shall be reimbursed to Landlord by Tenant, as Additional Rent, on demand.

SECTION 21.2. If the Expiration Date falls on a day which is not a Business Day, then Tenant's obligations under Section 21.1 shall be performed on or prior to such Business Day.

SECTION 21.3. If the Premises are not surrendered upon the expiration or other termination of this Lease, Tenant hereby indemnifies Landlord against liability resulting from delay by Tenant in so surrendering the Premises, including any claims made by any succeeding tenant or prospective tenant founded upon such delay and agrees to be liable to Landlord for (i) any payment or rent concession which Landlord may be required to make to any tenant obtained by Landlord for all or any part of the Premises in order to induce such tenant not to terminate its lease by reason of the holding-over by Tenant and (ii) the loss of the benefit of the bargain if any such tenant shall terminate its lease by reason of the holding-over by Tenant.

SECTION 21.4. Tenant's obligations under this Article 21 shall survive the expiration or termination of this Lease.

ARTICLE 22

POSSESSION

SECTION 22.1. If Landlord shall be unable to deliver possession of the Premises on the Commencement Date for any reason whatsoever, Landlord shall not be subject to any liability therefor and the validity of this Lease shall not be impaired thereby nor the Expiration Date extended, but the Commencement Date shall be postponed until five (5) Business Days following notice from Landlord that the Premises are available for occupancy by Tenant. Tenant expressly waives any right to rescind this Lease under any present or future statute and further expressly waives the right to recover any damages that may result from Landlord's failure to deliver possession of the Premises on the Commencement Date.

ARTICLE 23

NO WAIVER

SECTION 23.1. No act or thing done by Landlord or Landlord's agents during the Term shall be deemed an acceptance of a surrender of the Premises, and no agreement to accept such surrender shall be valid unless in writing signed by Landlord. No employee of Landlord or of Landlord's agents shall have any power to accept the keys to the Premises prior to the termination of this Lease. The delivery of keys to any employee of Landlord or of Landlord's agents shall not operate as a termination of this Lease or a surrender of the Premises.

SECTION 23.2. The failure of Landlord to seek redress for violation of, or to insist upon the strict performance of, any covenant or condition of this Lease shall not prevent a subsequent act, which would have originally constituted a violation, from having all of the force and effect of an original violation. The receipt by Landlord of Fixed Rent, Additional Rent or any other item of Rental with knowledge of the breach of any covenant of this Lease shall not be deemed a waiver of such breach. No provision of this Lease shall be deemed to have been waived by Landlord, unless such waiver shall be in writing and shall be signed by Landlord. No payment by Tenant or receipt by Landlord of a lesser amount than the Rental then due and payable shall be deemed to be other than on account of the earliest item(s) of Rental, or as Landlord may elect to apply the same, nor shall any endorsement or statement on any check or any letter accompanying any check or payment be deemed an accord and satisfaction, and Landlord may accept such check or payment without prejudice to Landlord's right to recover the balance due of the Rental or to otherwise pursue any other remedy in this Lease provided. This Lease contains the entire agreement between the parties and all prior negotiations and agreements are merged herein. Any executory agreement hereafter made shall be ineffective to change, discharge or effect an abandonment of this Lease in whole or in part unless such executory agreement is in writing and signed by the party against whom enforcement of the change, discharge or abandonment is sought.

ARTICLE 24

WAIVER OF TRIAL BY JURY

SECTION 24.1. Tenant hereby waives trial by jury in any action or proceeding brought by or against the Tenant with respect to any matters whatsoever arising out of or in any way connected with this Lease, the relationship of Landlord and Tenant, Tenant's use or occupancy of the Premises, whether during or after the Term, or for the enforcement of any remedy under any statute, emergency or otherwise. If Landlord shall commence any summary proceeding against Tenant, Tenant will not interpose any counterclaim of whatever nature or description in any such proceeding, and will not seek to consolidate such proceeding with any other action which may have been or will be brought in any other court by Tenant or Landlord.

ARTICLE 25

INABILITY TO PERFORM

SECTION 25.1. This Lease and the obligation of Tenant to pay Rental hereunder and to perform all of the other covenants and agreements hereunder on the part of Tenant to be performed shall in no way be affected, impaired or excused because Landlord is unable to fulfill any of Landlord's obligations under this Lease, expressly or implicitly to be performed by Landlord, or because Landlord is unable to make or is delayed in making any repairs, or is unable to supply or is delayed in supplying any services, if Landlord is prevented from or delayed in so doing by reason of acts of God, casualty, strikes or labor troubles, accident, governmental preemption in connection with an emergency, Requirements, conditions of supply and demand which have been or are affected by war or other emergency, or any other cause whatsoever, whether similar or dissimilar to the foregoing, beyond Landlord's reasonable control ("UNAVOIDABLE DELAYS").

ARTICLE 26

NOTICES

SECTION 26.1.

(A) Except as otherwise expressly provided in this Lease, any bills, statements, consents, notices, demands, requests or other communications given or required to be given under this Lease ("NOTICE(S)") shall be in writing and shall be deemed sufficiently given or rendered if delivered by hand (against a signed receipt) or if deposited with a nationally recognized overnight courier and in either case addressed:

IF TO TENANT:

4801 Woodway Drive, Suite 300E  
Houston, Texas 77056



WITH A COPY TO:

Bracewell & Patterson, L.L.P.  
711 Louisiana St., Suite 2900  
Houston, Texas 77002  
Attn: Thomas W. Adkins

(a) at Tenant's address first set forth in this Lease or (b) at any place where Tenant or any agent or employee of Tenant may be found if given subsequent to Tenant's vacating, deserting, abandoning or surrendering the Premises, and

IF TO LANDLORD:

17402 Bending Cypress  
Cypress, Texas 77429

and any Mortgagee who may have requested the same, by Notice given in accordance with the provisions of this Article 26, at the address designated by such Mortgagee,

or to such other address(es) as either Landlord or Tenant may designate as its new address(es) for such purpose by notice given to the other in accordance with the provisions of this Article 26.

(B) Notices shall be deemed to have been rendered or given (a) on the date delivered, if delivered by hand, or (b) on the day after being deposited with a nationally recognized overnight courier as provided in Section 26.1(A) hereof.

#### ARTICLE 27

##### LANDLORD'S AGREEMENT ON WAIVER

SECTION 27.1. Landlord agrees that from time to time the Tenant shall mortgage and grant security interest in the inventory, equipment, accounts, general intangibles and other personal property of the Tenant (collectively, the "Pledged Property") to Bank One, Texas, N.A., as Agent for a group of lenders (in such capacity, the "Agent"), or to such other lender or lenders from time to time, which Pledged Property may now or hereafter be situated upon the Premises. For valuable consideration, the receipt of which is hereby acknowledged, by the Landlord, the Landlord hereby waives all landlords' liens, whether contractual, statutory, constitutional or otherwise that the Landlord now has or hereafter may obtain against the Pledged Property, and all of the liens, security interests, claims and other interests that the Landlord now has or hereafter may obtain against the Pledged Property. The Landlord agrees that the Agent may, at any time upon reasonable notice to the Landlord, enter and remove the Pledged Property from the Premises. This waiver binds the Landlord, its successors, and assigns.

ARTICLE 28

BROKER

SECTION 28.1. Landlord represents and warrants to Tenant that Landlord has not dealt with any broker or Person in connection with this Lease. Tenant represents and warrants to Landlord that Tenant has not dealt with any broker or Person in connection with this Lease. The execution and delivery of this Lease by Tenant shall be conclusive evidence that Tenant acknowledges that Landlord has relied upon the foregoing representation and warranty. Tenant shall indemnify and hold harmless Landlord from and against any and all claims for commission, fee or other compensation by any broker or Person who claims to have dealt with Tenant in connection with this Lease and for any and all costs incurred by Landlord in connection with such claims, including, without limitation, attorneys' fees and disbursements. The provisions of this Article 28 shall survive the expiration or earlier termination of this Lease.

ARTICLE 29

INDEMNITY

SECTION 29.1. Tenant shall not do or permit any act or thing to be done in, at or upon the Premises that may subject any Indemnitee to any liability or responsibility for injury, damage to persons or property or to any liability by reason of the existence or application of, compliance with or violation of any Requirement, but shall exercise such control over the Premises as to protect each Indemnitee fully against any such liability and responsibility. Tenant shall indemnify and save harmless the Indemnitees from and against (a) all claims of whatever nature against the Indemnitees arising from any act, omission or negligence of Tenant or Persons Within Tenant's Control, (b) all claims against the Indemnitees arising from any accident, injury or damage whatsoever caused to any person or to the property of any person and occurring in or about the Premises during the Term or during Tenant's occupancy of the Premises, unless and to the extent caused by the gross negligence of Landlord or its shareholders, officers and employees, (c) all claims against the Indemnitees arising from any accident, injury or damage occurring outside of the Premises but anywhere within or about the Premises, where such accident, injury or damage results or is claimed to have resulted from an act, omission or negligence of Tenant or Persons Within Tenant's Control, and (d) any breach, violation or non-performance of any covenant, condition or agreement contained in this Lease to be fulfilled, kept, observed and performed by Tenant. This indemnity and hold harmless agreement shall include indemnity from and against any and all liability, claims, fines, suits, demands, costs and expenses of any kind or nature (including, without limitation, attorneys' fees and disbursements) incurred in or in connection with any such claim or proceeding brought thereon, and the defense thereof.

SECTION 29.2. If any claim, action or proceeding is made or brought against any Indemnitee, against which claim, action or proceeding Tenant is obligated to indemnify such Indemnitee pursuant to the terms of this Lease, then, upon demand by the Indemnitee, Tenant, at its sole cost and expense, shall resist or defend such claim, action or proceeding in the Indemnitee's name, if necessary, by such attorneys as the Indemnitee may select, including, without limitation, attorneys for the Indemnitee's insurer. The provisions of this Article 29 shall survive the expiration or earlier termination of this Lease.

ARTICLE 30

ADJACENT EXCAVATION

SECTION 30.1. If an excavation shall be made upon land adjacent to the Premises, or shall be authorized to be made, Tenant shall, upon reasonable advance notice, afford to the person or entity causing or authorized to cause such excavation, a limited license to enter upon the Premises for the purpose of doing such work as said person or entity deems necessary to preserve the walls of any building located on the Premises from injury or damage and to support the same by proper foundations without any claim for eviction or constructive eviction, damages or indemnity against Landlord, or diminution or abatement of Rental.

ARTICLE 31

RENEWAL OPTIONS

SECTION 31.1. Provided that the Tenant is not in default with respect to any of its obligations to the Landlord under and pursuant to the terms and conditions of this Lease at the time each Option (as such term is hereinafter defined) is to be exercised, the Tenant shall have the option to renew this Lease for two (2) additional five (5) year periods [the option with respect to each additional five (5) year period is referred to herein as an "OPTION" and, collectively, all of the options granted herein are referred to as the "OPTIONS"] as follows:

OPTION PERIOD 1 shall commence on July 1, 2002 and shall continue up to and including June 30, 2007.

OPTION PERIOD 2 shall commence on July 1, 2007 and shall continue up to and including June 30, 2012.

(each of the aforementioned option periods is individually referred to herein as an "OPTION PERIOD" and, collectively, all of the aforementioned Option Periods are referred to herein as "OPTION PERIODS")

SECTION 31.2. Each Option granted to the Tenant pursuant to the provisions of Section 31.1 hereof shall be exercised by the Tenant giving written notice to the Landlord of the Tenant's intent to exercise the Option not less than one-hundred eighty (180) days prior to the expiration of the Initial Term or not less than one-hundred eighty (180) days prior to the expiration of the Option Period which is then in effect, as the case may be. Time is of the essence in the exercise of the Options and should Tenant fail to exercise any of said Options by timely notice, said Options shall lapse and be of no further force or effect.

SECTION 31.3. In the event that the Tenant exercises the Option with respect to any Option Period, the Landlord and the Tenant hereby agree that this Lease shall continue in full force and effect and remain unamended during the applicable Option Period AND specifically, without limitation, that the Fixed Rent payable by the Tenant to the Landlord during such Option Period shall be increased on each anniversary date from and after the Commencement Date in accordance with the provisions of Article 8 hereof.

ARTICLE 32

RENT REGULATION

SECTION 32.1. If at any time or times during the Term of this Lease, the Rental reserved in this Lease is not fully collectible by reason of any Requirement, Tenant shall enter into such agreements and take such other steps as Landlord may request and as may be legally permissible to permit Landlord to collect the maximum rents that may from time to time during the continuance of such legal rent restriction be legally permissible (and not in excess of the amounts reserved under this Lease). Upon the termination of such legal rent restriction (a) the Rental shall become and thereafter be payable hereunder in accordance with the amounts reserved in this Lease for the remainder of the Term, and (b) Tenant shall pay to Landlord, if legally permissible, an amount equal to (i) the items of Rental that would have been paid pursuant to this Lease but for such legal rent restriction less (ii) the rents paid by Tenant to Landlord during the period or periods such legal rent restriction was in effect. This provision shall survive the expiration or earlier termination of this Lease to the maximum enforceable extent.

ARTICLE 33

COVENANT OF QUIET ENJOYMENT

SECTION 33.1. Landlord covenants that, upon Tenant paying all Fixed Rent and Additional Rent and observing and performing all the terms, agreements, covenants, provisions and conditions of this Lease on Tenant's part to be observed and performed, Tenant may peaceably and quietly enjoy the Premises, subject nevertheless to the terms and conditions of this Lease; provided, however, that no eviction of Tenant by reason of the foreclosure of any Mortgage now or hereafter affecting the Premises shall be construed as a breach of this covenant nor shall any action by reason thereof be brought against Landlord, and provided further that this covenant shall bind and be enforceable against Landlord or any successor to Landlord's interest, subject to the terms hereof, only so long as Landlord or any successor to Landlord's interest, is in possession and is collecting rent from Tenant but not thereafter.

ARTICLE 34

MISCELLANEOUS

SECTION 34.1. This Lease is presented for signature by Tenant and it is understood that this Lease shall not constitute an offer by or be binding upon Landlord unless and until Landlord shall have executed and delivered a fully executed copy of this Lease to Tenant.

SECTION 34.2. The obligations of Landlord under this Lease shall not be binding upon Landlord named herein after the sale, conveyance, assignment or transfer by such Landlord (or upon any subsequent landlord after the sale, conveyance, assignment or transfer by such subsequent landlord) of its interest in the Premises, as the case may be, and in the event of any such sale, conveyance, assignment or transfer, Landlord shall be and hereby is entirely freed and relieved of all covenants and obligations of Landlord under this Lease thereafter arising, and the transferee shall be deemed to have assumed, subject to the remaining provisions of this Section 34.2, all obligations of the Landlord under this Lease arising after the effective date of the

transfer. No trustee, partner, principal, shareholder, director or officer of Landlord (collectively, the "PARTIES") shall have any direct or personal liability for the performance of Landlord's obligations under this Lease, and Tenant shall look solely to Landlord's interest in the Premises to enforce Landlord's obligations hereunder and shall not otherwise seek any damages against Landlord or any of the Parties whatsoever. Tenant shall not look to any other property or assets of Landlord or any property or assets of any of the Parties in seeking either to enforce Landlord's obligations under this Lease or to satisfy a judgment for Landlord's failure to perform such obligations.

SECTION 34.3. Notwithstanding anything contained in this Lease to the contrary, all amounts payable by Tenant to or on behalf of Landlord under this Lease, whether or not expressly denominated Fixed Rent, Additional Rent or Rental, shall constitute rent for the purposes of Section 502(b)(7) of the Bankruptcy Code.

SECTION 34.4. Neither this Lease nor any memorandum of this Lease shall be recorded without the prior written consent of the Landlord, which consent may be withheld by the Landlord in its sole and absolute discretion.

SECTION 34.5. Except as otherwise expressly stated in this Lease, any consent or approval required to be obtained from Landlord may be granted by Landlord in its sole and absolute discretion. In any instance in which Landlord agrees not to act unreasonably, Tenant hereby waives any claim for damages against or liability of Landlord that Tenant may have based upon any assertion that Landlord has unreasonably withheld or unreasonably delayed any consent or approval requested by Tenant, and Tenant agrees that its sole remedy shall be an action or proceeding to enforce any related provision or for specific performance, injunction or declaratory judgment. If with respect to any required consent or approval Landlord is required by the express provisions of this Lease not to unreasonably withhold or delay its consent or approval, and if it is determined in any such proceeding referred to in the preceding sentence that Landlord acted unreasonably, the requested consent or approval shall be deemed to have been granted; however, Landlord shall have no liability whatsoever to Tenant for its refusal or failure to give such consent or approval. Tenant's sole remedy for Landlord's unreasonably withholding or delaying consent or approval shall be as provided in this Section 34.5.

SECTION 34.6. Landlord shall have the right at any time, and from time to time, to amend unilaterally the provisions of this Lease if Landlord is advised by its counsel that all or any portion of the Rental paid by Tenant to Landlord hereunder is, or may be deemed to be, unrelated business taxable income within the meaning of the United States Internal Revenue Code or regulations issued thereunder, and Tenant agrees that it will execute all documents necessary to effect any such amendment, provided that no such amendment shall increase Tenant's payment obligations or other liability under this Lease nor reduce Landlord's obligations hereunder.

SECTION 34.7. If Tenant shall remain in possession of the Premises after the Expiration Date, without the execution by both Tenant and Landlord of a new lease, Tenant, at the election of Landlord, shall be deemed to be occupying the Premises as a Tenant from month-to-month, at a monthly rental equal to three (3x) times the Rental payable during the last month of the Term, subject to all the other conditions, provisions and obligations of this Lease insofar as the same are applicable to a month-to-month tenancy.

SECTION 34.8. This Lease shall be construed without regard to any presumption or other rule requiring construction against the party causing this Lease to be drafted. If any words or phrases in this Lease are stricken out or otherwise eliminated, whether or not any other words or phrases have been added, this Lease shall be construed as if the words or phrases so stricken out or otherwise eliminated were never included in this Lease and no implication or inference shall be drawn from the fact that such words or phrases were stricken out or otherwise eliminated.

SECTION 34.9. If any of the provisions of this Lease, or the application thereof to any person or circumstance, shall, to any extent, be invalid or unenforceable, the remainder of this Lease, or the application of such provisions to persons or circumstances other than those as to whom or which it is held invalid or unenforceable, shall not be affected thereby and shall remain valid and enforceable, and every provision of this Lease shall be valid and enforceable to the fullest extent permitted by law.

SECTION 34.10. Landlord shall have the right to erect any gate, chain or other obstruction or to close off any portion of the Premises to the public at any time to the extent necessary to prevent a dedication thereof for public use.

SECTION 34.11. Tenant hereby represents to Landlord that it is not entitled, directly or indirectly, to diplomatic or sovereign immunity and Tenant agrees that in all disputes arising directly or indirectly out of this Lease Tenant shall be subject to service of process in, and the jurisdiction of the courts of, the State of Texas. The provisions of this Section 34.11 shall survive the expiration of this Lease.

SECTION 34.12. This Lease contains the entire agreement between the parties and all prior negotiations and agreements are merged into this Lease. Except as provided in Section 34.6 this Lease may not be changed, abandoned or discharged, in whole or in part, nor may any of its provisions be waived except by a written agreement that (a) expressly refers to this Lease, (b) is executed by the party against whom enforcement of the change, abandonment, discharge or waiver is sought and (c) is permissible under the Mortgage(s).

SECTION 34.13. Any apportionment or prorations of Rental to be made under this Lease shall be computed on the basis of a three hundred sixty (360) day year, with twelve (12) months of thirty (30) days each.

SECTION 34.14. The laws of the State of Texas applicable to contracts made and to be performed wholly within the State of Texas shall govern and control the validity, interpretation, performance and enforcement of this Lease without regard to principles of conflicts of law.

SECTION 34.15. If Tenant is a corporation, each person executing this Lease on behalf of Tenant hereby covenants, represents and warrants that Tenant is a duly incorporated or duly qualified (if foreign) corporation and is authorized to do business in the State of Texas (a copy of evidence thereof to be supplied to Landlord upon request); and that each person executing this Lease on behalf of Tenant is an officer of Tenant and that he or she is duly authorized to execute, acknowledge and deliver this Lease to Landlord (a copy of a resolution to that effect to be supplied to Landlord upon request).

SECTION 34.16. The captions are inserted only as a matter of convenience and for reference and in no way define, limit or describe the scope of this Lease nor the intent of any provision thereof.

SECTION 34.17. The covenants, conditions and agreements contained in this Lease shall bind and inure to the benefit of Landlord and Tenant and their respective legal representatives, heirs, successors, and, except as otherwise provided in this Lease, their assigns.

SECTION 34.18. For the purposes of this Lease and all agreements supplemental to this Lease, unless the context otherwise requires:

(A) The words "herein", "hereof", "hereunder" and "hereby" and words of similar import shall be construed to refer to this Lease as a whole and not to any particular Article or Section unless expressly so stated.

(B) Tenant's obligations hereunder shall be construed in every instance as conditions as well as covenants, each separate and independent of any other terms of this Lease.

(C) Reference to Landlord as having "no liability" or being "without liability" shall mean that Tenant shall not be entitled to terminate this Lease, or to claim actual or constructive eviction, partial or total, or to receive any abatement or diminution of rent, or to be relieved in any manner of any of its other obligations hereunder, or to be compensated for loss or injury suffered or to enforce any other right or liability whatsoever against Landlord under or with respect to this Lease or with respect to Tenant's use or occupancy of the Premises.

(D) Reference to "termination of this Lease" or "expiration of this Lease" and words of like import includes expiration or sooner termination of this Lease and the Term and the estate hereby granted or cancellation of this Lease pursuant to any of the provisions of this Lease or by law. Upon the termination of this Lease, the Term and estate granted by this Lease shall end at noon on the date of termination as if such date were the Fixed Expiration Date, and neither party shall have any further obligation or liability to the other after such termination except (i) as shall be expressly provided for in this Lease, and (ii) for such obligations as by their nature under the circumstances can only be, or by the provisions of this Lease, may be, performed after such termination, and, in any event, unless expressly otherwise provided in this Lease, any liability for a payment (which shall be apportioned as of such termination) which shall have accrued to or with respect to any period ending at the time of termination shall survive the termination of this Lease.

(E) Words and phrases used in the singular shall be deemed to include the plural and vice versa, and nouns and pronouns used in any particular gender shall be deemed to include any other gender.

(F) The rule of "ejusdem generis" shall not be applicable to limit a general statement following or referable to an enumeration of specific matters to matters similar to the matters specifically mentioned.

IN WITNESS WHEREOF, Landlord and Tenant have duly executed this Lease as of the day and year first above written.

"LANDLORD":

THOMAS J. BEATY

By: \_\_\_\_\_

BONNIE J. BEATY

By: \_\_\_\_\_

"TENANT":

ACCURATE AIR SYSTEMS, INC.

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_



## LEASE

THIS LEASE is dated as of the 1st day of July, 1997, by and between NOTHUM DEVELOPMENT, L.L.C., an Arizona limited liability company ("Lessor"), and TRI-CITY MECHANICAL, INC., an Arizona corporation ("Lessee").

## W I T N E S S E T H:

## ARTICLE 1

## DEFINITIONS

The following terms used in this Lease shall have the meanings described below:

**BUILDINGS.** All the buildings, and fixtures and equipment therein or thereon situated upon the Demised Premises, during the Lease Term, and any and all renewals, replacements, additions to and substitutions for any such Buildings and fixtures and equipment.

**DEFAULT RATE.** Fifteen percent (15%) per annum.

**DEMISED PREMISES.** The real property, exclusive of the Buildings more particularly described on EXHIBIT "A", together with the easements, rights, privileges and appurtenances thereto.

**EVENT OF DEFAULT.** The occurrence of any event described in ARTICLE 17.

**EXTENDED LEASE TERM.** One (1) additional period of sixty (60) months, commencing upon the expiration of the Initial Lease Term, when exercised by Lessee in accordance with SS.2.02.

**FEE MORTGAGE.** A mortgage on the fee interest in the Demised Premises, which shall be deemed to include a deed of trust and the note or other credit instrument secured thereby.

**FEE MORTGAGEE.** A mortgagee under a Fee Mortgage, or the trustee and beneficiary under a deed of trust.

**FORCE MAJEURE.** Any delay in Lessee's or Lessor's non-monetary obligations caused by acts of God or the public enemy, or by casualty or by strike, or by governmental restrictions upon the availability or use of labor or materials necessary to perform such obligations, or by reason of any other fact, matter or condition beyond the control of Lessee or Lessor, respectively.

**FORECLOSURE.** The exercise of remedies under a Fee Mortgage and the enforcement of the rights of a beneficiary under a deed of trust and the exercise of the power of sale thereunder and the tender and acceptance of a warranty deed in lieu of foreclosure or forfeiture.

## 1

**IMPOSITIONS.** All real estate taxes, personal property taxes, rental taxes (whether denominated as rental, privilege, sales, transportation, excise or otherwise), assessments (arising from an improvement district or otherwise), sewer rents, water meter and water charges, levies, license and permit fees, charges for public utilities and all other charges of whatsoever kind and nature and whether any of the foregoing be general or special, ordinary or extraordinary, or foreseen or unforeseen, which at any time during the Lease Term may be imposed upon the rent and other payments due hereunder, the Demised Premises, the Building and/or the Improvements.

**IMPROVEMENTS.** All improvements and structures other than Buildings at any time during the Lease Term erected or situated upon the Demised Premises, and any and all renewals, replacements, additions to and substitutions for any such Improvements.

**INITIAL LEASE TERM.** The term commencing on the Rent Commencement Date and ending upon the expiration of one hundred twenty (120) months thereafter.

**LEASE.** This agreement.

**LEASE DATE.** The date first set forth above, which shall be deemed to be the date of execution of this Lease by both parties.

**LEASE TERM.** Where no distinction is made, the Initial Lease Term and/or the Extended Lease Term(s).

**MINIMUM RENT.**

(a) Forty-Four Thousand One Hundred Seventy-Five and No/100 Dollars (\$44,175.00) representing the first month's Minimum Rent shall be payable upon the execution hereof.

(b) Minimum Rent shall increase on each second anniversary of the Rent Commencement Date by an amount equal to six percent (6%) of the Minimum Rent due for the preceding month.

(c) Minimum Rent during the Extended Lease Term shall be payable in accordance with EXHIBIT "B" attached hereto.

(d) Minimum Rent shall be payable on the first day of each month (except as provided in subparagraph (a) above). If the Rent Commencement

Date is on other than the first day of the month, the monthly rent for the first month and last month shall be prorated on a daily basis.

NEW IMPOSITIONS. Impositions arising as a result of the events more particularly described in SS.5.07.

PAD. The aggregate of the Demised Premises and the Improvements and Buildings thereon.

RENT COMMENCEMENT DATE. The date upon which the Lessor receives a Certificate of Occupancy for the Building and Improvements.

ARTICLE 2

DEMISED PREMISES--TERM OF LEASE--OPTION

ss.2.011. (a) Lessor, in consideration of the rents, covenants and agreements hereinafter reserved, on the part of Lessee to be performed, leases to Lessee, and Lessee leases from Lessor, the Pad, including all Buildings and Improvements therein or thereon as of the Rent Commencement Date, for the Lease Term, unless this Lease shall sooner terminate as hereinafter provided.

(b) Lessor hereby represents and warrants to Lessee that it is the owner of fee simple title to the Demised Premises subject to all matters of record.

ss.2.012. (a) Lessee shall have one (1) option to extend the Initial Lease Term for an additional period of sixty (60) months, such Extended Lease Term to begin upon the expiration of the Initial Lease Term. The same terms and conditions as herein set forth shall apply to the Extended Lease Term (except the option to renew), and the Minimum Rent shall be as set forth in ARTICLE 1. If Lessee shall elect to exercise the aforesaid options, it shall do so by giving written notice to Lessor not less than twelve (12) months prior to the expiration of the Initial Lease Term.

(b) Notwithstanding the foregoing, Lessee may exercise the option only if, at the time of notice of exercise of such option and as of the date of the commencement of the Extended Lease Term, an Event of Default does not then exist.

ARTICLE 3

RENT

ss.3.011. Lessee covenants and agrees to pay to Lessor during the entire Lease Term, Minimum Rent (commencing on the Rent Commencement Date) at the times, in the amounts and as provided in ARTICLE 1 and all other charges and amounts at the time provided for herein together with all sales, rental, excise or privilege taxes payable on such amounts. The Minimum Rent and other charges shall be paid to Lessor by Lessee without notice or demand and without abatement, deduction or set-off.

ss.3.012. Commencing on the Rent Commencement Date, Lessee covenants and agrees to pay all Impositions to Lessor, or as otherwise provided herein.

ss.3.013. It is the purpose and intent of Lessor and Lessee that the Minimum Rent shall be absolutely net to Lessor, so that this Lease shall yield, net to Lessor, the Minimum Rent specified herein and that all costs, operating expenses, Impositions, excise, rental, sales and privilege taxes, premiums, fees, interest, charges, expenses, reimbursements and obligations of every kind and nature whatsoever relating to the Pad, excepting only certain taxes of Lessor as provided in SS.4.02 and any Fee Mortgage which may arise or become due during or out of the term of this Lease, shall be paid or discharged by the Lessee, and that Lessor shall be indemnified and saved harmless by Lessee from and against such costs, operating expenses, Impositions, premiums, fees, interest, charges, expenses, reimbursements and obligations, and Lessee expressly covenants to pay all of the foregoing.

