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

FORM 10-Q

(Mark One)

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

For the quarterly period ended August 31, 2003

OR

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

For the transition period from ______ to ______

Commission File number 0-18716

MATRIX SERVICE COMPANY
(Exact name of registrant as specified in its charter)

DELAWARE	73-1352174
(State of incorporation)	(I.R.S. Employer Identification No.)

10701 E. Ute St., Tulsa, Oklahoma 74116-1517
(Address of principal executive offices and zip code)

Registrant's telephone number, including area code: (918) 838-8822

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of October 10, 2003, there were 9,642,638 shares of the Company's common stock, $0.01 par value per share, issued and 8,165,678 shares outstanding.

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PART I

FINANCIAL INFORMATION

ITEM 1. Financial Statements

Matrix Service Company
Consolidated Statements of Income
(in thousands, except share and per share data)

	Three Months Ended August 31, (unaudited)	
	2003	**2002**
Revenues	$ 158,762	$ 53,717
Cost of revenues	145,681	47,259
Net earnings of joint venture	857	—
Gross profit	13,938	6,458
Selling, general and administrative expenses	6,841	4,271
Restructuring, impairment and abandonment cost	(2)	(169)
Operating income	7,099	2,356
Other income (expense):		
Interest expense	(672)	(94)
Interest income	11	8
Other	66	293
Income before income tax expense	6,504	2,563
Provision for federal, state and foreign income tax expense	2,639	987
Net income	$ 3,865	$ 1,576
Earnings per share of common stock:		
Basic	$ 0.48	$ 0.20
Diluted	$ 0.45	$ 0.19
Weighted average number of common shares:		
Basic	8,091,799	7,858,532
Diluted (includes dilutive effect of stock options)	8,664,920	8,251,207

See Notes to Consolidated Financial Statements

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Matrix Service Company
Consolidated Balance Sheets
(in thousands)

	August 31, 2003	May 31, 2003
	(unaudited)	
ASSETS:		
Current assets:		
Cash and cash equivalents	$ 647	$ 775
Accounts receivable, less allowances (August 31-$1,093; May 31-$900)	59,675	66,603
Costs and estimated earnings in excess of billings on uncompleted contracts	32,909	23,421
Inventories	3,050	2,850
Income tax receivable	—	2,309
Deferred income taxes	1,899	2,479
Prepaid expenses	2,614	2,997
Total current assets	100,794	101,434
Property, plant and equipment at cost:		
Land and buildings	24,514	24,517
Construction equipment	29,615	28,768
Transportation equipment	11,393	11,260
Furniture and fixtures	6,010	6,142
Construction in progress	4,319	4,419
	75,851	75,106
Less accumulated depreciation	28,805	27,743
Net property, plant and equipment	47,046	47,363
Goodwill	51,276	51,292
Other assets	2,845	2,850
Total assets	$ 201,961	$ 202,939

See Notes to Consolidated Financial Statements

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Matrix Service Company
Consolidated Balance Sheets
(in thousands)

	August 31, 2003	May 31, 2003
	(unaudited)	
LIABILITIES AND STOCKHOLDERS' EQUITY:		
Current liabilities:		
Accounts payable	$ 38,930	$ 40,684
Billings on uncompleted contracts in excess of costs and estimated earnings	21,938	22,794
Joint venture	—	1,013
Accrued insurance	1,913	1,736
Income tax payable	1,430	1,570
Other accrued expenses	15,797	9,604
Current portion of long-term debt	4,414	4,892
Current portion of acquisition payable	974	854
Total current liabilities	85,396	83,147
Long-term debt	30,289	38,220
Acquisition Payable	7,671	7,682
Deferred income taxes	3,597	3,709
Stockholders' equity:		
Common stock	96	96
Additional paid-in capital	53,104	52,527
Retained earnings	30,169	26,304
Accumulated other comprehensive income	(542)	(567)
	82,827	78,360
Less: Treasury stock, at cost – August 31- 1,477,360 and May 31- 1,570,260	(7,819)	(8,179)
Total stockholders' equity	75,008	70,181
Total liabilities and stockholders' equity	$ 201,961	$ 202,939

See Notes to Consolidated Financial Statements

Matrix Service Company
Consolidated Statements of Cash Flow
(in thousands)

