

Edgar Filing: ACR GROUP INC - Form 10-K

ACR GROUP INC
Form 10-K
May 29, 2001

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-K
For Annual Reports Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934

For the Fiscal Year Ended
February 28, 2001

Commission File Number
0-12490

ACR GROUP, INC.
(Exact name of registrant as specified in its Charter)

Texas
(State or other jurisdiction of
incorporation or organization)

74-2008473
(I.R.S. Employer
Identification No.)

3200 Wilcrest Drive, Suite 440, Houston, Texas 77042
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (713) 780-8532

Securities registered pursuant to Section 12(b) of the Act: None
Securities registered pursuant to Section 12(g) of the Act:
Common Stock, par value \$.01 per share
(Title of class)

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

The aggregate market value of the common stock held by nonaffiliates of the
registrant on April 30, 2001 was \$4,393,209. The aggregate market value was
computed by reference to the last trading price as reported on the National
Association of Securities Dealers Automated Quotation System. For the purposes
of this response, Executive Officers, Directors and holders of more than 10% of
the Registrant's common stock are considered affiliates of the registrant.

The number of shares outstanding of the registrant's common stock as of April
30, 2001: 10,681,294 shares

Edgar Filing: ACR GROUP INC - Form 10-K

DOCUMENTS INCORPORATED BY REFERENCE

The registrant's definitive Proxy Statement for its Annual Meeting of Shareholders to be held in August 2001 is incorporated by reference in answer to Part III of this report.

2

TABLE OF CONTENTS

	Page

PART I	
Item 1. Business	4
Item 2. Properties	10
Item 3. Legal Proceedings	10
Item 4. Submission of Matters to a Vote of Security Holders	10
PART II	
Item 5. Market for Registrant's Common Equity and Related Stockholder Matters	10
Item 6. Selected Financial Data	11
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations	13
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	19
Item 8. Financial Statements and Supplementary Data	20
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	41
PART III	
Item 10. Directors and Executive Officers of the Registrant	41
Item 11. Executive Compensation	41
Item 12. Security Ownership of Certain Beneficial Owners and Management	41
Item 13. Certain Relationships and Related Transactions	41
PART IV	
Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K	42

3

Edgar Filing: ACR GROUP INC - Form 10-K

PART I

ITEM 1. BUSINESS.

General

ACR Group, Inc. (which, together with its subsidiaries is herein referred to as the "Company" or "ACRG") is a Texas corporation based in Houston. In 1990, the Company began to acquire and operate businesses engaged in the wholesale distribution of heating, ventilating, air conditioning and refrigeration ("HVACR") equipment and supplies. The Company acquired its first operating company in 1990. Since 1990, ACRG has acquired or started nine additional HVACR distribution companies and now has 48 branch operations in nine states. The Company plans to continue expanding in the Sunbelt of the United States and in other geographic areas with a high rate of economic growth, through both acquisitions and internal growth.

The HVACR Industry

The Company's interest in the HVACR distribution industry is a direct result of the business experience of its Chairman and President, Alex Trevino, Jr., who has been associated with the industry for over thirty years in varying capacities, first as owner of his own distribution company and then as president of various successor companies following the sale of his business.

The Company sells supplies and equipment to installing contractors and dealers and to other technically trained customers responsible for the installation, repair and maintenance of HVACR systems. Maintenance of a large and diverse inventory base is an important element in the Company's sales.

The HVACR supply industry is segmented into discrete categories. First, it serves both commercial and residential HVACR businesses. Each of these segments is further divided into two markets - new construction sales and replacement and/or repair sales. Some companies choose to specialize in serving the new construction markets while others focus on the repair/replacement market, commonly referred to as the "aftermarket." ACRG is not oriented toward any particular segment but instead concentrates on acquiring and developing profitable businesses in the Sunbelt region of the United States which have a significant market share within their segment of the HVACR distribution industry. The Company believes that its growth strategy is appropriate in view of the competitive nature of the HVACR industry and the continuing consolidation in that industry, discussed below.

There are many manufacturers of products used in the HVACR industry, and no single manufacturer dominates the market for a range of products. Some manufacturers

limit the number and territory of wholesalers that may distribute their products, but exclusivity is rare. Many manufacturers will generally permit any distributor who satisfies customary commercial credit standards to sell their products. In addition, there are some manufacturers, primarily of equipment, that distribute their own products through factory branches. The widespread availability of HVACR products to distributors results in significant competition. There are an estimated three thousand HVACR wholesale distributors in the United States, and there is no single company or group of companies that dominates the HVACR distribution industry. The industry traditionally has been characterized by closely-held businesses with operations limited to local or

Edgar Filing: ACR GROUP INC - Form 10-K

regional geographic areas; however, a process of consolidation in this industry is ongoing, as many of these companies reach maturity and face strategic business issues such as ownership succession, changing markets and lack of capital to finance growth. Management's goal is to attract the present owners and management of such businesses by offering certain advantages related to economies of scale: lower cost of products from volume purchasing, new product lines, and financial, administrative and technical support.

The Company believes that investing in the HVACR distribution industry has fewer economic risks than many other industries. Although the HVACR industry is affected by general economic conditions such as cycles in new home construction, sales of replacement equipment and repair parts for the existing base of installed air conditioning and heating systems provide a cushion against economic swings. The aftermarket is far less susceptible to changes in economic conditions than the new construction market and now represents approximately 70% of all units installed annually. This percentage should continue to increase as the base of installed systems expands. Much of the HVACR industry is also seasonal; sales of air conditioning and heating systems are generally largest during the times of the year when climatic conditions require the greatest use of such systems. Sales of refrigeration systems, which are generally to commercial customers, are subject to less seasonality.

The Company's operations are conducted through 10 subsidiaries that participate in the wholesale distribution of HVACR equipment and supplies:

ACR Supply, Inc.

The Company acquired ACR Supply, Inc. ("ACRS") in 1993, after making an initial investment in the company in 1991. At the end of fiscal 2001, ACRS had fifteen branches in Texas and one in Louisiana. Many of ACRS's branches have attained market share leadership in their respective areas. In major metropolitan areas such as San Antonio and Houston, ACRS encounters significantly more competition than in smaller cities. However, through aggressive sales efforts, the Houston branches have achieved a significant, but not dominant, share of their local HVACR markets.

5

ACRS sells primarily to licensed contractors serving the residential and light commercial (restaurants, strip shopping centers, etc.) markets. The company's sales mix is approximately 25% equipment and 75% parts and supplies, with the equipment and parts generally directed to the aftermarket and the supplies used principally in new construction.

Heating and Cooling Supply, Inc.

The Company acquired Heating and Cooling Supply, Inc. ("HCS") in 1990. HCS operates from one location in Las Vegas, Nevada. There are approximately 20 independent HVACR distributors in the Las Vegas area that compete with HCS. Management believes that HCS is among the top three of such distributors in terms of annual sales from branch operations in the local area.

Mirroring the rapid growth of the Las Vegas economy over the past decade, approximately 80% of HCS's sales are in the new construction market, and a majority of those sales are to the residential segment of the market. Unlike most HVACR distributors, HCS also has capabilities to service both the commercial plan and specifications market and specialty products markets. The company intends to direct greater attention to the HVACR aftermarket in the immediate future in an effort to gain higher margin business.

Total Supply, Inc.

Edgar Filing: ACR GROUP INC - Form 10-K

Total Supply, Inc. ("TSI") has operated as an HVACR wholesale distributor in Georgia since 1992. Since 1993, TSI has distributed the GMC brand of HVACR equipment in Georgia and now has the GMC distribution rights to almost the entire state of Georgia. TSI sells almost exclusively to the residential market, and management estimates that sales are approximately evenly split between new construction and the aftermarket. The company's sales mix is approximately 65% equipment and 35% parts and supplies. TSI has four branches located in the Atlanta metropolitan area, one branch in Warner Robins, a suburb of Macon, another in Savannah, Georgia and one in Dothan, Alabama.

Valley Supply, Inc.

In 1994, the Company organized Valley Supply, Inc. ("VSI") as an HVACR distributor in the Memphis, Tennessee trade area, which included southwestern Tennessee, northern Mississippi and western Arkansas. In 1997, the Company assigned to management of TSI the responsibility for VSI's operations, and in 1999, VSI gained the distribution rights for GMC equipment in the Nashville trade area. Approximately 73% of VSI's sales consisted of GMC equipment in fiscal 2001. In fiscal 2001, the Company closed its operation in Memphis, Tennessee to

6

concentrate its efforts on selling GMC equipment in the larger metropolitan areas of central and south central Tennessee.

Ener-Tech Industries, Inc.

In 1996, the Company acquired Ener-Tech Industries, Inc. ("ETI"), an HVACR distributor in Nashville, Tennessee. Unlike the Company's other HVACR distribution operations, ETI specializes in an industry subsegment. ETI sells controls and control systems to commercial and industrial end-users, HVACR contractors, dealers and other distributors. ETI also designs and assembles control systems used in commercial applications such as hospitals, restaurants and supermarkets. Such control systems perform a variety of functions including temperature control and monitoring, lighting control and energy management.

ETI is an authorized distributor for Honeywell, Inc. for much of Tennessee and parts of Kentucky. By providing engineering services and assembly processes for its customers in connection with the sale of control systems, ETI obtains a higher gross margin on its sales than the Company's other distribution businesses. Additionally, ETI's sales tend to be greater in the cooler seasons of the year, when gas controls are in higher demand.

Florida Cooling Supply, Inc.

