

ROLLINS INC  
Form 10-Q  
October 31, 2007

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM 10 Q**

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

**For the quarterly period ended September 30, 2007**

Commission File Number 1-4422

**ROLLINS, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of incorporation or organization)

**51-0068479**  
(I.R.S. Employer Identification No.)

**2170 Piedmont Road, N.E., Atlanta, Georgia**

(Address of principal executive offices)

**30324**

(Zip Code)

**(404) 888-2000**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer  Accelerated Filer  Non-Accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Rollins, Inc. had 67,464,796 shares of its \$1 par value Common Stock outstanding as of October 15, 2007.

## ROLLINS, INC. AND SUBSIDIARIES

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## ROLLINS, INC. AND SUBSIDIARIES

**PART 1 FINANCIAL INFORMATION**  
**ITEM 1. FINANCIAL STATEMENTS**  
**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**  
**AS OF SEPTEMBER 30, 2007 AND DECEMBER 31, 2006**  
(in thousands)  
(unaudited)

	<i>September 30,</i> <b>2007</b>	<i>December 31,</i> 2006
<b>ASSETS</b>		
Cash and cash equivalents	\$ 81,821	\$ 63,344
Trade receivables, short-term, net of allowance for doubtful accounts of \$6,001 and \$6,132, respectively	61,430	52,693
Materials and supplies	8,244	8,401
Deferred income taxes	16,969	19,435
Other current assets	8,382	7,200
Total Current Assets	176,846	151,073
Equipment and property, net	77,633	72,141
Goodwill	126,577	125,161
Customer contracts	65,641	67,761
Other Intangible Assets	9,167	9,294
Deferred income taxes	12,588	14,069
Trade receivables, long-term, net of allowance for doubtful accounts of \$1,334 and \$1,096, respectively	8,921	8,796
Other assets	6,039	4,880
Total Assets	\$ 483,412	\$ 453,175
<b>LIABILITIES</b>		
Capital leases	\$ 1,240	\$ 498
Accounts payable	22,589	16,309
Accrued insurance	13,277	14,310
Accrued compensation and related liabilities	42,533	47,305
Accrual for termite contracts	7,851	8,526
Other current liabilities	18,776	18,817
Unearned revenue	90,191	79,441
Total current liabilities	196,457	185,206
Capital leases, less current portion	881	124
Accrued insurance, less current portion	25,156	23,635
Accrual for termite contracts, less current portion	11,749	11,675
Accrued pension	6,946	6,946
Long-term accrued liabilities	17,561	14,130
Total Liabilities	258,750	241,716
Commitments and Contingencies		
<b>STOCKHOLDERS' EQUITY</b>		
Preferred stock, without par value; 500,000 authorized, no shares issued		
Common stock, par value \$1 per share; 170,000,000 and 99,500,000 shares authorized, respectively; 67,455,841 and 70,789,118 shares issued, Respectively	67,456	70,789
Treasury stock, par value \$1 per share; 0 and 2,898,074 shares, respectively		(2,898 )
Additional paid-in capital	14,272	11,737
Accumulated other comprehensive loss	(16,216 )	(17,784 )
Retained earnings	159,150	149,615
Total Stockholders' Equity	224,662	211,459
Total Liabilities and Stockholders' Equity	\$ 483,412	\$ 453,175