ARTICLE 4

PAYMENT OF TAXES, ASSESSMENTS AND CARRYING CHARGES

ss.4.011. Lessee shall pay or cause to be paid (except as provided in SS.4.02), before any fine, penalty, interest or cost may be added thereto, all Impositions, provided, however, that:

(a) if, by law, any Imposition may at the option of the Lessee be paid in installments (whether or not interest shall accrue on the unpaid balance of such Imposition), Lessee may exercise the option to pay the same, including any accrued interest on the unpaid balance of such Imposition, in installments and, in such event, shall pay only such installments as may become due during the term of this Lease as the same respectively become due and before any fine, penalty, further interest or cost may be added thereto; and

(b) any Imposition, except Impositions which have been converted into installment payments by Lessee, as referred to in SS.4.01(A), relating to a fiscal period of the taxing authority, a part of which period is included within the Lease Term and a part of which is included in a period of time after the expiration of the Lease Term, shall, whether or not such Imposition shall be assessed or become a lien upon the Demised Premises or the Building or the Improvements, or shall become payable, during the Lease Term, be adjusted between Lessor and Lessee as of the expiration of the Lease Term, so that Lessee shall pay that portion of such Imposition which that part of such fiscal period included in the period of time before the expiration of the Lease Term bears to such fiscal period, and Lessor shall pay the remainder thereof.

ss.4.012. Nothing herein contained shall require Lessee to pay municipal, state or federal income, gift, estate, inheritance or excess profits taxes assessed against Lessor.

ss.4.013. Lessee shall have the right to contest the amount or validity, in whole or in part, of any Imposition by appropriate proceedings diligently conducted in good faith, in which event, notwithstanding the provisions of SS.4.01, Lessee may postpone or defer payment of such Imposition if neither the Demised Premises, the Building nor the Improvements would by reason of such postponement or deferment be in danger of being forfeited or lost. Upon the termination of any such proceedings, Lessee shall pay the amount of such Imposition or part thereof, if any, as finally determined in such proceedings, the payment of which may have been deferred during the prosecution of such proceedings.

ss.4.014. Lessor shall join in any proceedings referred to in SS.4.03 if the provisions of any law, rule or regulation shall require that such proceedings be brought by or in the name of Lessor, in which event Lessor shall join in such proceedings or permit the same to be brought in its name, provided that Lessor shall not ultimately be subjected to any liability for the payment of any fees, including reasonable counsel fees, costs and expenses. Lessor may retain independent counsel in connection with any such proceedings and Lessee shall pay the actual, reasonable and necessary expenses therefor. Lessee shall indemnify Lessor from and against all claims arising from Lessee's contest of any Impositions.

ss.4.015. Lessor and Lessee agree to each furnish the other with whatever information, documents or records that may be required and otherwise cooperate so as to permit the Demised Premises

to be assigned a separate Maricopa County Tax Roll number. Lessee agrees that should the Demised Premises be separately assessed, Lessee shall pay such separately assessed Imposition(s) according to this Article.

ss.4.016. In the event the Demised Premises are not separately assessed, but are part of a larger parcel for assessment purposes (hereinafter referred to as the "larger parcel") then Impositions for which Lessee is responsible hereunder shall be a fractional portion of the Impositions on the larger parcel the numerator of which shall be the total area of the Demised Premises and the denominator of which shall be the total area of the larger parcel as to the "land" portion of such assessment. If, however, there are Buildings and Improvements on the Demised Premises, then the same calculation shall be made by comparing the area of the Buildings on the Demised Premises to the area of the buildings on the larger parcel and adding such amount to the "land" amount to determine Lessee's total share. With respect to any Impositions which under the laws then in force may be evidenced by improvement or other bonds, or may be paid in annual installments, only the amount of such annual installment (with appropriate proration for any partial year) and statutory interest shall be included with the computation of the Impositions levied against the Demised Premises.

ss.4.017. If at any time during the Lease Term, any authority having the power to tax shall alter the methods and/or standards of taxation and assessment, against the legal or equitable interests of Lessor or Lessor's lender in the Demised Premises or the remainder of the Pad in whole or in part, so as to impose a tax or taxes in lieu of or in addition to the tax or taxes in existence as of the date of this Lease, such taxes or assessments shall be paid by Lessee. Any special, unforeseen or extraordinary New Impositions, however described, shall be considered as "taxes" for the purposes of this Lease, excluding, however, from such taxes all general income taxes, gift taxes, inheritance taxes and estate taxes.

ss.4.018. Upon Lessor's notice to Lessee given at least fifteen (15) days prior to the first day of any month, Lessor may require Lessee to deposit with Lessor, in monthly installments, an amount equal to one-twelfth (1/12) of the sum of the estimated Impositions for the calendar year in which the notice was given ("Impounds"). Such estimate shall be based upon the prior calendar year's Impositions. The Impounds shall be payable at the same time and manner as Minimum Rent is due and payable under this Lease. If the Impounds for the Impositions for a calendar year are insufficient to fully discharge the Impositions for that calendar year, Lessor may notify Lessee at any time after the end of such calendar year, and Lessee shall within ten (10) days thereafter deposit with Lessor an amount equal to such deficiency. If the amount Lessee has paid in Impounds for the prior calendar year is greater than the amount of actual Impositions for such calendar year, then such excess shall, at the option of Lessee, be refunded to Lessee by February 15th of the subsequent calendar year or applied to the current year's Impound payments. If Lessee shall commit an Event of Default, then all Impound amounts then held by Lessor may be applied to any amounts due under this Lease whether for Minimum Rent, Impositions, late charges, interest or other charges, in any order Lessor may determine. Lessee shall not be entitled to interest on Impounds. If Impositions are not being paid by Lessor, Lessee has the right to pay Impositions directly. In the event Lessor shall fail to pay, for any reason, any taxes, assessments or Impositions as they become due, Lessee shall be given prompt notice thereof and, at the option of Lessee, Lessee may require that all Impositions be deposited in escrow, with an escrow company of Lessee's choosing. In that event, all costs associated with the escrow shall be paid equally by Lessor and Lessee.

#### ARTICLE 5

## SURRENDER

ss.5.011. Lessee covenants and agrees to not hold over without the express written consent of Lessor and shall on the last day of the Lease Term or upon any earlier termination of this Lease, or upon any entry or re-entry by Lessor upon the Demised Premises after an Event of Default, surrender and deliver up the Pad to the Lessor and, subject to the provisions of SS.14.03(B), in good order, condition and repair, reasonable wear and tear excepted.

ss.5.012. Any property of Lessee which shall remain on the Demised Premises, or in the Buildings, after the termination or expiration of this Lease and the removal of Lessee from the Demised Premises and the Buildings may, at the option of Lessor, be deemed to have been abandoned by Lessee and either may be retained by Lessor as its property or be disposed of in such manner as Lessor may see fit.

## ARTICLE 6

### INSURANCE

ss.6.011. Lessor shall, during the course of construction of the Building and the Improvements, keep the Pad and all fixtures and equipment installed therein by Lessor insured against loss or damage by fire and against loss or damage by such other risks now or hereafter embraced by "Special Form Property Insurance," so-called, and against such other risks or hazards and in such amounts as a Fee Mortgagee shall require. Thereafter, such insurance shall be maintained by Lessee during the Lease Term for a sum not less than one hundred percent (100%) of the full replacement value of the Buildings and Improvements erected upon the Demised Premises and not less than one hundred percent (100%) of the full replacement cost of the furniture, fixtures and equipment. Such insurance shall also insure the interest of Lessor and any Fee Mortgagee. A Standard Mortgagee Endorsement shall be provided for the benefit of such Fee Mortgagee. Flood hazard insurance shall also be maintained by Lessee if required by any Fee Mortgagee.

ss.6.012. In addition to the insurance required above, Lessee, at its sole cost and expense (except as provided below), shall purchase and maintain during the entire Lease Term:

(a) A "Commercial General Liability Insurance" policy, so called, insuring against claims for bodily injury, death or property damage, occurring in, on or about the Demised Premises, the Building and Improvements and on, in or about the adjoining streets, avenues, property and passageways, naming the Lessor and the Lessee as the insureds, such insurance to afford minimum protection, during the term of this Lease, of not less than the amounts required by any Fee Mortgagee and in any event in an initial amount of not less than Two Million Dollars (\$2,000,000.00). Such amount shall be increased upon the reasonable demand of Lessor. Reasonableness for the purposes of this subparagraph shall be determined by comparing the construction of the Building and Improvements and the use then being made of the Pad with other similarly constructed and operating facilities in the Phoenix metropolitan area.

(b) Such other insurance insuring against such risks, in such amounts with such protective provisions as may be reasonably required from time to time by any Fee

Mortgagee. Reasonableness for the purposes of this subparagraph shall be determined by comparing the construction of the Building and Improvements and the use then being made of the Pad with other similarly constructed and operating facilities in the Phoenix metropolitan area.

(c) "Business Income (and Extra Expense) Commercial Property Insurance - Rental Value only," so called, against loss of rent due to fire and the risks now or hereafter embraced by "Special Form Property Insurance," so-called, naming the Lessor as a loss payee.

ss.6.013. All insurance provided for in this ARTICLE 6 shall be effected under valid and enforceable policies issued by insurers of recognized responsibility which are licensed to do business in the State of Arizona and which have been approved by Lessor and any Fee Mortgagee as to the qualifications of insurers and the amounts of insurance to be written by each. Prior to the Rent Commencement Date, and thereafter not less than twenty (20) days prior to the expiration dates of the expiring policies theretofore furnished pursuant to this ARTICLE 6, originals of the policies or evidence thereof on form ACORD 27, in the case of bodily injury and property damage liability insurance, bearing notations evidencing the payment of premiums or accompanied by other evidence of such payment, shall be delivered by Lessee to the person or entity entitled to approve any insurance company as provided above in this section.

ss.6.014. Subject to ARTICLE 14 and to the provisions of any Fee Mortgage, the proceeds of any insurance required to be maintained by the provisions of this Article shall be payable to Lessor, or if paid to Lessee, Lessee shall immediately and simultaneously pay them to Lessor, and shall be used to restore the Demised Premises, Buildings and Improvements to their original approximate value, and to replace furniture, fixtures and equipment but for any use allowed by this Lease.

ss.6.015. Each insurance policy shall, to the extent obtainable, have attached thereto (a) an endorsement that such policy shall not be cancelled or materially changed without at least thirty (30) days' prior written notice to the Lessor and any Fee Mortgagee; and (b) an endorsement to the effect that no act or omission of the Lessee shall invalidate the interest of such person or entity entitled to such notice.

ss.6.016. Each policy of insurance shall name, as an additional insured, the Lessor and, in addition, such other persons, firms or corporations as may be required under the terms of any Fee Mortgage. Copies of such policies shall be delivered to Lessor.

ss.6.017. If, notwithstanding the provisions of SS.6.05, any insurance which Lessee is required to obtain and maintain is cancelled, Lessee shall, before such cancellation is effective (or, if such cancellation is effective upon receipt of notice, within five (5) business days of the date such notice is received), replace such insurance with other insurance providing essentially the same or better coverages and essentially the same or greater indemnity amounts. Lessee shall promptly deliver to Lessor evidence of such replacement insurance.

ss.6.018. If Lessee fails to obtain the replacement insurance as required by SS.6.07, then Lessor may (but shall not be required to) procure such replacement insurance on Lessee's behalf and charge Lessee the premiums together with a ten percent (10%) handling charge, payable upon demand.

ss.6.019. Lessor and Lessee each hereby waive any and all rights of recovery against the other or against the officers, employees, agents and representatives of the other on account of loss or damage occasioned to such waiving party or its property or the property of others under its control to the extent that such loss or damage is insured against under any Special Form Property Insurance policy which either may have in force at the time of such loss or damage. Lessee and Lessor shall, at the time of procuring the policies of insurance required under this Lease, give notice to the insurance carrier or carriers that the foregoing mutual waiver of right of recovery is contained in this Lease and each party shall cause each insurance policy obtained by it to provide that the insurance company waives any right of recovery, by way of subrogation, against either party in connection with any damage covered by any policy of insurance.

#### ARTICLE 7

##### LESSOR'S RIGHT TO PERFORM LESSEE'S COVENANTS

ss.7.011. If Lessee shall at any time fail to pay any sum, Imposition, cost or expense other than the Minimum Rent as provided in ARTICLE 3 which it is obligated to pay under the terms of this Lease, then Lessor, after fifteen (15) days' written notice to Lessee (or without notice or upon a shorter notice period in case of an emergency), and without waiving or releasing either party from any obligation under this Lease and without being considered an election of remedies, may, but shall be under no obligation to pay any such sum, Imposition, cost or expense; provided, however, that no such payment shall be made if Lessee has in fact paid the same before the expiration of the time period and has given notice to Lessor.

ss.7.012. If Lessee shall at any time fail to perform or observe any covenant or condition contained in this Lease, the performance of which involves something more than merely the payment of money, then Lessor, after thirty (30) days' written notice to Lessee (or without notice or upon a shorter notice period in case of an emergency), and without waiving or releasing Lessee from any obligation and without being considered an election of remedies, may perform the same for the account of Lessee and charge Lessee the actual cost of any such performance; provided, however, that if Lessee has in fact performed its obligation before the expiration of the notice period, or in the case of performance which by its nature cannot be completed within the notice period, has begun diligent performance of the same and is continuing such performance in a diligent fashion, and has given Lessor notice of such performance, then in such event, Lessor shall not commence such performance on its own part.

ss.7.013. All sums so paid or expended by Lessor and all costs and expenses, including reasonable attorneys' fees, incurred by Lessor in connection with the performance of any such act, together with interest thereon at the Default Rate from the respective dates of Lessor's making of each such payment or incurring of each such cost and expense, including reasonable attorneys' fees, shall be paid by Lessee to Lessor on demand.

#### ARTICLE 8

##### REPAIRS AND MAINTENANCE OF THE DEMISED PREMISES

ss.8.011. Throughout the entire Lease Term, Lessee, at its sole cost and expense, shall take good care of the Demised Premises, the Building and Improvements, and all plumbing, electrical and



HVAC systems located thereon or therein and all furniture, fixtures and equipment located therein and shall keep the same in first class order and condition, and make all necessary repairs and replacements thereto, interior and exterior, structural and nonstructural, ordinary and extraordinary or radical, foreseen and unforeseen with due diligence and in good faith. When used in this ARTICLE 8, the term "repairs" shall include all necessary replacements, renewals and alterations. All repairs made by Lessee shall be at least equal in quality and class to the original work. Lessee shall do, or cause others to do, all necessary repairs of supporting walls and walls of the Building and comply with all laws and ordinances with respect thereto and do every other act or thing for the safety and preservation thereof which may be necessary by reason of any excavation, subsurface construction, remodeling or other building operation upon any adjoining property or street, avenue, alley, or passageway. After the initial construction of the Building and Improvements, any subsequent modifications, improvements or alterations to the Pad, the cost of which exceeds Five Thousand Dollars (\$5,000.00), shall require Lessor's prior written consent to the plans therefor. Upon the expiration or earlier termination of this Lease, all electrical, plumbing and HVAC systems located on, in or under the Pad and all fixtures and equipment (except Lessee's personal property and equipment not attached to the Building) shall be surrendered to Lessor in good operating and clean condition, normal wear and tear excepted.

ss.8.012. The necessity for and adequacy of repairs to the Demised Premises, the Buildings and Improvements and the furnishings and equipment therein pursuant to SS.8.01 shall be measured by the standard which is appropriate for buildings of similar construction and class, provided that Lessee shall in any event make all repairs necessary to avoid any structural damage or injury to the Buildings.

ss.8.013. Subject to the provisions of SS.8.05, Lessee shall put, keep and maintain all portions of the Demised Premises, the Buildings and Improvements and the sidewalks, curbs, landscaping, entrances, passageways and all areas adjoining the same in a first class condition, clean and orderly, free of dirt, vermin, rubbish and unlawful obstructions.

ss.8.014. Lessor shall not be required to furnish any services or facilities, equipment or fixtures, or to make any repairs or alterations in or to the Pad and Lessee hereby assumes the full and sole responsibility for the condition, operation, repair, replacement, maintenance and management of the Pad. Lessee will inspect the Demised Premises on the Rent Commencement Date and will accept the Demised Premises in its "as is" condition, subject to any punchlist items and the provisions of SS.8.05.

ss.8.015. (a) Lessee shall not use the Demised Premises as a storage facility for any "Hazardous Substances," but Lessee may use and sell in a lawful manner on the Demised Premises those Hazardous Substances which are normal and customary in the conduct of Lessee's business. Lessee shall not install or use any underground storage tank or other underground receptacle on the Demised Premises, whether or not for Hazardous Substances.

(b) Lessee hereby agrees to indemnify Lessor and hold Lessor harmless for, from and against any and all losses, liabilities, including strict liability, damages, injuries, expenses, including reasonable attorneys' fees, costs of any settlement or judgment and claims of any and every kind whatsoever (including, without limitation, any losses, liabilities, including strict liability, damages, injuries, expenses, including reasonable attorneys' fees, costs of any settlement or judgment or claims asserted or arising under any Environmental Law [as defined in ss.8.05(c)(ii)]) paid, incurred or suffered by, or asserted against, Lessor by any person or entity or governmental agency for, with respect to, or as a direct or indirect result of, the presence on or under or the escape, seepage, leakage, spillage, discharge, emission, discharging

or release from or otherwise occurring on the Demised Premises of any Hazardous Substances during Lessee's possession of the Pad, except as caused by Lessor.

(c) (i) For purposes of this Lease, "Hazardous Substances" shall mean and include any contaminant, pollutant or hazardous or toxic substances, materials or wastes or other environmentally regulated materials including, but not limited to, those substances, materials and wastes listed in the United States Department of Transportation Table (49 CFR 172.101) or by the Environmental Protection Agency as hazardous substances, materials and wastes or which are or become regulated under any applicable local, state or federal law, code or ordinance, and all rules and regulations promulgated thereunder, including, without limitation, any material, waste or substance which is (i) petroleum, (ii) asbestos, (iii) polychlorinated biphenyls, (iv) designated as a "Hazardous Substance" pursuant to Section 311 of the Clean Water Act, 33 U.S.C. Section 1251 et seq. (33 U.S.C. Section 1321), or listed pursuant to Section 307 of the Clean Water Act (33 U.S.C. Section 13171, (v) defined as a "hazardous waste" pursuant to Section 1004 of the Resource Conservation and Recovery Act, 42 U.S.C. Section 6901 et seq. (42 U.S.C. Section 6903) or (vi) defined as a "Hazardous Substance" pursuant to Section 101 of the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. Section 9601 et seq. (42 U.S.C. Section 9601).

(ii) For purposes of this Lease, "Environmental Laws" shall mean and include all state, federal and local laws, codes and ordinances, and all rules and regulations promulgated thereunder, governing or in any way relating to the generation, handling, manufacturing, treatment, storage, use, transportation, spillage, leakage, dumping, discharge or disposal (whether legal or illegal, accidental or intentional) of any Hazardous Substances.

(d) If Lessee receives any notice of (i) the happening of any material event involving the spill, release, leak, seepage, discharge or cleanup of any Hazardous Substance into or upon (A) the air, (B) soils or any improvements located thereon, (C) soil vapors, (D) surface water or groundwater, or (E) the sewer, septic system or waste treatment, storage or disposal system servicing the Demised Premises (any of which is hereafter referred to as a "Hazardous Discharge"), or (ii) any complaint, order, citation, claim, directive or notice with regard to (F) air emissions, (G) spills, releases or discharges to soils or any improvements located thereon, soil vapors, surface water, groundwater or the sewer, septic system or waste treatment, storage or disposal systems servicing the Demised Premises, (H) noise emissions, (I) solid or liquid waste disposal, (J) the use, generation, storage, transportation or disposal of Hazardous Substances, or (K) other environmental, health or safety matters affecting Lessee, the Demised Premises, any improvements located thereon, or the business therein conducted (any of which is hereafter referred to as an "Environmental Complaint"), then Lessee shall immediately notify Lessor orally and in writing of said notice.

(e) Lessor shall have the right but not the obligation, and without limitation of Lessor's rights under this Lease, to enter onto the Demised Premises or to take such other actions as it deems necessary or advisable to clean up, remove, resolve or minimize the impact of, or otherwise deal with, any such Hazardous Substance or Environmental Complaint following receipt of any notice from any person or entity asserting the existence of any Hazardous Substance or an Environmental Complaint pertaining to any part of the Premises which could result in an order, suit or other action against Lessee or which, in the reasonable opinion of Lessor, could jeopardize its interest in the Premises.

(f) Lessor hereby represents and warrants to Lessee that it has received no notice of any violation of Environmental Laws, the existence of any Hazardous Substances on the Demised Premises, any Environmental Complaints, any Hazardous Discharges, or any other environmental conditions relating to the Demised Premises other than as set forth in the Phase I \_\_\_\_\_ prepared by \_\_\_\_\_ and dated \_\_\_\_\_, 19\_\_\_\_, a copy of which was received by Lessee on or about July \_\_, 1997.

#### ARTICLE 9

##### COMPLIANCE WITH LAWS, ORDINANCES AND REGULATIONS

ss.9.011. Throughout the entire Lease Term, Lessee, at its sole cost and expense, shall promptly comply with all present and future laws, ordinances, orders, rules, regulations and requirements of all federal, state and municipal governments, any national or local Insurance Rating Bureau, or any other body exercising functions similar to those of any of the foregoing, which may be applicable to the Demised Premises, the Buildings or the Improvements, or any part thereof, or the sidewalks, curbs, passageways, alleys, entrances, coverings or roof-like structures placed upon or extending over any sidewalk, or any space adjacent thereto, or to the use or manner of use of the Demised Premises, the Building or the Improvements, or any part thereof, or the owners, lessees or occupants thereof. The foregoing shall include the matters set forth in SS.8.05. Lessor hereby represents and warrants to Lessee that it has received no notice that the Demised Premises are not in compliance with any law, ordinance, order, rule, regulation or requirement of any federal, state or municipal governments, or any other body exercising functions similar to those of any of the foregoing.

ss.9.012. Lessee shall likewise observe and comply with, or shall cause to be observed and complied with, all the requirements of the general comprehensive liability insurance, the "Special Form Property Insurance," so called, and any other insurance policies at any time in force with respect to the Demised Premises, the Building and Improvements.

ss.9.013. Lessee shall have the right, after prior written notice to Lessor, to contest by appropriate legal proceedings, diligently conducted in good faith, in the name of Lessee or Lessor or both, without cost or expense to Lessor, the validity or application of any law, ordinance, order, rule, regulation or requirement of the nature referred to herein, subject to the following:

(a) If by the terms of any such law, ordinance, order, rule, regulation or requirement, compliance therewith pending the prosecution of any such proceeding may legally be delayed without the incurrence of any lien, charge, liability or penalty of any kind against the Demised Premises, the Building or the Improvements or Lessee's leasehold interest therein and without subjecting Lessor to any liability, civil or criminal, for failure so to comply therewith, Lessee may delay compliance therewith until the final determination of such proceeding.

(b) If any lien, charge or civil liability would be incurred by reason of any such delay, Lessee nevertheless, on the prior written consent of Lessor (such consent not to be unreasonably withheld), may contest as aforesaid and delay as aforesaid, provided that such delay would not subject Lessor to criminal liability and Lessee (i) furnishes to

Lessor security, reasonably satisfactory to Lessor against any loss or injury by reason of such contest or delay, and (ii) prosecutes the contest with due diligence and in good faith.

(c) Lessor shall, at Lessee's sole cost and expense, including reasonable attorneys' fees, execute and deliver any appropriate papers which may be necessary or proper to permit Lessee to contest the validity or application of any such law, ordinance, order, rule, regulation or requirement. Lessee shall indemnify Lessor from any loss, cost or expense arising from such proceedings.

#### ARTICLE 10

##### CONSTRUCTION; DISCHARGE OF LIENS

ss.10.01. Lessor shall be responsible for the construction of the Building and Improvements, in accordance with the provisions of this ARTICLE 10.

ss.10.02. Lessor has caused to be prepared the outline specifications and site plan for the Building and Improvements attached hereto as EXHIBITS "C" AND "D" (the "Preliminary Plans"). If Lessor has not already done so, Lessor shall choose an architect who shall cause to be prepared final plans for the construction of the Building and Improvements based upon the Preliminary Plans (the "Final Plans").

ss.10.03. After preparation of the Final Plans Lessor shall award a construction contract to a contractor. The contractor shall commence and diligently prosecute to completion, the construction of the Building and Improvements in substantial conformance with the Final Plans. Lessor's approval of the Final Plans for the Building and Improvements, shall not be deemed a representation or warranty that the Final Plans comply with all laws and ordinances. Lessor shall have no liability whatsoever for the Building or Improvements or construction defects or the failure of the contractor to construct the Buildings and Improvements in accordance with the Final Plans and all laws and ordinances. Lessor shall, and hereby does, assign to Lessee, on a non-exclusive basis all of the contractor's warranties and all other warranties in respect of such construction. Title to the Buildings and Improvements shall be in Lessor at all times. Lessor agrees, in its construction contract with a contractor, to give Lessee the right, during construction, to pay for additions to the construction project, at Lessee's sole expense, including additional contractor supervision costs and changes to work already completed. All such additions shall be communicated to the contractor through Lessor. The construction contract shall provide that Lessee or Lessee's subcontractor shall have reasonable access to the property to construct any Improvements or additions to the job site, with the consent of the contractor, and after approval of same by Lessor, such consent not to be unreasonably withheld.

ss.10.015. Lessee shall not create or permit to be created or to remain, and shall, as to any matter arising after the Lease Date caused by Lessee, discharge, any lien, encumbrance or charge (levied on account of any Imposition or any mechanic's or materialman's lien or any mortgage, security interest or otherwise) which might be or become a lien, encumbrance or charge upon the Demised Premises or the Building or any part thereof or the income therefrom having a priority or preference over or ranking on a parity with the interest of Lessor in the Demised Premises or the Building or Improvements or any part

thereof or the income therefrom, or which would have a parity or priority over any Fee Mortgage and Lessee shall not suffer any other matter or thing whereby the interest of Lessor or a Fee Mortgagee in the Demised Premises or any part thereof or Lessor's interest in the Demised Premises, the Building and Improvements or the income therefrom might be impaired; provided that any Imposition may, after the same becomes a lien on the Demised Premises or the Building, be paid or contested in accordance with ARTICLE 4 and any mechanic's, laborer's or materialman's lien may be discharged in accordance with SS.10.02. In order to further assure Lessor that no mechanic's, laborer's or materialmen's lien will be placed or remain against the Pad, Lessee, prior to any construction by Lessee costing more the Five Thousand Dollars (\$5,000.00), shall furnish to Lessor a bond or other assurances satisfactory to Lessor that such persons shall be paid.

ss.10.026. If any mechanic's or materialman's lien shall at any time be filed against the Demised Premises or the Building or Improvements or any part thereof (other than in connection with the initial construction contemplated by ARTICLE 10), Lessee, within thirty (30) days after notice of the filing thereof, shall cause the same to be discharged of record by payment, deposit, bond, order of a court of competent jurisdiction or otherwise. If Lessee shall fail to cause such lien to be discharged within such period, then, in addition to any other right or remedy, Lessor may, but shall not be obligated to, discharge the same either by paying the amount claimed to be due or by procuring the discharge of such lien by deposit or by bonding proceedings, and in any such event Lessor shall be entitled, if Lessor so elects, to compel the prosecution of an action for the enforcement of such lien by the lienor and to pay the amount of the judgment in favor of the lienor with interest, costs and allowances. Lessee agrees to reimburse and to pay to the Lessor on demand any amount so paid by Lessor and all costs and expense, including reasonable attorneys' fees, incurred by Lessor in connection therewith, together with interest thereon at the Default Rate from the respective dates of Lessor's notice to Lessee of the making of the payment or the incurring of the cost and expense, including such reasonable attorneys' fees.

#### ARTICLE 11

##### NO WASTE

ss.11.011. Lessee shall not do or suffer any waste to the Demised Premises or the Building or Improvements.

#### ARTICLE 12

##### USE OF DEMISED PREMISES

ss.12.011. Lessee shall continuously use the Pad for warehouse, general office, storage and metal fabrication and for no other purposes. Lessee shall not use or allow the Demised Premises or the Building or the Improvements or any part thereof to be used or occupied for any unlawful purpose or in violation of any laws and shall not suffer any act to be done or any condition to exist on the Demised Premises or the Building or Improvements or any part thereof or any article to be brought thereon, which may be dangerous, or which may, in law, constitute a nuisance, public or private, or which may make void or voidable any insurance then in force with respect thereto. Notwithstanding the foregoing permitted uses, the Demised Premises shall not be used for an adult bookstore, adult novelty shop, theater, adult theater, bar, nightclub, place of adult performances or the sale of pornography.

ss.12.012. Lessee shall not suffer or permit the Demised Premises or the Building or Improvements or any portion thereof, to be used by the public, as such, without restriction or in such manner as might reasonably tend to impair Lessor's title to the Demised Premises or to Lessor's reversionary interest in the Building and Improvements, or in such manner as might reasonably make possible a claim or claims of adverse possession by the public, as such, or of implied dedication of the Demised Premises or the Building or the Improvements or any portion thereof.

#### ARTICLE 13

##### ENTRY ON DEMISED PREMISES BY LESSOR

ss.13.011. In addition to Lessor's right of entry under any other provision of this Lease, Lessee shall permit Lessor and its authorized representatives to enter the Pad at all reasonable times after reasonable notice for the purpose of (a) inspecting the same, and (b) making any necessary repairs thereto and performing any work therein that may be necessary by reason of Lessee's failure to make any such repairs or perform any such work or to commence the same for thirty (30) days after written notice from Lessor or without notice in case of an emergency. Nothing herein contained shall create or imply any duty upon the part of Lessor to make any such repairs or do any such work.

ss.13.012. Lessor shall have the right to enter the Pad at all reasonable times during usual business hours and after reasonable telephone notice to Lessee for the purpose of showing the same to prospective purchasers, mortgagees, or lessees. Lessor may place "for sale" and/or "for lease" signs on the Demised Premises.

#### ARTICLE 14

##### DAMAGE OR DESTRUCTION

ss.14.011. In case of damage to or destruction of the Demised Premises or the Building or Improvements by fire or other casualty, Lessee, at Lessee's sole cost and expense, shall restore, repair, replace, rebuild or alter the same as nearly as possible to their value, condition and character immediately prior to such damage or destruction. Such restoration, repairs, replacements, rebuilding or alterations shall be commenced with due diligence, and in good faith, and prosecuted with due diligence and in good faith, subject to Force Majeure. In the event of damage to or the destruction of the Demised Premises and/or the Building and Improvements resulting in a loss exceeding in the aggregate Two Thousand Five Hundred Dollars (\$2,500.00), Lessee shall promptly give written notice thereof to Lessor.

ss.14.012. All insurance money shall be paid to and held by Lessor, or if paid to Lessee, Lessee shall immediately and simultaneously pay the insurance money to Lessor, and Lessor shall then pay such insurance money to Lessee during the course of reconstruction on account of such damage or destruction, less the actual cost, fees and expenses, if any, incurred in connection with the adjustment of the loss, and any amount deposited for demolition and reconstruction shall be applied to the payment of the cost of the demolition, restoration, repairs, replacement, rebuilding or alterations, including the cost of temporary repairs or the protection of property pending the completion or permanent restoration, repairs, replacements, rebuilding or alterations (all of which temporary repairs, protection of property and permanent restoration,

repairs, replacement, rebuilding or alterations are hereinafter collectively referred to as the "restoration"). Upon the completion of, and payment for, the restoration, any balance of the insurance money at the time available for distribution shall be paid to Lessee.

ss.14.013. If the Demised Premises and the Buildings and Improvements shall be damaged or destroyed by fire or other casualty within two (2) years prior to the expiration of the Lease Term and the cost of restoration exceeds the sum of Two Hundred Fifty Thousand Dollars (\$250,000.00), during any Lease Term, as estimated by a licensed architect or a licensed professional engineer, selected by Lessee and approved in writing by Lessor (such approval not to be unreasonably withheld and, if Lessor fails to act thereon within ten (10) days from time of receipt thereof, Lessor shall be deemed to have approved Lessee's selection) Lessee shall have the option of:

(a) restoring, repairing, replacing, rebuilding or altering the Demised Premises, Building and Improvements as provided in this Lease, or

(b) terminating this Lease by written notice to Lessor given within sixty (60) days after such destruction or damage.

ss.14.014. In the event of a termination under SS.14.03.(B), Lessee shall not be entitled to any portion of the proceeds of any insurance except for insurance which covers possessions of Lessee which Lessee has the right to remove pursuant to SS.8.01, including but not limited to, the fire insurance, all of which shall become the sole property of the Lessor.

ss.14.015. At the time of a termination under SS.14.03.(B), Lessee shall at once surrender and deliver up the Demised Premises and the Building and Improvements and the furnishings, equipment and records therein into the possession and use of Lessor and remove all of its personal effects unrelated to the operation of the Demised Premises. Lessee upon such termination, surrender and removal, shall be released and discharged from any and all obligations that would have otherwise thereafter accrued had this Lease not been so terminated.