In 1996, the Company organized Florida Cooling Supply, Inc. ("FCS") and opened four branch operations in west central Florida. The state of Florida is among the three largest in the United States in terms of installed HVACR systems. The Company's sales mix is approximately 32% equipment and 68% parts and supplies. In fiscal 2000, the operation in Winter Haven, Florida was closed. The customers from this area continued to be serviced from the Company's Lakeland, Florida location. In fiscal 2001, the Company opened branch operations in Gainesville and Jacksonville, Florida expanding its sales territory outside the Tampa Bay area of Florida.

Lifetime Filter, Inc.

In 1997, the Company acquired Lifetime Filter, Inc. ("LFI"), a manufacturer of

Edgar Filing: ACR GROUP INC - Form 10-K

air filters for the HVACR industry. LFI is based in Katy, Texas, a suburb of Houston. At that time, LFI manufactured principally semi-permanent electrostatic air filters that were sold by mail order to contractors and dealers across the country. The market demand for electrostatic filters has diminished since 1997, and the company expects that trend to continue.

7

Since 1997, in an effort to increase the size of its average sales order, LFI has added to its sales mix certain other HVACR supplies and parts that are suited for mail order delivery. In fiscal 2001, resale of HVACR products represented approximately 14% of LFI's sales.

In 1999, LFI began to manufacture disposable pleated air filters, which have greater filtering capability and a somewhat longer life than the traditional disposable fiberglass air filter. Pleated air filters are projected to have increasing demand in both commercial and residential applications and are more readily sold through the Company's existing wholesale distribution network. In fiscal 2001, sales of its pleated filters represented approximately 25% of LFI's gross sales. LFI is also evaluating opportunities to begin business-to-business sales of a variety of its filter products over the Internet.

West Coast HVAC Supply, Inc. d/b/a ACH Supply

In 1997, West Coast HVAC Supply, Inc. acquired the operating assets and liabilities of ACH Supply, Inc., ("ACH"). ACH had two branches located east of Los Angeles. In fiscal 1999, ACH opened a third branch in Canoga Park. The Company has attracted key employees with significant management experience working for a much larger HVACR wholesale distributor in southern California. ACH sells primarily HVACR parts and supplies, and, late in fiscal 2000, began distributing the Tappan brand of HVACR equipment. In fiscal 2001, the Company opened four new branches: Santa Ana and Redlands in the southern and eastern trade areas surrounding Los Angeles, and in Fresno and Bakersfield, expanding into the central California market areas. These two branches in central California distribute the Comfortmaker line of HVACR equipment.

Contractors Heating & Supply, Inc. ("CHS")

In 1997, CHS acquired certain of the assets, and assumed certain of the liabilities, of Contractors Heating and Supply Company, an HVACR distributor based in Denver, with branch operations in Colorado Springs and Glenwood Springs, Colorado, and in Albuquerque, New Mexico. CHS has operated in Denver since 1945, in Colorado Springs since 1959 and in Albuquerque since 1960, and is considered the market leader in each of its trade areas. CHS also operates a sheet metal shop in Colorado Springs, where products are fabricated for distribution through CHS's wholesale operations. Approximately 18% of CHS's total sales are products that it manufactures. In April 1999, CHS opened a distribution branch in Fort Collins, Colorado, and, in March 2000, acquired International Comfort Supply, Inc., a wholesale distributor based in El Paso, Texas. In fiscal 2001, the Company obtained the rights to distribute the Goodman line of equipment in all of its trade areas, and also opened a branch operation and distribution center in east Denver.

8

CAC Distributors, Inc.

In fiscal 2001, the Company organized CAC Distributors, Inc. ("CAC"), based in Houston. CAC has obtained the right to distribute the Frigidaire and Kelvinator brands of HVACR equipment in central and south Texas. CAC focuses

Edgar Filing: ACR GROUP INC - Form 10-K

solely on selling equipment, rather than supplies and parts, to a selective number of HVACR dealer-contractors. As an element of that strategy, CAC provides limited exclusivity and market protection to its customers. As of the end of fiscal 2001, CAC operates from a single branch location in north Houston.

Energy Service Business

In the early 1980's, the Company's primary business was the design, installation and management of integrated systems intended to reduce energy costs ("Systems") for users of commercial, industrial and institutional facilities. Pursuant to service contracts, customers paid ACRG a specified percentage of the utility cost savings attributable to the Systems over the term of the contract. In fiscal 2000, the Company reached an understanding with its final energy services customer to terminate services at the end of October 1999, with the customer agreeing to make a contract termination payment to the Company and to pay for all utility cost savings computed through the termination date. This process was completed in April 2000.

Executive Officers of the Registrant

The Company's executive officers are as follows:

Name	Age	Position with the Company
Alex Trevino, Jr.	64	Chairman of the Board and President
Anthony R. Maresca	50	Senior Vice President, Treasurer, and Chief Financial Officer
A. Stephen Trevino	38	Vice President, Secretary and General Counsel

Alex Trevino, Jr. has served as Chairman of the Board since 1988 and as President and Chief Executive Officer of the Company since July 1990. From September 1987 to February 1990, he served as President of Western Operations of the Refrigeration and Air Conditioning Group of MLX Corporation (now Pameco Corporation), which is a national distributor of HVACR equipment and supplies.

9

Anthony R. Maresca has been employed by the Company since 1985. In November 1985 he was elected Senior Vice President, Chief Financial Officer and Treasurer. Mr. Maresca is a certified public accountant.

A. Stephen Trevino has been employed by the Company since March 1999, initially serving as General Counsel and directing various administrative functions. He was elected Vice President and Secretary in August 2000.

Employees

As of February 28, 2001, the Company and its subsidiaries had approximately 400 full-time employees. Neither the Company nor its subsidiaries routinely use temporary labor. There are no Company employees represented by any collective bargaining units. Management considers the Company's relations with its employees to be good.

ITEM 2. PROPERTIES.

The Company and its subsidiaries occupy office and warehouse space under

Edgar Filing: ACR GROUP INC - Form 10-K

operating leases with various terms. Generally, a branch location will contain 10,000 to 25,000 square feet of showroom and warehouse space. Branch locations that include a subsidiary's corporate office will be larger. The Company owns the facilities occupied by LFI, the Pasadena, Texas branch of ACRS, and the Gainesville, Florida branch of FCS.

ITEM 3. LEGAL PROCEEDINGS.

As of February 28, 2001 the Company was not a party to any pending legal proceeding that is deemed to be material to the Company and its subsidiaries.

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

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year ended February 28, 2001.

PART II

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

Until May 2001, the Company's common stock traded on the NASDAQ Stock Market(R) under the symbol "ACRG." The table below sets forth the high and low sales prices based upon actual transactions.

10

Effective May 9, 2001, the Company's common stock was delisted from the Nasdaq Stock Market for failure to maintain a closing bid price of at least \$1.00 per share. The Company's common stock is now traded in the over-the-counter market under the symbol "ACRG" as before, or by the symbols "ACRG.OB", or "ACRG.BB", depending on the source of the quote.

	High	Low
	-----	-----
Fiscal Year 2001		
1st quarter ended 5/31/00	\$2.00	\$1.34
2nd quarter ended 8/31/00	1.64	1.00
3rd quarter ended 11/30/00	1.38	0.56
4th quarter ended 2/28/01	0.81	0.50
Fiscal Year 2000		
1st quarter ended 5/31/99	\$2.38	\$1.03
2nd quarter ended 8/31/99	1.97	1.13
3rd quarter ended 11/30/99	1.75	1.13
4th quarter ended 2/29/00	2.13	1.09

As of April 30, 2001, there were 479 holders of record of the Company's common stock. This number does not include the beneficial owners of shares held in the name of a broker or nominee.

The Company has never declared or paid cash dividends on its common stock. The Company's loan agreements with two lenders each expressly prohibit the payment of dividends by the Company. See Management's Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources, and Note 4 of Notes to Consolidated Financial Statements.

Edgar Filing: ACR GROUP INC - Form 10-K

ITEM 6. SELECTED FINANCIAL DATA.

The following selected financial data of the Company have been derived from the audited consolidated financial statements. This summary should be read in conjunction with the audited consolidated financial statements and related notes included in Item 8 of this Report. Since February 28, 1997, the increase in sales has resulted from acquisitions and internal expansion, as discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7. of this Report. The Company has never paid any dividends.

11

The Company has not recorded a provision for income taxes other than federal alternative minimum taxes and state income taxes for fiscal years 1997 through 2001 because of previously incurred net operating losses for which a tax benefit had not previously been recorded. Additionally, the Company determined in both fiscal 1998 and 1997 that further reductions in its deferred tax asset valuation allowance were appropriate, given expectations of higher future taxable income from recently acquired businesses. As a result, the Company recorded additional tax benefits of \$420,000 and \$360,000 in fiscal 1998 and 1997, respectively.