	Three Months Ended August 31, (unaudited)	
	2003	**2002**
Cash flow from operating activities:		
Net income	$ 3,865	$ 1,576
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,563	1,267
Deferred income tax	468	(52)
Gain on sale of equipment	(2)	(57)
Accretion of acquisition payable	109	—
Earnings of joint venture	(857)	—
Changes in current assets and liabilities increasing (decreasing) cash:		
Accounts receivable	9,113	(540)
Costs and estimated earnings in excess of billings on uncompleted contracts	(9,488)	1,506
Inventories	(200)	115
Prepaid expenses	383	(136)
Accounts payable	(4,991)	(3,744)
Billings on uncompleted contracts in excess of costs and estimated earnings	(3,362)	375
Accrued expenses	6,334	(1,773)
Income taxes receivable/payable	2,169	964
Other	(101)	—
Net cash used by operating activities	5,003	(499)
Cash flow from investing activities:		
Capital expenditures	(1,259)	(3,703)
Distribution from joint venture	701	—
Net effect of dissolution of joint venture	2,738	—
Proceeds from other investing activities	13	75
Net cash used in investing activities	$ 2,193	$ (3,628)

Cash flows from financing activities:		
Issuance of long-term debt	$ 67,570	$ 30,255
Repayments of long-term debt	(75,820)	(25,970)
Purchase of treasury stock	—	34
Issuance of stock	938	—
Net cash provided in financing activities	(7,312)	4,319
Effect of exchange rate changes on cash	(12)	(20)
Increase (Decrease) in cash and cash equivalents	(128)	172
Cash and cash equivalents at beginning of period	775	826
Cash and cash equivalents at end of period	$ 647	$ 998

See Notes to Consolidated Financial Statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1 – BASIS OF PRESENTATION

The consolidated financial statements include the accounts of Matrix Service Company (“Matrix”) and its subsidiaries, all of which are wholly owned. All significant inter-company balances and transactions have been eliminated in consolidation. Effective July 28, 2003, a construction joint venture partnership obtained in the Hake acquisition was dissolved. From the effective date forward, the operations of the joint venture assumed by Matrix are included in Matrix’s results of operations.

The accompanying unaudited consolidated financial statements have been prepared in accordance with Rule 10-01 of Regulation S-X for interim financial statements required to be filed with the Securities and Exchange Commission and do not include all information and footnotes required by generally accepted accounting principles for complete financial statements. However, the information furnished reflects all adjustments, consisting only of normal recurring adjustments that are, in the opinion of management, necessary for a fair statement of the results for the interim periods.

Certain amounts in prior period financial statements have been reclassified to conform to the current financial statement presentation.

The accompanying financial statements should be read in conjunction with the audited financial statements for the year ended May 31, 2003, included in Matrix’s Annual Report on Form 10-K for the year then ended. Matrix’s business is seasonal; therefore, results for any interim period may not necessarily be indicative of future operating results.

NOTE 2 – STOCK OPTION PLANS

Employee stock options are accounted for under Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees” (APB 25) and related interpretations. Under APB 25, because the exercise price of the Company’s employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized.

Pro forma information regarding interim net income and earnings per share is required by Statement of Financial Accounting Standards No. 123 and No. 148, and has been determined as if the Company had accounted for its employee stock options under the fair value method of that Statement. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions: risk-free interest rates of 2.21% to 6.74%; dividend yield of 0.0%; volatility factors of the expected market price of the Company’s stock of .420 to .860; and an expected life of the options of 2 to 5 years.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation."

	Three Months Ended August 31, (unaudited)	
	2003	2002
	(in thousands)	
Net Income as Reported	$3,865	$1,576
Compensation Expense from Stock Options	93	85
Pro Forma Net Income	$3,772	$1,491
Earnings per Common Share as Reported:		
Basic	$ 0.48	$ 0.20
Diluted	$ 0.45	$ 0.19
Pro Forma Earnings per Common Share:		
Basic	$ 0.47	$ 0.19
Diluted	$ 0.44	$ 0.18

NOTE 3 – SEGMENT INFORMATION

Matrix operates primarily in the United States and has operations in Canada. Prior to the acquisition of The Hake Group of Companies ("Hake") in the 4th quarter of fiscal 2003, Matrix was organized into three reportable segments – Aboveground Storage Tank Services, Plant Services and Construction Services. As a result of the Hake acquisition, the structure of the Company's internal organization changed in a manner that caused the Company's reportable segments to change. Matrix now has two reportable segments – Construction Services and Repair & Maintenance Services. The corresponding items of segment information for earlier periods have been restated.