#### ARTICLE 15

##### CONDEMNATION

ss.15.011. If at any time during the Lease Term, title to the whole or materially all of the Demised Premises shall be taken by the exercise of the right of condemnation or eminent domain, or by agreement between Lessor, Lessee and those authorized to exercise such right, this Lease shall terminate and expire on the date of such taking, and the Minimum Rent required to be paid by Lessee shall be apportioned and paid to the date of such taking. For purposes of this SS.15.01 "materially all of the Demised Premises" shall be deemed to have been taken if the portion of the Demised Premises not so taken cannot be so repaired or reconstructed so as to constitute a complete rentable structure capable of producing a pro portionately fair and reasonable net annual income, after the payment of all expenses thereof and all Minimum Rent and other charges required to be paid by Lessee hereunder and after performance of all covenants, agreements, terms and provisions herein and by law provided to be performed and paid by Lessee. The average net annual income produced by the Demised Premises during the two (2) year period (or such

shorter period if this Lease has not been in existence for two (2) years) immediately preceding such a taking shall be deemed to constitute a fair and reasonable net annual income for the purposes of this SS.15.01.

ss.15.012. In the event of the taking of the whole or materially all of the Demised Premises at any time during the Lease Term, the rights of Lessor and Lessee to share in the net proceeds of any award for the Demised Premises, Building and Improvements and damages upon any such taking shall be as follows and in the following order of priority:

(a) To Lessor, that portion of the award that shall represent compensation for the value of the Demised Premises the Building and Improvements.

(b) To Lessor, an amount representing the excess, if any, of the fair market value of the Leasehold for the Lease Term over the Minimum Rent payable hereunder.

(c) To Lessee (to the extent available after the payment in (a) and (b) above), the proceeds attributable to Lessee's personal property.

ss.15.013. If at any time during the Lease Term, title to less than the whole or less than materially all of the Demised Premises shall be taken as aforesaid, all of the award or awards resulting from said condemnation shall be held by Lessor and applied and paid over to the cost of demolition, repair and restoration in the same manner and subject to the same conditions as those provided in SS.SS.14.01 and 14.02 hereof with respect to insurance and other monies. Any balance remaining in the hands of Lessor after payment of such costs of demolition, repair and restoration as aforementioned, shall be retained by Lessor and the Minimum Rent adjusted as provided in SS.15.04.

ss.15.014. If title to less than the whole or less than materially all of the Demised Premises shall be taken as aforesaid, this Lease shall continue, but the Minimum Rent thereafter payable by Lessee shall be reduced from the date of such partial taking in the same proportion as the number of square feet in the Demised Premises left after the taking bears to the total number of square feet in the Demised Premises immediately prior to such taking. Notwithstanding the foregoing, there shall be no adjustment or abatement of Minimum Rent in the event that a portion of the Demised Premises are taken or dedicated to the public for the purposes of streets, roads, drainage, utilities, or other easements and such takings or dedications have no material detrimental impact on the business then being conducted on the Demised Premises.

ss.15.015. If the temporary use of the whole or any part of the Demised Premises or the Building or Improvements shall be taken by any lawful power or authority, by the exercise of the right of condemnation or eminent domain, or by agreement between Lessee and those authorized to exercise such right, Lessee shall give prompt notice thereof to Lessor, and the term of this Lease shall not be reduced or affected in any way. Lessee shall continue to pay in full the Minimum Rent and other charges required to be paid hereunder, without reduction or abatement, and Lessee shall be entitled to receive for itself any award or payment made for such use.



ARTICLE 16

MORTGAGES, ASSIGNMENTS, SUBLEASES AND  
TRANSFERS OF LESSEE'S INTEREST

ss.16.011. Lessee shall not assign, mortgage or transfer this Lease or sublease the whole or any portion of the Pad without Lessor's written consent, which consent shall not be unreasonably withheld. Lessor may request detailed information on the finances and operating history of any proposed assignee or sublessee. Lessor shall not be deemed to have unreasonably withheld its consent if it reasonably disapproves the financial condition or operational history of the proposed sublessee or assignee. Upon any assignment to which Lessor has consented, and the assumption of this Lease by the assignee, Lessee shall not be released from any obligations under this Lease falling due and arising out of events occurring after the date of the assignment and assumption. Lessor may condition its consent on the sublessee or assignee agreeing to pay Minimum Rent and other charges hereunder directly to Lessor rather than Lessee.

ss.16.012. Lessor's consent to any single assignment, sublease or other transfer of the whole or any portion of the Pad shall not be deemed to be a consent to any subsequent assignment, sublease or other transfer.

ss.16.03. Assignment, subleasing or any other transfer of this Lease shall not affect the viability or the right of Lessee to exercise any option in this Lease.

ARTICLE 17

DEFAULT

ss.17.011. The following occurrences shall be deemed Events of Default ("Events of Default"):

(a) if any monetary sum due hereunder, including without limitation, Minimum Rent and Impositions, shall not be paid within seven (7) days after written notice that same was not paid when due and payable as to the first such notice in any twelve (12) month period and within three (3) days after written notice that the same was not paid when due and payable as to all subsequent notices in any twelve (12) month period;

(b) Any failure by Lessee to observe or perform any other provision, covenant or condition of this Lease to be observed or performed by Lessee where such failure continues for thirty (30) days after written notice thereof by Lessor to Lessee, provided that if the nature of such failure is such that the same cannot reasonably be cured within such thirty (30) day period, Lessee shall not be deemed to have committed an Event of Default if it shall commence such cure within such thirty (30) day period after Lessor's notice and thereafter rectify and cure said failure within ninety (90) days;

(c) Abandonment of the Demised Premises by Lessee; or

(d) A general assignment by Lessee for the benefit of creditors, or the filing by or against Lessee of any proceeding under any insolvency or bankruptcy law, unless in the case of a proceeding filed against Lessee the same is dismissed within sixty (60) days, or the appointment of a trustee or receiver to take possession of all or substantially all of the assets of Lessee, unless possession is restored to Lessee within thirty (30) days, or any execution or other judicially authorized seizure of all or substantially all of Lessee's assets located upon the Demised Premises or of Lessee's interest in this Lease, unless such seizure is discharged within thirty (30) days, or Lessee's convening of a meeting of its creditors or any class thereof for the purpose of effecting a moratorium upon or composition of its debts;

(e) Any occurrence of one or more of the events set forth in SS.17.01(A), (B), (C) or (D) which is thereafter cured whether or not Lessor is obligated under this Lease to accept Lessee's tender of cure and whether or not such cure was timely made, but which has occurred in three (3) consecutive months or in any four (4) months of any twelve-month period.

ss.17.012. In the event of an Event of a Default by Lessee, Lessor, in addition to any other remedies available to it at law or in equity and without being considered an election of remedies, at its option, may without further notice or demand of any kind to Lessee or any other person:

(a) Declare the Lease Term ended and reenter the Demised Premises and the Buildings and take possession thereof and remove all persons therefrom, and Lessee shall have no further claim thereon or hereunder, except for any personal effects that Lessee uses on a day-to-day basis; or

(b) Without declaring this Lease ended, reenter the Demised Premises and the Buildings and occupy the whole or any part thereof for and on account of Lessee and collect any unpaid rentals and other charges, which have become payable, or which may thereafter become payable; or

(c) Even though Lessor may have reentered the Demised Premises and the Buildings, thereafter elect to terminate this Lease and all of the rights of Lessee in or to the Demised Premises and the Buildings.

ss.17.013. Should Lessor have reentered the Demised Premises and the Buildings under the provisions of SS.17.02(B), Lessor shall not be deemed to have terminated this Lease, or the liability of Lessee to pay any Minimum Rent or other charges thereafter accruing, or to have terminated Lessee's liability for damages under any of the provisions hereof, by any such reentry or by any action, in unlawful detainer or otherwise, to obtain possession of the Demised Premises, unless Lessor shall have notified Lessee in writing that it has elected to terminate this Lease. Lessee further covenants that the service by Lessor of any notice pursuant to the unlawful detainer statutes of the State where the Pad is situated and the surrender of possession pursuant to such notice shall not (unless Lessor elects to the contrary at the time of or at any time subsequent to the serving of such notices and such election is evidenced by a written notice to Lessee) be deemed to be a termination of this Lease.

ss.17.014. Should Lessor elect to terminate this Lease pursuant to the provisions of subparagraph SS.17.02(A) OR (C) above, Lessor may recover from Lessee as damages, the following:

(a) The worth at the time of award of any unpaid Minimum Rent which had been earned at the time of such termination; plus

(b) the worth at the time of award of the amount by which the unpaid Minimum Rent which would have been earned after termination until the time of award exceeds the amount of such rental loss Lessee proves could have been reasonably avoided; plus

(c) the worth at the time of award of the amount by which the unpaid Minimum Rent for the balance of the term after the time of award exceeds the amount of such rental loss that Lessee proves could be reasonably avoided; plus

(d) any other amount necessary to compensate Lessor for all the detriment proximately caused by Lessee's failure to perform its obligations under this Lease or which in the ordinary course of things would be likely to result therefrom, including, but not limited to any costs or expenses incurred by Lessor in (i) retaking possession of the Demised Premises and the Buildings, including reasonable attorneys' fees therefor, (ii) maintaining or preserving the Demised Premises and the Buildings after such Event of Default, (iii) preparing the Demised Premises and the Buildings for reletting to a new tenant, including repairs (iv) leasing commissions, or (v) any other costs necessary or appropriate to relet the Demised Premises and the Buildings; plus

(e) at Lessor's election, such other amounts in addition to or in lieu of the foregoing as may be permitted from time to time by the laws of the State where the Pad is situated.

ss.17.015. As used in SS.17.04 (A) and (B), the "worth at the time of award" is computed by allowing interest at the Default Rate. As used in SS.17.04 (C), the "worth at the time of award" is computed by discounting such amount at the discount rate of the Federal Reserve Bank situated nearest to the location of the Pad at the time of award plus one percent (1%).

ss.17.016. For all purposes of this Article, the term "other charges" shall be deemed to be all sums required to be paid by Lessee pursuant to the terms of this Lease. All such sums, other than the Minimum Rent, shall be computed on the basis of the greatest monthly amount thereof accruing during the immediately preceding sixty (60) month period, except that if it becomes necessary to compute such amount before such a sixty (60) month period has occurred then such amount shall be computed on the basis of the greatest monthly amount thereof accruing during such shorter period.

ss.17.017. In the event of an Event of Default by Lessee, Lessor may at its option permit all of Lessee's fixtures, furniture, equipment, improvements, additions and alterations to remain on the Demised Premises and in that event, and continuing during the length of said Events of Default, Lessor shall have the right to take the exclusive possession of such items and to use same, rent or charge free, until all Events of Defaults are cured or, at its option, at any time during the term of this Lease, to require Lessee to forthwith remove same. In the event of any entry or taking possession of the Demised Premises and the

Buildings as aforesaid, Lessor shall offer to Lessee the opportunity to remove Lessee's own personal effects that are used on a day-to-day basis. In the event Lessee declines after reasonable notice, Lessor shall have the right, but not the obligation, to remove therefrom all or any part of the personal property located therein and may place the same in storage at a public warehouse at the expense and risk of the Lessee or owner or owners thereof. In the event of any entry or taking possession of the Demised Premises after an Event of Default, Lessor shall use its reasonable good faith efforts to re-let the Demised Premises.

ss.17.018. The waiver by Lessor of any breach of any term, covenant or condition herein contained shall not be deemed to be a waiver of such term, covenant or condition or of any subsequent breach of the same or any other term, covenant or condition herein contained. The subsequent acceptance of amounts due hereunder by Lessor shall not be deemed to be a waiver of any preceding breach by Lessee of any term, covenant or condition of this Lease, other than the failure of Lessee to pay the particular rental so accepted, regardless of Lessor's knowledge of such preceding breach at the time of acceptance of such rental. No covenant, term, or condition of this Lease shall be deemed to have been waived by Lessor unless such waiver be in writing signed by Lessor.

ss.17.019. If Lessee shall fail to pay, when the same is due and payable, any Minimum Rent or any other charges or amounts hereunder (including without limitation, the late charge provided for in SS.17.10), or if Lessor shall advance any sums which Lessee is obligated to pay, or if Lessor incurs any expense on account of Lessee committing an Event of Default, such amounts shall bear interest at the Default Rate from the date after the due date (or in the event Lessor expends any sums, from the date of such expenditure) until paid.

ss.17.10. If Lessee shall fail to pay, during the first six (6) months of the Lease Term within ten (10) days after the same is due and payable, and thereafter throughout the Lease Term within five (5) days after the same is due and payable, any Minimum Rent or any other charges or amounts hereunder, Lessee shall pay to Lessor a late payment charge in the amount of five percent (5%) of the amount then due to cover Lessor's additional administrative expenses necessitated by Lessee's failure to make timely payment; provided, however, Lessor may not enforce such late payment charge for any Minimum Rent or any other charges or amounts hereunder due while Mike Nothum, Jr. is the president of Lessee and has the authority to direct the payment of such amounts. Lessor shall not be obligated to accept any payments which have accrued a late payment charge unless accompanied by the late payment charge. This provision for a late payment charge shall be in addition to all of Lessor's other rights and remedies under this Lease or at law or in equity, and shall not be construed as liquidated damages or as limiting Lessor's remedies in any manner.

ss.17.11. The remedies given to Lessor in this Article shall be in addition and supplemental to all other rights or remedies which Lessor may have at law, in equity or by statute.

## ARTICLE 18

### INDEMNITY--LIABILITY OF LESSOR

ss.18.011. Lessee agrees to indemnify, and save harmless, Lessor and its partners and their respective officers, directors, agents, Fee Mortgagees and employees from and against all liability (statutory or otherwise), claims, suits, demands, damages, judgments, costs, interest and expenses (including

counsel fees and disbursements) to which any of the same may (except insofar as it arises out of any wrongful act or negligence thereof) be subject or suffer by reason of, or by reason of any claim for, any injury to, or death of, any person or damage to property (including any loss of use thereof) or otherwise arising from or in connection with the use of, or from any work or thing whatsoever done in, any part of the Demised Premises (other than by Lessor or its employees or agents) during the Lease Term or during the period of time, if any, prior thereto during which Lessee has been given access for the purpose of doing work or otherwise, or arising from any condition of the Demised Premises resulting from any Event of Default by Lessee under this Lease or from any act or negligence of Lessee or any of its officers, directors, agents, contractors, servants, employees, licensees or invitees. In the event any action or proceeding is brought against Lessor its partners or their respective officers, directors, agents, Fee Mortgagees or employees, and upon notice from Lessor, Lessee shall defend the same at Lessee's expense by counsel satisfactory to Lessor.

ss.18.012. Lessor agrees to indemnify, and save harmless Lessee and its officers, directors, agents, and employees from and against all liability (statutory or otherwise) claims, suits, demands, damages, judgments, costs, interest and expenses (including counsel fees and disbursements) to which any of the same may (except insofar as it arises out of any wrongful act or negligence thereof) be subject or suffer by reason of, or by reason of any claim for, any injury to, or death of, any person or damage to property (including any loss of use thereof) or otherwise arising from or in connection with Lessor's negligent or intentional wrongful acts in or around the Pad (other than by Lessee or its employees or agents) during the Lease Term. In the event any action or proceeding is brought against Lessee, its partners or their respective officers, directors, agents or employees, arising out of any of the foregoing, and upon notice from Lessee, Lessor shall defend the same by Lessor's expense by counsel satisfactory to Lessee.

ss.18.013. The liability of Lessor to Lessee for any default by Lessor under the terms of this Lease shall be limited to the interest of Lessor in the Pad and Lessee agrees to look solely to Lessor's interest in the Pad for the recovery of any judgment from Lessor, it being understood and agreed that Lessor or its respective trustees, directors, officers, partners, employees, agents, beneficiaries or security holder shall not be bound by or assume any personal liability for any obligations of Lessor and such parties' respective properties shall not be subject to the claims of any other person or party in respect of any such liability. The limitation of liability provided in this paragraph is in addition to, and not in limitation of, any limitation of liability applicable to Lessor provided by law or any other contract, agreement or instrument.

#### ARTICLE 19

##### NOTICES

ss.19.011. All notices, demands or requests by either party to the other shall be deemed to have been properly served or given if sent by United States registered or certified mail, return receipt requested, postage prepaid, addressed to the parties at the addresses listed below, or to such other address as a party may from time to time designate by written notice to the other.

Lessor:                   Michael Nothum, Jr.  
  
                                  NOTHUM DEVELOPMENT, L.L.C.  
  
                                  1741 South Holbrook Lane

Tempe, Arizona 85281

With a copy to: Scott A. Rose, Esq.  
O'CONNOR, CAVANAGH, ET AL.  
One East Camelback Road, Suite 1100  
Phoenix, Arizona 85012-1656

Lessee: Bill George  
  
COMFORT SYSTEMS USA, INC.  
  
4801 Woodway, Suite 300 East  
Houston, Texas 77056

ss.19.012. Notices, demands or requests which may or shall be served or given by certified or registered mail hereunder shall be deemed sufficiently served or given for all purposes when deposited in the mail. Any notice, demand or request may be personally delivered (which shall include delivery by express courier service) addressed as set forth above, and shall be effective upon receipt.

#### ARTICLE 20

##### QUIET ENJOYMENT--CONVEYANCE AND MORTGAGES BY LESSOR-- SUBORDINATION AND ATTORNMENT

ss.20.011. Lessee upon timely paying the Minimum Rent and fully keeping, observing and performing all the terms, covenants, agreements, provisions, conditions and limitations of this Lease on Lessee's part to be kept, observed and performed, shall quietly have and enjoy the Demised Premises during the Lease Term without hindrance or molestation by Lessor or anyone lawfully claiming by, or through Lessor.

ss.20.012. In the event Lessor herein or any successor owner of the Demised Premises shall convey or otherwise dispose of the Demised Premises, then, upon the transfer of any insurance policies, and other monies or any other securities belonging to Lessee held by Lessor pursuant to the provisions of this Lease, to any such purchaser of the Demised Premises, all liabilities and obligations on the part of Lessor or successor owner as Lessor under this Lease, accruing after such conveyance or disposal, shall cease and terminate and each successor purchaser of the Demised Premises shall, without further agreement, be bound by Lessor's covenants and obligations but only during the period of such ownership respectively. Nothing herein contained shall be construed to release Lessor or any successor owner as Lessor from any liability or obligation which otherwise matured prior to the effective date of such conveyance or disposal.

20.013. This Lease is and shall automatically be subject to any Fee Mortgages which now or in the future may affect the Pad or any portion thereof and to all renewals, additions, modifications, consolidation, replacements and extensions thereof; and Lessee covenants and agrees, within ten (10) days after Lessor's written request, to execute, acknowledge and deliver upon request any and all documents or instruments requested by Lessor or necessary or proper to confirm the subordination of this Lease to any Fee Mortgages or any amendments thereto. The subordination provided herein is conditional upon Lessee's receipt from all Fee Mortgagees, of a non-disturbance agreement essentially providing that so long as Lessee has not committed an Event of Default, the Fee Mortgage shall not disturb the possession of Lessee.

ss.20.014. Notwithstanding anything to the contrary set forth herein, Lessee hereby attorns and agrees to attorn to any person, firm or corporation purchasing or otherwise acquiring the Pad, Demised Premises or the real property thereunder or any portion thereof at any sale or other proceeding or pursuant to the exercise of any rights, powers or remedies under a Fee Mortgage, as if such person, firm or corporation had been named as Lessor herein, it being intended hereby that if this Lease is terminated, cut off or otherwise defeated by reason of any act or actions by the owner or holder of any such Fee Mortgage, then, at the option of any such person, firm or corporation so purchasing or otherwise acquiring the Pad or any portion thereof, this Lease shall continue in full force and effect.

#### ARTICLE 21

##### CERTIFICATES BY LESSOR AND LESSEE

ss.21.011. Both Lessor and Lessee agree at any time and from time to time upon not less than twenty (20) days' prior written notice by the other party, to execute, acknowledge and deliver to the other party a statement in writing certifying that this Lease is unmodified and in full force and effect (or if there have been modifications, that the Lease is in full force and effect as modified and stating the modifications), and the dates to which the Minimum Rent has been paid, and stating whether or not the other party is in default in keeping, observing or performing any term, covenant, agreement, provision, condition or limitation contained in this Lease and, if in default, specifying each such default, it being intended that any such statement delivered pursuant to this SS.21.01 may be relied upon by the other party or any prospective purchaser or Fee Mortgagee or any assignee of any Fee Mortgagee or any proposed purchaser.

ss.21.012. Lessee's failure to deliver such statement within such time shall be conclusive upon Lessee (a) that this Lease is in full force and effect, without modification except as may be represented by Lessor; (b) that there are no uncured defaults in Lessor's performance; (c) that there are no uses of the Demised Premises which are prohibited by this Lease, and any federal, state or local statute, rule or regulation and that such uses conform with applicable zoning codes; and (d) that not more than one month's rent has been paid in advance.

#### ARTICLE 22

##### COVENANTS TO RUN WITH THE LAND

ss.22.011. The terms, covenants, agreements, provisions, conditions and limitations herein contained shall be construed as covenants running with the land and shall bind and inure to the benefit of Lessor, its successors and assigns, and Lessee, its successors and assigns, if any, except as otherwise provided herein.

ARTICLE 23

NON-MERGER OF ESTATES

ss.23.011. The leasehold estate of Lessor and the leasehold estate of the Lessee shall at all times be separate and apart, and shall in no event be merged, notwithstanding the fact that this Lease or the leasehold estate created hereby, or any interest in either thereof, may be held directly or indirectly by or for the account of any person who shall own the fee estate in the Demised Premises, and Lessee's interest in the Lease; and no such merger of estates shall occur by operation of law, or otherwise, unless and until all persons at the time having any interest in the fee interest in the Demised Premises and all persons having any interest in the Lease or the leasehold estate shall join in the execution of a written instrument effecting such merger of estates.

ARTICLE 24

APPROVAL

ss.24.011. Whenever in this Lease the approval or consent of any party is required or desired, unless otherwise expressly provided, such party shall not withhold or delay its approval or consent unreasonably, and unless a different time limit is provided in any section of this Lease, such approval or disapproval shall be given within twenty (20) days following receipt of request for such approval or consent, and if not so given, the same shall conclusively be deemed to have been approved by said party. Provided, however, any such request for approval or consent shall specifically refer to this SS.24.01 and shall also state that the party receiving the notice has twenty (20) days to approve or consent and that if it fails to do so, the approval or consent shall conclusively be deemed to have been approved or consented to.

ARTICLE 25

MEMORANDUM OF LEASE

ss.25.011. This Lease shall not be recorded, but a memorandum of this Lease shall be executed, delivered and recorded by the parties at the election of either party.

ARTICLE 26

SECURITY DEPOSIT

ss.26.01. If at any time during the Lease Term Mike Nothum, Jr. is no longer the president of Lessee and authorized to direct the payment of Minimum Rent or any other charges or amounts hereunder, in addition to Minimum Rent, Lessee shall pay to Lessor a Security Deposit in the amount of Forty-Four Thousand One Hundred Seventy-Five and No/100 Dollars (\$44,175.00). Said deposit shall be held by Lessor without liability for interest, as security for the faithful performance by Lessee of all of the terms of this Lease to be observed and performed by Lessee.



ss.26.02. If any sum payable by Lessee to Lessor shall be overdue and unpaid or should Lessor make payments on behalf of Lessee, or if Lessee shall fail to perform any of the terms of this Lease, then Lessor may, at its option and without prejudice to any other remedy that Lessor may have on account thereof, appropriate and apply the entire Security Deposit, or so much thereof as may be necessary to compensate Lessor, toward the payment of Minimum Rent or Impositions or loss or damage sustained by Lessor due to such breach on the part of Lessee; and Lessee shall upon demand restore the Security Deposit to the original sum.

ss.26.03. Lessor may deliver the Security Deposit to the purchaser of Lessor's interest in the Demised Premises and thereupon Lessor shall be discharged from any further liability with respect to the Security Deposit.

#### ARTICLE 27

##### SIGNS

ss.27.011. At its own expense, Lessee shall be allowed to place and install any lawful signs on the Demised Premises as allowed by the City of Chandler and any deed restrictions that may affect the Demised Premises.

#### ARTICLE 28

##### MISCELLANEOUS

ss.28.011. This Lease constitutes the entire agreement between the parties hereto with respect to the matters set forth herein and supersedes any and all other prior written or oral agreements or understandings with respect to this transaction. This Lease may not be modified in any respect except by instruments signed in writing by both parties hereto.

ss.28.012. In the event of any action or proceeding brought by either party against the other under this Lease the prevailing party shall be entitled to recover for the fees of its attorneys in such action or proceeding such amount as the court may adjudge as reasonable attorneys' fees.

ss.28.013. The covenants and conditions herein contained shall, subject to the provisions as to assignment, apply to and bind the heirs, successors, executors, administrators and assigns, if any, of the parties hereto.

ss.28.014. The words "Lessor" and "Lessee" as used herein shall include the plural as well as the singular. Words used in masculine gender include the feminine and neuter. The marginal headings and titles to the paragraphs of this Lease are not a part of this Lease and shall have no effect upon the construction or interpretation of any part hereof.

ss.28.015. This Lease, its construction, validity and effect, shall be governed and construed by and in accordance with the laws of the State of Arizona.

ss.28.016. It is understood and agreed between the parties hereto that their relationship at all times shall remain that of Lessor and Lessee, and that nothing herein contained shall be deemed, held or construed as the creation of a partnership or joint venture as between the parties hereto in the conduct of Lessee's business; nor shall Lessor be liable for any debts, liabilities or obligations incurred by Lessee in the conduct of its business.

ss.28.017. If any provision of this Lease shall be determined to be void by any court of competent jurisdiction, then such determination shall not affect any other provisions of this Lease and all such other provisions shall remain in full force and effect; and it is the intention of the parties hereto that if any provision of this Lease is capable of two constructions, one of which would render the provision void and the other of which would render the provision valid, then the provision shall have the meaning which renders it valid.

ss.28.018. Time is of the essence of this Lease and each and all of its provisions.

ss.28.019. The waiver by Lessor of any term, covenant or condition herein contained shall not be deemed to be a waiver of such term, covenant or condition or any subsequent breach of the same or any other term, covenant or condition herein contained. The subsequent acceptance of rent hereunder by Lessor shall not be deemed to be a waiver of any preceding breach by Lessee of any term, covenant or condition of this Lease, other than the failure of Lessee to pay the particular rental so accepted, regardless of Lessor's knowledge of such preceding breach at the time of acceptance of such rent.

ss.28.10. All the terms, covenants and conditions contained in this Lease to be performed by either party, if such party shall consist of more than one person or organization, shall be deemed to be joint and several.

ss.28.11. Lessee promises, covenants and agrees to not remain in possession of all or any part of the Demised Premises after the expiration of the Lease Term, without the express written consent of Lessor. No acceptance of Minimum Rent and no act or statement by any employee, servant or agent of Lessor shall constitute the consent of Lessor to Lessee's holding over. Should Lessee hold over without the express written consent of Lessor, such tenancy shall be at the sufferance of Lessor, and not a renewal hereof or an extension for any further term, and in such case, Minimum Rent and other monetary sums due here under shall be payable at three (3) times the amount set forth in this Lease and at the time specified in this Lease and such tenancy at sufferance shall be subject to every other term, covenant and agreement contained herein. Lessee understands that Lessor is relying on Lessee's covenant to not hold over and to surrender the Demised Premises at the termination of the Lease Term. In the event Lessee holds over, Lessee shall be liable for all Lessor's direct and consequential damages, including costs, fees, expenses, damages and attorney's fees incurred by Lessor as a result of Lessee's holding over without Lessor's express written consent, including, but not limited to, damages and expenses incurred by Lessor for its inability to deliver possession of the Demised Premises to a new lessee.

ss.28.12. Lessee and Lessor each hereby represent and warrant to the other party that it has had no dealings with any real estate broker, finder or agent in connection with the negotiations of this Lease and that it knows of no real estate broker, company, finder or agent who is or might be entitled to a commission in connection with the execution of this Lease and Lessee and Lessor each covenant and agree to indemnify and save the other party harmless from any and all loss, cost and liability that may arise from a breach of this warranty.

ss.28.13. No representations, inducements, understanding or anything of any nature whatsoever, made, stated or represented by Lessor or anyone acting for or on Lessor's behalf, either orally or in writing, have induced Lessee to enter into this Lease, and Lessee acknowledges, represents and warrants that Lessee has entered into this Lease under and by virtue of Lessee's own independent investigation.

ss.28.14. If Lessor desires to finance, refinance or sell the Demised Premises, any part thereof or the Building of which the Demised Premises are a part, Lessee and all guarantors of Lessee's performance hereunder shall deliver to any potential lender or purchaser designated by Lessor such financial statements of Lessee and such guarantors as may be reasonably required by such lender or purchaser, including but not limited to Lessee's financial statements for the past three (3) years. All such financial statements shall be received by Lessor and such lender or purchaser in confidence and shall be used only for the purposes herein set forth.

IN WITNESS WHEREOF, the Lessor and Lessee have each caused this Lease to be executed the day and year first above written.

LESSOR:

NOTHUM DEVELOPMENT, L.L.C.,  
an Arizona limited liability company

By: \_\_\_\_\_  
Michael Nothum, Jr., Member

LESSEE:

TRI-CITY MECHANICAL, INC.,  
an Arizona corporation

By: \_\_\_\_\_  
Its: \_\_\_\_\_

EXHIBIT "A"

[To Lease between NOTHUM DEVELOPMENT, L.L.C. and TRI-CITY MECHANICAL, INC. dated July \_\_, 1997]

DEMISED PREMISES

Approximately 6.5 acres located in Chandler, Arizona on Galveston Road, east of 56th Street.

EXHIBIT "B"

[To Lease between NOTHUM DEVELOPMENT, L.L.C. and TRI-CITY MECHANICAL, INC. dated July \_\_, 1997]

EXTENDED LEASE TERM MINIMUM RENT

Upon receipt by Lessor of a notice that Lessee is exercising an option to extend the Initial Lease Term as provided in ss.2.02 of the Lease, Lessor and Lessee shall attempt to determine the market rent for the Extended Lease Term, with the market rent to reflect the Minimum Rent which are of a type then typical in the rental market and to be based on the market rental for new leases being executed as of one year prior to the expiration of the Initial Lease Term including periodic increases (the "Valuation Date"). In determining the market rent for the Extended Lease Term, due consideration shall be given, among other things, to the length of the Extended Lease Term; the amount of the Minimum Rent; whether or not such Minimum Rent should be subject to periodic Consumer Price Index or other adjustments; allowances to Lessee for, and the making by Lessor of improvements; liability of Lessee for reimbursable expenses; and the respective maintenance responsibilities of Lessor and Lessee; provided, however, the market rent for the Extended Lease Term shall not be less than the Minimum Rent in effect at the end of the Initial Lease Term; the effect of all such considerations shall be reflected in the Minimum Rent and periodic adjustments to Minimum Rent; no other provisions of this Lease shall be modified; and Lessor shall have no tenant improvement construction obligations.