	(In thousands, except per share data)			
	Year Ended February 28 or 29,			
	2001	2000	1999	1998
	-----	-----	-----	-----
Income Statement Data:				
Sales	\$136,433	\$126,468	\$117,887	\$96,433
Gross profit	29,452	28,135	24,772	19,452
Operating income	772	4,077	3,317	2,482
Income before income taxes	(1,341)	2,482	1,568	1,568
Benefit (provision) for income taxes	(137)	(255)	(153)	(153)
Net (loss) income	\$ (1,478)	\$ 2,227	\$ 1,415	\$ 1,415
	=====	=====	=====	=====
Earnings per common share:				
Basic	\$ (0.14)	\$.21	\$.13	\$.13
	=====	=====	=====	=====
Diluted	\$ (0.14)	\$.20	\$.12	\$.12
	=====	=====	=====	=====

	As of February 28 or 29,			
	2001	2000	1999	1998
	-----	-----	-----	-----
Balance Sheet Data:				

Edgar Filing: ACR GROUP INC - Form 10-K

Working capital	\$ 21,170	\$ 18,072	\$ 15,614	\$13,
Total assets	54,582	44,842	45,103	41,
Long-term obligations	24,494	17,499	17,616	16,
Shareholders' equity	10,147	11,630	9,391	7,

12

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

Results of Operations

Operating income decreased to \$771,553 in fiscal 2001, from \$4,077,468 in fiscal 2000 and \$3,316,631 in fiscal 1999, representing a decrease of 81% in fiscal 2001 from an increase of 23% in fiscal 2000. The decrease in operating income in fiscal 2001 was attributable principally to the initial costs associated with the opening of eleven branch operations in fiscal 2001 and disappointing operating results at the Company's largest subsidiaries. The increase in operating income in fiscal 2000, compared to 1999, was attributable to improvement in the financial performance of the Company's larger, more established companies over prior years. The costs associated with new branch operations were largely anticipated, although delays in obtaining local regulatory approval for certain new facilities caused pre-opening expenses to exceed expectations. The decline in profitability of existing operations was not forecasted and generally mirrored an unexpectedly poor year in the HVACR industry. In the fourth quarter of fiscal 2001, the Company closed its Memphis, Tennessee branch operation after several years of substandard operating results. Net (loss) income was \$(1,477,593), \$2,226,633 and \$1,415,080 in fiscal 2001, 2000 and 1999, respectively.

Same-store sales were unchanged in fiscal 2001, after increasing 5% and 14% in fiscal 2000 and 1999, respectively. In fiscal 2001, although the Company recorded double-digit same-store sales increases in Florida and California, the gains at these relatively small operations were more than offset by flat or declining sales in Texas, Colorado and Georgia. The slowdown in business was not directly attributable to a single factor, but rather to a complex mix of factors, ranging from unfavorable weather conditions in certain geographic areas to operating issues. The increase in sales in fiscal 2000 occurred principally through internal expansion of branch operations, and compared to fiscal 1999, the decline in the rate of sales growth was more directly attributable to unfavorable weather conditions in Texas and Florida. In fiscal 1999, 54% of the increase in sales was attributable to operations that had been recently acquired.

The Company's gross margin percentage decreased to 21.6% in fiscal 2001, from 22.2% in fiscal 2000 and 21.0% in fiscal 1999. The decrease in gross margin for fiscal 2001 was attributable to both the new branch operations, which in some cases, reduced selling prices to gain initial business, and declines in the Texas, Nevada and Tennessee markets. The increase in gross margin percentage in fiscal 2000 from 1999 was a result of management's efforts to strengthen existing branch locations. The Company's gross margin percentage has also been favorably affected by purchasing arrangements that management has negotiated from its major suppliers, and by technology improvements that have enabled management to implement more sophisticated pricing strategies. In

addition, CHS manufactures products that account for approximately 18% of its sales revenue and, accordingly, achieves a higher gross margin percentage than if it purchased its inventory from outside suppliers.

Selling, general and administrative ("SG&A") costs as a percentage of sales were 21.1% in fiscal 2001, compared to 19.1% in fiscal 2000 and 18.2% in fiscal 1999. The increase in SG&A costs as a percentage of sales in both fiscal 2001 and 2000 was attributable to costs associated with new branch operations and personnel employed to support the Company's internal growth goals. In particular, SG&A costs are incurred at new branch operations before sales are generated and, after a branch is open, remain high as a percentage of sales as sales ramp up to expected levels. The emphasis on growth in central and southern California during fiscal 2001 especially impacted SG&A costs as occupancy and other operating costs tend to be significantly higher there compared to the Company's other market areas.

Net energy services income decreased 41% in fiscal 2001 following an increase of 182% from fiscal 1999 to fiscal 2000. The increase in fiscal 2000 was the result of the negotiated termination of the Company's contract with its last energy services customer and a resolution of unbilled services. The Company finalized all invoicing in early fiscal 2001.

Interest expense increased 24% in fiscal 2001 compared to fiscal 2000, after decreasing 1% in fiscal 2000 compared to fiscal 1999. In fiscal 2001, the increase was due both to increased average interest rates and to increased borrowings under the Company's revolving credit facility to finance the working capital requirements of the new branches opened in fiscal 2001. In fiscal 2000, the decrease was primarily due to favorable interest rates. In fiscal 2001, 2000 and 1999, interest expense was 1.8%, 1.6% and 1.7% of sales, respectively. Other non-operating income decreased 10% from fiscal 2000 to fiscal 2001, after an increase of 44% from fiscal 1999 to fiscal 2000, as the Company has more strictly enforced its policy to collect finance charges from customers with past due balances.

Current income tax expense consists principally of state income taxes. As a result of the Company's substantial tax loss carryforwards, the Company has minimal liability for Federal income taxes. See Liquidity and Capital Resources, below.

Liquidity and Capital Resources

Working capital increased from \$18.1 million in fiscal 2000 to \$21.2 million in fiscal 2001, principally as a result of financing the current assets used in the new branch operations with long-term debt under the Company's revolving credit facility. Accounts receivable represented 49 days of gross sales at the end of fiscal 2001 and 52 days at the

end of fiscal 2000. The increase in inventory from the end of fiscal 2000 to 2001 is generally located at the branches that were opened in fiscal 2001.

The Company has a loan agreement ("Agreement") with a commercial bank ("Bank") that was amended and restated in May 2000 to increase to \$25 million the amount that may be borrowed by the Company under a revolving credit facility and to provide facilities for the purchase of both real estate and capital assets. The Agreement terminates in May 2003, but is automatically extended for one-year

Edgar Filing: ACR GROUP INC - Form 10-K

periods unless either party gives notice of termination to the other. Prepayment penalties apply if the revolving credit facility is prepaid during the first two years of the term. Restrictive covenants of the Agreement prohibit the Company from paying dividends, prepaying any subordinated indebtedness or incurring certain other debt without the Bank's consent, and also require the Company to maintain certain financial ratios. As of February 28, 2001, the Company was not in compliance with certain of the required financial ratios. In March 2001, the Company and the Bank further amended the Agreement to waive such non-compliance through the end of fiscal 2001 and to revise the required financial ratios for fiscal 2002.

The interest rate on borrowings under the revolving credit facility is based on either the Bank's prime rate or LIBOR and varies depending on the Company's leverage ratio, as defined, determined quarterly. As of February 28, 2001, the applicable interest rate was either the prime rate or LIBOR plus 2.75%, and the Company had elected the LIBOR option (9.33%) for substantially all amounts outstanding under the facility. Borrowings under the revolving credit facility are limited to 85% of eligible accounts receivable and 50% of eligible inventory amounts (which increases to 65% of eligible inventory amounts during certain specified months of the year). At February 28, 2001, the Company's available credit under the facility was approximately \$510,000.

The Agreement provides a term loan facility of \$4 million for the purchase of real estate and improvements. At February 28, 2001, the Company's had indebtedness to the Bank under the facility of \$226,220, secured by a deed of trust on both the land and building occupied by a branch facility in the Houston area, which is repaid in equal monthly principal installments of \$2,400, plus interest. The Agreement also provides a capital expenditure term loan facility of \$1 million for capital assets acquired after March 2000 and an acquisition facility of up to \$5 million for the acquisition of other businesses, subject to approval by the Bank of specific transactions. As of February 28, 2001, the Company had not borrowed any amounts under either the capital expenditure facility or the acquisition facility. Both the real estate and the capital expenditures facility bear interest at a variable rate, which was the prime rate or LIBOR plus 2.75% at February 28, 2001. Borrowings under the acquisition facility also bear interest at a variable rate that is generally 0.25% higher than the rate applicable to the other term loan facilities. At February 28, 2001, the Company had outstanding borrowings

15

aggregating \$157,659 under a previous term loan arrangement bank for the purchase of capital assets. Such borrowings are repaid in equal monthly installments of \$7,883, plus interest. In April 2001, the Company borrowed \$487,500 under the real estate term loan facility, and \$429,353 under the capital expenditure facility. Such amounts are to be repaid in equal principal installments over 120 months and 60 months, respectively, plus interest.

At February 28, 2001, the Company was also not in compliance with certain of the required financial ratios contained in its loan agreement with The Catalyst Fund, Ltd. and an affiliate ("Catalyst"). See Note 4 of Notes to Consolidated Financial Statements. In May 2001, Catalyst waived such non-compliance for all periods through fiscal 2001 and for the first three quarters of fiscal 2002.

The Company made capital expenditures of \$3.2 million in fiscal 2001 for building and leasehold improvements, computer software, equipment and vehicles under capital leases. A significant majority of the assets acquired were in connection with the opening of new branch operations and the relocation of existing branch operations. Included in the capital expenditures were the purchase of a building in Gainesville, Florida for a new branch operation of FCS and the construction of a finished goods warehouse at LFI. The real estate

Edgar Filing: ACR GROUP INC - Form 10-K

purchase in Florida was partially financed by the sellers. The sellers financed \$825,000 for a term of 25 years at an interest rate of 8.25% per annum. The note is secured by a deed of trust on the real estate and all improvements.

The Company has approximately \$8.1 million in tax loss carryforwards which substantially expire by fiscal 2003. Such operating loss carryforwards will substantially limit the Company's federal income tax liabilities in the near future. Certain provisions of the Internal Revenue Code ("Code") regulate the amount of additional stock that the Company could issue without resulting in a change in ownership control, as defined in the Code. Should such a change in control be deemed to occur, the Company's ability to utilize its operating loss carryforwards would be severely restricted.