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	Construction Services	Repair & Maintenance Services	Other	Combined Total
Three Months ended August 31, 2003		(in millions)		
Gross revenues	$ 126.4	$ 35.4	$ —	$ 161.8
Less: Inter-segment revenues	(3.0)	—	—	(3.0)
Consolidated revenues	123.4	35.4	—	158.8
Gross profit	10.7	3.2	—	13.9
Operating income	6.1	1.0	—	7.1
Income before income tax expense	5.7	.8	—	6.5
Net income	3.4	.5	—	3.9
Segment assets	83.7	36.0	82.3	202.0
Capital expenditures	.6	.7	—	1.3
Depreciation and amortization expense	.9	.7	—	1.6
Three Months ended August 31, 2002				
Gross revenues	$ 34.0	$ 23.8	$ —	$ 57.8
Less: Inter-segment revenues	(4.1)	—	—	(4.1)
Consolidated revenues	29.9	23.8	—	53.7
Gross profit	4.0	2.5	—	6.5
Operating income	1.7	.5	.2	2.4
Income before income tax expense	1.7	.7	.2	2.6
Net income	1.1	.4	.1	1.6
Segment assets	39.2	39.8	23.5	102.5
Capital expenditures	1.9	1.8	—	3.7
Depreciation and amortization expense	.7	.6	—	1.3

NOTE 4 – ACQUISITION

On March 7, 2003, Matrix acquired all of the issued and outstanding capital stock of Hake Group, Inc. as well as all of the issued and outstanding minority interests in the majority-owned subsidiaries of Hake Group, Inc. As a result, Matrix acquired 100% ownership interests in Hake Group, Inc. and its subsidiaries (“Hake”). Also included in the acquisition was a 50% membership interest in Ragner Hake, LLC, a construction joint venture. Hake’s operating results have been included in Matrix’s consolidated financial statements since the acquisition date.

The acquisition was accounted for by the purchase method, and the purchase price of $54.0 million has been allocated to the assets acquired and liabilities assumed, based upon the estimated fair values of these assets and liabilities at the date of acquisition. The preliminary allocation of the purchase price to specific assets and liabilities was based, in part, upon outside appraisals of the fair value of Hake’s property, plant, equipment, and identifiable assets. The final purchase price is subject to adjustments, including a working capital adjustment and finalization of certain contracts. Expectations are that these will be finalized by March 2004. In addition, the Company recorded an accrual for estimated restructuring charges as part of the purchase price allocation. The restructuring charges primarily relate to provisions for costs of redundant facilities and functions. As the restructuring plan is completed, the accrual and purchase price allocation will be adjusted.

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The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of the acquisition:

	At March 7, 2003
	(in thousands)
Current Assets	$ 51,304
Property, Plant & Equipment	5,712
Intangible Assets	100
Goodwill	40,160
Total Assets acquired	97,276
Current Liabilities	40,691
Restructuring Accrual	1,500
Non-current Liabilities	1,076
Total Liabilities assumed	43,267
Net Assets acquired	$ 54,009

Matrix has not yet determined the assignment of Hake goodwill to specific reporting units. Currently, Hake goodwill is reported as part of the Other reporting segment. The goodwill of $40.2 million was recorded based on purchase price allocation, which represents the excess of purchase price paid to the estimated fair value of the net assets at date of acquisition.

NOTE 5 – REPORTING ACCUMULATED OTHER COMPREHENSIVE INCOME/LOSS

Other comprehensive income (loss) and accumulated other comprehensive income (loss) consisted of foreign currency translation adjustments and fair value adjustments of derivative instruments.

	Three Months Ended August 31, (unaudited)	
	2003	2002
	(in thousands)	
Net income	$3,865	$1,576
Other comprehensive income/(loss)	25	(181)
Comprehensive income	$3,890	$1,395

NOTE 6 – INCOME TAXES

Deferred income taxes are computed using the liability method whereby deferred tax assets and liabilities are recognized based on temporary differences between financial statement and tax basis of assets and liabilities using presently enacted tax rates.

NOTE 7 – NEW ACCOUNTING STANDARDS

The Financial Accounting Standards Board issued SFAS No. 143, "Accounting for Asset Retirement Obligation". SFAS No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The Company's adoption of the Statement effective June 1, 2003 did not have a material impact.

NOTE 8 – DEBT

At August 31, 2003, $3.0 million was outstanding under the Company's revolving bank credit agreement at LIBOR interest rates of 3.35% and 3.36%. There was $30.8 million remaining in availability with $9.5 million utilized by outstanding letters of credit which mature in 2003 and 2004. At August 31, 2003, the balance on the term loan stood at $31.3 million at LIBOR interest rates of 3.60% and 3.82%.

NOTE 9 – CONTINGENCIES

Unapproved Change Orders and Claims

As of August 31, 2003, accounts receivable and costs and estimated earnings in excess of billings on uncompleted contracts included revenues for unapproved change orders of approximately $4.8 million and claims of approximately $2.9 million. Generally, amounts related to unapproved change orders and claims will not be paid by the customer to Matrix until final resolution of related claims, and accordingly, collection of these amounts may extend beyond one year.

