ROLLINS INC
Form 10-Q
August 01, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10 Q

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

For the quarterly period ended June 30, 2007

Commission File Number 1-4422

ROLLINS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**51-0068479**
(State or other jurisdiction of incorporation or organization)	(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)

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

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 o Accelerated Filer x Non-Accelerated filer o

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

Yes o No x

Rollins, Inc. had 67,379,492 shares of its $1 par value Common Stock outstanding as of July 16, 2007.

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

	June 30, 2007	December 31, 2006
ASSETS		
Cash and cash equivalents	**$ 57,044**	$ 63,344
Trade receivables, short-term, net of allowance for doubtful accounts of $6,979 and $6,132, respectively	**62,118**	52,693
Materials and supplies	**8,740**	8,401
Deferred income taxes	**18,528**	19,435
Other current assets	**9,621**	7,200
Total Current Assets	**156,051**	151,073
Equipment and property, net	**77,634**	72,141
Goodwill	**125,974**	125,160
Customer contracts and other intangible assets, net	**76,048**	77,056
Deferred income taxes	**12,886**	14,069
Trade receivables, long-term, net of allowance for doubtful accounts of $1,135 and $1,096, respectively	**8,908**	8,796
Other assets	**5,873**	4,880
Total Assets	**$ 463,374**	$ 453,175
LIABILITIES		
Capital leases	**$ 1,270**	$ 498
Accounts payable	**24,712**	16,309
Accrued insurance	**14,225**	14,310
Accrued compensation and related liabilities	**40,052**	47,305
Accrual for termite contracts	**7,789**	8,526
Other current liabilities	**20,186**	18,817
Unearned revenue	**85,754**	79,441
Total current liabilities	**193,988**	185,206
Capital leases, less current portion	**1,013**	124
Accrued insurance, less current portion	**24,663**	23,635
Accrual for termite contracts, less current portion	**10,511**	11,675
Accrued pension	**6,946**	6,946
Long-term accrued liabilities	**17,943**	14,130
Total Liabilities	**255,064**	241,716
Commitments and Contingencies		
STOCKHOLDERS' EQUITY		
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; 71,463,604 and 70,789,118 shares issued, respectively	**71,464**	70,789
Treasury stock, par value $1 per share; 4,102,774 and 2,898,074 shares, respectively	**(4,103)**	(2,898)
Additional paid-in capital	**13,085**	11,737
Accumulated other comprehensive loss	**(17,556)**	(17,784)
Retained earnings	**145,420**	149,615
Total Stockholders' Equity	**208,310**	211,459
Total Liabilities and Stockholders' Equity	**$ 463,374**	$ 453,175

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

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ROLLINS, INC. AND SUBSIDIARIES

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	**2007**	2006
REVENUES				
Customer services	**$239,618**	$232,222	**$440,850**	$426,408
COSTS AND EXPENSES				
Cost of services provided	**121,601**	119,035	**228,437**	226,049
Depreciation and amortization	**6,911**	6,945	**13,597**	13,738
Sales, general and administrative	**76,787**	74,368	**143,828**	136,868
(Gain)/loss on sales of assets	**(89)**	2	**(96)**	1
Interest income	**(522)**	(344)	**(1,074)**	(636)
	204,688	200,006	**384,692**	376,020
INCOME BEFORE INCOME TAXES	**34,930**	32,216	**56,158**	50,388
PROVISION FOR INCOME TAXES				
Current	**13,455**	11,079	**19,793**	16,945
Deferred	**236**	1,807	**2,333**	3,210
	13,691	12,886	**22,126**	20,155
NET INCOME	**$21,239**	$19,330	**$34,032**	$30,233
NET INCOME PER SHARE - BASIC	**$0.32**	$0.29	**$0.51**	$0.45
NET INCOME PER SHARE - DILUTED	**$0.31**	$0.28	**$0.50**	$0.44
Weighted average shares outstanding - basic	**66,977**	67,556	**67,148**	67,243
Weighted average shares outstanding - diluted	**67,675**	69,243	**67,874**	69,040
DIVIDENDS PAID PER SHARE	**$0.075**	$0.063	**$0.150**	$0.125

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

ROLLINS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2007 AND 2006
(in thousands)
(unaudited)