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



## ROLLINS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME  
 FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006  
 (in thousands except for per share data)  
 (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
<b>REVENUES</b>				
Customer services	\$ 238,116	\$ 227,816	\$ 678,966	\$ 654,225
<b>COSTS AND EXPENSES</b>				
Cost of services provided	123,029	119,206	351,466	345,255
Depreciation and amortization	6,885	6,662	20,482	20,400
Sales, general and administrative	78,154	74,472	221,982	211,340
(Gain)/loss on sales of assets	(17 )	(17 )	(113 )	(15 )
Interest income	(466 )	(332 )	(1,540 )	(968 )
	207,585	199,991	592,277	576,012
<b>INCOME BEFORE INCOME TAXES</b>	<b>30,531</b>	<b>27,825</b>	<b>86,689</b>	<b>78,213</b>
<b>PROVISION FOR INCOME TAXES</b>				
Current	10,710	8,854	30,503	25,799
Deferred	1,056	1,934	3,389	5,144
	11,766	10,788	33,892	30,943
<b>NET INCOME</b>	<b>\$ 18,765</b>	<b>\$ 17,037</b>	<b>\$ 52,797</b>	<b>\$ 47,270</b>
<b>NET INCOME PER SHARE - BASIC</b>	<b>\$ 0.28</b>	<b>\$ 0.25</b>	<b>\$ 0.79</b>	<b>\$ 0.70</b>
<b>NET INCOME PER SHARE - DILUTED</b>	<b>\$ 0.28</b>	<b>\$ 0.25</b>	<b>\$ 0.78</b>	<b>\$ 0.69</b>
Weighted average shares outstanding - basic	66,608	67,068	66,966	67,184
Weighted average shares outstanding - diluted	67,318	68,700	67,687	68,926
<b>DIVIDENDS PAID PER SHARE</b>	<b>\$ 0.0750</b>	<b>\$ 0.0625</b>	<b>\$ 0.2250</b>	<b>\$ 0.1875</b>

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

## ROLLINS, INC. AND SUBSIDIARIES

**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006**  
(in thousands)  
(unaudited)

	<b>Nine Months ended</b>	
	<b>September 30,</b>	
	<b>2007</b>	<b>2006</b>
<b>OPERATING ACTIVITIES</b>		
Net Income	\$52,797	\$47,270
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	20,482	20,400
Provision for deferred income taxes	3,389	5,144
Stock Based Compensation Expense	2,381	-
(Gain)/loss on sales of assets	(113 )	(15 )
Excess tax benefits from share-based payments	(2,924 )	
Other, net	(113 )	3
(Increase)/decrease in assets		
Trade receivables	(8,675 )	(9,747 )
Materials and supplies	276	685
Other current assets	(1,153 )	138
Other non-current assets	(2,593 )	735
Increase/(decrease) in liabilities:		
Accounts payable and accrued expenses	850	3461
Unearned revenue	10,751	8,955
Accrued insurance	488	1,398
Accrual for termite contracts	(600 )	(3,900 )
Accrued pension		(5,000 )
Long-term accrued liabilities	3,295	(6,666 )
Net cash provided by operating activities	78,538	62,861
<b>INVESTING ACTIVITIES</b>		
Purchase of equipment and property	(13,512 )	(15,657 )
Acquisitions/dispositions of companies, net	(5,950 )	(5,050 )
Cash from Sales of Franchises		550
Proceeds from sales of assets	79	20
Net cash used in investing activities	(19,383 )	(20,137 )
<b>FINANCING ACTIVITIES</b>		
Dividends paid	(15,274 )	(12,790 )
Common stock purchased	(30,895 )	(19,452 )
Common stock options exercised	1,379	435
Principal Payments on Capital Lease Obligations	(1,532 )	(566 )
Excess tax benefits from share-based payments	2,924	
Other		(236)
Net cash used in financing activities	(43,398 )	(32,609 )
Effect of exchange rate changes on cash	2,720	607
Net increase in cash and cash equivalents	18,477	10,722
Cash and cash equivalents at beginning of year	63,344	43,065
Cash and cash equivalents at end of year	\$81,821	\$53,787
<b>Supplemental disclosure of cash flow information</b>		
Cash paid for interest	\$85	\$43
Cash paid for income taxes	\$27,541	\$21,338

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



## ROLLINS, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

Rollins, Inc. and Subsidiaries

(unaudited)