The Company expects that cash flows from operations and the borrowing availability under its revolving credit facility will provide sufficient liquidity to meet its normal operating requirements, debt service and expected capital expenditures. The Company does not presently plan to open new branch operations in fiscal 2002; rather, management is focused on achieving planned operating performance at the branches that were opened in fiscal 2001. Subject to limitations set forth in its loan agreement with the Bank, funds available under the Company's revolving credit facility may also be utilized to finance acquisitions. However, management is not presently evaluating any acquisition opportunities.

16

Seasonality

The Company's sales volume and, accordingly, its operating income vary significantly during its fiscal year. The highest levels of sales occur during the times of the year when climatic conditions require the greatest use of air conditioning, since the Company's operations are concentrated in the warmer regions of the United States. Accordingly, sales will be highest in the Company's second quarter ending August 31, and will be lowest in its fourth fiscal quarter.

Inflation

The Company does not believe that inflation has had a material effect on its results of operations in recent years. Generally, manufacturer price increases attributable to inflation uniformly affect both the Company and its competitors, and such increases are passed through to customers as an increase in sales prices.

Year 2000 Issue

Prior to December 31, 1999, the Company undertook various measures to address its state of readiness to deal with the problem commonly known as the Year 2000 issue. Such measures included installing an upgrade to its existing integrated application software and, at one of the Company's subsidiaries that does not use the Company's integrated software, purchasing new computer hardware and migrating the subsidiary's computer programs to the new hardware. The costs incurred by the Company to achieve year 2000 compliance were less than \$100,000 and were expensed as incurred.

Upon transitioning to Year 2000 in January 2000, the Company did not experience any related problems in its internal operations. To date, the Company has experienced no adverse effects as a result of suppliers, customers or service providers failing to adequately address the Year 2000 issue and further received assurances from its most significant suppliers that they were able to meet customer demands.

Edgar Filing: ACR GROUP INC - Form 10-K

While management believes that it took adequate steps to address the Year 2000 issue, there can be no assurance that such problems may not arise in the future. Should Year 2000 issues ultimately have a material adverse impact on significant business partners or key parties that provide the country's business and public service infrastructure, the Company's operations could be similarly affected.

Recently Issued Accounting Standards

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and

17

Hedging Activities" ("SFAS 133"). SFAS 133, as amended by Statement of Financial Accounting Standard No. 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FAS Statement No. 133" ("SFAS 137") which is effective for fiscal years beginning after June 15, 2000, requires all derivatives to be recognized at fair value on the balance sheet. The Company plans to adopt SFAS 133 beginning with the Company's fiscal year 2002. The change is not expected to have a significant effect on the Company's financial statements.

In February 2001, the Financial Accounting Standards Board ("FASB") issued a revised Exposure Draft, "Business Combinations and Intangible Assets - Accounting for Goodwill". The Exposure Draft would continue to require recognition of goodwill acquired in a business combination as an asset but would not permit amortization of goodwill as currently required by Accounting Principals Board Opinion No. 17 "Intangible Assets". Instead goodwill would be reviewed for impairment, that is, written down and expensed against earnings only in the periods in which the recorded value of goodwill exceeded its implied fair value. The FASB has indicated that a Statement addressing goodwill and intangible assets will be issued in the later half of July 2001. The Statement is expected to require these non-amortization and impairment rules to be applied to existing goodwill and intangible assets beginning with fiscal years starting after December 15, 2001. At February 28, 2001, the Company had goodwill of \$6.2 million, net of accumulated amortization. Amortization of goodwill charged to earnings was \$205,000 for the fiscal year ended February 28, 2001.

Safe Harbor Statement

This Annual Report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements, which are other than statements of historical facts. Forward-looking statements involve risks and uncertainties, which could cause actual results or outcomes to differ materially. The Company's expectations and beliefs are expressed in good faith and are believed by the Company to have a reasonable basis but there can be no assurance that management's expectations, beliefs or projections will be achieved or accomplished. The forward-looking statements in this document are intended to be subject to the safe harbor protection provided under the securities laws. In addition to other factors and matters discussed elsewhere herein, the following are important factors that, in the view of the Company, could cause actual results to differ materially from those discussed in the forward-looking statements: the ability of the Company to continue to expand through acquisitions, the availability of debt or equity capital to fund the Company's expansion program, unusual weather conditions, the effects of competitive pricing and general economic conditions.

Edgar Filing: ACR GROUP INC - Form 10-K

18

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is subject to market risk exposure related to changes in interest rates on its senior credit facility, which includes revolving credit and term notes. These instruments carry interest at a pre-agreed upon percentage point spread from either the prime interest rate or LIBOR. Under its senior credit facility the Company may, at its option, fix the interest rate for certain borrowings based on a spread over LIBOR for 30 days to 6 months. At February 28, 2001 the Company had \$23.3 million outstanding under its senior credit facility. Based on this balance, an immediate change of one percent in the interest rate would cause a change in interest expense of approximately \$233,000, or \$.02 per basic share, on an annual basis.

19

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS OF ACR GROUP, INC. AND SUBSIDIARIES

	Page

Report of Independent Auditors	21
Consolidated balance sheets as of February 28, 2001 and February 29, 2000	22
Consolidated statements of operations for the fiscal years ended February 28, 2001, February 29, 2000 and February 28, 1999	24
Consolidated statements of shareholders' equity for the fiscal years ended February 28, 2001, February 29, 2000 and February 28, 1999	25
Consolidated statements of cash flows for the fiscal years ended February 28, 2001, February 29, 2000 and February 28, 1999	26
Notes to Consolidated Financial Statements	28

20

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Shareholders

Edgar Filing: ACR GROUP INC - Form 10-K

ACR Group, Inc.

We have audited the accompanying consolidated balance sheets of ACR Group, Inc. and subsidiaries as of February 28, 2001 and February 29, 2000, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended February 28, 2001. Our audits also included the financial statement schedule listed in the index at Item 14(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 consolidated financial position of ACR Group, Inc. and subsidiaries at February 28, 2001 and February 29, 2000, and the consolidated results of their operations and their cash flows for each of the three years in the period ended February 28, 2001, in conformity with accounting principles generally accepted in the United States. Also in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth herein.

ERNST & YOUNG LLP

Houston, Texas
May 11, 2001

21

ACR GROUP, INC. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

AS OF FEBRUARY 28, 2001 AND FEBRUARY 29, 2000

ASSETS

	2001 -----	2000 -----
Current assets:		
Cash	\$ 171,249	\$ 107,035
Accounts receivable, net of allowance for doubtful accounts of \$670,432 in 2001 and \$532,300 in 2000	15,975,668	14,358,891
Inventory	23,833,400	18,445,097

Edgar Filing: ACR GROUP INC - Form 10-K

Prepaid expenses and other	642,912	386,896
Deferred income taxes	487,000	487,000
Total current assets	41,110,229	33,784,919
Property and equipment, net of accumulated depreciation	5,768,093	3,689,448
Deferred income taxes	973,000	973,000
Goodwill, net of accumulated amortization of \$897,844 in 2001 and \$693,329 in 2000	6,222,895	6,023,207
Other assets	507,350	370,929
Total assets	\$54,581,567	\$44,841,503

22

ACR GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

AS OF FEBRUARY 28, 2001 AND FEBRUARY 29, 2000

LIABILITIES AND SHAREHOLDERS' EQUITY

	2001	2000
	-----	-----
Current liabilities:		
Current maturities of long-term debt	\$ 826,016	\$ 1,597,790
Current maturities of capital lease obligations	130,185	190,465
Accounts payable	17,146,529	12,182,803
Accrued expenses and other liabilities	1,837,638	1,741,710
Total current liabilities	19,940,368	15,712,768
Long-term debt	24,229,774	17,303,237
Long-term capital lease obligations	264,233	195,615
Total liabilities	44,434,375	33,211,620
Shareholders' equity:		
Preferred stock, \$.01 par, authorized 2,000,000 shares, none outstanding		
Common stock, \$.01 par, authorized 25,000,000 shares, issued and outstanding 10,681,294 shares in 2001 and 10,670,634 shares in 2000	106,813	106,706
Additional paid-in capital	41,691,379	41,696,584

Edgar Filing: ACR GROUP INC - Form 10-K

Accumulated deficit	(31,651,000)	(30,173,407)
	-----	-----
Total shareholders' equity	10,147,192	11,629,883
	-----	-----
Total liabilities and shareholders' equity	\$ 54,581,567	\$ 44,841,503
	=====	=====

The accompanying notes are an integral part of these financial statements

23

ACR GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE FISCAL YEARS ENDED FEBRUARY 28, 2001, FEBRUARY 29, 2000
AND FEBRUARY 28, 1999

	2001	2000	1999
	-----	-----	-----
Sales	\$136,433,240	\$126,468,201	\$117,886,777
Cost of sales	106,981,285	98,333,567	93,115,088
	-----	-----	-----
Gross profit	29,451,955	28,134,634	24,771,689
Selling, general and administrative expenses	(28,726,419)	(24,135,567)	(21,494,841)
Energy services income, net	46,017	78,401	39,783
	-----	-----	-----
Operating income	771,553	4,077,468	3,316,631
Interest expense	(2,487,606)	(2,010,597)	(2,036,484)
Other non-operating income	374,778	414,733	288,178
	-----	-----	-----
Income (loss) before income taxes	(1,341,275)	2,481,604	1,568,325
Provision for income taxes:			
Current	136,318	254,971	153,245
	-----	-----	-----
Net income (loss)	\$ (1,477,593)	\$ 2,226,633	\$ 1,415,080
	=====	=====	=====
Earnings (loss) per common share:			
Basic	\$ (0.14)	\$.21	\$.13
	=====	=====	=====
Diluted	\$ (0.14)	\$.20	\$.12
	=====	=====	=====