	Six Months ended June 30, 2007	2006
OPERATING ACTIVITIES		
Net Income	**$ 34,032**	$ 30,233
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**13,597**	13,738
Provision for deferred income taxes	**2,333**	3,210
Stock Based Compensation Expense	**1,572**	1,500
(Gain)/loss on sales of assets	**(96)**	1
Excess tax benefits from share-based payments	**(2,924)**	(50)
Other, net	**(85)**	(496)
(Increase)/decrease in assets		
Trade receivables	**(9,492)**	(9,605)
Materials and supplies	**(339)**	537
Other current assets	**(2,389)**	(912)
Other non-current assets	**(1,231)**	(21)
Increase/(decrease) in liabilities:		
Accounts payable and accrued expenses	**1,362**	(193)
Unearned revenue	**6,314**	4,388
Accrued insurance	**943**	1,768
Accrual for termite contracts	**(1,900)**	1,000
Accrued pension		(5,000)
Long-term accrued liabilities	**3,763**	(5,146)
Net cash provided by operating activities	**45,460**	34,952
INVESTING ACTIVITIES		
Purchase of equipment and property	**(10,099)**	(11,351)
Acquisitions/dispositions of companies, net	**(4,343)**	(5,020)
Cash from Sales of Franchises		401
Proceeds from sales of assets	**58**	
Net cash used in investing activities	**(14,384)**	(15,970)
FINANCING ACTIVITIES		
Dividends paid	**(10,240)**	(8,556)
Common stock purchased	**(30,868)**	(17,290)
Common stock options exercised	**879**	381
Principal Payments on Capital Lease Obligations	**(1,451)**	(393)
Excess tax benefits from share-based payments	**2,924**	50
Other		73
Net cash used in financing activities	**(38,756)**	(25,735)
Effect of exchange rate changes on cash	**1,380**	909
Net decrease in cash and cash equivalents	**(6,300)**	(5,844)
Cash and cash equivalents at beginning of year	**63,344**	43,065
Cash and cash equivalents at end of year	**$ 57,044**	$ 37,221
Supplemental disclosure of cash flow information		
Cash paid for interest	**$ 53**	$ 90
Cash paid for income taxes	**$ 15,689**	$ 14,064

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

(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	$34,032					34,032	34,032
Pension liability, net of taxes	(1,152)				(1,152		(1,152)
Foreign currency translation adjustments	1,380				1,380		1,380
Comprehensive income	$34,260						
Dividends declared						(10,240)	(10,240)
Common Stock Purchases			(1,205)			(26,311)	(27,516)
Stock-based compensation		228		1,345			1,573
Common stock options exercised		447		(2,921)			(2,474)
Excess tax benefits from share-based payments				2,924			2,924
Balance at June 30, 2007		**$71,464**	**$(4,103)**	**$13,085**	**$(17,556)**	**$145,420**	**$208,310**

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

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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 June 30, 2007 and December 31, 2006, the results of its operations for the three and six months ended June 30, 2007 and 2006 and cash flows for the six months ended June 30, 2007 and 2006. All such adjustments are of a normal recurring nature. Operating results for the six months ended June 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 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, 2006. 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

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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 55 franchises as of June 30, 2007, including international franchises in Mexico, established in 2000, Panama, established in 2003, and Costa Rica, established in 2006, Honduras, established in 2007 and the United Arab Emirates, 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 five years. Notes receivable from franchises aggregated $4.3 million, $5.2 million, and $5.6 million as of June 30, 2007, December 31, 2006, and June 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 had a net loss of approximately $57 thousand in the second quarter of 2007, due to customer true-up adjustments, compared to a net gain of approximately $0.4 million in the second quarter of 2006 and was $67 thousand for the six months ended June 30, 2007 compared to $0.8 millions for the six months ended June 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 initial 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 June 30, 2007, December 31, 2006, and June 30, 2006, respectively. Royalties from franchises are accrued and recognized as revenues as earned on a monthly basis. Revenues from royalties were $0.9 million during the second quarter ended June 30, 2007 compared to $0.6 million during the second quarter ended June 30, 2006 and were $1.3 million for the six months ended June 30, 2007 compared to $1.1 million for the six months ended June 30, 2006. The Company s maximum exposure to loss relating to the franchises aggregated $2.2 million, $3.0 million, and $3.5 million at June 30, 2007, December 31, 2006 and June 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		
(in thousands)	**2007**	2006	2005
First Quarter	**$ 201,232**	$ 194,187	$ 183,915