Insurance Reserves

The Company is insured for worker's compensation, auto, general liability, pollution, and property claims with deductibles for self-insured retention of $500,000, $500, $50,000, $25,000, and $10,000 per incident, respectively. Management estimates the reserve for such claims based on knowledge of the circumstances surrounding the claims, the nature of any injuries involved, historical experience, and estimates of future costs provided by certain third parties. Accrued insurance at August 31, 2003 represents management's estimate of the Company's liability at that date. Changes in the assumptions underlying the accrual could cause actual results to differ from the amounts reported in the financial statements.

Matrix, as plaintiff, is currently in litigation in the Tulsa County district court in the State of Oklahoma over matters arising out of a workers compensation program with a former insurance provider. These matters involve contests over a letter of credit ("LOC") for $2.2 million, a bond for $2.1 million, and cash of $0.6 million pledged to secure Matrix's obligations under this prior program. The defendants filed a motion to transfer venue to the courts in Bermuda. A hearing on this motion and on whether current court ordered restraints on the collateral will remain in place was held on October 30, 2002. Venue was left in Tulsa County and the restraints on the collateral were left in place with the parties agreeing to negotiate terms satisfactory to both sides. Matrix agreed to replace the LOC and Bond with a strengthened LOC which will provide Matrix with more protection against the proceeds of the LOC being utilized for anything except issues directly related to Matrix's obligations under the workers compensation program. Matrix executed a letter of intent that requires the LOC to be reissued in a form mutually acceptable to both sides, requires the former insurance provider to pay all cash to the current provider for Matrix's claims, provides a process for the LOC's value to decline to zero based on an actuarial evaluation of potential claims, and also requires the Tulsa County action to be dismissed with prejudice (cannot refile). The parties have agreed to the form of the strengthened LOC in principle and the remaining issue is the form of trust account where any cash or receivables that are owed to Matrix will be deposited in such account for the sole benefit of Matrix. The insurance provider is awaiting final approval in a Pennsylvania State Court to determine the form of trust account for all policy holders similarly situated. There are no outstanding unpaid or pending claims with the former insurance provider. No amounts are reserved related to this issue.

Environmental Dispute

In March 2003, the South Coast Air Quality Management District ("AQMD") of the State of California filed a complaint in the Los Angeles County Superior Court for the Central District against a Matrix customer alleging multiple violations by the customer at its West Coast refinery for failure to comply with District Rules 203, 463, 1173, 1176, and 2004 of the AQMD that established a self-inspection and compliance reporting program for above ground stationary tanks used to store crude oil, gasoline and other petroleum products. The AQMD seeks damages of $320 million from the customer, which is a major, multi-national producer and refiner of oil and gas and a marketer of petroleum based products throughout the United States and many foreign countries.

Of the 54 causes of action made in the complaint, 31 relate to alleged violations of part (e) of Rule 463 for knowingly falsifying inspection reports, failing to conduct self-inspection of certain specified tanks, failing to bring non-complying tanks into compliance, and failing to comply with the reporting and record keeping requirements of Rule 463(e).

Matrix is not named in the AQMD complaint; however, counsel for the customer have made a formal demand upon Matrix to assume defense of the case and to indemnify them for any damages it may incur. The customer's demand was made pursuant to the terms of a Master Services Agreement entered into in May 1999 between Matrix and the customer. Matrix rejected the demands of the customer based upon its own belief as to the proper interpretation of the Master Services Agreement and the facts developed by Matrix since the AQMD filed its complaint in March 2003.

In response to the continued disagreement between the customer and Matrix, in June 2003, Matrix filed a declaratory judgment action against the customer in the Federal District Court for the Northern District of Oklahoma, seeking a declaration by the Court that the allegations by the customer against Matrix did not constitute a breach of the Master Services Agreement. Following a meeting between senior management of Matrix and the customer, Matrix and the customer mutually agreed to toll the dispute for at least four years and until there is resolution of the complaint filed by the AQMD against the customer, Matrix agreed to dismiss without prejudice its pending declaratory judgment action, the customer designated a senior officer that Matrix could contact directly if matters seemed to be road blocked again and the customer renewed a commitment to continue to provide Matrix with opportunities for work and new projects.

Despite what appears to be a favorable outcome to Matrix to date, the significant claim made by the AQMD against the customer remains outstanding. And while the exiting relationship between Matrix and its customer may be very positive, the possibility of incurring a significant civil penalty may still cause the customer to assert claims against Matrix that it believes may be valid under the Master Services Agreement. Matrix is not a party to any litigation regarding this matter and has conducted no discovery to date other than a review of its own records. There can be no assurance that Matrix will not become a party in litigation relating to this matter or what the outcome of any such litigation would be given the inherent uncertainty as to the outcome of any litigation.