Edgar Filing: ACR GROUP INC - Form 10-K

The accompanying notes are an integral part
of these financial statements

24

ACR GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

FOR THE FISCAL YEARS ENDED FEBRUARY 28, 2001, FEBRUARY 29, 2000
AND FEBRUARY 28, 1999

	No. of Shares Issued -----	Par Value -----	Additional Paid-In Capital -----
Balance, February 28, 1998	10,634,017	\$106,340	\$41,669,200
Exercise of options	25,000	250	13,500
Exercise of warrant	286	3	(3)
Issuance of warrant			2,000
Net income			
Balance, February 28, 1999	----- 10,659,303	----- 106,593	----- 41,684,697
Exercise of options	11,331	113	(113)
Issuance of warrant			12,000
Net income			
Balance, February 29, 2000	----- 10,670,634	----- 106,706	----- 41,696,584
Exercise of options	10,660	107	(12,205)
Issuance of warrant			7,000
Net income			
Balance, February 28, 2001	----- 10,681,294 =====	----- \$106,813 =====	----- \$41,691,379 =====

The accompanying notes are an integral part
of these financial statements

25

ACR GROUP, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE FISCAL YEARS ENDED FEBRUARY 28, 2001, FEBRUARY 29, 2000

Edgar Filing: ACR GROUP INC - Form 10-K

AND FEBRUARY 28, 1999

	2001	2000
	-----	-----
Operating activities:		
Net income	\$ (1,477,593)	\$ 2,226,633
Adjustments to reconcile net income		
to net cash provided by operating activities:		
Depreciation	1,036,390	861,342
Amortization	270,469	291,850
Issuance of warrants	7,000	12,000
Provision for bad debts	637,470	568,465
Loss (gain) on sale of assets	37,581	(19,292)
Changes in operating assets and liabilities:		
Accounts receivables	(1,872,974)	(718,317)
Inventory	(5,025,730)	4,079
Prepaid expenses and other assets	(568,968)	86,089
Accounts payable	4,167,589	(2,772,895)
Accrued expenses and other liabilities	80,802	152,022
	-----	-----
Net cash (used in) provided by operating activities	(2,707,964)	691,976
	-----	-----
Investing activities:		
Acquisition of property and equipment	(2,107,952)	(846,998)
Acquisition of businesses, net of cash acquired	(200,643)	-
Proceeds from disposition of assets	50,336	35,148
	-----	-----
Net cash used in investing activities	(2,258,259)	(811,850)
	-----	-----
Financing activities:		
Proceeds from long-term debt	6,621,653	1,686,877
Payments on long-term debt	(1,591,216)	(1,589,549)
Exercise of stock options	-	-
	-----	-----
Net cash provided by financing activities	5,030,437	97,328
	-----	-----
Net increase (decrease) in cash	64,214	(22,546)
	-----	-----
Cash at beginning of year	107,035	129,581
	-----	-----
Cash at end of year	\$ 171,249	\$ 107,035
	=====	=====

(continued)

26

ACR GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE FISCAL YEARS ENDED FEBRUARY 28, 2001, FEBRUARY 29, 2000,
AND FEBRUARY 28, 1999
(CONTINUED)

2001

2000

Edgar Filing: ACR GROUP INC - Form 10-K

Schedule of non-cash investing and financing activities:

Acquisition of subsidiaries:		
Fair value of assets acquired	793,712	
Fair value of liabilities assumed	817,915	
Goodwill	404,203	
Notes payable to sellers	152,000	
Purchase of property and equipment (net of cash):		
For notes payable	825,000	
Under capital leases	271,529	218,
Supplemental cash flow information:		
Interest paid	2,472,050	2,125,
Federal income taxes paid	16,477	35,

The accompanying notes are an integral part
of these financial statements

27

ACR GROUP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1 - Description of Business and Summary of Significant Accounting Policies

Description of Business

ACR Group, Inc.'s (the "Company") principal business is the wholesale distribution of heating, ventilating, air conditioning and refrigeration ("HVACR") equipment, parts and supplies in the southeastern United States, Texas, Nevada, New Mexico, Colorado and California. The Company operates as a single segment.

Principles of Consolidation

The consolidated financial statements include the accounts of ACR Group, Inc. and its subsidiaries, all of which are wholly owned. All significant intercompany accounts and transactions have been eliminated.

Use of Estimates

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

Revenue Recognition

Revenues are recognized when merchandise is either shipped or delivered to the customer.

Inventories

Inventories are valued at the lower of cost or market using the average cost method. Substantially all inventories represent finished goods held for

Edgar Filing: ACR GROUP INC - Form 10-K

sale. The Company has an arrangement with an HVACR equipment manufacturer and a field warehouse agent whereby HVACR equipment is held for sale in bonded warehouses located at the premises of certain of the Company's operations, with payment due only when products are sold. Such inventory is accounted for as consigned merchandise and is not recorded on the Company's balance sheet. The cost of such inventory held in the

28

bonded warehouses was \$11,562,340 at February 28, 2001 and \$11,864,555 at February 29, 2000.

The terms of the consignment agreement with the supplier further provide that the Company must purchase merchandise not sold within a specified period of time. The Company believes that substantially all consigned merchandise will be sold in the ordinary course of business before any purchase obligation is incurred.

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization are provided on the straight-line method over the following estimated useful lives.

Buildings	20-40 years
Leasehold improvements	Primary term of the lease
Furniture and fixtures	5-7 years
Vehicles	3-6 years
Other equipment	3-10 years

Goodwill

Goodwill represents the excess cost of companies acquired over the fair value of their tangible assets. Substantially all goodwill is being amortized on a straight-line basis over 40 years. The carrying value of goodwill is reviewed if the facts and circumstances suggest that it may be impaired. If this review indicates that goodwill will not be recoverable, as determined based on the undiscounted cash flows of the entity acquired over the remaining amortization period, the Company's carrying value of the goodwill will be reduced by the estimated shortfall of the discounted cash flows.

Income Taxes

The Company and its subsidiaries file a consolidated federal income tax return. The Company uses the liability method in accounting for income taxes. Under the liability method, deferred tax assets and liabilities are determined based on differences between 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 differences are expected to reverse.

Stock-Based Compensation

The Company measures compensation cost for stock-based compensation plans using the intrinsic value method of accounting.

29

Supplier/Sources of Supply

The Company currently purchases a majority of its HVACR equipment and

Edgar Filing: ACR GROUP INC - Form 10-K

repair parts from two primary suppliers. The Company has not encountered any significant difficulty to date in obtaining equipment and repair parts to support its operations at current or expected near-term future levels. However, any disruption in these supply sources could have an adverse effect upon the Company's operations.

Recently Issued Accounting Standards

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133, as amended by Statement of Financial Accounting Standard No. 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FAS Statement No. 133" ("SFAS 137") which is effective for fiscal years beginning after June 15, 2000, requires all derivatives to be recognized at fair value on the balance sheet. The Company plans to adopt SFAS 133 beginning with the Company's fiscal year 2002. The change is not expected to have a significant effect on the Company's financial statements.

In February 2001, the Financial Accounting Standards Board ("FASB") issued a revised Exposure Draft, "Business Combinations and Intangible Assets - Accounting for Goodwill". The Exposure Draft would continue to require recognition of goodwill acquired in a business combination as an asset but would not permit amortization of goodwill as currently required by Accounting Principals Board Opinion No. 17 "Intangible Assets". Instead goodwill would be reviewed for impairment, that is, written down and expensed against earnings only in the periods in which the recorded value of goodwill exceeded its implied fair value. The FASB has indicated that a Statement addressing goodwill and intangible assets will be issued in the latter half of July 2001. The Statement is expected to require these non-amortization and impairment rules to be applied to existing goodwill and intangible assets beginning with fiscal years starting after December 15, 2001. At February 28, 2001, the Company had goodwill of \$6.2 million, net of accumulated amortization. Amortization of goodwill charged to earnings was \$205,000 for the fiscal year ended February 28, 2001.

2 - Acquisitions

In January 1999, the Company, through a wholly owned subsidiary, entered into a Purchase Agreement pursuant to which it acquired all of the issued and outstanding capital stock of Beaumont A/C Supply, Inc. ("BACS"), a Texas corporation for \$850,000. As consideration for the acquisition, the Company paid \$521,747 cash and issued a

30

promissory note for \$328,253. The note is due and payable in 12 quarterly installments of principal and interest commencing March 31, 1999. The excess of the final purchase price over the estimated fair value of the net assets acquired was \$456,000, which was recorded as goodwill, to be amortized on a straight-line basis over 10 years. Pro forma results of operations relating to this acquisition are not presented because the effects of the acquisition would not be material.

In March 2000, the Company, through a wholly owned subsidiary, entered into a Purchase Agreement pursuant to which it acquired all of the issued and outstanding capital stock of International Comfort Supply, Inc., a Texas corporation for \$380,000. As consideration for the acquisition, the Company paid \$228,000 cash and issued a promissory note for \$152,000. The note is due and payable in 6 equal semi-annual installments of principal and interest commencing September 1, 2000. The excess of the final purchase price over the

Edgar Filing: ACR GROUP INC - Form 10-K

estimated fair value of the net assets acquired was \$404,203, which was recorded as goodwill, to be amortized on a straight-line basis over 40 years. Pro forma results of operations relating to this acquisition are not presented because the effects of the acquisition would not be considered material.

The acquisitions described above were accounted for using the purchase method of accounting, and the consolidated financial statements include the operating results from the respective dates of acquisition.

