SUNAIR SERVICES CORP
Form 10-K
January 13, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended September 30, 2009

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 No. 1-04334

SUNAIR SERVICES CORPORATION

(Exact name of registrant as specified in its charter)

Florida	**59-0780772**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

315 Groveland Street

Orlando, Florida 32804

(407) 645-2500

(Address and telephone number, including area code, of registrant s principal executive offices)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, par value $.10 per share	American Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ¨ No x

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 or Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). 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. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).   Yes ¨   No x

The aggregate market value of the voting stock held by non-affiliates of the Registrant was approximately $4,853,918 as of March 31, 2009 based on the closing price of stock on the American Stock Exchange on said date. For purposes of the foregoing computation, all executive officers, directors and 10% beneficial owners of the Registrant are deemed to be affiliates. Such determination should not be deemed to be an admission that such executive officers, directors or 10% beneficial owners are, in fact, affiliates of the registrant.

As of December 29, 2009, there were no issued and outstanding shares of the Registrant s common stock.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Part III (Items 12) is incorporated by reference from the Registrant s definitive proxy statement filed on November 20, 2009.

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CAUTIONARY STATEMENTS ABOUT

FORWARD-LOOKING STATEMENTS

Certain statements in this Annual Report on Form 10-K, other than purely historical information, including estimates, projections, statements relating to the business plans, objectives and expected operating results of Sunair Services Corporation and the assumptions upon which those statements are based, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements generally are identified by the words believe, project, expect, anticipate, estimate, intend, strategy, plan, may, should, will, would, will be, result, and similar expressions. Forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties which may cause actual results to differ materially from the forward-looking statements. Sunair Services Corporation undertakes no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

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PART I

ITEM 1. DESCRIPTION OF BUSINESS

Overview

Sunair Services Corporation (Sunair, the Company, us, we or our) is a Florida corporation organized in 1956. We changed our corporate nar from Sunair Electronics, Inc. to Sunair Services Corporation in November of 2005. During fiscal 2008, we operated in two business segments: Lawn and Pest Control Services and Telephone Communications. Our Lawn and Pest Control Services segment provides lawn care and pest control services to both residential and commercial customers. Our Telephone Communications segment which installs and maintains telephone and fixed wireless systems was sold in September 2008 representing the completion of our strategy to shed our legacy businesses and focus on our core business which is providing lawn and pest control services to our customers.

On February 8, 2005, we closed a transaction with Coconut Palm Capital Investors II, Ltd. (Coconut Palm), pursuant to a stock purchase agreement which we entered into on November 17, 2004. Coconut Palm purchased from us 5,000,000 Units for an aggregate purchase price of $25 million. Each Unit consisted of (i) one share of our common stock, (ii) one warrant to purchase one share of our common stock at an exercise price of $6.00 per share with a term of three years and (iii) one warrant to purchase one share of our common stock at an exercise price of $7.00 per share with a term of five years. In connection with the investment by Coconut Palm, we formed a new Lawn and Pest Control Services segment for future acquisitions and operations.

Effective upon the closing of the Coconut Palm transaction, we entered into a management services agreement with an affiliate of Coconut Palm, RPC Financial Advisors, LLC (RPC), pursuant to which RPC agreed to provide management services for us. Richard C. Rochon and Mario B. Ferrari, both of whom are affiliates of Coconut Palm and each of whom are members of our Board of Directors and principal shareholders of the Company, are also affiliates of RPC. On January 7, 2008, the Company entered into a management services agreement (Management Services Agreement or the Amended Management Services Agreement) with RPC, which superseded and replaced the management services agreement (the Previous Management Services Agreement) dated February 8, 2005, as amended between the Company and RPC. The Amended Management Services Agreement is for a term of three years, commencing on February 8, 2008 and expiring on February 7, 2011. Pursuant to the Amended Agreement, RPC provides the Company with services similar to those provided under the prior management services agreement. We pay RPC a monthly management fee equal to one (1%) of the monthly gross revenues of the Company, which are payable monthly based on the preceding quarter. RPC will also receive a transaction fee of 2% of the Aggregate Consideration received by the Company in a Transaction (as such capitalized terms are defined in the Amended Management Services Agreement). After the initial term of three years, the Amended Management Services Agreement will automatically renew for successive one year terms, unless either RPC or the Company terminates the agreement upon 30 days notice. Please see Note 17 Related Parties in our consolidated financial statements included herein in Item 8.