Second Quarter	**239,618**	232,222	214,326
Third Quarter	**N/A**	227,816	209,346
Fourth Quarter	**N/A**	204,653	194,830
Year ended December 31,	**$ 440,850**	$ 858,878	$ 802,417

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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:

	Three months ended June 30,		Six months ended June 30,	
(in thousands except per share data)	**2007**	2006	**2007**	2006
Basic and diluted earnings available to stockholders (numerator):	**$ 21,239**	$ 19,330	**$ 34,032**	$ 30,233
Shares (denominator):				
Weighted-average shares outstanding Basic	**66,977**	67,556	**67,148**	67,243
Effect of dilutive securities:				
Employee stock options and restricted shares	**698**	1,687	**726**	1,797
Weighted-average shares outstanding Diluted	**67,675**	69,243	**67,874**	69,040
Per share amounts				
Basic income per common share	**$ 0.32**	$ 0.29	**$ 0.51**	$ 0.45
Diluted income per common share	**$ 0.31**	$ 0.28	**$ 0.50**	$ 0.44

The Company bought back 612,700 shares of the Company s common stock on the open market during the second quarter ended June 30, 2007 under its authorized repurchase program at a weighted average price of $22.84 per share, with a total of 1,204,700 shares repurchased during the six months ended June 30, 2007 at a weighted average price of $22.84 per share. Rollins has had a buyback program in place for a number of years and has routinely purchased shares when it felt the opportunity was desirable. The Board authorized the purchase of 4.0 million additional shares of the Company s common stock at its quarterly meeting on April 26, 2005. This authorization enables the Company to continue the purchase of Rollins, Inc. shares when appropriate, which is an important benefit resulting from the Company s strong cash flows. Accordingly, 1,053,944 shares remain authorized for purchase. The stock buy-back program has no expiration date.

NOTE 3. RECENT ACCOUNTING PRONOUNCEMENTS

In September 2006, the FASB issued *SFAS No. 157, Fair Value Measurements.* SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 is effective for the Company on January 1, 2008 and is not expected to have a significant impact on the Company s financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Liabilities* (SFAS 159). SFAS 159 is effective as of the beginning of the first fiscal year beginning after November 15, 2007, and is effective for the Company January 1, 2008. SFAS 159 provides companies with an option to report selected financial assets and liabilities at fair value that are not currently required to be measured at fair value. Accordingly, companies would then be required to report unrealized gains and losses on these items in earnings at each subsequent reporting date. The objective is to improve financial reporting by providing companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for the Company on January 1, 2008 and is not expected to have a significant impact on the Company s financial statements.

In July 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48), which provides criteria for the recognition,

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ROLLINS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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measurement, presentation and disclosure of uncertain tax positions. The Company is subject to the provisions of FIN 48 as of January 1, 2007, and has analyzed filing positions in all of the federal, state and foreign filing jurisdictions where it is required to file income tax returns, as well as all open years in those jurisdictions. As a result of the implementation of FIN 48, the Company has recognized an increase of $1.68 million in the liability for unrecognized tax benefits, which was accounted for as a decrease to the January 1, 2007 balance of retained earnings. As of the adoption date the Company had gross tax affected unrecognized tax benefits of $6.1 million. The total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate is $3.8 million. There have been no significant changes to these amounts during the quarter ended June 30, 2007.

The Company and its subsidiaries are subject to U.S. federal income tax as well as income tax of multiple state and foreign jurisdictions. In many cases our uncertain tax positions are related to tax years that remain subject to examination by the relevant taxing authorities. The tax returns for 2002 and 2003 are currently under examination by the Internal Revenue Service. In addition, the Company has subsidiaries in various state jurisdictions that are currently under audit for years ranging from 1996 through 2005. With few exceptions, we are no longer subject to U.S. federal, state and local, or non-U.S., income tax examinations for years prior to 2002.

It is reasonably possible that the amount of the unrecognized benefit with respect to our unrecognized tax positions will increase or decrease in the next 12 months. These changes may be the result of settlement of ongoing federal and state audits. However, quantification of an estimated range cannot be made at this time.

The Company s policy is to record interest and penalties related to income tax matters in income tax expense. Accrued interest and penalties were $1.1 million and $1.3 million as of January 1, 2007 and June 30, 2007, respectively.