(in thousands)	Comprehensive income (loss)	Common stock	Treasury stock	Paid-in- capital	Accumulated other comprehensive income (loss)	Retained Earnings	Total
Balance at December 31, 2006		\$ 70,789	(2,898 )	\$ 11,737	\$ (17,784 )	\$ 149,615	\$ 211,459
Cumulative effect adjustment FIN 48.						(1,676 )	(1,676 )
Net Income	\$ 52,797					52,797	52,797
Pension liability, net of taxes	(1,152 )				(1,152 )		(1,152 )
Foreign currency translation adjustments	2,720				2,720		2,720
Comprehensive income	\$ 54,365						
Dividends declared						(15,274 )	(15,274 )
Common Stock Purchases				(1,205 )		(26,312 )	(27,516 )
Common Stock Retired		(4,103 )	4,103				
Stock-based compensation		220		2,161			2,381
Common stock options exercised		550		(2,550 )			(2,001 )
Excess tax benefits from share-based payments				2,924			2,924
<b>Balance at September 30, 2007</b>		<b>\$ 67,456</b>	<b>\$</b>	<b>\$ 14,272</b>	<b>\$ (16,216 )</b>	<b>\$ 159,150</b>	<b>\$ 224,662</b>

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

ROLLINS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

NOTE 1. BASIS OF PREPARATION AND OTHER

**Basis of Preparation** - The consolidated financial statements included herein have been prepared by Rollins, Inc. (the Company), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission applicable to quarterly reporting on Form 10-Q. These consolidated financial statements have been prepared in accordance with Statement of Financial Accounting Standard No. 94, *Consolidation of All Majority-Owned Subsidiaries* (SFAS 94) and Rule 3A-02(a) of Regulation S-X. In accordance with SFAS 94 and Rule 3A-02(a) of Regulation S-X, the Company's policy is to consolidate all subsidiaries and investees where it has voting control. The Company does not have any subsidiaries or investees where it has less than a 100% equity interest or less than 100% voting control, nor does it have any interest in other investees, joint ventures, or other variable interest entities that require consolidation under FASB interpretation No. 46, *Consolidation of Variable Interest Entities* (FIN 46R).

Footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted as permitted by such rules and regulations. These consolidated financial statements should be read in conjunction with the financial statements and related notes contained in the Company's annual report on Form 10-K for the year ended December 31, 2006.

In the opinion of management, the consolidated financial statements included herein contain all adjustments necessary to present fairly the financial position of the Company as of September 30, 2007 and December 31, 2006, the results of its operations for the three and nine months ended September 30, 2007 and 2006 and cash flows for the nine months ended September 30, 2007 and 2006. All such adjustments are of a normal recurring nature. Operating results for the nine months ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007.

The Company has only one reportable segment, its pest and termite control business. The Company's results of operations and its financial condition are not reliant upon any single customer or a few customers or the Company's foreign operations.

**Estimates Used in the Preparation of Consolidated Financial Statements** - The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the accompanying notes and financial statements. Actual results could differ from those estimates.

**Cash and Cash Equivalents** - The Company considers all investments with an original or purchased maturity of three months or less to be cash equivalents. Short-term investments, all of which are cash equivalents, are stated at cost, which approximates fair market value.

**Goodwill and Other Intangible Assets** - In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, the Company classifies intangible assets into three categories: (1) intangible assets with definite lives subject to amortization; (2) intangible assets with indefinite lives not subject to amortization; and (3) goodwill. The Company does not amortize intangible assets with indefinite lives and goodwill. Goodwill and other intangible assets with indefinite useful lives are tested for impairment annually or more frequently if events or circumstances indicate the assets might be impaired. Such conditions may include an economic downturn or a change in the assessment of future operations. The Company

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performs impairment tests of goodwill at the company level. Such impairment tests for goodwill include comparing the fair value of the appropriate reporting unit (the Company) with its carrying value. The Company performs impairment tests for indefinite-lived intangible assets by comparing the fair value of each indefinite-lived intangible asset unit to its carrying value. The Company recognizes an impairment charge if the asset's carrying value exceeds its estimated fair value. The Company completed its most recent annual impairment analyses as of September 30, 2007. Based upon the results of these analyses, the Company has concluded that no impairment of its goodwill or other intangible assets was indicated.

## ROLLINS, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

**Impairment of Long-Lived Assets** - In accordance with SFAS 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the Company's long-lived assets, such as property and equipment and intangible assets with definite lives are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Based upon the results of these analyses, the Company has concluded that no impairment of its long-lived assets was indicated.

**Comprehensive Income (Loss)** Other Comprehensive Income (Loss) results from foreign currency translations, unrealized gain/losses on marketable securities and changes in the pension liability.