3 - Property and Equipment

Property and equipment consisted of the following at the end of February:

	2001	2000
	-----	-----
Land	\$ 309,693	\$ 224,593
Building and leasehold improvements	3,517,616	1,830,967
Furniture and fixtures	230,067	205,029
Vehicles	1,364,892	1,462,752
Other equipment	4,615,316	3,576,185
Energy management equipment	-	223,111
	-----	-----
	10,037,584	7,522,637
Less accumulated depreciation	(4,269,491)	(3,833,189)
	-----	-----
Net property and equipment	\$ 5,768,093	\$ 3,689,448
	=====	=====

31

Capitalized lease assets of \$785,755 and \$1,126,627 together with accumulated amortization of \$265,850 and \$620,762 are included in property and equipment as of February 28, 2001 and February 29, 2000, respectively. Amortization expense is included with depreciation expense.

4 - Debt

Debt is summarized as follows at the end of February:

	2001	2000
	-----	-----
Revolving line of credit	\$22,585,856	\$16,086
Real estate loan	266,220	295
Equipment term loan	157,659	252
Notes payable - Catalyst Fund and affiliate	891,559	1,466
Note payable to sellers of real property	815,299	
Notes payable to sellers of companies		
acquired (note 2)	263,380	742
Other	75,817	57

Edgar Filing: ACR GROUP INC - Form 10-K

	-----	-----
	25,055,790	18,901
Less current maturities	(826,016)	(1,597)
	-----	-----
Long-term debt, less current maturities	\$24,229,774	\$17,303
	=====	=====

The Company has a loan agreement ("Agreement") with a commercial bank ("Bank") that was amended and restated in May 2000 to increase to \$25 million the amount that may be borrowed by the Company under a revolving credit facility and to provide facilities for the purchase of both real estate and capital assets. The Agreement terminates in May 2003, but is automatically extended for one-year periods unless either party gives notice of termination to the other. Prepayment penalties apply if the revolving credit facility is prepaid during the first two years of the term. Restrictive covenants of the Agreement prohibit the Company from paying dividends, prepaying any subordinated indebtedness or incurring certain other debt without the Bank's consent, and also require the Company to maintain certain financial ratios. As of February 28, 2001, the Company was not in compliance with certain of the required financial ratios. In March 2001, the Company and the Bank further amended the Agreement to waive such non-compliance through the end of fiscal 2001 and to revise the required financial ratios for fiscal 2002.

32

The interest rate on borrowings under the revolving credit facility is based on either the Bank's prime rate or LIBOR and varies depending on the Company's leverage ratio, as defined, determined quarterly. As of February 28, 2001, the applicable interest rate was either the prime rate or LIBOR plus 2.75%, and the Company had elected the LIBOR option (9.33%) for substantially all amounts outstanding under the facility. Borrowings under the revolving credit facility are limited to 85% of eligible accounts receivable and 50% of eligible inventory amounts (which increases to 65% of eligible inventory amounts during certain specified months of the year). At February 28, 2001, the Company's available credit under the facility was approximately \$510,000.

The Agreement provides a term loan facility of \$4 million for the purchase of real estate and improvements. At February 28, 2001, the Company's had indebtedness to the Bank under the facility of \$226,220, secured by a deed of trust on both the land and building occupied by a branch facility in the Houston area, which is repaid in equal monthly principal installments of \$2,400, plus interest. The Agreement also provides a capital expenditure term loan facility of \$1 million for capital assets acquired after March 2000 and an acquisition facility of up to \$5 million for the acquisition of other businesses, subject to approval by the Bank of specific transactions. As of February 28, 2001, the Company had not borrowed any amounts under either the capital expenditure facility or the acquisition facility. Both the real estate and the capital expenditures facility bear interest at a variable rate, which was the prime rate or LIBOR plus 2.75% at February 28, 2001. Borrowings under the acquisition facility also bear interest at a variable rate that is generally 0.25% higher than the rate applicable to the other term loan facilities. At February 28, 2001, the Company had outstanding borrowings aggregating \$157,659 under a previous term loan arrangement bank for the purchase of capital assets. Such borrowings are repaid in equal monthly installments of \$7,883, plus interest. In April 2001, the Company borrowed \$487,500 under the real estate term loan facility, and \$429,353 under the capital expenditure facility. Such amounts are to be repaid in equal principal installments over 120 months and 60 months, respectively, plus interest.

In fiscal 1998, the Company obtained loans aggregating \$1.54 million from The

Edgar Filing: ACR GROUP INC - Form 10-K

Catalyst Fund, Ltd. ("Catalyst") and an affiliate of Catalyst to pay certain outstanding indebtedness to St. James Capital Partners, L.P. ("St. James"), and also borrowed \$450,000 from Catalyst for an acquisition. The Company previously borrowed \$1 million from Catalyst in 1993. Such borrowings all bear interest at 12 1/2% per annum, payable monthly, and have varying principal repayment schedules. The aggregate outstanding principal at February 28, 2001 is to be repaid in monthly installments of \$48,750 through August 2001, \$30,000 from September 2001 through December 2002, and the remaining unpaid balance in January 2003. The Catalyst loans are all secured by the stock and operating assets of certain of the Company's subsidiaries and an assignment of proceeds from life insurance policies on the Company's President. Catalyst has subordinated its security interests to the Bank. In connection with the January 1998 loans, the Company

33

granted Catalyst a warrant to purchase 175,000 shares of the Company's common stock at a price of \$2.06 per share, exercisable at any time before February 28, 2003. The proceeds of the January 1998 loans were allocated between the debt and the warrant, resulting in a debt discount of \$50,000, which is being amortized to expense over the term of the loan. In connection with the 1993 loan, the Company granted Catalyst a warrant to purchase 1,000,000 shares of the Company's common stock at a price of \$0.59 per share and, in connection with the amendment to the repayment schedule of the 1993 loan during fiscal 1998, the expiration date of the warrant was extended until February 28, 2003 (see Note 7). Covenants of the Company's loan agreement with Catalyst, which covers all of the Catalyst loans, prohibit dividends and restrict additional borrowings without Catalyst's consent, and also require the Company to maintain specified financial ratios. As of February 28, 2001, the Company was not in compliance with certain of the required financial ratios. In May 2001, Catalyst waived such non-compliance for all periods through fiscal 2001 and for the first three quarters of fiscal 2002.

In August 2000, the Company purchased real estate in Gainesville, Florida to be occupied as a branch operation for approximately \$957,000. Of the purchase price, the sellers financed \$825,000 for a term of 25 years at an interest rate of 8.25% per annum. The note is secured by a deed of trust on the real estate and all improvements.

The notes payable to sellers include debt incurred in connection with three acquisitions from fiscal 1996 to fiscal 1999 and are payable in installments over terms of three to five years. The seller notes payable at February 28, 2001 bear interest at 10% per annum, and are unsecured and subordinated to the Company's indebtedness to the Bank.

Based upon the borrowing rates currently available to the Company for debt instruments with similar terms and average maturities, the carrying value of long-term debt approximates fair value.

Future maturities of debt are \$826,016 in 2002, \$613,452 in 2003, \$22,850,495 in 2004, \$33,459 in 2005, \$32,412 in 2006, and \$699,956 after 2006.

5 - Lease Commitments

The Company leases warehouse and office equipment and vehicles under capital leases. Future minimum lease payments under capital leases are as follows:

34

Edgar Filing: ACR GROUP INC - Form 10-K

Year ending February 28 or 29,	Capital lease payments
-----	-----
2002	\$ 158,898
2003	129,922
2004	86,428
2005	53,777
2006	19,433

Total minimum lease payments	448,458
Less amounts representing interest	(54,040)

Present value of future minimum lease payments	394,418
Less current maturities of capital lease obligations	(130,185)

Long-term obligations under capital leases	\$ 264,233
	=====

Additionally, the Company leases its corporate offices, office and warehouse space occupied by its HVACR operations and office equipment and vehicles under non-cancelable operating lease agreements that expire at various dates through 2010. The leases for its branch facilities often require that the Company pay the taxes, insurance and maintenance expenses related to the leased properties. Certain of the Company's lease agreements include renewal and/or purchase options. Future minimum lease payments under such leases are: \$4,127,863 in 2002, \$3,486,460 in 2003, \$2,789,793 in 2004, \$1,995,036 in 2005, \$1,300,143 in 2006 and \$2,405,694 after 2006.

Rental expenses were \$4,093,554, \$3,012,236 and \$2,414,026 in 2001, 2000 and 1999, respectively.

6 - Income Taxes

The Company recognizes a tax benefit from a net operating loss carryforward if it is more likely than not that such benefit will ultimately be realized. Such a tax benefit is recorded on the balance sheet as a deferred tax asset. To the extent that it cannot be determined that such tax benefit will more likely than not be realized, a valuation allowance is established against the deferred tax asset. The deferred tax asset is classified as current to the extent that a tax benefit is expected to be realized in the next fiscal period. The difference between the income tax provision computed at the statutory federal income tax rate and the financial statement provision for taxes is summarized below:

35

	Year Ended February	
	-----	-----
	2001	2000
	-----	-----
Tax at statutory rate	\$ (456,034)	\$ 84

Edgar Filing: ACR GROUP INC - Form 10-K

Increase (reduction) in tax expense
resulting from:

Change in valuation allowance	7,608,209	(1,558,000)
Nondeductible expenses	87,603	87,603
State income taxes	143,270	143,270
Expired tax credits and expired NOL carryforwards	(7,246,730)	68,000
	-----	-----
Actual income tax provision	\$ 136,318	\$ 25,000
	=====	=====

As of February 28, 2001 and February 29, 2000, the Company had net operating loss carryforwards of \$8.1 million and \$28.9 million, respectively, which are available to offset future taxable income, substantially all of such carryforwards will expire by 2003. In addition, as of February 28, 1999, the Company had investment and research and development tax credit carryforwards of approximately \$0.8 million which expired during fiscal 2000. For financial reporting purposes, the Company has recognized a valuation allowance of \$2.0 million and \$9.0 million as of February 28, 2001 and February 29, 2000, respectively, to offset the deferred tax assets related primarily to the loss carryforward and the credit carryforwards. The decrease in the valuation allowance for fiscal 1999 and 2000 was principally due to the expiration of net operating loss carryforwards. There are no other significant components of the Company's deferred tax assets and liabilities as of February 28, 2001.