On May 2, 2007 the FASB issued FIN 48-1, Definition of Settlement in FASB Interpretation No. 48. The definition of settlement in FIN 48-1 does not have a material effect on the cumulative effect adjustment as recorded by the Company upon adoption of FIN 48.

In June 2007, the Emerging Issues Task Force (EITF) issued Issue 06-11 Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards . The guidance in EITF Issue 06-11 addresses how an employer should account for the income tax benefits related to dividend or dividend equivalent payments made to employees holding certain share-based payment awards. Entities are required to recognize tax benefits realized from dividend or dividend equivalents paid to employees for certain share-based payment awards as an increase to additional paid-in capital and include such amounts in the pool of excess tax benefits available to absorb future tax deficiencies on share-based payment awards. EITF Issue 06-11 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2007 (January 1, 2008 for calendar-year entities). Entities should apply the consensus prospectively to income tax benefits of dividends on equity-classified employee share-based payment awards that are declared in fiscal years beginning after December 15, 2007. We are currently in the process of evaluating the effects of the adoption of EITF Issue 06-11 on our consolidated results of operations, cash flows, and financial position.

NOTE 4. CONTINGENCIES

Orkin, one of the Company s subsidiaries, is a named defendant in Mark and Christine Butland et al. v. Orkin Exterminating Company, Inc., et al. pending in the Circuit Court of Hillsborough County, Tampa, Florida. The plaintiffs filed suit in March of 1999 and are seeking monetary damages and injunctive relief. The Court ruled in early April 2002, certifying the class action lawsuit against Orkin. Orkin appealed this ruling to the Florida Second District Court of Appeals, which remanded the case back to the trial court for further findings. In December 2004 the Court issued a new ruling certifying the class action. Orkin appealed this new ruling to the Florida Second District Court of Appeals. In June 2006, the Florida Second District Court of Appeals issued a ruling denying certification of the class. Following the Plaintiffs motion for rehearing, the court upheld its prior decision that class certification was improper but also ruled that the Plaintiffs can return to the trial court and attempt to certify a narrower class. Orkin will oppose any effort by the Plaintiffs to do so. Orkin believes this case to be without merit and intends to defend itself vigorously through trial, if necessary. At this time, the final outcome of the litigation cannot be determined. However, in the opinion of management, the ultimate resolution of this matter will not have a material adverse effect on the Company s financial position, results of operations or liquidity.

ROLLINS, INC. AND SUBSIDIARIES

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(unaudited)

Additionally, in the normal course of business, Orkin is a defendant in a number of lawsuits or arbitrations, which allege that plaintiffs have been damaged as a result of the rendering of services by Orkin. Orkin is actively contesting these actions. Also, some lawsuits or arbitrations have been filed (Ernest W. Warren and Dolores G. Warren, et al. v. Orkin Exterminating Company, Inc., et al.; and Francis D. Petsch, et al. v. Orkin Exterminating Company, Inc., et al.; John Maciel v. Orkin, Inc., et. al.; and Jennifer Poulson v. Orkin, Inc et. al.) in which the plaintiffs are seeking certification of a class. The cases originate in Georgia, Florida, and California. In Warren, the Superior Court of Cobb County, Marietta, Georgia, ruled in August 2006, certifying the class action against Orkin. Orkin has appealed this ruling to the Georgia Court of Appeals. Petsch and Poulson have been resolved on an individual basis with the Plaintiffs dismissing their cases including their class action allegations. The Company believes the pending cases to be without merit and intends to defend itself vigorously through trial, if necessary. At this time, the final outcome of the litigation cannot be determined. However, in the opinion of management, the ultimate resolution of these matters will not have a material adverse effect on the Company s financial position, results of operations or liquidity.

Orkin is involved in certain environmental matters primarily arising in the normal course of business. In the opinion of management, the Company s liability under any of these matters would not materially affect its financial condition or results of operations. Consistent with the Company s responsibilities under these regulations, the Company undertakes environmental assessments and remediation of hazardous substances from time to time as the Company determines its responsibilities for these purposes. As these situations arise, the Company accrues management s best estimate of future costs for these activities. Based on management s current estimates of these costs, management does not believe these costs are material to the Company s financial condition or operating results or liquidity.

NOTE 5.