Joint Venture Dispute

In March 2000, the Company entered into a joint venture partnership agreement for the construction of a pulp and paper project. In May 2001, the joint venture became impaired and Matrix fully reserved the net investment amount. Trade receivables include a $1.3 million balance from this affiliated joint venture, which is believed to be fully recoverable. The joint venture is currently in litigation with the owner of the pulp and paper project and has indicated recoveries sought are in excess of the payable to Matrix.

Bankrupt Customer

On September 30, 2003, a customer of Matrix filed for Chapter 11 bankruptcy protection. Matrix has accounts receivable and costs and estimated earnings in excess of billings on uncompleted contracts from the customer of approximately $5 million at August 31, 2003. As a result of the customer’s bankruptcy, the Company has provided a reserve for its estimated potential loss, which management believes is adequate. Matrix will continue to assess the adequacy of the reserve as additional information becomes available.

Other

The Company is a defendant in various other legal actions and is vigorously defending against each of them. It is the opinion of management that none of such legal actions will have a material effect on the Company’s financial position.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Forward Looking Statements

Certain matters discussed in this report include forward-looking statements. Forward-looking statements can generally be identified or recognized as those statements predicated upon or preceded by words such as "believes," "anticipates," "expects," "plans," "estimates," "should," "could" or similar expressions. Matrix is making these forward-looking statements in reliance on the "safe harbor" protections provided under the Private Securities Litigation Reform Act of 1995.

Forward-looking statements are subject to a number of uncertainties that could cause actual results to differ materially from any results projected, forecasted, estimated, or budgeted, including the following:

- The timing and planning of maintenance projects at customer facilities in the refinery industry, which could cause adjustments for seasonal shifts in product and service demands.
- Changes in general economic conditions in the United States.
- Changes in laws and regulations to which Matrix is subject, including tax, environmental, and employment laws and regulations.
- The cost and effects of legal and administrative claims and proceedings against Matrix or its subsidiaries.
- Conditions of the capital markets Matrix utilizes to access capital to finance operations.
- The ability to raise capital in a cost-effective way.
- The effect of changes in accounting policies.
- The ability to manage growth and to assimilate personnel and operations of acquired businesses, specifically related to the acquisition of the Hake Group of Companies.
- The ability to control costs.
- Severe weather, which could cause project delays and/or a decline in labor productivity.
- Changes in foreign economies, currencies, laws, and regulations, especially in Canada where Matrix has made direct investments.
- Political developments in foreign countries, especially in Canada where Matrix has made direct investments.
- The ability of Matrix to develop expanded markets and product or service offerings as well as its ability to maintain existing markets.
- The need to develop a learning curve in bidding and managing projects in a new industry.
- Technological developments, high levels of competition, lack of customer diversification, and general uncertainties of governmental regulation in the energy industry.
- The ability to recruit, train and retain project supervisors with substantial experience.
- A downturn in the petroleum storage operations or hydrocarbon processing operations of the petroleum and refining industries.
- Changes in the labor market conditions that could restrict the availability of workers or increase the cost of such labor.
- The negative effects of a strike or work stoppage.
- Exposure to construction hazards related to the use of heavy equipment with attendant significant risks of liability for personal injury and property damage.
- The use of significant production estimates for determining percent complete on construction contracts could produce different results upon final determination of project scope.
- The inherent inaccuracy of estimates used to project the timing and cost of exiting operations of non-core businesses.
- The risk associated with a potential bankruptcy of a customer or subcontractor.

Results of Operations

THREE MONTHS ENDED AUGUST 31, 2003 COMPARED TO AUGUST 31, 2002

Consolidated Overview

Prior to the acquisition of The Hake Group of Companies (“Hake”) in the 4th quarter of fiscal 2003, Matrix was organized into three reportable segments – Aboveground Storage Tank Services, Plant Services and Construction Services. As a result of the Hake acquisition, the structure of the Company’s internal organization changed in a manner that caused the Company’s reportable segments to change. Matrix now has two reportable segments – Construction Services and Repair & Maintenance Services. The corresponding items of segment information for earlier periods have been restated. All operations are contained within these segments. Therefore, significant fluctuations in revenues, gross profits, and operating income will be discussed below. Matrix’s revenues fluctuate based on the changing product mix and are dependent on the level and timing of customer releases of new business and on other matters such as project schedules.

Consolidated selling, general and administrative cost as a percent of revenue decreased to 4.3% for the quarter ended August 31, 2003 compared to 8.0% for the quarter ended August 31, 2002. This reduction of 46.3% is the result of leveraging the fixed cost structure with an increasing volume of business.

Other income in the first quarter of fiscal 2003 consisted largely of $0.2 million in proceeds from an insurance settlement for flood damage sustained at our Houston facility in fiscal 2002.