7 - Stock Option Agreements and Equity Transactions

Effective March 1, 1998, both the President and the Chief Financial Officer of the Company entered into employment contracts that expire February 28, 2002 and in connection therewith, were granted options to purchase 300,000 and 100,000 shares of the Company's common stock ("Stock"), respectively, at \$2.24 per share. Such options vest on March 1, 2006. The option agreements further provide for accelerated vesting if the market price of Stock, as defined in the agreements, reaches specified levels prior to the stated vesting date. During fiscal 2000 and 2001, the President acquired Stock through the cashless exercise of options that had been granted under a previous employment agreement by redeeming mature shares. In fiscal 2000, he exercised 25,000

36

options at \$0.76 per share, resulting in the net issuance of 11,331 shares of Stock, and in fiscal 2001, he exercised 25,000 options at \$0.77 per share, resulting in the net issuance of 10,660 shares of Stock.

In connection with its financing provided to the Company, St. James received a warrant to acquire 280,000 shares of the Company's common stock at an exercise price of \$1.625 per share, exercisable at any time before January 2002. In connection with its loan to the Company, Catalyst received a warrant to purchase 1,000,000 shares of the Company's common stock at a price of \$.59 per share, exercisable at any time before February 2003. See Note 4. In connection with a January 1998 loan to the Company (see Note 4) Catalyst and an affiliate received warrants to purchase an aggregate of 175,000 shares of the Company's common stock at a price of \$2.06 per share, exercisable at any time before February 2003. Certain of these warrants outstanding, pursuant to which 1,175,000 shares of common stock may be acquired, contain a put option under

Edgar Filing: ACR GROUP INC - Form 10-K

certain limited circumstances. The features enabling the holder to exercise the put option are either within management's control or, at the Company's option, provide for a net cash or net share (non-redeemable preferred shares with a defined coupon rate) settlement.

During fiscal 1999, the Company engaged Magnum Financial Group, L.L.C. ("Magnum") to promote interest in the Company's equity securities. In connection with these activities, Magnum received warrants to acquire 75,000 shares of the Company's common stock with exercise prices for 25,000 shares each at \$2.50, \$3.00 and \$3.50 per share. The warrants are immediately vested and can be exercised at any time before December 2001. The weighted average fair value of the warrants at the date of grant was approximately \$.20 per share and is being recognized as compensation expense over the service period.

In fiscal 1997, the Company established the 1996 Stock Option Plan for key employees and directors of the Company and its subsidiaries. The plan provides for the granting of up to 500,000 non-qualified and/or incentive stock options. 255,500, 161,500 and 134,500 options were granted in fiscal 2001, 2000 and 1998 respectively (none in fiscal year 1999 or 1997) of which 42,000, 24,000 and 19,500 expired in fiscal 2001, 2000 and 1999, respectively, and 34,000 shares of common stock were available for future grants at February 28, 2001. Options granted under the plan are immediately vested.

In fiscal 2002, the Company will revalue certain warrants issued to The Catalyst Fund, Ltd. The warrants to acquire 175,000 shares of the Company's common stock at \$2.06 per share will be revalued to \$0.59 per share. This modification resulted in a new measurement date for the warrants. The cost to revalue said options will be expensed over the remaining term of the loan.

37

A summary of the Company's stock option activity and related information follows:

	Year Ended February 29 or			
	2001		2000	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding - beginning of year	767,500	\$2.09	655,000	\$2.18
Granted	255,500	1.12	161,500	1.50
Exercised	(40,000)	.74	(25,000)	.76
Forfeited	(42,000)	1.31	(24,000)	1.73
	941,000	1.92	767,500	2.09
Outstanding - end of year	941,000	1.92	767,500	2.09
Exercisable - end of year	225,500	2.33	199,667	2.17
Weighted average fair value of				

Edgar Filing: ACR GROUP INC - Form 10-K

The numerator used in the calculations of both basic and diluted earnings per share for all periods presented was net income. The denominator for each period presented was determined as follows:

39

	Year Ended February 28 or 29,		
	2001	2000	1999
Denominator:			
Denominator for basic earnings per share - weighted average shares	10,676,198	10,667,801	10,637,
Effect of dilutive securities:			
Employee stock options	16,260	21,819	49,
Warrants	407,909	582,495	665,
Dilutive potential common shares	424,169	604,314	714,
Denominator for diluted earnings per share - adjusted weighted average shares and assumed conversions	11,100,367	11,272,115	11,351,

10 - Quarterly Results (Unaudited)

In thousands of dollars
(except per share amounts)

	Quarter		
	First	Second	Third
Fiscal Year Ended February 28, 2001			
Sales	\$33,178	\$40,209	\$33,650
Gross Profit	7,115	8,633	7,171
Net Income	200	886	(767)
Earnings Per Common Share:			
Basic	.02	.08	(.07)
Diluted	.02	.08	(.07)
Fiscal Year Ended February 29, 2000			
Sales	\$33,206	\$38,107	\$29,198
Gross Profit	7,196	8,278	6,660
Net Income	652	1,614	381
Earnings Per Common Share:			
Basic	.06	.15	.04
Diluted	.06	.14	.03

40

Edgar Filing: ACR GROUP INC - Form 10-K

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

None

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.

Incorporated by reference.

ITEM 11. EXECUTIVE COMPENSATION.

Incorporated by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

Incorporated by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

Incorporated by reference.

41

PART IV

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

(a) (1) Financial Statements included in Item 8.

See Index to Financial Statements of ACR Group, Inc. set forth in Item 8, Financial Statements and Supplementary Data.

(a) (2) Index to Financial Statement Schedules included in Item 14.

The following financial statement schedule for the years ended February 28, 2001 and 1999 and February 29, 2000 is included in this report:

Schedule II - Valuation and Qualifying Accounts

All other schedules are omitted because they are not applicable or the required information is included in the financial statements or notes thereto.

(a) (3) Exhibits

Edgar Filing: ACR GROUP INC - Form 10-K

The following exhibits are filed with or incorporated by reference into this report. The exhibits which are denoted by an asterisk (*) were previously filed as a part of, and are hereby incorporated by reference from, either (a) Annual Report on Form 10-K for fiscal year ended June 30, 1991 (referred to as "1991 10-K"), or (b) Annual Report on Form 10-K for fiscal year ended February 28, 1993 (referred to as "1993 10-K"), or (c) Form S-8 Registration Statement under the 1933 Act for Registrant, Registration No. 333-16325 filed November 18, 1996 (referred to as "RS 333-16325"), or (d) Current Report on Form 8-K dated January 24, 1997, or (e) Annual Report on Form 10-K for fiscal year ended February 28, 1997 (referred to as "1997 10-K"), or (f) Annual Report on Form 10-K for fiscal year ended February 28, 1998 (referred to as "1998 10-K"), or (g) Annual Report on Form 10-K for fiscal year ended February 29, 2000 (referred to as "2000 Form 10-K").

42

Exhibit Number	Description
-----	-----
* 3.1	Restated Articles of Incorporation (Exhibit 3.1 to 1991 10-K)
* 3.2	Articles of Amendment to Articles of Incorporation (Exhibit 3.2 to 1993 10-K)
* 3.3	Amended and Restated Bylaws (Exhibit 3.2 to 1991 10-K)
* 3.4	Amendment to Bylaws dated December 8, 1992 (Exhibit 3.4 to 1993 10-K)
* 4.1	Specimen of Common Stock Certificate of ACR Group, Inc. (Exhibit 4.1 to 1993 10-K)
*10.1	Employment Agreement between the Company and Alex Trevino, Jr. dated as of March 1, 1998 (Exhibit 10.1 to 1998 10-K)
*10.2	Stock Option Agreement between the Company and Alex Trevino, Jr. dated as of March 1, 1998 (Exhibit 10.2 to 1998 10-K)
*10.3	Employment Agreement between the Company and Anthony R. Maresca dated as of March 1, 1998 (Exhibit 10.3 to 1998 10-K)
*10.4	Stock Option Agreement between the Company and Anthony R. Maresca dated as of March 1, 1998 (Exhibit 10.4 to 1998 10-K)
*10.5	Registration Rights Agreement by and between the Company, Alex Trevino, Jr. and Anthony R. Maresca (Exhibit 10.5 to 1998 10-K)
*10.6	Note Agreement between The Catalyst Fund, Ltd., as Lender, and the Company, ACR Supply, Inc., Fabricated Systems, Inc. and Heating and Cooling Supply, Inc., as Borrowers, dated as of May 27, 1993 (Exhibit 10.18 to 1993 10-K)