Lessor, within thirty (30) days after the later of the Valuation Date or the receipt of Lessee's option notice, shall present Lessee in writing with the proposed market rental. If Lessee is dissatisfied with the proposed market rental presented by Lessor, Lessee may, by delivery to Lessor of notice within ten (10) days thereafter, elect to rescind Lessee's exercise of the option, in which event all rights of Lessee under this EXHIBIT "B" shall terminate. If Lessee does not so rescind Lessee's notice of exercise, then Lessee shall, within thirty (30) days after receipt of Lessor's proposed market rental, either accept the market rental proposed by Lessor or present Lessor in writing with its proposed market rental. Within five (5) days thereafter, Lessor shall either accept Lessee's proposal market rental or notify Lessee that the proposed market rental is unacceptable. If the proposed market rental is unacceptable to Lessor, and/or if Lessor and Lessee are unable to agree as to the renewal market rental at least six (6) months prior to the expiration of the Initial Lease Term, Lessor and Lessee will jointly appoint an appraiser to determine whether the market rental (including adjustment provisions) first proposed by Lessor or the market rental (including adjustment provisions) first proposed by Lessee is the rental which most accurately reflects the fair market rental at the Valuation Date. If Lessor and Lessee fail to agree upon an appraiser with five (5) months prior to the expiration of the Initial Lease Term, such appraiser will be appointed by the then President of the Local Chapter of The American Society of Appraisers and will be experienced in the appraisal of office, commercial and industrial properties in the Phoenix metropolitan area. The decision of such appraiser will be in writing and in duplicate; will be delivered to each of the parties to the Lease; and will either select all aspects of Lessor's first proposal (including adjustment provisions) or of Lessee's first proposal (including adjustment provisions) as the market rental provisions most reflective of the fair market conditions at the Valuation Date. The fair market rental provisions selected by the appraiser shall then be the rental rate provisions for the Extended Lease Term, subject to the limitations and adjustments to such market rental rate

set forth in this EXHIBIT "B" for determining the actual rental payable for the Extended Lease Term. The fee of the appraiser will be paid equally by Lessor and Lessee. If no determination is made prior to the commencement of the Extended Lease Term, Lessee will continue to pay to Lessor the Minimum Rent with bi-annual adjustments in effect at the end of the Initial Lease Term immediately preceding such Extended Lease Term and, upon such fair market rental being determined, Lessee will pay to Lessor the difference between the rent already paid by Lessee for the Extended Lease Term and the actual amount of rent attributable to the Extended Lease Term through the date of such determination. Upon the determination of the fair market rental as aforesaid, the parties will enter into an amendment to the Lease stating the Minimum Rent for the Extended Lease Term.

EXHIBIT "C"

[To Lease between NOTHUM DEVELOPMENT, L.L.C. and TRI-CITY MECHANICAL, INC. dated  
July \_\_, 1997]

OUTLINE SPECIFICATIONS

EXHIBIT "D"

[To Lease between NOTHUM DEVELOPMENT, L.L.C. and TRI-CITY MECHANICAL, INC. dated  
July \_\_, 1997]

SITE PLAN



## LEASE AGREEMENT

THIS AGREEMENT made and entered into the 1st day of November, 1996 by and between SAMUEL MATTHEWS LAWRENCE, JR., hereinafter referred to as "Lessor", and the S.M. LAWRENCE COMPANY, INCORPORATED, a Tennessee corporation, hereinafter referred to as "Lessee"; witnesseth:

1. PREMISES AND TERM. For and in consideration of the rents herein reserved and of the covenants and agreements herein contained on the part of the part of the Lessee to be kept, observed, and performed, the Lessor has demised and leased, and does by these presents demise and lease unto the Lessee that certain described real estate, together with the improvements thereon, more fully described on the attached Exhibit "A", which Exhibit "A" is, by this reference, made a part of this Lease Agreement.

TO HAVE AND TO HOLD the premises therein described with all the rights, privileges, easements, and appurtenances thereunto belonging unto the Lessee for the term commencing on November 1, 1996 and ending on the 31st day of October, 1997

2. RENTAL. The rental to be paid by Lessee to Lessor shall be the sum of One Hundred Ten Thousand Four Hundred Dollars (\$110,400.00) and same shall be payable in equal monthly payments of NINE THOUSAND TWO HUNDRED DOLLARS AND NO 100 (\$9,200.00) per month in advance.

3. USE OF PREMISES. Unless Lessor's written consent to other uses be first obtained, Lessee's use of the demised premises shall be confined to manufacturing, warehousing, selling, fabricating, office, engineering and research purposes incidental thereto. Lessee shall not use or occupy the premises for any unlawful purpose and shall comply with all laws, ordinances, rules and regulations, and all covenants, conditions and restrictions of record applicable to the premises or the use or occupancy thereof. Lessee shall neither commit nor permit any waste or nuisance on the premises, nor use the premises or any part thereof or permit the same to be used in any manner that will impair the structural strength of or injure any building or improvement on the premises or adjacent thereto. Lessee shall not do or permit any act on the premises or permit the use of the same

in any manner that will violate or make inoperative any policy of fire or other hazard insurance carried on the premises or any part thereof.

4. LESSOR'S COVENANTS. The Lessor agrees:

A. That Lessee, on paying the rental herein specified and observing Lessee's agreements hereof, shall and may peaceably and quietly have, hold, and enjoy the premises during the term hereof unless and until terminated as herein provided.

B. That all machinery, equipment, fixtures, and appurtenances installed by Lessee, the cost of which shall not have been paid by Lessor, regardless of how attached or affixed to the premises, shall be deemed to remain personal property and may be removed prior to the termination of this lease, but Lessee shall repair any damages occasioned by such removal.

C. That Lessee may at any time during the term hereof, at its sole risk and expense, do such remodeling, altering, or adding to the demised premises as it may desire to do.

D. To give Lessee immediate notice in writing of any proposal for a taking by the exercise of eminent domain or otherwise of any portion of the demised premises by public authority.

5. LESSEE'S COVENANTS. The rent shall be net to Lessor and toward this end, the Lessee agrees:

A. To pay when due the rent and all charges for water, gas, electricity, heat, power, sewer, garbage, and other services supplied to it at the demised premises.

B. To maintain all improvements on the demised property in as good condition as when received, including but not limited to repairs to the walls, roof, interior and exterior of the improvements on the leased premises, all plate glass, all windows, all plumbing, sewer, lighting,

heating, and other utility systems, all roads and/or parking areas located on the leased premises including the removal of snow and ice, and shall keep the premises clean and neat, and to do so as needed without notice from the Lessor.

C. To save Lessor harmless and indemnified from any injury, loss, claim or damage to any person or personal property while on or about the premises unless same be due to the negligence or lawful misconduct of Lessor.

D. To permit Lessor of his agents to examine the premises at reasonable times.

E. To procure any licenses or permits required by any use of the premises by Lessee.

F. To pay to the public authorities charged with the collection thereof, on or before the last day that the same may be paid without interest or penalty, all real estate taxes and government impositions in lieu of or in substitution for real estate taxes and all betterment assessments, which taxes, impositions or assessments are levied or assessed on the premises including payment of a pro-rata share of any taxes levied for the year, any part of which is included in this lease term.

G. To keep the buildings on the demised premises insured against fire, the perils covered by the extended coverage, with vandalism, malicious mischief coverage as a minimum, such insurance to be written in companies reasonably satisfactory to Lessor, the cost of such insurance to be paid by Lessee.

H. To carry with respect to the demised premises, with insurance companies reasonably acceptable to Lessor, public liability insurance with limits of not less than One Hundred

Thousand Dollars (\$100,000.00) for injury to any one person, and Five Hundred Thousand Dollars (\$500,000.00) for damage in any one accident, and property damage insurance with limits of not less than Twenty-Five Thousand (\$25,000.00). Lessor shall be named as additional insured on all such policies as his interest may appear.

I. Peaceably to yield up the premises at the end of the term as the same may be extended hereunder in as good a state of repair as at the commencement thereof, ordinary wear and tear and damage by fire and other casualty alone excepted.

J. Not to assign this lease or permit any transfer thereof by operation of law, or sublet all or any part of the premises.

6. MUTUAL COVENANTS OF LESSOR AND LESSEE. It is covenanted and agreed by and between Lessor and Lessee:

A. In case during this lease the premises, or any part thereof, shall be taken by any exercise of the right of eminent domain or substantially damaged by any public or other authority, or shall receive any substantial direct or consequential damage thereby, which results in the Lessee being deprived of the use and occupation of twenty-five percent (25%) of the floor area in any one building or of such area of the demised premises as renders same unsuitable for the continuation of the Lessee, this lease may be terminated either on the date possession is taken by the taking authority or when such damage occurs. Lessee must make such election within forty-five (45) days following the taking and/or damage and must evidence same by written notice to Lessor within the forty-five (45) day period. In the event Lessee does not elect to terminate, a just proportion of the rent shall be abated until the premises shall have been put in usable condition by the Lessor. The

Lessor shall have the option to terminate this lease agreement if, in its opinion, the loss or damage from property so taken renders it impracticable or undesirable to continue with such lease. This option to the Lessee must be exercised within forty-five (45) days after such taking or damage and must be evidenced by written notice of such intention given to Lessee within the forty-five (45) day period.

B. Lessor reserves and excepts all rights to damages to the premises and buildings and the leasehold hereby created now accrued or hereafter accruing by reason of any exercise of the right of eminent domain and by way of confirmation, Lessee hereby grants to Lessor all Lessee's rights to such damages and covenants to execute and deliver such further instruments of assignment thereof as Lessor may from time to time request.

C. In case any portion of the building situated on the demised premises as presently contemplated shall be rendered permanently untenable during the term of this lease by fire or other casualty with respect to which Lessee is required to insure, Lessee may require Lessor, at Lessor's expense, to the extent only of the insurance proceeds received by Lessor, forthwith to replace, restore or rebuild the damaged, injured or destroyed portions thereof to substantially the same condition as existing immediately prior to the damage, injury or destruction, or Lessee itself may replace, restore or rebuild the damaged, injured or destroyed premises, requiring contribution for Lessor for the cost of such replacement, restoration or rebuilding to the extent of the insurance proceeds paid to Lessor as a result of such damage, injury or destruction. If the injury or damage to the building is such that the Lessee is deprived of the use and Occupancy of more than fifty percent (50%) of the floor area, then at the election of Lessee, this lease may be terminated forthwith.

If Lessee elects not to terminate the lease, and it is impractical to repair or restore the damaged building, then, if Lessee shall so elect, such building shall be replaced with a structure of corresponding floor area representing the then current design, the design or location of such structure to be selected by Lessor after consultation with Lessee and so far as Lessor shall deem practical, in compliance with Lessee's wishes. It is understood that in no event shall Lessor's obligation to restore replace or rebuild, or to make contribution exceed in amount the sum of the insurance proceeds shall be insufficient to pay for the cost of such replacement, restoration or rebuilding of such damaged or destroyed portions of the premises, and Lessee has by written notice requested Lessor to replace, restore or rebuild, then Lessee shall pay the additional sum or sums required, above such insurance proceeds received. Repair, restoration and rebuilding need not include alterations, changes or improvements made by and at the expense of Lessee, nor fixtures and equipment which the Lessee was entitled to remove.

D. If Lessee shall neglect or fail to perform or observe any of the Lessee's covenants herein, and such neglect or failure shall continue for more than five (5) days after written notice thereof to Lessee with respect to the covenant to pay rent, and more than fifteen (15) days after written notice to Lessee thereof with respect to any other of Lessee's covenants, or if the leasehold hereby created shall be taken on execution, or by other process of law, or if any assignment shall be made of Lessee's property for the benefit of creditors, or if a receiver, guardian, conservator, trustee in bankruptcy or similar officer shall be appointed to take charge of all or any part of Lessee's property by a court of competent jurisdiction, or if Lessee commits any act of bankruptcy, or if a petition is filed by Lessee under any bankruptcy law, or if a petition is filed against Lessee under any

bankruptcy law and the same shall not be dismissed within ninety (90) days from the date upon which it is filed, then, and in any of such cases, Lessor lawfully may immediately or at any time thereafter and without demand or notice, enter upon the premises or any part thereof in the name of the whole and repossess the same as of Lessor's former estate, and expel Lessee and those claiming through or under Lessee and remove their effects, forcibly if necessary, without being deemed guilty of any manner of trespass and without prejudice to any remedies which might otherwise be used for arrears of rent or preceding breach of covenant, and upon such entry this Lease shall terminate; and Lessee covenants that, in case of such termination or in case of termination under the provisions of statute by reason of the default of Lessee, Lessee will forthwith pay to Lessor as damages a sum equal to the amount by which the rent called for hereunder for the remainder of the original term, or if extended, of any such extended term, exceeds the fair rental value of the premises for the remainder of the original term or any extension thereof.

E. No consent or waiver, express or implied, by Lessor, to or of any breach of any covenant, condition or duty of Lessee, shall be construed as a consent or waiver to or of any other breach of the same or any other covenant, condition or duty. All notices hereunder shall be served by hand delivery or by registered mail and, if intended for Lessor shall be addressed to Lessor at P.O. Box 638, Jackson, Tennessee, or to such other address as may be requested by Lessor in writing, and if intended for Lessee, shall be addressed to 245 Preston, Jackson, Tennessee. Unless repugnant to the context, the words "Lessor" and "Lessee" appearing herein shall be construed to refer to the person or persons, natural or corporate, named above as Lessor or as Lessee as the case

may be, and the heirs, executors, administrators, successors and assigns of such person or persons, and those claiming through or under them or any of them.

F. If Lessee shall abandon or vacate the premises, the same may be relet by Lessor for such rent, and upon such terms as it may deem fit, and Lessor agrees to use reasonable efforts to so relet to minimize damages; and if a sufficient sum shall not be thus realized monthly after paying the expense of such reletting and collecting to satisfy the rent hereby reserved, Lessee agrees to satisfy and pay all deficiencies as the same may become due during each month of the remaining period of this lease, it is agreed by the parties hereto that the demised premises shall not be deemed to have been vacated or abandoned by Lessee as referred to in this or any other paragraph of this lease so long as a watchman shall be maintained on the premises by Lessee.

IN WITNESS WHEREOF, the parties hereto have individually, or by their duly authorized officer, hereunto set their hands the day and date above written

/S/ SAM LAWRENCE, JR.

S.M. LAWRENCE COMPANY, INC.

BY /S/ FRANK LAWRENCE  
President

STATE OF TENNESSEE  
COUNTY OF MADISON

Personally appeared before me SARAH C. SEELEY, a Notary Public in and for said State and County, duly appointed, commissioned, qualified and action, SAMUEL MATTHEWS LAWRENCE, JR., the within named Lessor, with whom I am personally acquainted, and who acknowledged that he executed the foregoing Lease Agreement for the purposes therein contained.

WITNESS, my hand and seal, at office, this 1ST day of NOVEMBER, 1996.

/S/ SARAH C. SEELEY  
NOTARY PUBLIC

My Commission expires:

3-19-2000

STATE OF TENNESSEE  
COUNTY OF MADISON

BEFORE ME, SARAH C. SEELEY , a Notary Public in and for the said State of County, personally acquainted, and who, upon oath, acknowledged himself to be President of S.M. Lawrence Co., Inc., the within named Lessee and that he as such President, being authorized so to do, executed the foregoing Lease Agreement for the purposes therein contained.

WITNESS, my hand and seal, at office, this 1ST day of NOVEMBER, 1996.

/S/ SARAH C. SEELEY  
NOTARY PUBLIC

My Commission expires:

3-19-2000



EXHIBIT "A"

BEGINNING at a stake in the north margin of Preston Street in the Third Ward of the City of Jackson, TN, at its intersection with the west right-of-way margin of the old Illinois Central Railroad Company (now Illinois Central Gulf); runs thence north with said west margin of right-of-way 600 feet to a stake; runs thence westwardly and parallel to the north right-of-way margin of Preston Street to a stake in the east margin of the right-of-way of the old Gulf, Mobile & Ohio Railroad Company (now also Illinois Central Gulf); runs thence in a southerly direction with the eastern margin of said right-of-way to a stake in the north margin of Preston Street; thence in an easterly direction with the north margin of Preston Street to the point of beginning.

Also included is the building at 251 Preston Street known as the pipe fabricating shop (Quanset Hut), and the metal building at the rear of the property known as the sheet metal building.

## LEASE AGREEMENT

THIS AGREEMENT made and entered into this 1st day of April, 1986 by K and P Warehouse #1, Grand Rapids, Michigan, 49508, hereinafter called "Lessor", and Quality Trane Heating and Cooling, Inc., Grand Rapids, Michigan, 49508, hereinafter called "Lessee".

## W I T N E S S E T H

The Lessor, in consideration of Lessee's Covenants and agreements herein contained, has demised and leased, and by these presents does demise and lease unto Lessee, premises located in 3395 Kraft Avenue, Kent County, State of Michigan.

The Parties hereto further mutually covenant and agree as follows:

1.1 RENTAL Lessee covenants and agrees to pay to Lessor as rental for said premises during the original one (1) year term hereof an agreed rental of One Hundred Ninety Two Thousand and 00/100 Dollars (\$192,000.00), payable in equal monthly installments of Sixteen Thousand and 00/100 Dollars (\$16,000.00) in advance, payable on the first day of each month during the term hereof.

1.2 This is a gross lease and all other charges such as utilities, insurance, real property taxes shall be included in rental payments.

2.1 TERM. The term of this Lease shall be one (1) year, commencing April 1, 1986.

2.2 LEASE YEAR. "Lease Year" shall mean each twelve (12) month period, beginning with the first day of the term of the Lease, and each yearly anniversary thereof, provided that the beginning date of the term of this Lease is on the first of the month.

3.1 WAIVER OF SUBROGATION. The parties hereto desire to eliminate the right of either party to assign by way of subrogation, to any insurance company carrying insurance on their respective properties, any cause of action which any of the parties hereto may have against the other party, because of negligence, resulting in any loss to property which is thus insured, and now, therefore, it is agreed by the parties hereto as follows:

(a) Lessor and Lessee each mutually waive and relinquish any and all rights and release the other from any claims for loss or damage which they, or it, might have against the other on account of any claims for loss or damage to property owned by it or them caused by the alleged negligence of the other party, or their or its employees or persons on the within demised premises and common area facilities by permission of the other party, as to which loss or damage the party suffering the same is protected by insurance coverage and as to which the party suffering the same is reimbursed by an insurer.

(b) Each of the parties hereto will use good faith efforts to procure from the carrier of the insurance on its property an endorsement on all its policies of insurance carried by it, substantially in the following language:

"It is hereby stipulated that this insurance shall not be invalidated should the insured waive in writing prior to a loss any or all right of recovery against any party for loss occurring to the property described herein or affected thereby."

4.1 MAINTENANCE OF PREMISES. It is agreed by the parties thereto as follows:

(a) Except as otherwise provided in this Lease, Lessee agrees to maintain and to make all necessary repairs to the demised premises, and to keep the demised premises and all improvements in the same condition as of the date it takes possession excepting reasonable wear and tear.

(b) Lessee further covenants to operate and keep the demised premises in clean and sanitary condition according to all applicable laws and codes.

(c) Lessee shall maintain and keep in good condition for the term of this Lease and renewals thereof, the driveways and parking areas.

(d) Lessee agrees that it will make no structural changes or alterations in the building on the demised premises without first obtaining the written consent of the Lessor. The Lessee shall have the right of making such non-structural alterations in and about the demised premises as Lessee may determine are desirable in connection with its business operation under this Lease.

(e) Lessor agrees to make all necessary structural repairs and repairs to the exterior roof as needed.

5.1 DAMAGE OR DESTRUCTION AND RESTORATION OF FIRE OR CASUALTY DAMAGE. If the demised premises shall be damaged or destroyed by fire or other casualty, Lessor at Lessor's sole cost and expense, shall promptly and diligently proceed to repair, rebuild or replace such building or other improvements, so as to restore them to the condition in which they were immediately prior to such damage or destruction. During any period of reconstruction to the extent

that the leased premises are not usable by the Lessee, the rents shall be abated for that portion of the building.

6.1 DEFAULTS: REMEDIES. Defaults. The occurrence of any one or more of the following events shall constitute a default and breach of this Lease by Lessee.

(a) The vacating and abandonment of the premises by Lessee.

(b) The failure of Lessee to make any payment of rent or any other payment required to be made by Lessee hereunder, as and when due, where such failure shall continue for a period of fifteen (15) days after written notice thereof from Lessor to Lessee.

(c) The failure by Lessee to observe or perform any of the covenants, conditions or provisions of this Lease to be observed or performed by Lessee, other than described in Paragraph (b) above, where such failure shall continue for a period of thirty (30) days provided that Lessee shall not be deemed to be in default if more than 30 days is required to cure such default and Lessee commences such cure within said (30) day period and thereafter diligently prosecutes such cure to completion; provided further, that if the nature of Lessee's default is such that it is not reasonably susceptible of being cured, Lessee shall be deemed to be in default immediately after written notice thereof has been given by Lessor to Lessee.

(d) (i) The making by Lessee of any general assignment, or general arrangement for the benefit of creditors; (ii) the filing by or against Lessee for a petition to have Lessee adjudged a bankrupt or a petition for reorganization or arrangement under any law relating to bankruptcy (unless, in the case of a petition filed against Lessee, the same is dismissed within 60 days); (iii) the appointment of a trustee or receiver to take possession of substantially all of Lessee's

assets located at the demised premises or of Lessee's interest in the Lease, where possession is not restored to Lessee within (30) days; or (iv) the attachment, execution or other judicial seizure of substantially all of Lessee's assets located at the demised premises or of Lessee's interest in the Lease, where such seizure is not discharged within (30) days.

(e) The levy under execution upon the leasehold interest of Lessee or the attachment thereof by process of law, provided such levy or attachment is not discharged or stayed by appeal or otherwise within a period of sixty (60) days.

(f) The recording of this instrument as set forth in Paragraph 13.2 herein.

6.2 RIGHT TO CURE DEFAULTS. If Lessee shall fail to comply fully with any of its obligations under this Lease (including, without limitation, its obligations to make repairs, comply with all laws, ordinances and regulations and pay all bills for utilities), then Lessor shall have the right, at its option after notice to Lessee (except that in an emergency, notice is not required) to cure such breach at Lessee's expense. Lessee agrees to reimburse Lessor as additional rental for all costs and expenses incurred as a result thereof together with interest thereon promptly upon demand, at a rate equal to the "Prime Rate" (as hereinafter defined) plus one and one half percent (1-1/2%). If, however, payment of interest at such rate by Lessee (or by the Tenant then in possession having succeeded to the Lessee's interest in accordance with the terms of this Lease) should be unlawful, I.E., violative of the usury statutes or otherwise, then "interest" shall, as against such party, be computed at the maximum lawful rate payable by such party. "Prime Rate" shall mean the rate being charged at the time in question by Michigan National Bank (Lansing Office) for short-term (90 day) unsecured loans made to its preferred customers.

7.1 COVENANT OF QUIET ENJOYMENT. Lessor covenants that Lessee, upon performing its covenants and agreements herein set forth, shall and may peacefully and quietly have, hold and enjoy demised premises during the term hereof and any renewal terms.

8.1 RETURN OF PREMISES AT EXPIRATION OF LEASE. Lessee agrees upon termination hereof, to return demised premises to Lessor in as good condition as the same are or may be put by either party, reasonable wear and tear excepted.

9.1 EMINENT DOMAIN. If the whole of the leased premises shall be taken by any public authority under the power of eminent domain, the lease term shall cease as of the day possession shall be taken by such public authority, and Lessee shall pay rent up to that date with an appropriate refund by Lessor of such rent as may have been paid in advance for any period subsequent to the date possession is taken. If less than all of the leased premises shall be so taken, the lease shall cease only on the parts so taken as of the day possession shall be taken by such public authority; and Lessee shall pay rent up to that day with appropriate refund by Lessor of such rent as may have been paid in advance for any period subsequent to the date possession is taken and thereafter the rental shall be equitably adjusted. Lessor shall, at its expense, make all necessary repairs or alterations to the basic building and exterior work so as to constitute the remaining premises a complete architectural unit, provided that Lessor shall not be obligated to undertake any such repairs and alterations if the cost thereof exceeds the award. If the leased premises so taken leaves space no longer suitable for Lessee for the purposes set forth in this Lease, then the lease term shall cease and Lessee shall pay rent up to the day possession is taken, with an appropriate refund by Lessor of such rent as may have been paid in advance for any period subsequent to the date of

the taking of possession. If more than twenty-five percent (25%) of the floor area of the building in which the leased premises are located shall be taken under the power of eminent domain, Lessor may, by 60 days' advance notice in writing to Lessee delivered on or before the day of surrendering possession to the public authority, terminate this Lease and rent shall be paid or refunded as of the date of termination. Compensation awarded for any taking under the power of eminent domain, whether for the whole or a part of the leased premises, shall be the property of Lessor.

10.1 OPTION TO RENEW. Provided this lease is not in default, Lessor, at its sole discretion, may provide an option to renew this Lease for an additional three (3) year term on the same terms and conditions as provided herein, except that increases in the operating cost of utilities, property taxes and insurance over the base year rental period will be passed on to Lessee.

11.1 ESTOPPEL CERTIFICATE.

(a) Lessee shall, at any time upon not less than ten (10) days prior written notice from Lessor, execute, acknowledge and deliver to Lessor a statement in writing (i) certifying that this Lease is unmodified and in full force and effect (or if modified, stating the nature of such modification and certifying that this Lease, as so modified, is in full force and effect), and stating the date to which the rent and other charges are paid in advance, if any, and (ii) acknowledging that there are not, to Lessee's knowledge, any uncured defaults on the part of the Lessor hereunder, or specifying such defaults if any care claimed. Any such statement may be conclusively relied upon by any prospective purchaser or encumbrance of the premises.

(b) Lessee's failure to deliver such statement within such time shall be conclusive upon Lessee (i) that this Lease is in full force and effect, without modification except as may be

represented in good faith by Lessor, (ii) that not more than one month's rent has been paid in advance, (iii) that there are no uncured defaults in Lessor's performance.

11.2 RECORDING. Lessee shall not record this Lease without Lessor's prior written consent and such recordation shall, at the option of Lessor, constitute a noncurable default of Lessee hereunder. Either party shall, upon request of the other, execute, acknowledge and deliver to the other, a "short form" memorandum of this Lease for recording purposes.

11.3 COVENANTS AND CONDITIONS. Each provision of this Lease performable by Lessor or Lessee shall be deemed both a covenant and a condition.

11.4 ATTORNEY'S FEES. If either party brings an action to enforce the terms hereof or declare rights hereunder, the prevailing party in any such action shall be entitled to recover reasonable attorney's fees as fixed by the Court.

11.5 HOLDING OVER. If Lessee remains in possession of the premises or any part thereof after the expiration of the term hereof, without the express consent of Lessor, such occupancy shall be a tenancy from month to month at a rental in the amount of the last monthly rental plus all other charges payable hereunder, and upon all the terms hereof applicable to a month to month tenancy.

11.6 CORPORATE AUTHORITY. If Lessee is a corporation, each individual executing this Lease on behalf of said corporation represents and warrants that he is duly authorized to execute and deliver this Lease on behalf of said corporation, in accordance with a duly adopted resolution of the Board of Directors of said corporation, and that this Lease is binding upon said corporation in accordance with its terms. If Lessee is a corporation, Lessee shall, within (30) days after



execution of this Lease, deliver to Lessor a certified copy of a resolution of the Board of Directors of said corporation authorizing or ratifying the execution of this Lease.

12.1 USE. Lessee agrees that, unless and to the extent that Lessee shall obtain Lessor's prior written approval, Lessee will not use or allow to be used, the demised premises, for any purpose other than Warehousing, subject, however, to zoning ordinances, all rules, regulation, laws, ordinances, statutes and requirements of all governmental authorities and the Board of Fire Insurance Underwriters, and any similar bodies, having jurisdiction thereof, which Lessee agrees to comply with at its sole cost and expense, and such conditions, restrictions and other encumbrances, if any, to which the demised premises are subject at the time of execution and delivery of this Lease.

13.1 CONDITION OF PREMISES. Lessee hereby accepts the demised premises in their condition existing as of the date of the execution hereof, except for completion of construction to Lessee's satisfaction, subject to all applicable zoning, municipal, county and state laws, ordinances and regulations governing this Lease subject thereto and to all matters disclosed thereby and by any exhibits attached hereto. Lessee acknowledges that neither Lessor nor Lessor's agent has made any representation or warranty as to the suitability of the demised premises for the conduct of Lessee's business. Lessee agrees to accept the parking lots and roadways in their present condition. Lessor has the right to pave the parking lots and roadways at its sole discretion.

14.1 LESSOR DEFINED. The term "Lessor" as used in this Lease means only the owner or the mortgagee in possession for the time being of the demised premises, or the owner of a lease of the land of the demised premises, and/or the buildings and improvements thereon, so that in the event of and upon any assignment, sale or demise of Lessor's interest in the demised premises,

Lessor shall be and hereby is entirely freed and relieved of all obligations of Lessor hereunder, except obligations accrued prior to the effective date of such assignment, provided that the assignee, or purchaser assumes and agrees to observe and perform all obligations of Lessor hereunder, and provided further that the then Lessee is given notice of such assignment, sale or lease.

15.1 NOTICES. Any notice required or permitted to be given hereunder shall be in writing and may be served personally or by certified mail, return receipt requested or Proof of Mailing addressed to Lessor and Lessee respectively at the addresses set forth on the first page of this Lease.

16.1 MORTGAGES. Lessee agrees to execute any instrument to evidence priority or subordination of this Lease over, or to any mortgage or deed of trust from time to time as may be required by Lessor, provided that in the event of subordination, the Mortgagee or Trustee under any such mortgage or deed of trust shall acknowledge the validity of this Lease, and agree to provide for its continuance and not to disturb Lessee's possession so long as the Lessee is not in default hereunder.

17.1 CONTENTS INSURANCE. Lessee shall carry, at its own expense, all fire and casualty insurance on its own fixtures, equipment and inventory located on the leased premises.

18.1 ASSIGNMENT AND SUBLETTING. Lessee shall not have the right to sublease the premises or assign its rights under this Lease in whole or in part without Lessor's prior written consent (which will not be unreasonably withheld) first obtained. Notwithstanding any such sublease or assignment, however, the Lessee named herein and all assignees of its interest hereunder

shall remain liable for the performance of all Lessee's obligations contained in this Lease unless released in writing.

18.2 ASSIGNMENT BY LESSOR. The Lessor shall have the right to assign its rights under this Lease in whole or in part and/or sell, or transfer its estate in the demised premises, subject to all of the Lessee's rights and interests hereunder.

19.1 ADVERTISING DISPLAY. Lessor and Lessee agree that all signs and advertising displayed outside of the demised premises shall be only that which advertises the business carried on upon the demised premises, and that Lessor shall control the location, character and size thereof, and that no sign shall be displayed excepting such as shall be approved in writing by Lessor, all such approvals not to be unreasonably withheld.

20.1 BINDING EFFECT. This agreement shall be binding upon and the benefits hereof shall insure to the heirs, successors and assigns of the parties hereto.