**Franchising Program** Orkin had 58 franchises as of September 30, 2007, including international franchises in Mexico, established in 2000, Panama, established in 2003, and Costa Rica, established in 2006, along with Honduras, the United Arab Emirates, the Dominican Republic and South Korea all of which were established in 2007. Transactions with franchises involve sales of customer contracts to establish new franchises, initial franchise fees and royalties. The customer contracts and initial franchise fees are typically sold for a combination of cash and notes due over periods ranging up to 5 years for domestic franchises. Notes receivable from franchises aggregated \$4.1 million, \$5.2 million, and \$5.1 million as of September 30, 2007, December 31, 2006, and September 30, 2006, respectively. The Company recognizes gains from the sale of customer contracts at the time they are sold to franchises and collection on the notes is reasonably assured. The Company experienced a slight gain of \$0.1 million for the nine months ended September 30, 2007 and a net loss of \$0.7 million for the nine months ended September 30, 2006, these amounts are included as revenues in the accompanying Consolidated Statements of Income. Initial domestic franchise fees are deferred for the duration of the contract period and are included as unearned revenue in the Consolidated Statements of Financial Position. Deferred franchise fees amounted to \$2.1 million, \$2.2 million, and \$2.0 million at September 30, 2007, December 31, 2006, and September 30, 2006, respectively. Royalties from franchises are accrued and recognized as revenues as earned on a monthly basis. Revenues from royalties and fees were \$0.8 million in the third quarter of 2007 compared to \$0.6 million in the third quarter of 2006 and were \$2.2 million for the nine months ended September 30, 2007 compared to \$1.7 million for the nine months ended September 30, 2006. The Company's maximum exposure to loss relating to the franchises aggregated \$2.0 million, \$3.0 million, and \$3.1 million at September 30, 2007, December 31, 2006 and September 30, 2006, respectively.

**Fair Value of Financial Instruments** The Company's financial instruments consist of cash, cash equivalents, trade and notes receivables, accounts payable and other short-term liabilities. The carrying amounts of these financial instruments approximate their fair values.

**Seasonality** The business of the Company is affected by the seasonal nature of the Company's pest and termite control services. The increase in pest pressure and activity, as well as the metamorphosis of termites in the spring and summer (the occurrence of which is determined by the timing of the change in seasons), has historically resulted in an increase in the revenue of the Company's pest and termite control operations during such periods as evidenced by the following chart.

**Consolidated Net Revenues**  
(in thousands)

	Total Net Revenues		
	2007	2006	2005
First Quarter	\$201,232	\$194,187	\$183,915
Second Quarter	239,618	232,222	214,326
Third Quarter	238,116	227,816	209,346

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Fourth Quarter	N/A	204,653	194,830
Year ended December 31,	<b>\$678,966</b>	\$858,878	\$802,417

## ROLLINS, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

## NOTE 2. EARNINGS PER SHARE

In accordance with SFAS No. 128, *Earnings Per Share* (EPS), the Company presents basic EPS and diluted EPS. Basic EPS is computed on the basis of weighted-average shares outstanding. Diluted EPS is computed on the basis of weighted-average shares outstanding plus common stock options outstanding and unvested restricted stock awards during the period which, if exercised or vested, would have a dilutive effect on EPS. A reconciliation of the number of weighted-average shares used in computing basic and diluted EPS is as follows:

(in thousands except per share data)	Three months ended		Nine months ended	
	September 30, 2007	2006	September 30, 2007	2006
Basic and diluted earnings available to stockholders (numerator):	<b>\$ 18,765</b>	\$ 17,037	<b>\$ 52,797</b>	\$ 47,270
Shares (denominator):				
Weighted-average shares outstanding - Basic	<b>66,608</b>	67,068	<b>66,966</b>	67,184
Effect of dilutive securities:				
Employee stock options and restricted shares	<b>710</b>	1,632	<b>721</b>	1,742
Weighted-average shares outstanding Diluted	<b>67,318</b>	68,700	<b>67,687</b>	68,926
Per share amounts				
Basic income per common share	<b>\$ 0.28</b>	\$ 0.25	<b>\$ 0.79</b>	\$ 0.70
Diluted income per common share				