43

Edgar Filing: ACR GROUP INC - Form 10-K

- *10.7 First Amendment to Note Agreement by and among The Catalyst Fund, Ltd., the Company, ACR Supply, Inc., Total Supply, Inc. f/k/a Fabricated Systems, Inc., Heating and Cooling Supply, Inc. and West Coast HVAC Supply, Inc., dated as of April 14, 1997 (Exhibit 10.7 to 1998 10-K)
 - *10.8 Second Amendment and Restated Note Agreement by and between the Company, all subsidiaries of the Company, The Catalyst Fund, Ltd., and Southwest/Catalyst Capital, Ltd., dated as of January 28, 1998 (Exhibit 10.8 to 1998 10-K)
 - *10.9 Warrant for the Purchase of 750,000 Shares of Common Stock of the Company issued to The Catalyst Fund, Ltd. dated January 28, 1998 (Exhibit 10.9 to 1998 10-K)
 - *10.10 Warrant for the Purchase of 50,000 Shares of Common Stock of the Company issued to The Catalyst Fund, Ltd. dated January 28, 1998 (Exhibit 10.10 to 1998 10-K)
 - *10.11 Warrant for the Purchase of 125,000 Shares of Common Stock of the Company issued to Southwest/Catalyst Capital, Ltd. dated January 28, 1998 (Exhibit 10.11 to 1998 10-K)
 - *10.12 Registration Rights Agreement between The Catalyst Fund, Ltd. and the Company dated as of January 28, 1998 (Exhibit 10.12 to 1998 10-K)
 - *10.13 Registration Rights Agreement between Southwest/Catalyst Capital, Ltd. and the Company dated as of January 28, 1998 (Exhibit 10.13 to 1998 10-K)
 - *10.14 Amended and Restated Loan and Security Agreement between the Company and Bank of America, N.A. dated as of May 25, 2000. (Exhibit 10.15A to 2000 10-K)
 - 10.15 First Amendment to Amended and Restated Loan and Security Agreement between the Company and Bank of America, N.A. dated as of March 30, 2001.
 - *10.16 Purchase Agreement by and among the Company, Richard O'Leary, Lifetime Filter, Inc. and O'Leary Family Partnership, Ltd. (Exhibit 2.1 to Form 8-K dated January 24, 1997)
- 44
- *10.17 1996 Stock Option Plan of ACR Group, Inc. (Exhibit 4 to RS 333-16325)
 - *10.18 Agreement of Purchase and Sale by and between the Company and St. James Capital Partners, L.P. dated as of January 24, 1997 (Exhibit 10.15 to 1997 10-K)
 - *10.19 10% Convertible Promissory Note of the Company issued to St. James Capital Partners, L.P. dated as of January 24, 1997 (Exhibit 10.16 to 1997 10-K)
 - *10.20 Warrant to Purchase 280,000 Shares of Common Stock of the Company issued to St. James Capital Partners, L.P. dated January 24, 1997 (Exhibit 10.17 to 1997 10-K)

Edgar Filing: ACR GROUP INC - Form 10-K

- *10.21 Registration Rights Agreement between St. James Capital Partners, L.P. and the Company dated as of January 24, 1997 (Exhibit 10.18 to 1997 10-K)
- 21.1 Subsidiaries of the Company
- 23.1 Consent of Independent Auditors

(b) Reports on Form 8-K

No report on Form 8-K was filed during the period from December 1, 2000 to February 28, 2001.

(c) Exhibits

See Item 14(a)(3), above.

45

SCHEDULE II

ACR GROUP, INC. AND SUBSIDIARIES VALUATION AND QUALIFYING ACCOUNTS

FOR THE FISCAL YEARS ENDED FEBRUARY 28, 2001 AND 1999 AND FEBRUARY 29, 2000

Description	Balance at beginning of period	Additions	
		Charged to costs and expenses	Charged to other accounts
Year ended February 28, 2001:			
Allowance for doubtful accounts:			
Accounts receivable	\$532,300	\$637,470	\$ -
Year ended February 29, 2000:			
Allowance for doubtful accounts:			
Accounts receivable	\$684,487	\$568,465	\$ -
Year ended February 28, 1999:			
Allowance for doubtful accounts:			
Accounts receivable	762,709	569,138	9,931(2)

- (1) Accounts/notes and related allowance written off.
- (2) Allowance related to accounts receivable of acquired companies.

46

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities

Edgar Filing: ACR GROUP INC - Form 10-K

Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ACR GROUP, INC.

Date: May 29, 2001

By: /s/ Anthony R. Maresca

Anthony R. Maresca
Senior Vice President and
Chief Financial Officer

Pursuant to the requirement of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature

/s/ Alex Trevino, Jr. ----- Alex Trevino, Jr.	Chairman of the Board, President and Chief Executive Officer (Principal executive officer)	May 29, 2001
/s/ Anthony R. Maresca ----- Anthony R. Maresca	Senior Vice President, Chief Financial Officer and Director (Principal financial and accounting officer)	May 29, 2001
/s/ Ronald T. Nixon ----- Ronald T. Nixon	Director	May 29, 2001
/s/ Roland H. St. Cyr ----- Roland H. St. Cyr	Director	May 29, 2001
/s/ A. Stephen Trevino ----- A. Stephen Trevino	Vice President, General Counsel	May 29, 2001

47

EXHIBIT INDEX

Exhibit Number -----	Description -----
* 3.1	Restated Articles of Incorporation (Exhibit 3.1 to 1991 10-K)
* 3.2	Articles of Amendment to Articles of Incorporation (Exhibit

Edgar Filing: ACR GROUP INC - Form 10-K

3.2 to 1993 10-K)

- * 3.3 Amended and Restated Bylaws (Exhibit 3.2 to 1991 10-K)
- * 3.4 Amendment to Bylaws dated December 8, 1992 (Exhibit 3.4 to 1993 10-K)
- * 4.1 Specimen of Common Stock Certificate of ACR Group, Inc. (Exhibit 4.1 to 1993 10-K)
- *10.1 Employment Agreement between the Company and Alex Trevino, Jr. dated as of March 1, 1998 (Exhibit 10.1 to 1998 10-K)
- *10.2 Stock Option Agreement between the Company and Alex Trevino, Jr. dated as of March 1, 1998 (Exhibit 10.2 to 1998 10-K)
- *10.3 Employment Agreement between the Company and Anthony R. Maresca dated as of March 1, 1998 (Exhibit 10.3 to 1998 10-K)
- *10.4 Stock Option Agreement between the Company and Anthony R. Maresca dated as of March 1, 1998 (Exhibit 10.4 to 1998 10-K)
- *10.5 Registration Rights Agreement by and between the Company, Alex Trevino, Jr. and Anthony R. Maresca (Exhibit 10.5 to 1998 10-K)
- *10.6 Note Agreement between The Catalyst Fund, Ltd., as Lender, and the Company, ACR Supply, Inc., Fabricated Systems, Inc. and Heating and Cooling Supply, Inc., as Borrowers, dated as of May 27, 1993 (Exhibit 10.18 to 1993 10-K)
- *10.7 First Amendment to Note Agreement by and among The Catalyst Fund, Ltd., the Company, ACR Supply, Inc., Total Supply, Inc. f/k/a Fabricated Systems, Inc., Heating and Cooling Supply, Inc. and West Coast HVAC Supply, Inc., dated as of April 14, 1997 (Exhibit 10.7 to 1998 10-K)
- *10.8 Second Amendment and Restated Note Agreement by and between the Company, all subsidiaries of the Company, The Catalyst Fund, Ltd., and Southwest/Catalyst Capital, Ltd., dated as of January 28, 1998 (Exhibit 10.8 to 1998 10-K)
- *10.9 Warrant for the Purchase of 750,000 Shares of Common Stock of the Company issued to The Catalyst Fund, Ltd. dated January 28, 1998 (Exhibit 10.9 to 1998 10-K)
- *10.10 Warrant for the Purchase of 50,000 Shares of Common Stock of the Company issued to The Catalyst Fund, Ltd. dated January 28, 1998 (Exhibit 10.10 to 1998 10-K)
- *10.11 Warrant for the Purchase of 125,000 Shares of Common Stock of the Company issued to Southwest/Catalyst Capital, Ltd. dated January 28, 1998 (Exhibit 10.11 to 1998 10-K)
- *10.12 Registration Rights Agreement between The Catalyst Fund, Ltd. and the Company dated as of January 28, 1998 (Exhibit

Edgar Filing: ACR GROUP INC - Form 10-K

10.12 to 1998 10-K)

- *10.13 Registration Rights Agreement between Southwest/Catalyst Capital, Ltd. and the Company dated as of January 28, 1998 (Exhibit 10.13 to 1998 10-K)
- *10.14 Amended and Restated Loan and Security Agreement between the Company and Bank of America, N.A. dated as of May 25, 2000. (Exhibit 10.15A to 2000 10-K)
- 10.15 First Amendment to Amended and Restated Loan and Security Agreement between the Company and Bank of America, N.A. dated as of March 30, 2001.
- *10.16 Purchase Agreement by and among the Company, Richard O'Leary, Lifetime Filter, Inc. and O'Leary Family Partnership, Ltd. (Exhibit 2.1 to Form 8-K dated January 24, 1997)
- *10.17 1996 Stock Option Plan of ACR Group, Inc. (Exhibit 4 to RS 333-16325)
- *10.18 Agreement of Purchase and Sale by and between the Company and St. James Capital Partners, L.P. dated as of January 24, 1997 (Exhibit 10.15 to 1997 10-K)
- *10.19 10% Convertible Promissory Note of the Company issued to St. James Capital Partners, L.P. dated as of January 24, 1997 (Exhibit 10.16 to 1997 10-K)
- *10.20 Warrant to Purchase 280,000 Shares of Common Stock of the Company issued to St. James Capital Partners, L.P. dated January 24, 1997 (Exhibit 10.17 to 1997 10-K)
- *10.21 Registration Rights Agreement between St. James Capital Partners, L.P. and the Company dated as of January 24, 1997 (Exhibit 10.18 to 1997 10-K)
- 21.1 Subsidiaries of the Company
- 23.1 Consent of Independent Auditors