IN WITNESS WHEREOF, the parties hereto have caused this instrument to be executed this 1st day of April, 1986.

WITNESS:

LESSOR:

\_\_\_\_\_  
\_\_\_\_\_

\_\_\_\_\_  
Robert Powers, K & P Warehouse #1

LESSEE:

\_\_\_\_\_  
Gordon Kamstra, Quality Trane  
\_\_\_\_\_

SECOND AMENDMENT TO LEASE

THIS SECOND AMENDMENT TO LEASE is made this \_\_\_\_\_ day of May, 1992, between ROBERT J. POWERS, d/b/a K & P WAREHOUSE #1, whose address is 3395 Kraft Avenue, S.E., Grand Rapids, Michigan 49512, as Lessor, and QUALITY AIR HEATING & COOLING, INC., a Michigan corporation, whose address is 3395 Kraft Avenue, S.E., Grand Rapids, Michigan 49512, as Lessee, with reference to the following:

RECITALS

A. Lessor and Lessee (then known as Quality Trane Heating and Cooling, Inc.) entered into a Lease Agreement dated April 1, 1986 for premises (the "Premises") located at 3395 Kraft Avenue, S.E., Grand Rapids, Michigan (the "Lease Agreement").

B. The Lease Agreement was amended by an amendment dated April 1, 1990 (the "First Amendment").

C. Underlying Michigan Strategic Fund bond issues with respect to the Premises and contiguous premises commonly known as 3427 Kraft Avenue, S.E., Grand Rapids, Michigan are being refunded. The refunding bond issue is known as the "Michigan Strategic Fund Adjustable Rate Demand Limited Obligation Revenue Refunding Bonds K & P Warehouse Project" dated as of May 1, 1992" (the "Bonds"). This Second Amendment is made in connection with the issuance of the Bonds.

AGREEMENT

In consideration of their mutual covenants, the parties agree as follows:

1. Lessor and Lessee hereby cancel the First Amendment and agree that the First Amendment is of no effect.

2. The first sentence following the word "Witnesseth" in the Lease Agreement is deleted in its entirety and the following is inserted in its place:

Lessor, in consideration of Lessee's covenants and agreements herein contained, has demised and leased, and by these presents does demise and lease unto Lessee premises located at 3395 Kraft Avenue, S.E., Grand Rapids, Michigan (the "Premises") and premises located at 3427 Kraft Avenue, S.E., Grand Rapids, Michigan ("Property No. 2"). The parties acknowledge that the rights of Lessee with respect to Property No. 2 are subject to the rights of Envirotronics, Inc., a Michigan corporation, as lessee under a lease dated September 14,

1987 between K & P Warehouse No. 2, as lessor, and Envirotronics, Inc., as lessee, as such lease may be amended or renewed (the "Second Lease") for a portion of Property No. 2.

3. Paragraph 1.1 of the Lease Agreement is deleted in its entirety and the following is inserted in its place:

Lessee covenants and agrees to pay to Lessor as monthly rental during the term of the Lease, for the Premises and for Property No. 2 the greater of (a) Eighteen Thousand Four Hundred and 00/100 Dollars (\$18,400) or (b) one-twelfth (1/12) of the sum of (i) all costs and charges required to be paid by Lessor under this Agreement and by the lessor under the Second Lease, on an annualized basis, including without limitation, utilities, insurance, real property taxes, and repairs required to be made by Lessor under this Agreement and by the lessor under the Second Lease, and (ii) the scheduled annual debt service, including principal and interest, required to be paid on the Bonds, as this amount may change from time to time. Rental shall be payable in advance on the first day of each month during the term of this Lease Agreement.

4. Paragraph 2.1 is deleted in its entirety and the following is inserted in its place:

The remaining term of this Lease shall be thirteen (13) years, commencing May 1, 1992 and terminating April 30, 2005.

5. Paragraph 10.1 of the Lease Agreement is deleted in its entirety.

6. This Second Amendment to Lease Agreement shall be effective as of May 1, 1992.

7. As modified by this Second Amendment to Lease, the Lease Agreement is ratified and affirmed.

ROBERT J. POWERS, d/b/a  
K & P WAREHOUSE NO. 1, Lessor

\_\_\_\_\_  
Robert J. Powers

QUALITY AIR HEATING & COOLING,  
INC., Lessee

---

Robert J. Powers, President

-3-

April 1, 1990

This agreement made and entered into this first day of April, 1990 by Robert Powers DBA K & P Warehouse #1, Grand Rapids, MI 49508 herein after called "lessor," and Quality Air Heating and Cooling, Inc., Grand Rapids, MI 49508 herein after called "lessee."

WITNESSETH

Both Parties agree to extend the terms of the lease dated April 1, 1986 with the following modifications:

- A. Lessor's name is to be Quality Air Heating & Cooling, Inc.
- B. The term of this lease shall be one (1) year, commencing April 1, 1990.
- C. Rental shall be \$220,800 payable in monthly installments of \$18,400.
- D. Option to renew this lease for an additional three (3) year term shall be granted on the same terms and conditions as paragraph 10.1 of the original lease agreement.

In witness whereof, the parties here to have caused this instrument to be executed this 1st day of April, 1990.

Witness: Lessor:

\_\_\_\_\_

\_\_\_\_\_  
Robert Powers, K & P Warehouse #1

Lessor:

\_\_\_\_\_

\_\_\_\_\_  
Robert Powers,  
Quality Air Heating & Cooling, Inc.



## COMMERCIAL AND INDUSTRIAL LEASE

J&amp;J INVESTMENTS; LANDLORD AND CONTRACT SERVICE, INC; TENANT

## COMMERCIAL AND INDUSTRIAL LEASE

THIS LEASE made and entered into this 1ST day of March, 1997, by and between J&J INVESTMENTS hereinafter called "Landlord," and CONTRACT SERVICE, INC. hereinafter called "Tenant."

## WITNESSETH:

In consideration of the covenants and promises contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, it is agreed by the parties hereto as follows:

## I. DEFINITIONS:

## 1. DEMISED PREMISES:

Landlord hereby leases to Tenant and Tenant hereby leases from Landlord all those certain premises consisting of a two-story masonry block building containing approximately 21,000 square feet, situated on a parcel of land in a complex known as 3210 and 3222 Washington Street (240 West 3222 South) in the City of South Salt Lake, State of Utah (the Demised Premises') for the term and upon the rental herein set forth. The complex commonly known as 3210 and 3222 Washington Street, South Salt Lake City, Utah, is shown on Exhibit A attached hereto ( the 'Complex').

Tenant shall also have the right to the exclusive use of the fenced yard and parking areas located on the property of the Complex fronting on Washington Street and the joint use of the fenced yard located at the rear of the property of the Complex fronting on 300 West Street with any other tenants of the property of the Complex. However, this right shall be subject to the exclusive control and management of Landlord. Landlord shall have the right, from time to time, to establish and modify and enforce reasonable rules and regulations with respect to parking."

## 2. PROPORTIONATE SHARE:

As used in Section III, paragraphs 1 (a), 3, 5 and 6 and elsewhere herein, "proportionate share" or "tenant's share" means that fraction, the numerator of which is the number of square

feet leased by the Tenant in the Demised Premises and the denominator which is the number of square feet in the Complex.

## II. TERM:

TO HAVE AND TO HOLD said premises unto Tenant for a term of five years beginning on 1st day of March, 1997, and ending on the 28th day of February, 2002.

## III. TERMS AND CONDITIONS OF LEASE:

This Lease is made on the following terms and conditions, which are expressly agreed to by Landlord and Tenant:

1. **BASE RENT:** The Tenant agrees to pay as base rental to Landlord, at the address specified in this Lease or at such other place Landlord may from time to time designate in writing, the sum of: SIX HUNDRED SIXTY SEVEN THOUSAND FIFTY SIX AND 00/100 DOLLARS (\$667,056). Said sum to be lawful money of the United States payable as follows: \$ 17,560 less \$2,620 (a previous deposit received) shall be paid upon the execution of this Lease of which \$10,060.00 represents the first month's rent and of which \$7500.00 represents the security deposit. Then beginning on April 1, 1997 and until February 28, 1998 Tenant shall pay Landlord the sum of \$10,060.00. Then beginning March 1, 1998 and on the first day of the month of each month thereafter until February 28, 1999 the Tenant shall pay \$10,563.00 to the Landlord. Then beginning on March 1, 1999 and on the first day of each month thereafter until February 28, 2000 the Tenant shall pay \$11,091.00 to the Landlord. Then beginning March 1, 2000 and on the first day of each month thereafter until February 28, 2001 the Tenant shall pay \$11,646.00 to the Landlord. Then beginning March 1, 2001 and on the first day of each month thereafter until February 28, 2002 the Tenant shall pay \$12,228.00 to the Landlord.

(a) **ADDITIONAL RENT:** In addition to Tenant's monthly base rent, Landlord will collect from Tenant its proportionate share of the operating expenses attributable to the Demised Premises on a monthly basis. The following items are included as operating expenses:

1. Real estate taxes
2. Fire and liability insurance
3. Common utilities and water and sewer charges

The estimated cost for 1997 is 3.55 cents per square foot or \$745 per month. At year

end the actual operating costs shall be determined by Landlord and any adjustment in such estimate shall be made with appropriate additional payments by or refunds to Tenant, as appropriate.

- (b) SECURITY DEPOSIT: Tenant contemporaneously with the execution of this lease, has deposited with Landlord the sum of \$7500.00 receipt of which is hereby acknowledged by Landlord, said deposit being given to secure the faithful performance by the Tenant of all of the terms, covenants and conditions of this lease by the Tenant to be kept and performed during the term hereof. Tenant agrees that if the Tenant shall fail to pay the rent herein reserved promptly when due, said deposit may, at the option of the Landlord (but Landlord shall not be required to) be applied to any rent due and unpaid, and if the Tenant violates any of the other terms, covenants and conditions of this Lease, said deposit shall be applied to any damages suffered.

Nothing contained in this paragraph shall in any way diminish or be construed as waiving any of the Landlord's other remedies as provided herein, or by law. If the security deposit is applied by Landlord for the payment of overdue rent or other sums due and payable to Landlord by Tenant hereunder, then Tenant shall, on the written demand of Landlord, forthwith remit to Landlord a sufficient amount in cash to restore said security deposit to its original amount, and Tenant's failure to do so within fifteen (15) days after receipt of such demand, shall constitute a breach of this lease. Should Tenant comply with all of the terms, covenants and conditions of this lease and promptly pay all of the rental herein provided for as it falls due, and all other sums payable by Tenant to Landlord hereunder, said security deposit shall be returned in full to Tenant at the end of the term of this lease, or upon the earlier termination of this lease pursuant to the provisions hereof, except in the event the demised premises are sold as a result of the exercise of any power of sale under any mortgage or deed of trust, in which event this lease shall be automatically amended to delete any reference to this paragraph and Tenant shall be entitled to immediate reimbursement of its security deposit from the party then holding said deposit.

- (c) LATE CHARGES: In the event Tenant fails to pay said rental (including any additional rental due hereunder) within ten (10) days of the due date, a late charge of ten percent (10%) shall be due and payable to Landlord.

2. RENEWAL OPTIONS: Provided that the Tenant is not in default under this Lease, Tenant shall have the option to renew the Term of this Lease as to the entire Demised Premises for a period of (60) months (the "First Renewal Term" ) to commence at the expiration of the initial Term of this lease, and to renew the First Renewal Term of this Lease as to the entire Demised Premises for an additional period of sixty (60) months (the "Second Renewal

Term") to commence at the expiration of the First Renewal Term. Tenant must exercise its option to renew by delivering written notice of such election to Landlord not less than six (6) months nor more than twelve (12) months prior to the expiration of the Term or the First Renewal Term, as applicable. Any such renewal of this Lease shall be upon the same terms and condition of this Lease, except:

- (a) The Leasehold improvements will be provided to Tenant in their then-existing condition (on an "as is basis") at the time each Renewal Term commences; and
- (b) At the time the First Renewal Term and the Second Renewal Term commence Landlord may adjust the Base Rent under the initial term (i) during the first Renewal Term, up to the Prevailing Market Rate, as hereinafter defined, and (ii) during the Second Renewal Term, up to the Prevailing Market Rate. The term "Prevailing Market Rate" shall mean the base rent per square foot of rentable area being charged for similar space in comparable premises in comparable location in Salt Lake City, Utah at the time the Renewal Terms commence; notwithstanding paragraph (b) above.
- (c) During each Renewal Term, the Base Rate shall escalate by at least five percent (5%) over the prior year's rental rate.

3. AUTHORIZED USE: Tenant shall use the Demised Premises for the following purpose, and for no other purpose whatsoever, without the written consent of Landlord first had and obtained: officing, sales, workshop, sheet metal fabrication, warehousing distribution.

Tenant shall not commit or knowingly permit any waste of the Demised Premises or use the same for any unlawful purpose. The Tenant will comply with all applicable federal, state and local laws, ordinances and regulations relating to the Demised Premises and its use and operation by the Tenant.

(a) Hazardous Material:

- 1. Tenant agrees not to keep, use or permit to be kept or used on the Demised Premises any flammable fluids, explosives or any "hazardous substance," "solid waste," or "hazardous waste" as said terms are defined in 42 U.S.C. 9601(14), and 40 C.F.R. 261.1 et seq. in violation of applicable law without the prior written permission of Landlord.
- 2. Tenant shall comply with all obligations imposed by environmental laws and all other restrictions and regulations upon the use, generation, storage or disposal of Hazardous Materials by tenant, its agents or employees at, to or from the Demised

Premises.

3. Tenant shall deliver promptly to Landlord true and correct copies of all notices received by Tenant from any governmental authority with respect to the use, generation, storage or disposal by Tenant of Hazardous Materials at, to or from the Demised Premises and shall immediately notify Landlord both by telephone and in writing of any unauthorized discharge of Hazardous Materials by Tenant that Tenant reasonably believes imposes and imminent hazard to the Demised Premises, the public or the environment.
4. Tenant shall complete fully, truthfully and promptly any questionnaires sent by Landlord with respect to Tenant's generation, storage and disposal of Hazardous Materials at, to or from the Demised Premises, which questionnaires are required by governmental authorities.
5. If Landlord conducts any environmental inspections as a result of its reasonable belief that Tenant's activities have or are likely to result in a violation of environmental laws or a release of Hazardous Materials on the Demised Premises and such violation by Tenant has actually occurred, then Tenant shall pay to Landlord as additional rent, the costs incurred by Landlord for such inspections.
6. Tenant shall cease immediately upon notice from Landlord any activity which violates any environmental laws.
7. After notice to and approval by Landlord, which approval shall not be unreasonably withheld, Tenant shall promptly remove, cleanup, dispose of or otherwise remediate, in accordance with environmental laws and good commercial practice, any Hazardous Materials on, under or about the Demised Premises caused by Tenant's acts on the Demised Premises.
8. Tenant agrees to indemnify, defend and hold Landlord and its officers, partners, directors, shareholders, employees and agents harmless from any claims, judgments, damages, fines, penalties, costs, liabilities (including sums paid in settlement of claims) or loss, including attorneys' fees, consultants' fees, and expert fees which arise during or after the term of this lease or renewals thereof in connection with the presence of Hazardous Materials in the soil, ground water or soil vapor on or under the Demised Premises or the Complex caused by the acts or negligent omissions of Tenant, its officers, employees or agents. Without limiting the generality of the foregoing, this indemnification obligation of Tenant shall survive the expiration of this Lease and specifically covers costs incurred in connection with any investigation of site conditions or any clean up,

remedial, removal or restoration work required by any federal, state or local governmental agency or political subdivision because of the presence or suspected presence of Hazard Materials in the soil, ground water or soil vapor on or under the Demised Premises and the Complex caused by the acts or negligent omissions of Tenant, its officers, employees or agents.

- (b) ADA. Tenant shall comply with the Americans with Disabilities Act of 1990 (ADA) and the regulations promulgated thereunder relating to any alterations, additions or improvements which Tenant makes to the Demised Premises. Tenant hereby expressly assumes all responsibility for compliance with the ADA relating to the interior, non-structural portions of the Demised Premises and Tenant's specific use of the Demised Premises. Any alterations to the interior, non-structural portions of the Demised Premises made by Tenant for the purpose of complying with the ADA or which otherwise require compliance with the ADA, shall be done in accordance with the provisions of this Lease; provided, that Landlord's consent to such alterations shall not constitute either Landlord's assumption, in whole or in part, of Tenant's responsibility for compliance with the ADA, or a representation or confirmation by Landlord that such alterations comply with the provisions of the ADA."

4. PAYMENT OF TAXES AND OTHER ASSESSMENTS: Tenant shall pay its proportionate share when they are due of all property taxes, license fees and assessments levied or imposed which are attributable to the Demised Premises or measured by the rent payable hereunder during the term of this Lease or any extension thereof, by Federal, state, municipal or other governmental authority excluding federal income tax or gift tax; provided, however, that no law or practice postponing the payment of such taxes, assessments or charges until after the termination of this Lease shall relieve Tenant of the obligation to make such payments. Payment of such taxes shall be made by Tenant to Landlord not later than thirty (30) days following the date on which Landlord provides Tenant with written evidence of such taxes in the form of a copy of the tax return or notice. If Tenant fails to pay any of such taxes, charges or other impositions when due, Landlord may pay the same under the provisions of paragraph 20, hereinafter set forth. Anything herein to the contrary notwithstanding, if Tenant deems excessive or illegal any such tax or assessment, Tenant may defer payment thereof so long as the validity or the amount thereof is contested by Tenant in good faith, in which case Tenant shall furnish to Landlord a bond, in form reasonably satisfactory to Landlord, in an amount equal to the amount of taxes or assessments so contested, w bond shall guarantee the payment thereof with interest and penalties thereon.
5. CONDITION OF THE PREMISES: Tenant accepts the Demised Premises in the condition they are in at the time of its taking thereof. Tenant agrees, if, during the term of this Lease, Tenant shall change the usual method of conducting Tenant's business on the Demised Premises, or should Tenant install thereon or therein any new facilities, Tenant will, at the sole cost and expense of Tenant, make alterations or improvements in or to the

Demised Premises which may be required by reason of any Federal or state law, or by any municipal ordinance, oprr regulation applicable thereto. Landlord warrants that the building, on date of occupancy, meets all currently applicable Federal, state and municipal laws and ordinances.

6. TENANT'S PAYMENT FOR PROPERTY INSURANCE: Tenant shall pay its proportionate share of insurance maintained by the Landlord which are attributable to the Demised Premises against the perils of fire, the "extended coverages", vandalism and mischief, and all risks to the building as well as coverage for six months rent loss due to business interruption from the covered risks. The amount of insurance coverage shall be in an amount equal to ninety percent (90%) of the replacement value of the Demised Premises. Tenant shall be responsible for any damage to premises as a result of forced entry into the Demised Premises or burglary thereof. Also, Tenant shall maintain insurance coverage for Tenant's personal property improvements, and alterations to the premises. This insurance shall cover the same risks and shall be for the same percentage of replacement value as the insurance maintained by the Landlord. The proceeds from such insurance shall be used to replace Tenant's personal property and to restore its improvements and alterations. Both Landlord and Tenant shall be named as coinsureds for this coverage maintained by the Tenant. Landlord shall be given thirty (30) days notice prior to cancellation or termination of this insurance policy.

7. REPAIR AND CARE OF BUILDING AND PAYMENT OF UTILITIES BY TENANT: Tenant shall pay all charges, when due, including but not limited to charges for water, heat, gas, electricity and other public utilities used on the Demised Premises, including all replacements of light bulbs, tubes, ballasts and starters within a reasonable time after they burn out.

Tenant agrees, at its sole cost and expense, to keep the interior of the Demised Premises and the grounds outside the Demised Premises in good condition, and to keep the sidewalks, driveways and parking lots of the Demised Premises free from snow and ice, and agrees to pay for all labor, materials and other repairs to, and replacement of, the electrical wiring, plumbing, air-conditioning and heating systems. Tenant shall also be responsible to clean and paint the interior of the Demised Premises such that it is returned to Landlord in the same condition as received by Tenant, normal wear and tear excepted.

Tenant also agrees to pay its proportionate share for:

1. Mowing of grass, care of shrubs, and general landscaping, if any;
2. The cleaning and painting of the exterior of the premises as reasonably deemed desirable by the Landlord for maintaining the Demised Premises in a clean, attractive and sanitary condition; and
3. The removal of snow and ice, as may be reasonably possible, from driveways and

parking lots.

8. REPAIR OF BUILDING BY LANDLORD: Landlord agrees for the term of this Lease, at Landlord's sole cost and expense to maintain the roof in good condition and repair, and to repair any latent defects in the exterior walls, floor joists, and foundations, and to repair any defects or any damage that might result from acts of Landlord or Landlord's representatives. Landlord shall not, however, be obligated to repair any such damage until written notice of the need of repair shall have been given to Landlord by Tenant and, after such notice is so given, Landlord shall have a reasonable time in which to make such repairs.
9. ALTERATIONS OF BUILDING AND INSTALLATION OF FIXTURES AND OTHER APPURTENANCES: Tenant may, with written consent of Landlord, which consent shall not be unreasonably withheld or delayed, but at Tenant's sole cost and expense in a good and workmanlike manner, make such alterations and repairs to the Demised Premises as Tenant may require for the conduct of its business without, however, materially altering the basic character of the building or improvements, or weakening any structure on the Demised Premises. Tenant shall have the right, with the written permission of Landlord, to erect, at Tenant's sole cost and expense, such temporary partitions, including office partitions, as may be necessary to facilitate the handling of Tenant's business and to install telephone and telephone equipment and wiring, and electrical fixtures, additional lights and wiring and other trade appliances. Any alterations or improvements to the Demised Premises, including partitions, all electrical fixtures, lights and wiring shall, at the option of Landlord, become the property of Landlord, at the expiration or sooner termination of this Lease. Should Landlord request Tenant to remove all or any part of the above mentioned items, Tenant shall do so prior to the expiration of this Lease and repair the Demised Premises as described below. Temporary moveable shelves, bins, and machinery installed by Tenant shall remain the property of Tenant and may be removed by Tenant at any time; provided, however, that all covenants, including rent due hereunder to Landlord shall have been complied with and paid. At the expiration or sooner termination of this Lease, or any extension thereof, Tenant shall remove said shelves, bins and machinery and repair, in a good workmanlike manner, all damage done to the Demised Premises by such removal.
10. ERECTION AND REMOVAL OF SIGNS: Tenant may, if building policy and city ordinances permit, place suitable signs on the Demised Premises for the purpose of indicating the nature of the business carried on by Tenant in said premises; provided, however that such signs shall be in keeping with other signs in the district where the Demised Premises are located; and provided, further, that the location and size of such signs shall be approved by Landlord prior to their erection. Signs shall be removed prior to the expiration of this lease and any damage to the Demised Premises caused by installation or removal of signs shall be repaired at expenses of the Tenant. All work shall be completed in a good workmanlike manner.
11. GLASS: Tenant agrees to immediately replace, at its sole cost and expense, all glass into

the Demised Premises if broken or damaged during the term of this Lease with glass of the same quality as that broken or damaged.

12. **RIGHT OF ENTRY BY LANDLORD:** Tenant, shall permit inspection of the Demised Premises during reasonable business hours by Landlord or Landlord's agents or representatives for the purpose of ascertaining the condition of the Demised Premises and in order that Landlord may make such repairs as may be required to be made by Landlord under the terms of this Lease. Sixty (60) days prior to the expiration of this Lease, Landlord may post suitable notice on the Demised Premises that the same are "For Rent" and may show the Demised Premises to prospective tenants at reasonable times. Landlord may not, however, thereby unnecessarily interfere with the use of Demised Premises by Tenant.
13. **ASSIGNMENT AND SUBLETTING:** Neither this Lease nor any interest herein may be assigned by Tenant voluntarily or involuntarily, or by operation of law, and neither all nor any part of the Demised Premises shall be sublet by Tenant without the written consent of Landlord first had or otherwise obtained; however, Landlord agrees not to withhold its consent unreasonably for Tenant to assign or sublet the Demised Premises. In the event the Demised Premises should be sublet, as herein provided, at an increased rental, fifty (50%) percent of said increase shall be paid to Landlord by Tenant as additional rental. Any assignment or subletting shall not release Tenant from its obligations under this lease.

Notwithstanding the preceding paragraph, Tenant may transfer, assign or sublet this Lease to an "Affiliate," as hereinafter defined, without Landlord's consent. An Affiliate shall mean (i) a person or entity that controls or is controlled by or under common control with Tenant, (ii) a person or entity that survives a merger or consolidation with or into Tenant and (iii) a person or entity to which all or substantially all of the assets of Tenant may be sold, transferred or conveyed, whether by operation of law, by contract or otherwise. The term "control" means, with respect to an entity, the ownership, directly or indirectly, of more than fifty percent (50%) of the voting securities of such entity, or the power to direct the management or policies of such entity, whether by operation of law, by contract or otherwise. With respect to either party's assignment or subletting permitted hereunder without the other party's consent, the assigning party shall provide written notice of such assignment or subletting to the other party within thirty (30) days of the effective date of such assignment or sublet.

14. **DAMAGE OR DESTRUCTION:** If the Demised Premises or any part thereof shall be damaged or destroyed by fire or other casualty, Landlord shall promptly repair all such damage and restore the Demised Premises without expense to Tenant, subject to delays due to adjustment of insurance claims, strikes and other causes beyond Landlord's control. If such damage or destruction shall render the Demised Premises untenable in whole or in part, the rent shall be abated wholly or proportionately as the case may be until the damage shall be repaired and the Demised Premises restored. If the damage or destruction shall be so extensive as to require the substantial rebuilding, i.e., expenditure of fifty (50%) percent



or more of replacement cost of the building or buildings on the demised premises, Landlord or Tenant may elect to terminate this Lease by written notice to the other given within thirty (30) days after the occurrence of such damage or destruction. Landlord and Tenant hereby release each other from responsibility for loss or damage occurring on or to the Demised Premises or the premises of which they are a part or to the contents of either thereof, caused by fire or other hazards ordinarily covered by fire and extended coverage insurance policies and each waives all rights of recovery against the other for such loss or damage. Willful misconduct lawfully attributable to either party, whether in whole or in part a contributing cause of the casualty giving rise to the loss or damage, shall not be excused under the foregoing release and waiver.

15. INJURIES AND PROPERTY DAMAGE: Tenant agrees to indemnify and hold harmless Landlord of and from any and all claims of any kind or nature arising from Tenant's use of the Demised Premises during the term hereof, and Tenant hereby waives all claims against Landlord for damage to goods, ware, merchandise or for injury to persons in and upon the Demised Premises from any cause whatsoever, except such as might result from the negligence of Landlord or Landlord's representatives or from failure of Landlord to perform its obligation hereunder within a reasonable time after notice in writing by Tenant requiring such performance by Landlord. Tenant shall at all times during the term hereof keep in effect in responsible companies, acceptable to Landlord, liability insurance in the names of and for the benefit of Tenant and Landlord with limits as follows:

Bodily Injury, \$2,000,000.00 each occurrence; Property Damage, \$100,000.00; or in lieu thereof, a combined limit of bodily injury and property damage liability of not less than \$2,000,000.00.

Such insurance may, at Tenant's election, be carried under any general blanket coverage of Tenant. A renewal policy shall be procured not less than ten (10) days prior to the expiration of any policy. Each original policy or a certified copy thereof, or a satisfactory certificate of the insurer evidencing insurance carried with proof of payment of the premium shall be provided by Tenant upon the request of Landlord. Tenant shall have the right to settle and adjust all liability claims and all other claims against the insuring companies, but without subjecting Landlord to any liability or obligation.

16. SURRENDER OF PREMISES: Tenant agrees to surrender the Demised Premises at the expiration, or sooner termination, of the term of this Lease, or any extension thereof, in the same condition as when said premises were delivered to Tenant, or as altered, pursuant to the provisions of this Lease, ordinary wear, tear and damage by the elements excepted, and Tenant shall remove all of its personal property. Tenant agrees to pay a reasonable cleaning charge should it be necessary for Landlord to restore or cause to be restored the premises to the same condition as when said premises were delivered to Tenant.

17. **HOLDOVER:** Should the Landlord permit Tenant to holdover the Demised Premises or any part thereof, after the expiration of the term of this Lease, then and unless otherwise agreed in writing, such holding over shall constitute a tenancy from month-to-month only, and shall in no event be construed as a renewal of this Lease and all provisions of this Lease not inconsistent with a tenancy from month-to-month shall remain in full force and effect. During the month-to-month tenancy, Tenant agrees to give Landlord thirty (30) days prior written notice of its intent to vacate premises. Tenant agrees to vacate the premises upon thirty (30) days prior written notice from Landlord. The rental for the month-to-month tenancy shall be equal to 150% of the rental payable for the last month of the previous term of this Lease.
18. **QUIET ENJOYMENT:** If and so long as Tenant pays the rents reserved by this Lease and performs and observes all the covenants and provisions hereof, Tenant shall quietly enjoy the demised premises, subject, however, to the terms of this Lease, and Landlord will warrant and defend Tenant in the enjoyment and peaceful possession of the demised premises throughout the terms of this Lease.
19. **WAIVER OF COVENANTS:** The failure of any party to enforce the provisions of this Lease shall not constitute a waiver unless specifically stated in writing, signed by the party whose rights are deemed waived, regardless of a party's knowledge of a breach hereunder.
20. **DEFAULT:** If Tenant shall make default in the fulfillment of any of the covenants and conditions hereof except default in payment of rent, Landlord may, at its option, after fifteen (15) days prior notice to Tenant, make performance for Tenant and for the purpose advance such amounts as may be necessary. Any amounts so advanced, or any expense incurred, or sum of money paid by Landlord by reason of the failure of Tenant to comply with any covenant agreement, obligation or provision of this Lease, or in defending any action to which Landlord may be subjected by reason of any such failure for any reason of this Lease, shall be deemed to be additional rent for the Demised Premises and shall be due and payable to Landlord on demand. The acceptance by Landlord of any installment of fixed rent, or of any additional rent due under this or any other paragraph of this lease, shall not be a waiver of any other rent then due nor of the right to demand the performance of any other obligation of the Tenant under this Lease. Interest shall be paid to Landlord on all sums advanced by Landlord at an annual interest rate of 2% over the prime rate charged by FIRST SECURITY BANK.
- If Tenant shall make default in fulfillment of any of the covenants or conditions of this Lease (other than the covenants for the payment of rent or other amounts) and any such default shall continue for a period of thirty (30) days after notice, then Landlord may, at its option, terminate this Lease by giving Tenant written notice of such termination and, thereupon, this Lease shall expire as fully and completely as if that day were the date definitely fixed for the expiration of the term of this Lease and Tenant shall quit and surrender the Demised Premises.
21. **DEFAULT IN RENT, INSOLVENCY OF TENANT:** If Tenant shall make default in the payment of the rent reserved hereunder, or any part thereof, or in making any other payment

herein provided for, and any such default shall continue for a period of ten (10) days, after written notice to Tenant, or if the Demised Premises or any part thereof shall be abandoned or vacated or if Tenant shall be legally dismissed therefrom by or under any authority other than Landlord, or if Tenant shall file a voluntary petition in bankruptcy or if Tenant shall file any petition or institute any proceedings under any insolvency or United States Bankruptcy Code or any amendment thereto hereafter made, seeking to effect its reorganization or a composition with its creditors, or if any proceedings based on the insolvency of Tenant or relating to bankruptcy proceedings are commenced and remain unstayed for forty-five (45) days, a receiver or trustee shall be appointed for Tenant or the Demised Premises or if any proceedings shall be commenced for the reorganization of Tenant or if the leasehold estate created hereby shall be taken on execution or by any process of law or if Tenant shall admit in writing its inability to pay its obligations generally as they become due, then Landlord, in addition to any other rights or remedies it may have, shall have the immediate right of re-entry and may remove all persons and property from the Demised Premises. Such property may be removed and stored in a public warehouse or elsewhere at the cost of and for the account of Tenant. Landlord may elect to reenter, as herein provided, or Landlord may take possession pursuant to this Lease and relet the Demised Premises or any part thereof for such term or terms (which may be for a term extending beyond the term of this Lease) and at such rental or rentals and upon such other terms and conditions as Landlord in the exercise of Landlord's sole discretion may deem advisable with the right to make alterations and repairs to said premises. Upon each subletting, Tenant shall be immediately liable for and shall pay to Landlord, in addition to any indebtedness due hereunder, the costs and expenses of such reletting including advertising costs, brokerages fees, any reasonable attorney's fees incurred and the cost of such alterations and repairs incurred by Landlord, and the amount, if any, by which the rent reserved in this Lease for the period of such reletting (up to but not beyond the term of this Lease) exceeds the amount agreed to be paid as rent for the Demised Premises for said period by such reletting. If Tenant has been credited with any rent to be received by such reletting and such rents shall not be promptly paid to Landlord by the new Tenant, such deficiency shall be calculated and paid monthly by Tenant. No such re-entry or taking possession of the Demised Premises by Landlord shall be construed as an election by Landlord to terminate this Lease unless the termination thereof be decreed by a court of competent jurisdiction or stated specifically by the Landlord in writing addressed to Tenant. Notwithstanding any such reletting without termination, Landlord may at any time thereafter elect to terminate this Lease for such previous breach. Should Landlord at any time terminate this Lease for any breach, in addition to any other remedy Landlord may have, Landlord may recover from Tenant all damages Landlord may incur by reason of such breach, including the cost of recovering the Demised Premises including attorney's fees, court costs, and storage charges and including the worth at the time of such termination of the excess, if any, of the amount of rent and charges equivalent to rent reserved in this Lease for the remainder of the stated term over the then chargeable rent on the premises for the remainder of the stated term, all of which amounts shall be immediately due and payable from Tenant to Landlord. In no event, shall this Lease or any rights or privileges hereunder be an asset of Tenant under any bankruptcy, insolvency or reorganization proceedings.