The effective tax rates for the quarters ended August 31, 2003 and 2002 were 40.6% and 38.5% respectively. The increase is due to Matrix’s Federal tax rate increasing 1% and the generation of more income in states with higher tax rates.

Construction Services

Revenues for Construction Services in the quarter ended August 31, 2003 were $123.4 million, compared to $29.9 million in the comparable quarter of the prior year, an increase of $93.5 million or 312.7% due to significantly higher construction work on the east coast primarily from the Hake Group of Companies, which was acquired by Matrix in March 2003. In addition, continued growth in construction revenues from Matrix’s west coast operations contributed to the increase. These increases were partially offset by declines in new tank construction and product sales.

Construction Services gross margins declined from 13.4% in the first quarter of fiscal 2003 to 8.7% in the first quarter of fiscal 2004 due to the inclusion of lower margin Hake work in the mix of business, including two large power projects and a Chapter 11 filing on September 30, 2003 by one of Hake’s customers, to lower margins on new tank construction, and to a lower volume of product sales. In addition, gross margins were negatively impacted by the dissolution of a joint venture partnership that was previously acquired as a part of the Hake acquisition in March 2003. The Company is now performing low margin work that was previously performed by the joint venture. Gross profit increased from $4.0 million in the first quarter of fiscal 2003 to $10.7 million in the first quarter of fiscal 2004, an increase of 167.5% due primarily to an increase in the volume of business which was partially offset by lower margins.

Operating income and income before income tax expense for the quarter ended August 31, 2003 of $6.1 million and $5.7 million respectively, were significantly better than the $1.7 million and $1.7 million respectively produced for the quarter ended August 31, 2002 primarily as a result of the higher gross profits partially offset by higher interest and selling, general and administrative expenses.

Repair & Maintenance Services

Revenues from Repair & Maintenance Services increased 48.7% from $23.8 million in the first quarter of fiscal 2003 to $35.4 million in the first quarter of fiscal 2004. The increase of $11.6 million was due primarily to the inclusion of Hake repair and maintenance service activity and moderate growth in tank repair and maintenance work. Routine plant maintenance and turnaround activity increased in the first quarter of fiscal 2004 as compared to the first fiscal quarter of fiscal 2003, but continued to be below expectations.

Gross margins of 9.0% for the quarter ended August 31, 2003 were lower than the gross margins of 10.5% for the quarter ended August 31, 2002 due primarily to the inclusion of lower margin Hake repair and maintenance work and a decline in the level of routine plant maintenance and turnaround activities which were insufficient to cover the higher fixed cost structure resulting from Matrix's geographical expansion last year. Gross profit increased from $2.5 million in the first quarter of fiscal 2003 to $3.2 million in the first quarter of fiscal 2004, an increase of 28.0% due to the increased volume of business, partially offset by the lower margins.

Operating income for the quarter ended August 31, 2003 of $1.0 million increased from $0.5 million for the quarter ended August 31, 2002 primarily due to increased gross profit. Income before income tax expense increased from $0.7 million for the first quarter of fiscal 2003 to $0.8 million for the first quarter of fiscal 2004 as higher gross profits were mostly offset by higher interest and selling, general and administrative expenses.

Financial Condition & Liquidity

Matrix's cash and cash equivalents totaled approximately $0.6 million at August 31, 2003 and $0.8 million at May 31, 2003.

Matrix has financed its operations recently with cash from operations and from advances under a credit agreement. In connection with the acquisition of Hake on March 7, 2003, the Company replaced its existing credit agreement with a new $87.5 million senior credit facility entered into with a group of banks. The agreement was subsequently amended and restated on May 22, 2003. The credit agreement for borrowings consists of a five-year term loan up to $32.5 million and a three-year $55 million revolving credit facility. Availability under the revolving credit facility is based on Matrix's level of eligible accounts receivable. The Company pays either Prime or LIBOR-based interest on funds borrowed under the term loan while funds borrowed on a revolving basis can also bear interest on a Prime or LIBOR-based option. At August 31, 2003, $3.0 million was outstanding under the revolver and $31.3 million was outstanding under the five-year term loan. In addition, $9.5 million of the revolver was utilized by outstanding letters of credit, which mature in 2003 and 2004. $30.8 million remains available under the revolver at August 31, 2003. At August 31, 2003, the Company was paying interest of 3.60% and 3.82% on the term loans and interest of 3.35% and 3.36% on the revolver. The credit agreement requires maintenance of certain financial ratios, limits the amount of additional borrowings, and prohibits the payment of dividends. The credit facility is secured by all accounts receivable, inventory, intangibles, real property, and proceeds related thereto of Matrix and certain of its subsidiaries, including Hake Group of Companies.