22. ENFORCEMENT: In the event either party shall enforce the terms of this Lease by suit or otherwise, the party at fault shall pay the costs and expenses incident thereto, including reasonable attorney's fees.
23. FAILURE TO PERFORM COVENANT: Any failure on the part of either party to this Lease to perform any obligations hereunder, other than Tenant's obligation to pay rent, and any delay in doing any act required hereby shall be excused if such failure or delay is caused by any strike, lockout, governmental restriction or any similar cause beyond the control of the party so failing to perform, to the extent and for the period that such continues.
24. RIGHTS OF SUCCESSORS AND ASSIGNS: The covenants and agreements contained in this Lease will apply to, inure to the benefit of, and be binding upon the parties hereto, their heirs, distributees, executors, administrators, legal representatives, permitted assigns, and upon their respective successors in interest except as expressly otherwise hereinabove provided.
25. TIME: Time is of the essence of this Lease and every term, covenant and condition herein contained.
26. LIENS: Tenant agrees not to permit any lien for monies owing by Tenant to remain against the Demised Premises for a period of more than thirty (30) days following discovery of the same by Tenant; provided, however, that if tenant posts a bond in the amount of the lein nothing herein contained shall prevent Tenant, in good faith and for good cause from contesting the claim or claims of any person, firm or corporation growing out of Tenant's operation of the Demised Premises or costs of improvements by Tenant on the said premises, and the postponement of payment of such claim or claims, until such contest shall finally be decided not to be a violation of this Lease or any covenant thereof. Should any such lien be filed and not released or discharged or action not commenced to declare the same invalid within thirty (30) days after discovery of the same by Tenant, Landlord may at Landlord's option (but without any obligation so to do) pay and discharge such lien and may likewise pay and discharge any taxes, assessments or other charges against the Demised Premise which Tenant is obligated hereunder to pay and which may or might become a lien on said premises. Tenant agrees to repay any sum so paid by Landlord upon demand therefor, as provided for in paragraph 20 herein.
27. SUBORDINATION: This Lease shall be subject and subordinate to all mortgages, deeds of trust and related security instruments which may now or hereafter encumber the Demised Premises and to all renewals, modifications, consolidations, replacements and extensions thereof and to each advance made thereunder, provided that Tenant has received from the holder thereof an agreement that Tenant will not be disturbed in its possession of the Demised Premises, or have its rights under this Lease modified or terminated other than pursuant to the terms of this Lease. In the event of the enforcement by the trustee or the beneficiary under any such mortgage or deed of trust of the remedies provided for by law or by such mortgage or deed of trust, Tenant will, upon the request of any person or party succeeding to the interest of said trustee or beneficiary as a result of such enforcement (and

subject to the aforesaid recognition of Tenant's rights under the Lease), automatically become the tenant of, and attorn to, such successor in interest without change in the terms or provisions of this Lease.

28. **DEFAULT BY LANDLORD:** Except where the provisions of this Lease grant Tenant an express, exclusive remedy, or expressly deny Tenant a remedy, if:
- (a) Landlord fails to pay amount payable by Landlord hereunder and such failure to pay continues and remains unremedied for a period of fifteen (15) days after written notice thereof given by Tenant to Landlord; or
  - (b) Landlord fails to perform or observe any covenant, term, provision or condition of this Lease that interferes in any material respect with Tenant's use and enjoyment of the Demised Premises, and such failure continues for a period of thirty (30) days after written notice thereof given by Tenant to Landlord; provided, however, if the nature of the default is such that it cannot be cured with the exercise of Landlord's reasonable and good faith efforts within the thirty (30) day period, Landlord shall have up to ninety (90) days from the date of Tenant's notice to cure such default, provided Landlord undertakes such curative action within the thirty (30) day period and diligently and continuously proceeds with such curative action using Landlord's reasonable and good faith efforts;

then, Tenant may deliver a second notice to Landlord, and if such default shall continue uncured by Landlord and/or its mortgagee for an additional thirty (30) days after the delivery of such second notice, Tenant shall have the right to exercise one or more of the following options, but not (i) and (ii) simultaneously: (i) Tenant may cure the default which, in the case of a monetary default, may be effected by the withholding of or offsetting against rent, and Landlord shall reimburse Tenant (which reimbursement may be effected through the withholding of or offsetting against rent) for all reasonable sums expended in so curing said default, (ii) Tenant may terminate this Lease and (iii) Tenant may pursue all other remedies at law or in equity to which Tenant may be entitled. Tenant may not terminate this Lease because of Landlord's default unless specifically permitted pursuant to this paragraph or unless otherwise specifically provided in this Lease. Tenant specifically agrees that the cure of any default by and Landlord mortgagee shall be deemed a cure by Landlord under this Lease.

29. **CONSTRUCTION OF LEASE:** Words of any gender used in this Lease shall be held to include any other gender, and words in the singular number shall be held to include the plural when the sense requires.
30. **SIGNING OF DOCUMENTS:** Tenant shall sign and deliver any instrument or documents necessary or appropriate to evidence any such attornment or subordination or agreement to do so. Such subordination and attornment documents may contain such provisions as are customarily required by any ground Landlord, beneficiary under a deed of trust or mortgagee. If Tenant fails to do so within ten (10) days after written request, Tenant

hereby makes, constitutes and irrevocably appoints Landlord, or any transferee successor of Landlord, the attorney-in-fact of Tenant to execute and deliver any such instrument or document.

31. ESTOPPEL CERTIFICATES:

(a) Upon Landlord's written request, Tenant shall execute, acknowledge and deliver to Landlord a written statement certifying: (i) that none of the terms or provisions of this Lease have been changed (or if they have been changed, stating how they have been changed); (ii) that this Lease has not been canceled or terminated; (iii) the last date of payment of the Base Rent and other charges and the time period covered by such payment; (iv) that Landlord is not in default under this Lease (or, if Landlord is claimed to be in default, stating why); and (v) such other matters as may be reasonably required by Landlord or the holder of a mortgage, deed of trust or lien to which the Property is or becomes subject. Tenant shall deliver such statement to Landlord within ten (10) days after Landlord's request. Any such statement by Tenant may be given by Landlord to any prospective purchaser or encumbrancer of the Property. Such purchaser or encumbrancer may rely conclusively upon such statement as true and correct.

32. TENANT'S FINANCIAL CONDITION: Within ten (10) days after written request from Landlord, Tenant shall deliver to Landlord most recent financial statements made as are reasonably required by Landlord to verify the net worth of Tenant, or any assignee, subtenant, or guarantor of Tenant. In addition, Tenant shall deliver to any lender designated by Landlord any financial statements required by such lender to facilitate the financing or refinancing of the Property. Tenant represents and warrants to Landlord that each such financial statement is a true and accurate statement as of the date of such statement. All financial statements shall be confidential and shall be used only for the purposes set forth herein.

33. PARAGRAPH HEADINGS: The paragraph headings as to the contents of particular paragraphs herein, are inserted only for convenience and are in no way to be construed as part of such paragraph or as a limitation on the scope of the particular paragraph to which they refer.

34. NOTICES: It is agreed that all notices required or permitted to be given hereunder, or for purposes of billing, process, correspondence, and any other legal purposes whatsoever, shall be deemed sufficient if given by a communication in writing by United States mail, postage prepaid and certified and addressed as follows:

If to Landlord, at the following address:

J&J investments

2030 MapleHollow Way  
Bountiful, Utah 84010  
(801) 292-6546

If to Tenant, at the following address:

Contract Service Inc.  
PO Box 65429  
Salt Lake City, Utah 84165-0429

35. **GOVERNING LAW:** The terms of this Agreement shall be governed by and construed in accordance with Utah law.
36. **DOCUMENTATION:** The parties hereto agree to execute such additional documentation as may be necessary or desirable to carry out the intent of this Agreement.
37. **CONTINGENCY REGARDING USE:** This Lease is contingent upon there being no restrictions, covenants, agreements, laws, ordinances, rules or regulations, which would prohibit Tenant from using the above described premises for the purposes described herein.
38. **INDEMNIFICATION OF LANDLORD:** Tenant, as a material part of the consideration to be rendered to Landlord under this Lease, shall hold Landlord exempt and harmless from any damage or injury to any person, or the goods, wares and merchandise of any person, arising from the use of the Demised Premises by Tenant, or from the failure of the Tenant to keep the premises in good condition and repair, as herein provided.
39. **EMINENT DOMAIN:** If at any time during the term of this Lease the entire Demised Premises or any part thereof shall be taken as a result of the exercise of the power of eminent domain or by an agreement in lieu thereof, this Lease shall terminate as to the part so taken as of the date possession is taken by the condemning authority. If all or any substantial portion of the Demised Premises shall be taken, Landlord may terminate this Lease at its option, by giving Tenant written notice of such termination within thirty (30) days of such taking. If all or a portion of the premises taken are so substantial that Tenant's use of the Demised Premises is substantially impaired, Tenant may terminate this Lease pursuant to this Article. Unless terminated as herein provided for, this Lease shall remain in full force and effect, except that the rent payable by Tenant hereunder shall be reduced in the proportion that the area of the premises so taken bears to the total premises. Landlord shall be entitled to and Tenant hereby assigns to Landlord the entire amount of any award in connection with such taking. Nothing in this Article shall give Landlord any interest in or preclude Tenant from seeking, on its own account, any award attributable to the taking of personal property or trade fixtures belonging to Tenant, or for the interruption of Tenant's business.

41. ENTIRE AGREEMENT: This Lease constitutes the entire agreement and understanding between the parties with respect to the subject matter hereof and supersedes all prior discussions, understandings and agreements.
42. REPRESENTATION REGARDING AUTHORITY: The persons who have executed this Lease represent and warrant that they are duly authorized to execute this Lease in their individual or representative capacity as indicated.
- Amendment of this Lease may not be altered or amended except by a subsequent written agreement executed by all of the parties hereto.
43. REVIEW OF DOCUMENTS: The parties hereto represent that they have read and understand the terms of this Lease, and that they have sought legal counsel to the extent deemed necessary in order to protect their respective interests.
44. KEYS & LOCKS: Tenant, upon the termination of the Tenancy, shall deliver to the Landlord all the keys to the offices, rooms and restrooms which have been furnished to the Tenant.
45. AUCTION, FIRE OR BANKRUPTCY SALE: Tenant shall not conduct any auction nor permit any fire or bankruptcy sale to be held on the Demised Premises.
46. CARPETING DAMAGE AND CHAIRMATS: Tenant agrees to be responsible for the replacement of carpeting in the Demised Premises.
47. MEDIATION AND ARBITRATION. If any dispute or claim in law or equity arises out of this Lease, Tenant and Landlord agree in good faith to attempt to settle such dispute or claim by mediation under the Commercial Mediation rules of the American Arbitration Association. If such mediation is not successful in resolving such dispute or claim, then such dispute or claim shall be decided by neutral binding arbitration before a single arbitrator in accordance with the Commercial Arbitration rules of the American Arbitration Association in Salt Lake City, Utah. Judgment upon the award rendered by the arbitrator may be entered in any court having jurisdiction thereof. However, this paragraph does not apply to disputes or claims arising under Section 78, Chapter 36, of the Utah Code.



IN WITNESS WHEREOF, the parties hereto have caused these presents to be executed as of the day and year first above written.

LANDLORD:

TENANT:

J&J INVESTMENTS

CONTRACT SERVICE, INC.

BY: \_\_\_\_\_

BY: \_\_\_\_\_

## AMENDMENT TO LEASE AGREEMENT

THIS AMENDMENT TO LEASE AGREEMENT (this "Agreement") is made and entered into on this 13th day of March, 1997, by and between COOK PROPERTIES, INC. ("Cook Properties"), and TECH HEATING AND AIR CONDITIONING, INC. ("Lessee").

## W I T N E S S E T H:

WHEREAS, Cook Properties and Lessee intended to enter into that certain Lease dated April 2, 1995 (the "Lease"), covering approximately 10,850 square feet of space (the "Leased Premises") located at 30300 Bruce Industrial Parkway, Solon, Ohio.

WHEREAS, Cook Properties and Lessee desire to correct, amend and modify the Lease as more particularly provided herein;

NOW, THEREFORE, in consideration of the premises, the mutual promises herein contained and other good and valuable consideration, the receipt and sufficiency of all of which is hereby acknowledged and confessed, Cook Properties and Lessee hereby agree as follows:

1. Cook Properties and Lessee acknowledge and agree that the Lease contains an error in the first paragraph of the Lease where reference is made to Tech Heating and Air Conditioning, Inc., at 30300 Bruce Industrial Parkway, in Solon, Ohio, as the "Lessor" under the Lease.

2. WHEREAS, Cook Properties and Lessee acknowledge and agree that it was the intent of both Cook Properties and Lessee at the time the Lease was executed that the "Lessor" under the Lease was to be Cook Properties.

3. Cook Properties and Lessee acknowledge and agree that for all purposes under the Lease all references to Lessor shall mean Cook Properties, and the purpose of this Amendment is to correct the incorrect, inadvertent reference that appears in the Lease where reference is made to Tech Heating and Air Conditioning, Inc. as "Lessor" and correct all references to "Lessor" to refer to Cook Properties.

4. Cook Properties and Lessee agree that the corrections made pursuant to this Amendment shall relate back to the date the Lease was executed and any rights and/or obligations of "Lessor" under the Lease shall be interpreted to refer to the rights and obligations of Cook Properties commencing on the date the Lease was originally executed.

In the event of any conflict in the terms, provisions, or conditions of the Lease and this Amendment, the provisions of this Amendment shall prevail.

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

LESSOR:

COOK PROPERTIES, INC.

/s/ BOB COOK  
Bob Cook  
Title: President

LESSEE:

TECH HEATING AND AIR CONDITIONING,  
INC.

/s/ BOB COOK  
Bob Cook  
Title: President

THE STATE OF OHIO                   SS.  
  SS.  
COUNTY OF CUYAHOGA               SS.

The foregoing instrument was acknowledged before me, a Notary Public, on this 13TH day of MARCH, 1997 by Bob Cook, as PRESIDENT of COOK PROPERTIES, INC.

(SEAL)

/s/ MARIA A. SZENTE  
Notary Public in and for  
The State of Ohio

Print Name: MARIA A. SZENTE  
Commission Expires: 9/27/2000

THE STATE OF OHIO                   SS.  
  SS.  
COUNTY OF CUYAHOGA               SS.

The foregoing instrument was acknowledged before me, a Notary Public, on this 13TH day of MARCH , 1997 by Bob Cook, as PRESIDENT of TECH HEATING AND AIR CONDITIONING, INC.

(SEAL)

/s/ MARIA SZENTE  
Notary Public in and for  
The State of Ohio

Print Name: MARIA A. SZENTE  
Commission Expires: 9/27/2000

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TECH HEATING AND AIR CONDITIONING, INC.  
MAIN BUILDING

- I. 5,750 sq. ft. of finished conditioned office space at \$10.14 per sq. ft.
- II. 5,140 sq. ft. of heated warehouse space at \$500 per sq. ft.

LEASE AGREEMENT

THIS LEASE, made this APRIL 2, 1995, between Tech Heating and Air Conditioning, Inc., at 30300 Bruce Industrial Parkway, in Solon, Ohio, hereinafter called "Lessor," Tech Heating and Air Conditioning, Inc. hereinafter collectively called "Lessee."

WITNESSETH

Lessor leases to Lessee and Lessee rents from Lessor approximately 10,850 square feet of space (the "Premises"), in the warehouse building located at 30300 Bruce Industrial Parkway, in Solon, Ohio (the "Building") together with the non-exclusive right to use a pro-rata share of the parking spaces, upon the terms and provisions set forth in this lease.

1. TERM-POSSESSION

- (a) The term of this lease shall be 60 months, commencing on APRIL 2, 1995 (the "Commencement Date ") and ending on APRIL 2, 2000.

2. RENT

- (a) Lessee covenants and agrees to pay to Lessor the Base Rent, Escalation Payments and additional rents and charges set forth in this Lease sometimes collectively hereinafter referred to as ("Rent") without demand, deduction or set-off at the address of Lessor set forth above or such other place as Lessor may designate in writing.
- (b) As Base Rent for the Premises, Lessee shall pay Lessor the sum of EIGHTY FOUR THOUSAND DOLLARS (\$84, 000.00), annually during the initial term of this lease, payable in equal monthly installments of SEVEN THOUSAND DOLLARS (\$ 7,000.00) each in advance on the day of each and every calendar month. Rent payable for any period less than a calendar month shall be pro-rated on a daily basis.
- (c) In addition to Base Rent, Lessee shall pay to Lessor as additional rent the Escalation Payments in accordance with the provisions of Section 3 hereof.
- (d) All overdue installments of rent, 15 day past the 1st of the month shall bear interest from the date such installments is due at the rate of one and one-half percent (1 1/2%) per month until paid. Annual percentage rate is eighteen percent (18%).

3. ESCALATION RENTS

- (a) Lessee shall pay Lessor, as additional rent, for each lease year commencing with the sixth (6th) lease year an amount equal to four percent (4%) in excess of the total rent payable during the prior average lease year.
- (b) "Lease Year" shall mean each period of twelve (12) consecutive months beginning on the first (1st) day of June of each year, during the term of this lease.
- (c) Such additional rent for every lease year which follows the second lease year shall be billed and paid as follows:
  - 1. Prior to the beginning of any such lease year, Lessor shall deliver to Lessee a statement showing the aggregate amount of such additional rent that will be payable to the then current lease year. Lessee shall pay Lessor such sum in equal monthly installments on the first day of each and every month during such lease year.
  - 2. If a statement mentioned in Section (c) (1) shall not have been delivered until the lapse of one or more months of this lease year, for which such payments are to be made, Lessee shall make equal monthly payments of any such increase over the balance of the then current lease year.
- (d) The escalation rent shall be four percent (4%) of the gross rental (base rent and escalation rent) payable during the previous lease year and shall be cumulative.

4. LESSOR'S WORK OBLIGATIONS

- (a) No representation respecting the condition of the Premises or the Building has been made by Lessor to Lessee unless expressly contained herein and none shall be implied in law.

5. USE

- (a) Tech Heating and Air Conditioning, Inc. shall use and occupy the Premises for office and warehouse space.
- (b) Lessee shall not use or permit the Premises to be used for any unlawful business or purpose. Lessee at its sole cost and expense shall comply with all laws, orders and regulations of Federal, State, county and municipal authorities and with any

directions of any public officer which shall impose any liability, order or duty upon Lessor or Lessee with respect to Lessee's use or occupancy of the Premises.

6. UTILITIES

- (a) Lessee shall pay for all utilities serving or used in connection with Lessee's occupancy of the Premises, including, without limitation, electricity, gas, water and telephone. Lessee's use of any such services shall never exceed the capacity of the mains, feeders, ducts, and conduits bringing such service to the Premises or of the outlets, risers, wiring, piping, ductwork and other means of distribution of such service within the premises.

Lessee shall pay to Lessor as additional rent fifteen percent (15%) of all common utilities for the Premises, including, without limitation, electricity, gas and water. Monthly, Lessor shall bill Lessee for its percentage share, based on Lessor's single bill for each utility.

- (b) Lessee shall not use any electrical equipment which will overload or interfere with the electrical installations of the Building. Light bulbs, tubes, starters, ballasts and their equivalents used or consumed on Lessee's Premises shall be paid or by Lessee in addition to rental and other charges provided herein.

7. INTERRUPTION OF UTILITIES AND SERVICES

- (a) Lessor does not warrant that any of the services stipulated in Paragraphs 5 and 6 above shall be free from interruption, fluctuation or suspension. Any interruption or suspension of, or fluctuation in, any service to the Building or Premises shall not be deemed an eviction or disturbance of Lessee's use and possession of the Premises, or any part thereof, nor render possession of the Premises, or any part thereof, nor render Lessor liable to Lessee for damages, nor relieve Lessee from performance of Lessee's covenants and agreements hereunder.

8. OPERATING EXPENSES

- (a) Lessee shall pay to Lessor as additional rent FIFTY PERCENT (50% of all costs and expenses (except real estate taxes) paid or incurred by or on behalf of lessor in connection with the operation, servicing, and maintenance of the Premises, (i. e. snowplowing and lawn maintenance). In addition, Lessee shall pay to Lessor FIFTY PERCENT (50%) of the increase in real estate taxes payable for the year 1989 over the tax bills for the year 1988 after building completions.



9. REPAIR AND MAINTENANCE OF PREMISES BY LESSEE

- (a) Lessee shall make at Lessee's expense all repairs and replacements required to keep the Premises and the fixtures and improvements therein in good working condition and repair except structural repairs, which shall be made by Lessor. All repairs or replacements of the Premises and Building required as a result of Lessee's or its agents, employees or contractor's misuse, neglect, act of negligence or by reason of Lessee's tenancy therein shall be made by Lessee at Lessee's expense. All replacements made by Lessee shall maintain sufficient heat within the Premises to prevent the freezing of pipes and other damage. Any such damage from insufficient heat shall be the responsibility of the Lessee.

Lessee shall not make any alterations, additions, improvements or other changes in or to said Premises, or installation without Lessor's prior written consent in each and every instance.

10. MECHANIC'S LIEN

- (a) If, because of any alleged act of Lessee or anyone claiming under Lessee, any mechanic's or other lien shall be filed against Lessor's estate in the Premises (whether or not such lien is valid or enforceable), Lessee shall, at Lessee's own cost and expense, cause the same to be discharged of record by payment of bonding within thirty (30) days after the date of filing thereof and Lessee shall also indemnify and save harmless Lessor from and against any and all costs, expenses, claims, losses or damages, including reasonable counsel fees, resulting from the filing of any such mechanic's or other lien. Nothing in this Lease shall be construed as a consent on Lessor's estate in the Building to any lien or liability under any law relating to liens.

11. RIGHTS RESERVED BY LESSOR

Lessor reserves the following rights:

- (a) Lessor will provide door glass lettering and tenant sign in front of building.
- (b) To enter the Premises at all reasonable notice upon reasonable notice
- (i) for making of such inspections, repairs alterations or additions of or to the Premises or the Building as Lessor may deem necessary or desirable.
- (ii) to exhibit the Premises to others in the last six (6) months of lease term.

(iii) for any purpose whatsoever related to the safety, protection or preservation of the Premises or the Building.

12. LOSS OR DAMAGE TO PROPERTY

- (a) All property belonging to Lessee or others located in or outside of the Premises or Building, shall be there at the sole risk of Lessee or such others, and unless caused by Lessor's negligence, Lessor and Lessor's agents and employees shall not be liable for the theft, loss or misappropriation thereof, nor for any damage or injury thereto, nor for death or injury of Lessee or any of its officers, agents, employees, customers, invitees or contractors or any other person, or for damage to property caused by fire, casualty, water, rain, sprinklers, snow, frost, ice steam, heat, cold dampness, failing plaster, water coming through the roof, walls or foundations, explosion, sewers or sewage, gas, odors, noise, the bursting or leaking of pipes, plumbing, electrical wiring and equipment and fixtures of all kinds, or by any act or neglect of other tenants or occupants of the Building, or any other person, or caused in any manner whatsoever, nor shall Lessor be liable for any latent defect in the Premises.

13. INDEMNIFICATION AND INSURANCE

- (a) Unless caused by Lessor or Lessor's agents and employees, Lessee shall indemnify Lessor and save Lessor harmless from and against any and all claims, actions damages, liability and expense in connection with loss, damage or injury to persons or property occurring in, on above or arising out of the Premises the use or occupancy thereof, or the conduct or operation of Lessee's business, or occasioned wholly or in part by any act or omission of Lessee's business, or part by any act or omission of Lessee's business, or occasioned wholly or in part by any act or omission of Lessee, its agents, contractors, employees or invitees.
- (b) Lessee shall maintain in full force and effect comprehensive general liability insurance policies naming Lessor as an additional insured in companies licensed to do business in Ohio with minimum single limits of \$1,000,000 on account of bodily injuries to or death of one or more than one person as a result of an accident or occurrence and \$250,000 on account of damage to property. Lessee shall deposit certificates of such insurance with Lessor prior to take occupancy of the Premises and within ten (10) days prior to the expiration of any such policies.
- (c) Lessee shall maintain fire, extended coverage and other hazard insurance policies covering Lessee's personal property and contents in such amounts as Lessee shall desire.

- (d) Lessee shall pay to Lessor any increase in Lessor's insurance policies resulting from Lessee's use or occupancy of the Premises.
- (e) Lessor and Lessee agree that in the event the Premises or any part of the building, or the equipment, contents or other personal property therein, are damaged or destroyed by fire or other casualty that is coverable under a standard fire and extended coverage policy or is covered by the insurance of the Lessor or Lessee, regardless of cause or origin, including negligence, the rights, if any, of any party against the other, or against the employees or agents of any party, with respect to such damage or destruction and with respect to any loss of the parties, are hereby waived; provided, however, that if such damage is insured and if there shall not prohibit a claim against a party for the amount of the deductible.

14. DAMAGE AND DESTRUCTION

- (a) If the Premises or Building, respectively, be damaged by fire or other casualty to such extent that the cost of restoration, as estimated by Lessor, will equal or exceed thirty percent (30%) of the replacement value of the Premises or Building (exclusive of foundation), as the case may be, just prior to the occurrence of the damage, or if any damage shall occur as a result of a fire or other casualty in the last one and one-half (1 1/2) years of the term of this Lease, Lessor may, not later than the ninetieth (90th) day following the damage, terminate this lease by giving Lessee written notice of such election and this Lease shall be deemed to terminate on the third (3rd) day after the giving of said notice. Lessee shall surrender possession of the Premises within ten (1) days thereafter, and the Rent shall be apportioned as of the date of the damage or destruction.
- (b) If this Lease shall not be terminated in accordance with the rights granted herein, Lessor shall, following receipt of their insurance proceeds, restore the Premises to its condition immediately preceding said damage to the extent possible, within one hundred twenty (120) days from the date of such damage or destruction, subject to delays beyond Lessor's reasonable control; and Lessee shall have no right to terminate this Lease; provided, however, that if Lessor shall not substantially complete the repair or restoration of the Premises within one hundred twenty (120) days following the date of such damage or destruction, so that the Premises are ready for occupancy, then, Lessee as its sole remedy, shall have the right to terminate this Lease by delivering written notice to Lessor within one hundred thirty (130) days following the date of such damage or destruction.

Lessee, not Lessor, shall restore fixtures, equipment, furniture and other personal property owned by Lessee. In the event that Lessee shall be unable to use any space in the Premises as a result of a fire or other casualty, until demised premises are a fully repaired and ready for occupancy, the Base Rent shall be abated on a per diem basis, pro-rata for the portion of the Premises which Lessee is unable to use because of such fire or other casualty.

15. SUBORDINATION

- (a) Lessor reserves the right to subject and subordinate this Lease to all mortgages which may now or hereafter affect the Premises, and to any and all advances made thereunder and all renewals, modifications, consolidations, replacements and extensions thereof. Lessee covenants and agrees to executed within fifteen (15) days after receipt of request therefor and instrument Lessor or its lenders may request in confirmation of such subordination provided, however that Lessor shall obtain an agreement of such mortgage providing in substance that so long as Lessee shall be in default under this Lease, Lessee's tenancy will not be distributed by any default under such mortgage. Any alleged uncomplicated or defective construction or maintenance work by Lessor shall not be an excuse for failure to execute the subordination agreement. Lessee agrees to attorn to any mortgagee or purchaser in a foreclosure sale as Lessor under this Lease.

16. ASSIGNMENT AND SUBLETTING

Lessee shall not without first obtaining Lessor's written consent:

- (a) Assign, mortgage, hypothecate or convey this Lease or any interest therein voluntarily or by operation of law;
- (b) Sublet the Premises or any part thereof, or
- (c) Permit the use or occupancy of the Premises or any part thereof by anyone other than Lessee.

17. HOLDING OVER

- (a) Should Lessee remain in possession of the Premises after the expiration of the term of this Lease without the written consent of Lessor, then without diminishing in any respect Lessor's other remedies with respect to Lessee's failure to vacate the Premises at the end of the term, Lessee shall be a tenant at sufferance and such tenancy shall

otherwise be subject to all of the covenants and agreements of this lease, at a monthly rental equal to one hundred fifty percent (150%) of the monthly installment of Rent then otherwise payable hereunder; provided, however, that either Lessor or Lessee has the right to terminate the Lease at any time thereafter upon thirty (30) days prior written notice to the other.