Effective June 1, 2001, the Company entered into an interest rate swap agreement for an initial notional amount of $6.0 million with a commercial bank, effectively providing a fixed interest rate of 7.23% for the five-year period on the term note of the Company's previous credit facility. The Company pays 7.23% and receives LIBOR + 1.5% calculated on the notional amount. Net receipts or payments under the agreement will be recognized as an adjustment to interest expense. At August 31, 2003, the balance on the notional amount stood at $5.1 million at an interest rate of 2.62%. The fair value of the swap at August 31, 2003 was a liability of $0.4 million. The swap agreement expires in 2006. If LIBOR decreases, interest payments received and the market value of the swap position also decrease.

Operations of Matrix provided $5.0 million of cash for the three months ended August 31, 2003 as compared with using $0.5 million of cash for the three months ended August 31, 2002, representing an increase of approximately $5.5 million. The increase was due primarily to the increase in net income coupled with decreased working capital needs in the current year as compared to the prior year.

Capital expenditures during the three months ended in August 31, 2003 totaled approximately $1.3 million primarily for the purchase of transportation equipment, small tools, and construction and fabrication equipment. $9.0 million has been budgeted for total capital expenditures for fiscal 2004.

In August 1998, the Board of Directors authorized a purchase of 142,000 shares of Matrix stock. In March 1999, the Board of Directors authorized the Initial Stock Buyback Program, which permitted the purchase of up to $4,000,000 in Matrix stock. Under this Initial Program, Matrix purchased 958,200 shares. In October 2000, the Board of Directors authorized the Second Stock Buyback Program, which permitted the purchase of up to 20% (i.e., 1,723,753 shares) of the common stock outstanding at that time. To date, Matrix has purchased 1,058,400 shares under the Second Program and has authorization to purchase an additional 665,353 shares.

It is Matrix's intent to utilize these purchased treasury shares solely for the satisfaction of stock issuance under its 1990 and 1991 Incentive Stock Option Plans, its 1995 Nonemployee Director Stock Option Plan and its proposed 2003 Stock Option Plan that will be submitted to stockholders for their approval at the next annual meeting of stockholders.

Matrix believes that its existing funds, amounts available from borrowing under its existing credit agreement, and cash generated by operations will be sufficient to meet the working capital needs through fiscal 2004 and for the foreseeable time thereafter unless significant expansions of operations not now planned are undertaken, in which case Matrix would need to arrange additional financing as a part of any such expansion.

The preceding discussion contains forward-looking statements including, without limitations, statements relating to Matrix' plans, strategies, objectives, expectations, intentions, and adequate resources that are made pursuant to the "safe harbor" provision of the Private Securities Litigation Reform Act of 1995. Readers are cautioned that such forward-looking statements contained in the financial condition and liquidity section are based on certain assumptions, which may vary from actual results. Specifically, the capital expenditure projections are based on management's best estimates, which were derived utilizing numerous assumptions of future events.

Outlook

The environment for capital work is very positive both for work under contract and bidding activity. The Construction Services' backlog at the end of the quarter was $207 million. Repair and Maintenance Services remain soft although we are anticipating a pick-up by the middle of our fiscal year, particularly in turnaround work, which should have a positive impact on gross margins. Although Matrix is anticipating record results for fiscal 2004, the Company is still concerned with the slow activity in repair and maintenance and the final outcome of its customer's Chapter 11 filing. As a result, the Company is holding its earnings guidance for fiscal 2004 at a range of $1.50 to $1.65 per fully diluted share despite very strong earnings in the first quarter of fiscal 2004. Revenues are anticipated to be in a range of $525 to $550 million.

Environmental

Matrix is a participant in certain environmental activities in various stages involving assessment studies, cleanup operations, and/or remedial processes.

In connection with our sale of Brown and affiliated entities in 1999, environmental assessments turned up a number of deficiencies relating to storm water permitting, air permitting, asbestos, soil and water contamination, and waste handling and disposal. Appropriate State of Georgia agencies were notified and corrective actions initiated. The remediation was substantially completed during fiscal 2003.

Matrix closed or sold the business operations of its San Luis Tank Piping Construction Company, Inc. and West Coast Industrial Coatings, Inc. subsidiaries, which were located in California. Although Matrix does not own any land or buildings used in these subsidiaries, we would be liable for any environmental exposure while operating at the facility, a period from June 1, 1991 to May 31, 2001. At the present time, the environmental liability that could result from the testing is unknown; however, Matrix has purchased a pollution liability insurance policy with $5 million of coverage for all operations.

Matrix has other fabrication operations in Tulsa, Oklahoma; Catoosa, Oklahoma; Bristol, Bethlehem, and Holmes, Pennsylvania; Bellingham, Washington and Orange, California, which could subject the Company to environmental liability. It is unknown at this time if any such liability exists but based on the types of fabrication and other manufacturing activities performed at these facilities and the environmental monitoring that we undertake, Matrix does not believe it has any material environmental liabilities at these locations.

Matrix builds aboveground storage tanks and performs maintenance and repairs on existing aboveground storage tanks. A defect in the manufacturing of new tanks or faulty repair and maintenance on an existing tank could result in an environmental liability if the product stored in the tank leaked and contaminated the environment. Matrix currently has liability insurance with pollution coverage of $5 million, but the amount could be insufficient to cover a major claim.

ITEM 4. Controls and Procedures

We maintain controls and other procedures that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. In response to recent legislation, we implemented changes to our disclosure controls and procedures, primarily to formalize and document procedures already in place and to establish a disclosure committee consisting of some of our officers and other management.

As of the end of the period covered by this report, an evaluation was performed with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of these disclosure controls and procedures. Based on this evaluation, management, including our Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures are effective.

We do not expect that our disclosure controls and procedures or our other internal controls can prevent all error and all fraud or that our evaluation of these controls and procedures can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. The benefits of controls and procedures must be considered relative to their costs, and the design of any system of controls is based in part upon assumptions about the likelihood of future events. There is reasonable assurance that the design will succeed in achieving its stated goals under all reasonably foreseeable future conditions. Over time, controls and procedures may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of these and other inherent limitations in controls and procedures, misstatements or omissions due to error or fraud may occur and not be detected.

Subsequent to the date of our evaluation described above, we have not made any significant changes, including corrective actions with regard to significant deficiencies or material weaknesses, in our internal controls or in other factors that could significantly affect these controls.

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PART II
OTHER INFORMATION

ITEM 6. Exhibits and Reports on Form 8-K:

Exhibit 31.1:	Certification Pursuant to Section 302 of Sarbanes-Oxley Act of 2002 – CEO.
Exhibit 31.2:	Certification Pursuant to Section 302 of Sarbanes-Oxley Act of 2002 – CFO.
Exhibit 32.1:	Certification Pursuant to 18 U.S.C. 1350 (section 906 of Sarbannes-Oxley Act of 2002) – CEO
Exhibit 32.2:	Certification Pursuant to 18 U.S.C. 1350 (section 906 of Sarbannes-Oxley Act of 2002) – CFO

Reports on Form 8-K: During the first quarter of fiscal 2004, a Form 8-K dated August 12, 2003 was filed pursuant to Item 12 (Results of Operation and Financial Condition).

Signature

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

MATRIX SERVICE COMPANY

/s/ Michael J. Hall

Date: October 10, 2003

By: Michael J. Hall
Michael J. Hall Vice President-Finance Chief Financial Officer signing on behalf of the registrant and as the registrant’s chief accounting officer.

Exhibit 31.1

CERTIFICATIONS

I, Bradley S. Vetal, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Matrix Service Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)), for the registrant and have:
   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s first fiscal quarter that has materially affected, or is reasonably likely to materially effect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent function):
   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
   b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: October 10, 2003

/s/ Bradley S. Vetal

Bradley S. Vetal
President and Chief Executive Officer

Exhibit 31.2

CERTIFICATIONS

I, Michael J. Hall, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Matrix Service Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)), for the registrant and have:
   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's first fiscal quarter that has materially affected, or is reasonably likely to materially effect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 10, 2003

/s/ Michael J. Hall

Michael J. Hall
Vice President – Finance and Chief Financial Officer

EXHIBIT 32.1

Certification Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant
Section 906 of Sarbannes-Oxley Act of 2002

In connection with the Quarterly Report of Matrix Service Company (The “Company”) on Form 10-Q for the period ending August 31, 2003 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Bradley S. Vetal, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbannes-Oxley Act of 2002, that based on our knowledge:

(1) Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

This certification is deemed to accompany this Quarterly Report on Form 10-Q, but is not deemed “filed” for purpose of Section 18 of the Securities Exchange Act of 1934, an amended, or otherwise.

Date: October 10, 2003

/s/ Bradley S. Vetal

Bradley S. Vetal
President and Chief Executive Officer

Certification Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant
Section 906 of Sarbannes-Oxley Act of 2002

In connection with the Quarterly Report of Matrix Service Company (The "Company") on Form 10-Q for the period ending August 31, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael J. Hall, Vice President, Finance and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbannes-Oxley Act of 2002, that based on our knowledge:

(1) Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

This certification is deemed to accompany this Quarterly Report on Form 10-Q, but is not deemed "filed" for purpose of Section 18 of the Securities Exchange Act of 1934, an amended, or otherwise.

Date: October 10, 2003

/s/ Michael J. Hall

Vice President – Finance
and Chief Financial Officer