18. SURRENDER AT END OF TERM

- (a) Upon the expiration or earlier termination of the term hereof Lessee shall surrender the Premises together with all installations, improvements and permanent alterations therein (other than Lessee's furniture, trade fixtures, furnishings, business office machines and equipment which shall remain Lessee's property and shall be removed by Lessee) in as good condition and repair on the date Rent is first payable, reasonable use and wear and loss or damage by fire or other casualty excepted.
- (b) Lessee shall repair at Lessee's expense any damage to the Premises or Building caused by the removal of any property or items from the Premises and Building and any of the same not so removed or removed and not properly repaired, may be removed and/or repaired by Lessor, and Lessee agrees to pay the cost thereof and to indemnify Lessor and hold Lessor harmless therefrom. If Lessee shall not remove any of its personal property at the end of the term, Lessor may treat such property as abandoned by Lessee and such property shall belong absolutely to Lessor.

Notwithstanding anything in this Lease to the contrary, all portions of the heating, air conditioning, plumbing, electrical and mechanical systems and equipment, all wall and floor covering and all light fixtures shall not be removed by lessee and shall remain in the Premises and belong to Lessor.

19. LESSOR'S REMEDIES UPON DEFAULT

- (a) Lessee covenants and agrees that if:
  - (i) Lessee shall fail, neglect or refuse to pay in full any installment of Rent or other moneys agreed by it to be paid under the term of this Lease, and if any such default shall continue for a period of fifteen (15) days from the date such installment or payment was due; or
  - (ii) Any voluntary or involuntary petition or similar pleading under the United States Bankruptcy Code as now hereafter amended shall be filed by or against Lessee, or any voluntary or involuntary proceeding in any court shall be

instituted to declare Lessee insolvent or unable to pay Lessee's debts, and any involuntary filing shall not be Lessee's debts, and any involuntary filing shall not be dismissed or discharged within sixty (60) days thereafter; or

- (iii) Lessee makes an assignment of its property for the benefit of creditors or if the Premises be taken under a levy of execution or attachment in any action against Lessee and such levy, attachment or assignment is not dismissed or discharged within thirty (30) days; or
  - (iv) Lessee shall fail to perform any covenant or provisions of this Lease for a period of fifteen (15) days after the giving of notice thereof in writing by Lessor (but Lessee shall not be deemed in default of any provisions for the making of repairs within said fifteen (15) day period and proceeds therewith with due diligence). Provided however, that Lessee shall not be in default if it continues to pay rent, notwithstanding the fact that Lessee has abandoned the Premises, as long as Lessee gives Lessor thirty (30) days written notice to all other remedies given to Lessor in law or in equity, may be written notice terminate this Lease, or without terminating this Lease or without notice, re-enter the Premises immediately, and by force if necessary, and to remove all persons and their property therefrom, using such force in effecting such removal as may be necessary and advisable to recover possession of the Premises whether possession be in Lessee or a third (3rd) person, without being deemed guilty of any manner or trespass.
- (b) In the event of re-entry by Lessor and/or termination of this Lease, Lessor may, without being obligated to do so, relet the whole or any portion thereof with additional space, for any period equal to, greater or less than the remainder of the term of this Lease, for any sum (including any rental concessions and rent-free occupancy) which it may deem suitable and satisfactory, and for any use and purpose which it may deem appropriate.
- (c) As part of Lessor's damage for Lessee's default, Lessor shall be entitled to receive all of Lessor's expenses, including without limitation, commissions and the cost of repairs, as well as Rent or damages equal to the Rent and all other sums due from Lessee at such time and for the remainder of the term of this lease.

Any amounts Lessor receives from any new occupant shall be applied to the foregoing damage, Lessee remaining liable for any deficiency.

- (d) No termination of this Lease nor any taking or recovering of possession of the Premises shall deprive Lessor of any of its remedies or actions against Lessee or shall relieve Lessee from its liability for Rent and damages hereunder. The failure of Lessor to relet, or if relet, to collect the Rent under such reletting shall not release or affect Lessee's liability for damages hereunder. All remedies available to Lessor are declared to be cumulative and concurrent.

20. NOTICES

- (a) Any notices required to be served upon Lessee shall be deemed sufficiently given if in writing, mailed by registered or certified, postage prepaid and addressed to Lessee at the address indicated on the first page of this Lease, or at the Premises, and the time of giving or making such notice or demand shall be deemed to be the time when the same is mailed as herein provided. Any notice by Lessee to Lessor may be in writing sent by registered or certified mail, postage prepaid, addressed to Lessor at 30300 Bruce Industrial Parkway, Solon, Ohio 44139. Lessee and/or Lessor may change their address by giving notice to the other party as provided herein.
- (b) No delay on the part of Lessor in exercising any right, power or privilege hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power or privilege preclude an other, or further exercise thereof or the exercise of any other right, power or privilege.
- (c) Any acceptance or surrender, waiver or release by Lessor and any cancellation, termination or modification of this lease must be in writing signed by Lessor's satisfaction, and Lessor may accept the same without prejudice to Lessor's right to recover any balance due to pursue any other remedy in this Lease provided.

21. NO WAIVER

- (a) No receipt of money by Lessor from Lessee with knowledge of the breach of any covenants of this Lease, or after the termination hereof, or after the commencement of any suit, or after judgment for possession of the premises shall be deemed a waiver of such breach, nor shall its reinstate, continue or extend the term of this Lease or affect any such notice, demand, suit or judgment.
- (b) No delay on the part of Lessor in exercising any right, power or privilege hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power or privilege preclude any other, or further exercise thereof or the exercise of any other right, power or privilege.

- (c) Any acceptance or surrender, waiver or release by Lessor and any cancellation, termination or modification of this Lease must be in writing signed by Lessor's satisfaction, and Lessor may accept the same without prejudice to Lessor's right to recover any balance due to pursue any other remedy in this Lease provided.

22. BROKER

- (a) Lessee represents and warrants to Lessor that no real estate broker, agent or finder was involved in making, negotiating or consummating this Lease.

23. TRANSFER OF LESSOR'S INTERESTS; LIABILITY OF LESSOR

- (a) If Lessor should sell or otherwise transfer Lessor's interest in the Building, Lessor shall thereafter have no liability to Lessee under this Lease or any modification or amendment thereof or extensions or renewals thereof, except for such liabilities which might have accrued prior to the date of such sale or transfer of Lessor's interest.
- (b) If Lessor shall fail to perform any covenant, term or condition of this Lease upon Lessor's part to be performed or if Lessee shall have any claim against Lessor arising out of arty provision of this Lease, statute or common law, and as a consequence of such default or claim Lessee shall recover a money judgment against Lessor, such judgment shall be satisfied only out of the proceeds received at a judicial sale upon the execution and levy against the right, title and interest of Lessor in the Building, and in the rents or other income from such property receivable by Lessor. Lessor shall have no personal or individual liability under this Lease.

24. SECURITY DEPOSIT

- (a) Lessee has or will deposit with Lessor the sum of \$0.00 as security for the faithful performance and observance by Lessee, of the terms, provisions and conditions of this lease; it is agreed that in the event Lessee defaults in respect of any of the terms provisions, and conditions of this lease, including, but not limited to, the payment of rent and additional rent, Lessor may use, apply or retain the whole or any part of the security so deposited to the extent required for the payment of any rent and additional rent, or any other sum as to which Lessee is in default or for any sum which Lessor may extend or may be required to extend the reason of Lessee's default in respect to any of the terms, covenants and conditions of this lease, including but not limited to, any damages or deficiencies in the reletting of this Premises whether such damages or deficiencies accrue before or after summary proceedings or other re-entry by



Lessor. In the event that Lessee shall fully and faithfully comply with all of the terms, provisions, covenants and conditions of this Lease, the security shall be returned to Lessee after the date fixed as the end of the Lease and after delivery of entire possessions of demised Premises to Lessor. Lessee further covenants that it will not assign or encumber or attempt to assign or encumber the moneys deposited herein as security, and neither Lessor nor its successor assigned shall be bound by any such assignment, encumbrance, attempted assignment or attempted encumbrance.

25. OWNERSHIP OR ALTERATION

- (a) All installations, alternations, improvements or addition to the Premises (other than Lessee's personal property) made by Lessor or Lessee shall become the Lessor's property upon installation and shall remain in or upon the Premises upon termination.

26. MISCELLANEOUS

- (a) The holding of any court that any provision of this Lease is invalid or unenforceable shall not affect the remaining provisions of the Lease which shall remain in full force and effect. This Lease contains the entire agreement of the parties and shall not be modified in any manner except by an instrument in writing signed by the parties or their respective successors in interest. Time is expressly declared to be of the essence for all provisions of this Lease. The paragraph headings of this Lease are for convenience only and shall not be used in the interpretation of any of its provisions. This Lease shall not be recorded, but either party shall execute at the request of the other an instrument in recordable form setting forth the names of the parties and the terms of this Lease. If more than one person shall execute this Lease as Lessee, then each person executing this Lease shall jointly and severally be liable hereunder.

27. RULES AND REGULATIONS

- (a) Lessee and Lessee's servants, employees, agents, visitors and licensees shall observe faithfully, and comply strictly with any Rules and Regulations as Lessor or Lessor's agents may from time to time adopt. Notice of any additional Rules or Regulations shall be given in such manner as Lessor may elect.

28. AUTHORITY TO EXECUTE LEASE

- (a) If Lessee is a corporation, each person(s) signing this Lease as an officer represents to the Lessor that such person(s) is authorized to execute this Lease without the necessity of obtaining any other signatures from any other officers, that the execution of this Lease has been authorized by the Board of Directors of the corporation, and that this lease is fully binding upon the Lessee.

IN WITNESS WHEREOF, the parties hereto have set their hands to counterparts, each of which shall have the same force and effect as if it were an original, this APRIL 2, 1995, as to Lessor, and this APRIL 2, 1995, as to Lessee.

ACKNOWLEDGMENT

Signed in the presence of: "Lessor"

/S/ LINDA KONTUR

By: \_\_\_\_\_  
Tech Heating and Air Conditioning, Inc.  
"Lessee"

By: /S/ BOB COOK  
Bob Cook

STATE OF OHIO                    ss.  
COUNTY OF CUYAHOGA        ss.     SS:

The foregoing instrument was acknowledged before me, a Notary Public on this 2nd day of April, 1995 by Bob Cook.

(SEAL)

/S/ MARIA SZENTE  
Notary Public  
Maria A. Szente

STATE OF OHIO                    ss.  
COUNTY OF CUYAHOGA        ss.     SS:

The foregoing instrument was acknowledged before me, a Notary Public on this 2nd day of April, 1995 by Bob Cook, President of Tech, Inc., an Ohio corporation, on behalf of said corporation and by Bob Cook, individually.

(SEAL)

/S/ MARIA SZENTE  
Notary Public  
Maria A. Szente

THIS INSTRUMENT PREPARED BY:  
Howard S. Chapman  
Attorney at Law  
25250 Rockside Road  
Bedford Heights, Ohio 44146  
(216) 439-3400



## CREDIT AGREEMENT

\$75,000,000.00 REVOLVING CREDIT LOAN

AMONG

COMFORT SYSTEMS USA, INC.  
AS THE COMPANY,THE SUBSIDIARIES OF THE COMPANY  
LISTED AS GUARANTORS HEREIN

AND

BANK ONE, TEXAS, N.A.,  
AS THE AGENT

AND

THE BANKS NAMED HEREIN

DATED AS OF JULY 2, 1997

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CREDIT AGREEMENT

This CREDIT AGREEMENT dated as of July 2, 1997 (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, TEXAS, N.A., individually as a Bank ("BOT") and as agent for the other Banks (in such capacity together with any other Person who becomes the agent, the "AGENT").

The Company has requested that the Banks provide the Company with a revolving credit facility, pursuant to which the Banks will commit to make loans of up to \$75,000,000.00 including a letter of credit facility not to exceed \$5,000,000.00 to the Company for general corporate purposes, including working capital, financing permitted acquisitions and the issuance of letters of credit.

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

ARTICLE I  
DEFINITIONS; ACCOUNTING TERMS; INTERPRETATION

SECTION 1.01. DEFINITIONS. As used in this Agreement, the following terms shall have the following meanings:

"ADMINISTRATIVE QUESTIONNAIRE" means the questionnaire attached hereto as EXHIBIT 1.01(A) to be completed by each Bank and returned to the 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.

"AGENT" 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 BOT most recently announced by BOT 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 Agent from three federal funds brokers of recognized standing selected by it. If, for any reason, the 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 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.

"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.

"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.

"BANKRUPTCY CODE" has the meaning specified in SECTION 10.01(E).

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

"BOT" means Bank One, Texas, N.A., 910 Travis, 7th Floor, Houston, Texas 77002.

"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.

"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 and all other duties and obligations of the Banks hereunder.

"COMMITMENT FEE" has the meaning specified in SECTION 4.01(A).

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

"CONSOLIDATED TANGIBLE NET WORTH" means, at any date, an amount equal to the consolidated stockholders' equity of the Company and its subsidiaries LESS intangibles of such Persons determined in accordance with GAAP as of such date.

"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.

"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%), and (b) Eurodollar Rate Advances, the rate per annum which would otherwise be applicable plus three percent (3%).

"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.

"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), plus depreciation and amortization, provided, the calculations of EBITDA after the acquisition of assets or entities permitted under Section 7.05(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.

"EFFECTIVE DATE" means the date on which all conditions to make an Advance set forth in SECTION 5.01 are first met or waived in accordance with SECTION 12.01 hereof.

"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 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.

"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 Agent by prime banks in whatever Eurodollar interbank market may be selected by the 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 10.01.

"EXECUTION DATE" means the date upon which this Agreement shall have been executed by the Company, the Guarantors, the Banks, and the Agent.

"FEDERAL FUNDS EFFECTIVE RATE" has the meaning specified in the definition of the term "ALTERNATE BASE RATE."

"FEES" has the meaning specified in SECTION 4.01.

"FINANCIALS" has the meaning specified in SECTION 6.07.

"FUNDED DEBT" means all indebtedness for borrowed money evidenced by a written document and subject to periodic, 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 9.01.

"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 or (e) 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 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 (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 of, indebtedness or obligations of another Person of the kinds referred to in clauses (a) through (d) above.

"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.

"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.

"ISSUING BANK" means, for each Letter of Credit, BOT.

"LETTER OF CREDIT" has the meaning specified in SECTION 3.01(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 Funded Debt to EBITDA ratio:

FUNDED DEBT/EBITDA RATIO	LETTER OF CREDIT FEE
-----	-----
(less than) 1.00	.875%
(greater than or equal to) 1 but (less than) 1.50	1.125%
(greater than or equal to) 1.50 but (less than) 2.00	1.375%
(greater than or equal to) 2.00 but (less than) 2.50	1.875%

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 3.03(C).

"LETTER OF CREDIT REQUEST" has the meaning specified in SECTION 3.02(A).

"LIEN" means, when used with respect to any Person, any mortgage, lien, charge, pledge, security interest 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 2.01.



"LOAN DOCUMENTS" means this Agreement and the other documents described in ARTICLE V hereof, the Notes, the Notice of Advance, and the corporate resolutions authorizing the Loan Documents.

"MAJORITY BANKS" means Banks holding at least 51% 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 Funded Debt to EBITDA ratio:

FUNDED DEBT/ EBITDA RATIO	EURODOLLAR RATE ADVANCE	ALTERNATE BASE RATE ADVANCE
(less than) 1.00	1.00%	0.00%
(greater than or equal to) 1 but (less than) 1.50	1.25%	0.00%
(greater than or equal to) 1.50 but (less than) 2.00	1.50%	0.00%
(greater than or equal to) 2.00 but (less than) 2.50	2.00%	0.25%

If sufficient information does not exist to calculate the Margin, Eurodollar Rate Advances shall not be available to the Company and the Margin for Alternate Base Rate Advances shall be deemed to be 0%.

"MARGIN PERIOD" means (a) the period from the Effective Date through the date that the first quarterly financial statements are delivered pursuant to Section 7.01(a) and (b) thereafter, 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 7.01(A) or SECTION 7.01(B), as the case may be, 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 financial condition, business or operations of the Company individually or the Company and its Subsidiaries taken as a whole or (b) a material impairment of the collective ability of the Company and its Subsidiaries to make payment hereunder or under any Note or the right of any Bank to enforce any of its remedies to collect any amounts owing under the Loan Documents.

"MATURITY DATE" means a date which is three years after the Execution Date.

"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).

"NOTE" has the meaning specified in SECTION 2.02.

"NOTE" and "NOTES" have the meaning specified in SECTION 2.02.

"NOTICE OF ADVANCE" has the meaning provided in SECTION 2.03(A).

"NOTICE OF CONVERSION" has the meaning provided in SECTION 2.05.

"NOTICE OF DEFAULT" has the meaning specified in SECTION 10.02.

"OBLIGATIONS" means all the obligations of the Company 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 11.03.

"OTHER FINANCINGS" has the meaning specified in SECTION 11.03.

"PAYMENT OFFICE" means the office of the Agent located at 1111 Fannin Street, Houston, Texas 77002, or such other office as the 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 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; (h) inchoate Liens arising under ERISA to secure contingent liabilities of the Company and its Subsidiaries; and (i) Liens on assets of Subsidiaries to secure indebtedness to the Company provided same are collaterally assigned to the Agent, provided further, such Liens may be incurred only to the extent the underlying Indebtedness is otherwise permitted under the terms of this Agreement.

"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.

"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 Agent to make payments hereunder for the account of such Bank free of deduction or withholding of income and other taxes.

"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.

"REGULATIONS A, D, G, T, U AND X" means Regulations A, D, G, T, U and X of the Board as the same are from time to time in effect, and all official rulings and interpretations thereunder or thereof.

"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.

"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.

"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.

"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 1.01(B);

"TOTAL COMMITMENT" means the sum of the Commitments for each Bank totaling a maximum of \$75,000,000.00 for all Banks.

"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 1.02. 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 1.03. 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 1.04. 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.

## ARTICLE II THE LOANS

SECTION 2.01. 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 Execution 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 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 Total Commitment, (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, in the aggregate at any time outstanding and together with all Letter of Credit Obligations, not exceed the Total Commitment. There shall be no further Advances after the Maturity Date.

SECTION 2.02. 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 2.02(A).

SECTION 2.03. 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 Agent (i) in the case of an Alternate Base Rate Advance, not later than 10:00 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 2.03

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 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 2.04. 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 Agent shall credit the amounts so received to the general deposit account of the Company maintained with the Agent in immediately available funds or as otherwise directed by the Company.

(b) Unless the Agent shall have been notified by any Bank prior to disbursement of the Advance by the Agent that such Bank does not intend to make available to the Agent such Bank's portion of the Advance to be made on such date, the Agent may assume that such Bank has made such amount available to the Agent on such Advance Date and the 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 Agent by such Bank and the Agent has made available same to the Company, the 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 Agent's demand therefor, the Agent shall promptly notify the Company, and the Company shall pay such corresponding amount to the Agent within two (2) Business Days after demand therefor. The 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 Agent to the Company to the date such corresponding amount is recovered by the Agent, at a rate per annum equal to 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 2.05. 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. 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 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 Agent written notice (each a "NOTICE OF CONVERSION"), substantially in the form of EXHIBIT 2.05

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 10:00 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 Agent shall thereafter promptly notify each Bank of such Notice of Conversion.

SECTION 2.06. 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 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 described in SECTIONS 2.10(F), 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 2.07. MANDATORY REPAYMENTS.

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 Total Commitment, in the amount of such excess. 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.

SECTION 2.08. 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 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 2.09. 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 2.08, 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 12.08, 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 12.08, 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 on each Designated Payment Date during any Interest Period in excess of three (3) months 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 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 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 Agent to so notify the Company shall not reduce the Company's liability for the amount owed.

(f) The Company shall pay to the 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 Agent on the dates and at the times specified in SECTION 2.03 or SECTION 2.05, 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 2.05); 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 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 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 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 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 of 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 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).

(c) Each Bank will notify the Company through the 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 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 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 12.08, 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 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 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 Agent, each such Bank shall provide the Agent and the Company with the Prescribed Forms. Unless the Company and the Agent have received such Prescribed Forms, the 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 Agent or unless otherwise required by law, make all payments in full to the Agent without deducting any withholding or similar taxes.

ARTICLE III  
LETTERS OF CREDIT

SECTION 3.01. 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 letters of credit (the "LETTERS OF CREDIT"), up to a maximum amount outstanding at any one time for all Letters of Credit of \$5,000,000.00, 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 Total Commitment or (ii) the expiry date or, in the case of any Letter of Credit containing an expiry date that is extendible 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 Revolving Credit Maturity Date) if any of the conditions precedent to such renewal set forth in SECTION 5.02 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 the Maturity Date.

SECTION 3.02. 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 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 3.02 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 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 3.01, shall not be in an amount greater than is permitted under clause (i) of SECTION 3.01(A) and shall be in such form as may be reasonably approved from time to time by the Issuing Bank and the Company.

(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 Agent and the 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.

SECTION 3.03. 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 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 Agent, which shall promptly notify each Bank thereof. Each Bank shall immediately pay to the 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 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 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 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 11.05(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 SUCH PERSON'S SOLE OR CONTRIBUTORY NEGLIGENCE, BUT NOT FROM THE GROSS NEGLIGENCE OR WILLFUL MISCONDUCT OF SUCH PERSON. 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) and, to the extent not inconsistent therewith, the Uniform Commercial Code of the State of Texas, shall not result in any liability of the Issuing Bank to the Company.



SECTION 3.04. INCREASED COSTS. (a) Notwithstanding any other provision herein, but subject to SECTION 12.08, if any Bank shall have determined in good faith that any change after the Execution Date of any law, rule, regulation or guideline or the application or effectiveness of any applicable law or regulation or any change after the Execution 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 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 Agent of any event occurring after the date of this Agreement which will entitle such Bank to compensation pursuant to subsection (a) above, as promptly as practicable. A certificate of such Lender (i) stating that the compensation sought to be recovered pursuant to this SECTION 3.04 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 subsection (a) above may be delivered to the Company (with a copy to the Agent) and shall be conclusive absent manifest error. The Company shall pay to the 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 3.04(B), such Bank shall only be entitled to recover compensation for such events occurring over a period of 120 days.

(c) Except as expressly provided in SECTION 3.04(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 3.05. 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 4.01. FEES. Subject to SECTION 12.08 hereof, the Company agrees to pay the following fees (the "FEES"):

(a) The Company agrees to pay to the Agent for the ratable account of the Banks a Commitment fee (the "COMMITMENT FEE") for the period from and including the Execution Date to the Maturity Date, respectively, 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 Execution Date and on the Maturity Date.

FUNDED DEBT/ EBITDA RATIO -----	COMMITMENT FEE -----
(less than) 1.00	12.5 basis points
(greater than or equal to) 1 but (less than) 1.50	25.0 basis points
(greater than or equal to) 1.50 but (less than) 2.00	25.0 basis points
(greater than or equal to) 2.00 but (less than) 2.50	37.5 basis points

(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 that one certain Fee Letter among the Company, the Agent, BOT and Bank One Capital Markets dated May 13, 1997 and executed by the Company on May 16, 1997.

ARTICLE V  
CONDITIONS PRECEDENT

SECTION 5.01. CONDITIONS PRECEDENT TO THE INITIAL ADVANCE. The obligation of each Bank to make its initial Advance to the Company is subject to the occurrence of or receipt by the Agent of the following, all in form and substance satisfactory to the Agent, and, where relevant, executed by all appropriate parties:

(a) this Agreement (which includes the Guaranty);

(b) one Note for each Bank;

(c) a Notice of Advance with respect to the initial Advance meeting the requirements of SECTION 2.03(A);

(d) a certificate of an officer and of the secretary or an assistant secretary of the Company certifying, (i) true and complete copies of each of the articles or certificate of incorporation, as amended and in effect of the Company and each of the Guarantors, the bylaws, as amended and in effect, of the Company and each of the Guarantors and 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, (ii) the incumbency and specimen signatures of the officers of the Company and each of its Subsidiaries executing any documents on its behalf and (iii) that there has been no change in the businesses or financial condition of the Company which could reasonably be expected to have a Material Adverse Effect since December 31, 1996.

(e) a favorable, signed opinion addressed to the Agent and the Banks from Bracewell & Patterson, L.L.P., counsel to the Company and the Guarantors;

(f) the payment to the Agent and the Banks of all Fees owing on the Execution Date and all reasonable fees and expenses (including the reasonable fees and disbursements of Andrews & Kurth L.L.P.) agreed upon by such parties to be paid on the Execution Date;

(g) 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) The consummation of the initial public offering of the stock of the Company pursuant to the S-1 Registration Statement filed with the Securities and Exchange Commission on March 26, 1997, as amended, at a minimum share price of \$8.00 per share with gross proceeds of at least \$48,800,000.

The acceptance of the benefits of the initial Credit Event shall constitute a representation and warranty by the Company to the 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.

SECTION 5.02. CONDITIONS PRECEDENT TO ALL CREDIT EVENTS. The obligation of the Banks to make any Advance is, including, without limitation, the initial Advance, subject to the further conditions precedent that on the date of such Credit Event:

(a) The representations and warranties set forth in ARTICLE VI 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 Advance (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 Agent and the Banks that such representations and warranties are true and correct in all material respects by submitting a Notice of Advance.

(b) The Company shall have complied with the provisions of SECTION 2.03 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 7.01.

(e) The Agent shall have received such other approvals or documents as the 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 Agent and each of the Banks that all of the conditions specified in this Section above exist as of that time.

SECTION 5.03. 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 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 Agent and the Banks:

SECTION 6.01. 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 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 6.02. 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 6.03. 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 6.04. 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. All agreements of the Company relating to the lending of money or the issuance of letters of credit by any party in existence on the Execution Date are described hereto on SCHEDULE 6.04. 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 6.05. 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 6.06. 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 except those listed on SCHEDULE 6.06 hereof.

SECTION 6.07. FINANCIAL STATEMENTS. Prior to the Execution Date, the Company has furnished to the Banks its audited consolidated balance sheet, audited consolidated income statement and statement of cash flows for the twelve (12) months ended December 31, 1996 (such financials, 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 Execution Date, no Material Adverse Effect has occurred since December 31, 1996.

SECTION 6.08. 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 6.09. 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 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 and to finance acquisitions permitted hereunder.

(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.

SECTION 6.16. SUBSIDIARIES AND ASSETS. The Subsidiaries listed on SCHEDULE 6.16 are all of the Subsidiaries of the Company as of the Execution Date and the address given for such Guarantors is the correct mailing address as of the Execution Date.

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 have at such time (a) capital sufficient to carry on their businesses and transactions and (b) assets, the fair market value of which exceeds their consolidated liabilities (as reflected on the Financials or on the financial statements most recently delivered to the Banks).

#### 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 Notes have been paid in full and the Commitments have terminated:

SECTION 7.01. 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 month, and within forty-five (45) days after the close of each fiscal quarter, the



consolidated and consolidating balance sheet of the Company and its Subsidiaries as of the end of such period and the related consolidated and consolidating 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 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.

(b) As soon as available, and in any event within one hundred twenty (120) days after the close of each fiscal year of the Company, the audited consolidated and the unaudited consolidating balance sheets of the Company and its Subsidiaries as at the end of such fiscal year and the related consolidated and consolidating 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.

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

(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 7.07;

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 SECTIONS 7.01(A) and 7.01(B), a compliance certificate of a Responsible Officer in the form attached hereto as EXHIBIT 7.01(D) 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 whether the Company was in compliance with the provisions of SECTIONS 8.10 through 8.14 as at the end of such fiscal period or year, as the case may be.

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

(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 Agent or any Bank through the Agent may reasonably request.

SECTION 7.02. 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 Agent or such Bank may reasonably request. Such inspections 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.

SECTION 7.03. 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 Agent a listing of all such insurance and such other certificates and other evidence thereof, on or prior to the Execution Date hereof and annually thereafter.

(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 7.04. 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.

SECTION 7.05. 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, the rights and franchises of each of the Company and its Subsidiaries.

SECTION 7.06. 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 7.07. 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 7.08. ADDITIONAL SUBSIDIARIES. The Company will cause any Person that becomes a Subsidiary subsequent to the Execution Date, within ten (10) Business Days after becoming a Subsidiary, to execute a Guaranty or a counterpart of this Agreement and deliver same to the Agent, PROVIDED if said Subsidiary is not incorporated under the laws of the United States or one of its states or territories, no such guaranty will be required if the Company makes arrangements, satisfactory to the Agent, in its sole discretion, regarding restrictions on transfer of funds or other assets by the Company or any Subsidiary to said new foreign Subsidiary.

SECTION 7.09. PAYMENT OF CERTAIN INDEBTEDNESS. The Company shall (a) repay in full all of the Indebtedness described on Schedule 8.03(b)(ii) and (b) obtain, and where applicable record in all appropriate locations, releases of liens for all real and personal property securing same, in each case on or before September 1, 1997.

#### 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 Commitments have terminated:

SECTION 8.01. 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 Execution Date.

SECTION 8.02. CONSOLIDATION, MERGER OR SALE OF ASSETS. Except as previously disclosed to the Agent, 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 sell or otherwise dispose of all or any substantial part of their property or assets (other than sales of inventory and surplus or obsolete assets in the ordinary course of business provided that any disposal does not prejudice the Banks in any way), including the capital stock of any Subsidiary, except for (a) mergers permitted under SECTION 8.05(D), (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 and (c) mergers by a wholly-owned Subsidiary of the Company with another Person in connection with an investment permitted under SECTION 8.05(D).

SECTION 8.03. 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 Execution Date and described in the Financials or, if not shown, listed on SCHEDULE 8.03(B)(I) and (II) (but subject to SECTION 7.09);

(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 issued 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;

(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 8.05 hereof;

(g) current and deferred taxes;

(h) Other Indebtedness not in excess of \$2,000,000.00 in the aggregate at any time outstanding;

(i) Subordinated Debt incurred by Borrower solely in connection with investments permitted by SECTION 8.05(D);

(j) Indebtedness assumed or acquired in connection with Investments permitted under SECTION 8.05(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; and

(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 subparagraphs (a) through (i) above.

SECTION 8.04. 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 (nor will they covenant with any other Person not to grant such a Lien to the Agent, except:

(a) Liens existing on the Execution Date and listed on SCHEDULE 8.04(A);

(b) Liens securing currently secured Indebtedness permitted under SECTION 8.03(B) or (h) above;

(c) Permitted Liens;

(d) Liens securing Indebtedness permitted under SECTION 8.03(H) AND 8.03(J); and

(e) 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.

SECTION 8.05. 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 8.05(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 8.03(F);

(d) 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 Execution Date, (i) in which the Company or one of its wholly owned Subsidiaries is the surviving entity, (ii) at a time when no Default or Event of Default exists hereunder and (iii) the cash portion of the purchase price for any one such Investment does not exceed \$10,000,000.00;

(e) other Investments not exceeding \$500,000.00 in the aggregate at any one time outstanding;

(f) Investments in the form of stock buybacks allowed under SECTION 8.06; and

(g) Investments in capital stock of wholly-owned Subsidiaries of the Company.

SECTION 8.06. RESTRICTED PAYMENTS. The Company will not pay any dividends 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, except to the extent that the consideration therefor consists solely of shares of stock (including warrants, rights or options relating thereto) of the Company or is approved by the Majority Banks; PROVIDED, the Company may purchase the stock of departing officers and employees upon their departure in a maximum, aggregate amount not to exceed \$500,000.00 in the aggregate or such larger amount at the Agent's written consent.

SECTION 8.07. CHANGE IN ACCOUNTING. The Company will not and will not permit any Subsidiary to, change its method of accounting 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 or (c) changes required by GAAP. The Company shall advise the Agent in writing promptly upon making any material change to the extent same is not disclosed in the financial statements required under SECTION 7.01 hereof. In the event of any such change, the Company, the Banks and the Agent agree to negotiate amendments to SECTIONS 8.10 through 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 8.08. 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 Event of Default to make any voluntary prepayments of principal or interest on any other of the Company's Indebtedness.

SECTION 8.09. 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. CURRENT RATIO. The Company will not permit the ratio of Current Assets to Current Liabilities to be less than 1.25 to 1.0.

SECTION 8.11. FUNDED DEBT TO EBITDA RATIO. The Company will not as of the last day of any fiscal quarter permit the ratio of its total Funded Debt on such day to EBITDA for the four (4) quarters then ended to be greater than 2.5 to 1.0 at any time during the term hereof.

SECTION 8.12. FUNDED DEBT TO CONSOLIDATED TANGIBLE NET WORTH RATIO. The Company will not permit as of the last day of any fiscal quarter the ratio of (a) its total Funded Debt

minus investable cash and Permitted Investments on such day to (b) Consolidated Tangible Net Worth plus Subordinated Debt on such day, to be greater than 1.25 to 1.0 at any time during the term hereof.

SECTION 8.13. CAPITAL EXPENDITURES. The Company will not permit total consolidated capital expenditures (including Capitalized Lease Obligations but exclusive of Investments permitted under SECTION 8.05(D) to be greater than two percent (2%) of gross revenues for any fiscal year during the term hereof.

SECTION 8.14. INTEREST COVERAGE RATIO. The Company will not permit as of the last day of any fiscal quarter the ratio EBITDA less depreciation for the four (4) quarters ended on such day to required cash Interest Expense for such period to be less than 4.0 to 1. This interest coverage ratio shall be calculated on a year to date basis during the initial four quarter period during the term hereof and on a rolling four (4) quarter basis thereafter.

#### ARTICLE IX GUARANTY

SECTION 9.01. 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 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 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 9.02. 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 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 Agent or any Bank; or

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

SECTION 9.03. 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 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 Agent, any Bank or any of their respective properties or (ii) any settlement or compromise of any such claim effected by the 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 Guaranteed Obligations or otherwise; and the Guarantors, jointly and severally, shall be liable to pay the Agent and the Banks, and hereby do indemnify the 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 Agent or any Bank in the defense of any claim made against it that any payment or proceeds received by the 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 9.04. WAIVER OF SUBROGATION. Notwithstanding any payment or payments made by any Guarantor hereunder, or any set-off or application by the Agent or any Bank of any security or of any credits or claims, no Guarantor will assert or exercise any rights of the Agent or any Bank or of such Guarantor against the Company to recover the amount of any payment made by such Guarantor to the 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 Agent or any Bank against the Company, or any security that the 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 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 Agent and the Banks and shall forthwith be paid to the 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 9.05. 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 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 Agent and the Banks and shall forthwith be paid to the Agent to be credited and applied to the Guaranteed Obligations, whether matured or unmatured.

SECTION 9.06. 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 Agent or any Bank institute suit, collection proceedings or take any other action to collect the Guaranteed Obligations, including any requirement that the 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 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 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 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 9.07. 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 10.01. 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

(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 or observe or cause any Subsidiary to fail to perform or observe (i) any duty or covenant contained in ARTICLE VIII of this Agreement or (ii) any other 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; 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 instrument of Indebtedness in excess of \$2,500,000 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, 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; 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 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, which with other outstanding judgments and orders against the Company and its Subsidiaries equal or exceed \$500,000.00 in the aggregate (to the extent not covered by insurance as to which the respective insurer has acknowledged coverage), shall be entered against the Company or any Subsidiary and (i) within 30 days after entry thereof such judgment 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 (ii) any enforcement proceeding shall have been commenced (and not stayed) by any creditor or upon such judgment; or

(h) a Change of Control shall occur.

SECTION 10.02. PRIMARY REMEDIES. In any such event, and at any time after the occurrence of any of the above described events, the 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 10.01(E) or SECTION 10.01(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 the principal of and any accrued and unpaid interest in respect of all Advances, and all 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 Bank's 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.

SECTION 10.03. OTHER REMEDIES. Upon the occurrence and during the continuance of any Event of Default, the 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 AGENT

SECTION 11.01. AUTHORIZATION AND ACTION. Each Bank hereby irrevocably appoints and authorizes the 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 the Agent by the terms hereof, together with such powers as are reasonably incidental thereto. The Agent may perform any of its duties hereunder by or through its agents and employees. The duties of the Agent shall be mechanical and administrative in nature; the Agent shall not 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 the 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), the Agent shall not 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 the Agent shall not be required to take any action which exposes the Agent to 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 11.02. AGENT'S RELIANCE. (a) Neither the Agent 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 THE 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, the Agent: (i) may treat the payee of each Note and the Obligations as the holder thereof until the Agent receives written notice of the assignment or transfer thereof signed by such payee and in form satisfactory to the Agent; (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 11.03. AGENT AND AFFILIATES; BOT 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, BOT and each other Bank who may become the Agent 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 the Agent; and the term "Bank" or "Banks" shall, unless otherwise expressly indicated, include BOT and any such other Bank, in their individual capacities. BOT, each other Person who becomes the Agent and their respective Affiliates may be engaged in, 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 depository 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 the 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 the 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 11.04. BANK CREDIT DECISION. Each Bank acknowledges and agrees that it has, independently and without reliance upon the Agent or any other Bank and based on the financial statements referred to in SECTION 7.01 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 the 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 11.05. AGENT'S INDEMNITY. (a) The Agent shall not 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 the Agent's satisfaction by the Banks against loss, cost, liability and expense. If any indemnity furnished to the Agent 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 Agent (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 the Agent in any way relating to or arising out of this Agreement or any action taken or omitted by the Agent under this Agreement, the Notes and the other Loan Documents. Without limitation of the foregoing, each Bank agrees to reimburse the Agent promptly upon demand for its ratable share of any out-of-pocket expenses (including reasonable counsel fees) incurred by the Agent in connection with the preparation, execution, administration, or enforcement of, or legal advice in respect of rights or responsibilities under, this Agreement, the Notes and the other Loan Documents to the extent that the 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 the Agent for any portion of such liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses or disbursements due to the Agent resulting from the Agent's gross negligence or willful misconduct. EACH BANK AGREES, HOWEVER, THAT IT EXPRESSLY INTENDS, UNDER THIS SECTION, TO INDEMNIFY THE 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 THE AGENT'S SOLE ORDINARY OR CONTRIBUTORY NEGLIGENCE.

SECTION 11.06. SUCCESSOR AGENT. The Agent may resign at any time by giving written notice thereof to the Banks and the Company and may be removed as 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. 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 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 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 Agent under this Agreement, the Notes and the other Loan Documents.

SECTION 11.07. NOTICE OF DEFAULT. The Agent shall not be deemed to have knowledge or notice of the occurrence of any Default or Event of Default hereunder unless the 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 the Agent receives such notice, the Agent shall give notice thereof to the Banks; PROVIDED, HOWEVER, if such notice is received from a Bank, the Agent also shall give notice thereof to the Company. The 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 10.01 and SECTION 10.02.

#### ARTICLE XII MISCELLANEOUS

SECTION 12.01. AMENDMENTS. No amendment or waiver of any provision of this Agreement, any Note or any other Loan Document, nor consent to any departure by the Company herefrom or therefrom, shall in any event be effective unless the same shall be in writing and signed by the Company, as to amendments, and by the Majority Banks in all cases, and then, in any case, such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given PROVIDED, no such amendment shall be effective unless signed by all of the Banks if it attempts to: (a) change the definition of "COMMITMENT", "DESIGNATED PAYMENT DATE", "MAJORITY BANKS", "MARGIN" or "MATURITY DATE"; (b) modify this Section or SECTIONS 4.01 (a) or (b) ; (c) release any Guarantor; (d) to waive any Default under SECTION 10.01(A) or (e), in any other manner change

the repayment terms of the Loans, including required principal payments, the rate, amount or time of interest payments or the reimbursement obligations under any Letter of Credit.

SECTION 12.02. 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.  
4801 Woodway Drive, Suite 300E  
Houston, Texas 77056  
Telephone No.: (713) 964-2685  
Telecopy No: (713) 964-2657  
Attention: J. Gordon Beittenmiller

(b) If to the Agent:

Bank One, Texas, N.A.  
910 Travis, 7th Floor  
Houston, Texas 77002  
Telephone No.: (713) 751-3828  
Telecopy No: (713) 751-6199  
Attention: Mr. H. Gale Smith, Jr.

and to:

Andrews & Kurth L.L.P.  
4200 Texas Commerce Tower  
Houston, Texas 77002  
Telephone No.: (713) 220-4274  
Telecopy No.: (713) 220-4285  
Attention: Mr. Douglas J. Dillon

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 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 Agent pursuant to ARTICLE II shall not be effective until actually received by the 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 12.03. NO WAIVER; REMEDIES. No failure on the part of any Bank or the 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 12.04. COSTS, EXPENSES AND TAXES. The Company agrees to pay on demand: (a) all reasonable out-of-pocket costs and expenses of the 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 Agent with respect thereto and with respect to advising the 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 Agent such as appraisers, environmental consultants, accountants or similar Persons, PROVIDED THAT, prior to any Event of Default hereunder, the 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 the Agent and each assignment of the Notes.

SECTION 12.05. INDEMNITY. (a) The Company shall and hereby does indemnify the 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, and the Company shall reimburse 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 12.06. 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.

SECTION 12.07. 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 Texas 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. The Agent, each Bank and the Company further agree that insofar as the provisions of Article 5069-1.04, of the Revised Civil Statutes of Texas, 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 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 Article 5069-15.01 ET SEQ. do not apply to this Agreement, any Note issued hereunder or the other Loan Documents.

SECTION 12.08. 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 Agent or any Bank, or charged, contracted for, reserved, taken or received by the 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 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 12.09. 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. The Company may not 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 12.04 and the Company shall continue to deal solely and directly with the 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 12.01 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.

(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 and the 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 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 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 Agent (an "ASSIGNMENT AND ACCEPTANCE") and any Note subject to such assignment and (iii) no assignment shall be effective until receipt by the 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 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 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 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.

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.

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 that 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 TEXAS, IN HARRIS COUNTY OR OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF TEXAS 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 12.02 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 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.

(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 CLAUSE (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 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. 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 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.

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.

BORROWER:

COMFORT SYSTEMS USA, INC.

By: \_\_\_\_\_  
J. Gordon Beittenmiller  
Chief Financial Officer

GUARANTORS:

ACCURATE AIR SYSTEMS, INC.  
ATLAS COMFORT SERVICES USA, INC.  
ATLAS AIR CONDITIONING COMPANY  
CONTRACT SERVICE, INC.  
EASTERN HEATING & COOLING, INC.  
EASTERN REFRIGERATION CO., INC.  
FREEWAY HEATING & AIR CONDITIONING, INC.  
LAWRENCE SERVICE, INC.  
QUALITY AIR HEATING & COOLING, INC.  
SEASONAIR, INC.  
S.M. LAWRENCE COMPANY, INC.  
STANDARD HEATING & AIR CONDITIONING COMPANY  
TECH HEATING AND AIR CONDITIONING, INC.  
TECH MECHANICAL, INC.  
TRI-CITY MECHANICAL, INC.  
WESTERN BUILDING SERVICES, INC.

By: \_\_\_\_\_  
J. Gordon Beittenmiller  
Vice President

AMOUNT OF COMMITMENT:

\$75,000,000.00

AGENT/BANK:

BANK ONE, TEXAS, N.A.,  
as Agent and Individually, as a Bank

By: \_\_\_\_\_  
H. Gale Smith, Jr.

BANKS:

AMOUNT OF COMMITMENT:

\$ \_\_\_\_\_

\_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

ADDRESS FOR NOTICE:

AMOUNT OF COMMITMENT:

\$ \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

ADDRESS FOR NOTICE:

## INDEMNITY AGREEMENT

This Indemnity Agreement ("Agreement") is made and entered into by and between Comfort Systems USA, Inc., a Delaware corporation ("Company"), and the individuals listed on ANNEX A to this Agreement (individually, "Indemnitee").

## INTRODUCTION

Indemnitee is a director and/or officer of the Company. The parties desire that the Company provide indemnification (including advancement of expenses) to Indemnitee against any and all liabilities asserted against Indemnitee to the fullest extent permitted by the Delaware General Corporation Law ("Act"), as the Act presently exists and may be expanded from time to time. Based on such premise, and for certain good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereby agree as follows:

1. CONTINUED SERVICE. Indemnitee will serve at the will of the Company or under separate contract, if such exists, as a director and/or officer of the Company for so long as Indemnitee is duly elected and qualified in accordance with the Bylaws of the Company or until Indemnitee tenders his or her resignation to the Company.

2. INDEMNIFICATION. The Company shall indemnify Indemnitee as follows:

2.1. The Company shall indemnify Indemnitee when Indemnitee was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the Company), by reason of the fact that Indemnitee is or was a director, officer, employee or agent of the Company, or is or was serving at the request of the Company as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by Indemnitee in connection with such action, suit or proceeding if Indemnitee acted in good faith and in a manner Indemnitee reasonably believed to be in or not opposed to the best interests of the Company, and, with respect to any criminal action or proceeding, had no reasonable cause to believe that Indemnitee's conduct was unlawful. The termination of any action, suit or proceeding by judgment, order, settlement or conviction or upon a plea of nolo contendere or its equivalent shall not, of itself, create a presumption that Indemnitee did not act in good faith and in a manner which Indemnitee reasonably believed to be in or not opposed to the best interests

of the Company, and, with respect to any criminal action or proceeding, had reasonable cause to believe that Indemnitee's conduct was unlawful.

2.2. The Company shall indemnify Indemnitee when Indemnitee was or is a party or is threatened to be made a party to any threatened, pending or completed action or suit by or in the right of the Company to procure a judgment in its favor by reason of the fact that Indemnitee is or was a director, officer, employee or agent of the Company, or is or was serving at the request of the Company as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise against expenses (including attorneys' fees) actually and reasonably incurred by Indemnitee in connection with the defense or settlement of such action or suit if Indemnitee acted in good faith and in a manner that Indemnitee reasonably believed to be in or not opposed to the best interests of the Company and except that no indemnification pursuant to this Agreement shall be made in respect of any claim, issue or matter as to which Indemnitee shall have been adjudged to be liable to the Company unless and only to the extent that the Court of Chancery or the court in which such action or suit was brought shall determine upon application that, despite the adjudication of liability but in view of all the circumstances of the case, Indemnitee is fairly and reasonably entitled to indemnity for such expenses which the Court of Chancery or such other court shall deem proper.

2.3. Any indemnification under Sections 2.1 and 2.2 (unless ordered by a court) shall be made by the Company only as authorized in the specific case upon a determination, in accordance with the procedures set forth in Section 3, that indemnification of Indemnitee is proper in the circumstances because Indemnitee has met the applicable standard of conduct set forth in such Sections 2.1 and 2.2. Such determination shall be made (1) by the board of directors of the Company by a majority vote of a quorum consisting of directors who were not parties to such action, suit or proceeding, or (2) if such a quorum is not obtainable, or, even if obtainable a quorum of disinterested directors so directs, by independent legal counsel in a written opinion, or (3) by the stockholders of the Company.

2.4. Expenses (including attorneys' fees) incurred by Indemnitee in defending any civil, criminal, administrative, or investigative action, suit or proceeding shall be paid by the Company in advance of the final disposition of such action, suit or proceeding, as authorized in the manner provided in Section 2.3, within 14 days after the receipt by the Company from Indemnitee of a Statement of Undertaking in substantially the form set forth in Exhibit A, in which Indemnitee (1) states that Indemnitee has reasonably incurred actual expenses in defending a civil, criminal, administrative, or investigative action, suit or proceeding and (2) undertakes to repay such amount if it shall ultimately be determined that Indemnitee is not entitled to be indemnified by the Company as authorized in this Section 2.

2.5. The indemnification and advancement of expenses provided by, or granted pursuant to, this Section 2 shall not be deemed exclusive of any other rights to which Indemnitee may be entitled under any bylaw, agreement, vote of stockholders or disinterested directors or otherwise, both as to action in Indemnitee's official capacity and as to action in another capacity while holding such office, shall continue after Indemnitee has ceased to be a director, officer, employee or agent of the Company, and shall inure to the benefit of the heirs, executors and administrators of Indemnitee.

3. DETERMINATION OF RIGHT TO INDEMNIFICATION. For the purpose of making the determination of whether to indemnify Indemnitee in a specific case under Section 2.3, the board of directors of the Company, independent legal counsel or stockholders, as the case may be, shall make the determination in accordance with the following procedures:

3.1. Indemnitee shall submit to the board of directors a Statement of Request for Indemnification in substantially the form set forth in Exhibit B, in which Indemnitee states that Indemnitee has met the applicable standard of conduct set forth in Sections 2.1 and 2.2.

3.2. Indemnitee's submission of a Statement of Request for Indemnification to the board of directors shall create a rebuttable presumption that Indemnitee has met the applicable standard of conduct set forth in Sections 2.1 and 2.2 and, therefore, is entitled to indemnification under Section 2. The board of directors, independent legal counsel or stockholders, as the case may be, shall determine, within 30 days after submission of the Statement of Request for Indemnification, specifically that Indemnitee is so entitled, unless it or they shall possess clear and convincing evidence to rebut the foregoing presumption, which evidence shall be disclosed to Indemnitee with particularity in a sworn written statement signed by all persons who participated in the determination and voted to deny indemnification.

4. MERGER, CONSOLIDATION OR CHANGE IN CONTROL. If the Company is a constituent corporation in a merger or consolidation, whether the Company is the resulting or surviving corporation or is absorbed as a result thereof, or if there is a change in control of the Company, Indemnitee shall stand in the same position under this Agreement with respect to the resulting, surviving or changed corporation as Indemnitee would have with respect to the Company if its separate existence had continued or if there had been no change in the control of the Company.

5. CERTAIN DEFINITIONS. For the purposes of this Agreement, the following terms shall have the indicated meanings and understandings:

5.1. The term "other enterprise" shall include, among others, employee benefit plans and civic, non-profit and charitable organizations, whether or not incorporated.



5.2. The term "fines" shall include any excise taxes assessed on Indemnatee with respect to any employee benefit plan.

5.3. The term "serving at the request of the Company" shall include any service, at the request or with the express or implied authorization of the Company, as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, which service imposes duties on, or involves services by, Indemnatee with respect to such corporation, partnership, joint venture, trust or other enterprise, its participants or beneficiaries. If Indemnatee acted in good faith and in a manner Indemnatee reasonably believed to be in or not opposed to the best interests of such other enterprise, its participants or beneficiaries, Indemnatee shall be deemed to have acted in a manner not opposed to the best interests of the Company.

5.4. The term "change of control" shall include any change in the ownership of a majority of the outstanding voting securities of the Company or in the composition of a majority of the members of the board of directors of the Company.

6. ATTORNEYS' FEES. If Indemnatee institutes any legal action to enforce Indemnatee's rights under this Agreement, or to recover damages for breach of this Agreement, Indemnatee, if Indemnatee prevails in whole or in part, shall be entitled to recover from the Company all fees and expenses (including attorneys' fees) incurred by Indemnatee in connection therewith.

7. DEPOSIT OF FUNDS IN TRUST. If the Company voluntarily decides to dissolve or to file a petition for relief under the applicable bankruptcy, moratorium or similar laws, then not later than 10 days prior to such dissolution or filing, the Company shall deposit in trust for the sole and exclusive benefit of Indemnatee a cash amount equal to all amounts previously authorized to be paid to Indemnatee hereunder, such amounts to be used to discharge the Company's obligations to Indemnatee hereunder. Any amounts in such trust not required for such purpose shall be returned to the Company. This Section 7 shall not apply to the dissolution of the Company in connection with a transaction as to which Section 4 applies.

8. AMENDMENTS TO ACT. This Agreement is intended to provide indemnity to Indemnatee to the fullest extent allowed under Delaware law. Accordingly, to the extent permitted by law, if the Act permits greater indemnity than the indemnity set forth herein, or if any amendment is made to the Act expanding the indemnity permissible under Delaware law, the indemnity obligations contained herein automatically shall be expanded, without the necessity of action on the part of any party, to the extent necessary to provide to Indemnatee the fullest indemnity permissible under Delaware law.

9. MISCELLANEOUS PROVISIONS.

9.1. SURVIVAL. The provisions of this Agreement shall survive the termination of Indemnitee's service as a director or officer of the Company.

9.2. ENTIRE AGREEMENT. This Agreement constitutes the full understanding of the parties and a complete and exclusive statement of the terms and conditions of their agreement relating to the subject matter hereof and supersedes all prior negotiations, understandings and agreements, whether written or oral, between the parties, their affiliates, and their respective principals, shareholders, directors, officers, employees, consultants and agents with respect thereto.

9.3. AMENDMENTS AND WAIVERS. No alteration, modification, amendment, change or waiver of any provision of this Agreement shall be effective or binding on any party hereto unless the same is in writing and is executed by all parties hereto.

9.4. MODIFICATION AND SEVERABILITY. If a court of competent jurisdiction declares that any provision of this Agreement is illegal, invalid or unenforceable, then such provision shall be modified automatically to the extent necessary to make such provision fully legal, valid or enforceable. If such court does not modify any such provision as contemplated herein, but instead declares it to be wholly illegal, invalid or unenforceable, then such provision shall be severed from this Agreement, this Agreement and the rights and obligations of the parties hereto shall be construed as if this Agreement did not contain such severed provision, and this Agreement otherwise shall remain in full force and effect.

9.5. ENFORCEABILITY. This Agreement shall be enforceable by and against the Company, the Indemnitee and their respective executors, legal representatives, administrators, heirs, successors and assignees.

9.6. GOVERNING LAW. This Agreement shall be governed by, construed under, and enforced in accordance with the laws of the State of Delaware without reference to the conflict-of-laws provisions thereof.

9.7. MULTIPLE COUNTERPARTS. This Agreement may be executed by the parties hereto in multiple counterparts, each of which shall be deemed an original for all purposes, and all of which together shall constitute one and the same instrument.

The parties hereto have executed this Agreement to be effective as of \_\_\_\_\_, 1997.

COMPANY:

Comfort Systems USA, Inc.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

INDEMNITEE:

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

ANNEX A

Steven S. Harter  
Robert J. Powers  
Michael Nothum, Jr.  
Robert R. Cook  
Brian S. Atlas  
Thomas J. Beaty  
Fred M. Ferreira  
John C. Phillips  
Samuel M. Lawrence III  
Alfred J. Giardenelli, Jr.  
Charles W. Klapperich  
J. Gordon Beittenmiller  
Reagan S. Busbee  
William George, III  
Larry Martin  
John Mercandante, Jr.

EXHIBIT A

STATEMENT OF UNDERTAKING

STATE OF \_\_\_\_\_ SS.  
   SS.  
COUNTY OF \_\_\_\_\_ SS.

I, \_\_\_\_\_, being first duly sworn, depose and say as follows:

1. This Statement of Undertaking is submitted pursuant to the Indemnity Agreement dated \_\_\_\_\_, between \_\_\_\_\_, a Delaware corporation ("Company"), and me.

2. I am requesting the advancement of certain actual expenses which I have reasonably incurred in defending a civil or criminal action, suit or proceeding by reason of the fact that I am or was a director and/or officer of the Company.

3. I hereby undertake to repay this advancement of expenses if it is ultimately determined that I am not entitled to be indemnified by the Company.

4. I am requesting the advancement of expenses in connection with the following action, suit or proceeding:

I have executed this Statement of Undertaking on .

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Print Name

Subscribed and sworn to before me on \_\_\_\_\_.

\_\_\_\_\_  
Notary Public in and for  
said state and county  
My commission expires: \_\_\_\_\_

EXHIBIT B

STATEMENT OF REQUEST FOR INDEMNIFICATION

STATE OF \_\_\_\_\_ SS.  
  SS.  
COUNTY OF \_\_\_\_\_ SS.

I, \_\_\_\_\_, being first duly sworn, depose and say as follows:

1. This Statement of Request for Indemnification is submitted pursuant to the Indemnity Agreement dated \_\_\_\_\_, between \_\_\_\_\_, a Delaware corporation ("Company"), and me.

2. I am requesting indemnification against expenses (including attorneys' fees) and, with respect to any action not by or in the right of the Company, judgments, fines and amounts paid in settlement, all of which have been actually and reasonably incurred by me in connection with a certain action, suit or proceeding to which I am a party or am threatened to be made a party by reason of the fact that I am or was a director and/or officer of the Company.

3. With respect to all matters related to any such action, suit or proceeding, I acted in good faith and in a manner I reasonably believed to be in or not opposed to the best interests of the Company, and, with respect to any criminal action or proceeding, I had no reason to believe that my conduct was unlawful.

4. I am requesting indemnification in connection with the following suit, action or proceeding:

I have executed this Statement of Request for Indemnification on \_\_\_\_\_.

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Print Name

Subscribed and sworn to before me on \_\_\_\_\_.

\_\_\_\_\_  
Notary Public in and for  
said state and county  
My commission expires: \_\_\_\_\_

## INDEMNITY AGREEMENT

This Indemnity Agreement ("Agreement") is made and entered into by and between Comfort Systems USA, Inc., a Delaware corporation ("Company"), and Notre Capital Ventures II, L.L.C., a Texas limited liability company ("Indemnitee").

## INTRODUCTION

Indemnitee is an organizer and promoter of the Company and has provided, and continues to provide, the Company with valuable expertise in connection with the organization of the Company and the formulation of its strategy regarding the consolidation of the HVAC industry and related matters. In consideration of these services, the Company has agreed to indemnify Indemnitee against any and all liabilities asserted against the Indemnitee or its managers, officers, directors, employees, agents, members, partners and owners (collectively, the "Indemnified Parties") in connection with or as a result of Indemnitee's status as an organizer and/or promoter (as that term is defined in Rule 405 under the Securities Act of 1933, as amended) of the Company. Based on such premise, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereby agree as follows:

1. INDEMNIFICATION. The Company shall indemnify the Indemnified Parties as follows:

1.1. The Company shall indemnify the Indemnified Parties when any of such Indemnified Parties was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil (including under federal and/or state securities laws), criminal, administrative or investigative, by reason of the fact that the Indemnified Parties, or any of them, is or was an organizer and/or promoter of the Company, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by such Indemnified Parties in connection with such action, suit or proceeding.

1.2. Expenses (including attorneys' fees) incurred by the Indemnified Parties, or any of them, in defending any such civil (including under federal and/or state securities laws), criminal, administrative, or investigative action, suit or proceeding shall be paid by the Company in advance of the final disposition of such action, suit or proceeding, within 14 days after the receipt by the Company from the Indemnified Parties, or any of them, of notice in which such Indemnified Party states that it has reasonably incurred actual expenses in defending a civil (including under federal and/or state securities laws), criminal, administrative, or investigative action, suit or proceeding by reason of the fact that such Indemnified Party is or was an organizer and/or promoter of the Company.

1.3. The indemnification and advancement of expenses provided by, or granted pursuant to, this Section 1 shall not be deemed exclusive of any other rights to which the Indemnified Parties may be entitled under any law or agreement, and shall continue after each of the Indemnified Parties has ceased to be an organizer and/or promoter of the Company.

2. ATTORNEYS' FEES. If the Indemnified Parties, or any of them, institute any legal action to enforce their rights under this Agreement, or to recover damages for breach of this Agreement, such Indemnified Parties, if they prevail in whole or in part, shall be entitled to recover from the Company all fees and expenses (including attorneys' fees) incurred by such Indemnified Parties, or any of them, in connection therewith.

3. DEPOSIT OF FUNDS IN TRUST. If the Company voluntarily decides to dissolve or to file a petition for relief under the applicable bankruptcy, moratorium or similar laws, then not later than 10 days prior to such dissolution or filing, the Company shall deposit in trust for the sole and exclusive benefit of the Indemnified Parties a cash amount equal to all amounts previously authorized to be paid to the Indemnified Parties hereunder, such amounts to be used to discharge the Company's obligations to the Indemnified Parties hereunder. Any amounts in such trust not required for such purpose shall be returned to the Company.

4. MERGER, CONSOLIDATION OR CHANGE IN CONTROL. If the Company is a constituent corporation in a merger or consolidation, whether the Company is the resulting or surviving corporation or is absorbed as a result thereof, or if there is a change in control of the Company, The Indemnified Parties shall stand in the same position under this Agreement with respect to the resulting, surviving or changed corporation as the Indemnified Parties would have with respect to the Company if its separate existence had continued or if there had been no change in the control of the Company.

## 5. MISCELLANEOUS PROVISIONS.

5.1. SURVIVAL. The provisions of this Agreement shall survive the termination of any of the Indemnified Parties' status as an organizer and/or promoter of the Company.

5.2. ENTIRE AGREEMENT. This Agreement constitutes the full understanding of the parties and a complete and exclusive statement of the terms and conditions of their agreement relating to the subject matter hereof and supersedes all prior negotiations, understandings and agreements, whether written or oral, between the parties, their affiliates, and their respective principals, shareholders, directors, officers, employees, consultants and agents with respect thereto.

5.3. AMENDMENTS AND WAIVERS. No alteration, modification, amendment, change or waiver of any provision of this Agreement shall be effective or binding on any party hereto unless the same is in writing and is executed by all

parties hereto.

5.4. MODIFICATION AND SEVERABILITY. If a court of competent jurisdiction declares that any provision of this Agreement is illegal, invalid or unenforceable, then such provision shall be modified automatically to the extent necessary to make such provision fully legal, valid or enforceable. If such court does not modify any such provision as contemplated herein, but instead declares it to be wholly illegal, invalid or unenforceable, then such provision shall be severed from this



Agreement, this Agreement and the rights and obligations of the parties hereto shall be construed as if this Agreement did not contain such severed provision, and this Agreement otherwise shall remain in full force and effect.

5.5. ENFORCEABILITY. This Agreement shall be enforceable by and against the Company, the Indemnified Parties and their respective successors and assignees.

5.6. GOVERNING LAW. This Agreement shall be governed by, construed under, and enforce in accordance with the laws of the State of Delaware without reference to the conflict-of-laws provisions thereof.

5.7. MULTIPLE COUNTERPARTS. This Agreement may be executed by the parties hereto in multiple counterparts, each of which shall be deemed an original for all purposes, and all of which together shall constitute one and the same instrument.

The parties hereto have executed this Agreement on June 27, 1997.

COMPANY:

Comfort Systems USA, Inc.

By: /S/ FRED M. FERREIRA  
Name: Fred M. Ferreira  
Title: Chief Executive Officer

INDEMNITEE:

Notre Capital Ventures II, L.L.C.

By: /S/ STEVEN S. HARTER  
Name: Steven S. Harter  
Title: President

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the use of our reports (and to all references to our Firm) included in or made a part of this registration statement.

ARTHUR ANDERSEN LLP

Houston, Texas  
July 28, 1997