In June 2005 with the acquisition of Middleton Pest Control, Inc., we made a strategic decision to become a leading provider of lawn and pest control services focusing primarily on residential customers. Previously, we had operated through two business segments: High Frequency Radio and Telephone Communications. Since that time we have executed our strategy and shifted our focus to the Lawn and Pest Control Services segment which resulted in a series of acquisitions and divestitures planned to enable us to grow our core business, Lawn Care and Pest Control Services, and shed our legacy businesses (Telephone Communications and High Frequency Radio).

During the fiscal years ended September 30, 2008 and 2009, our acquisitions and divestitures have been as follows:

Acquisitions:

October 2007 we acquired substantially all the assets of Marshall Pest Control of SW FL, Inc. (Marshall).

Divestitures:

September 2008 we sold all the issued and outstanding stock of Telecom FM Limited (Telecom FM), a wholly owned subsidiary operating in our Telephone Communications business segment.

We have completed the execution of our strategy to divest our legacy businesses (Telephone Communications and High Frequency Radio) and will continue to focus on growing our core business, Lawn and Pest Control Services.

Entry into Agreement and Plan of Merger:

On September 28, 2009, the Company, Massey Services, Inc. (Massey), and Buyer Acquisition Company, Inc. (Merger Sub) entered into an Agreement and Plan of Merger (the Merger Agreement) pursuant to which Merger Sub, would merge with and into the Company, the Company would become a wholly-owned subsidiary of Massey, and all outstanding shares of common stock of the Company (other than shares held by the Massey, Merger Sub or their affiliates) would be converted into the right to receive an amount per share in cash of $2.75. Buyer Acquisition Company, Inc., a Florida corporation and a wholly owned subsidiary of Massey, was formed solely for the purpose of entering into the Merger Agreement with Sunair and completing the Merger, and has not conducted any business operations. Further information about the Merger is included on Form 8-K as filed with the Securities and Exchange Commission (SEC) on October 1, 2009, which information is incorporated herein by reference.

Subsequent Event

In connection with the Merger between our Company, Massey and Merger Sub, Sunair filed a preliminary proxy statement with the SEC on October 2, 2009 and on November 20, 2009 Sunair filed the definitive proxy statement with the SEC. On December 14, 2009, our shareholders, voting at a special meeting (Special Meeting), approved the Merger of Sunair with and into Massey. In a press release issued December 14, 2009, Sunair announced the approval of the merger agreement by its shareholders at the Special Meeting. Subsequently, on December 16, 2009, Sunair closed the Merger and Massey announced the same in its press release dated December 17, 2009. As a result of the Merger, Merger Sub merged with and into Sunair, Sunair became a wholly-owned subsidiary of Massey, and all outstanding shares of common stock of Sunair other than shares held by Massey, Merger Sub or their affiliates were converted into the right to receive an amount per share in cash of $2.75. Information about the Merger and the effects of the Merger is included on Form 8-K filed by Sunair with the SEC on December 23, 2009, which information is incorporated herein by reference. Additional information about the Merger can be found in the Definitive Proxy Statement as filed with the SEC on November 20, 2009, which is attached to this Form 10-K as Exhibit 99.1 and incorporated herein by reference. Information regarding post-closing mergers involving Sunair and its affiliates is included on Form 8-K under Item 1.01 as filed with the SEC on December 23, 2009, which information is incorporated herein by reference.

The Lawn and Pest Control Services Segment

The Lawn and Pest Control Services segment acquired its first company on June 7, 2005, through the acquisition by our subsidiary, Sunair Southeast Pest Holdings, Inc., of all of the outstanding capital stock of Middleton Pest Control, Inc., a lawn and pest control company with operations throughout the state of Florida. The aggregate purchase price for the outstanding capital stock of Middleton was $50.0 million, which was comprised of: (i) $35.0 million in cash; (ii) $5.0 million in the form of a subordinated promissory note; and (iii) 1,028,807 shares of our common stock. We also incurred closing costs of $1.6 million and assumed $1.4 million of liabilities for a total purchase price of $53.0 million. On July 29, 2005, Middleton acquired substantially all of the assets of Four Seasons, a pest control and lawn care services company located in Central Florida, for approximately $1.4 million in cash.

In fiscal 2006, Middleton acquired four pest control companies. On December 16, 2005, Middleton acquired substantially all of the assets of Spa Creek, a pest control and termite services company located in Central Florida, for approximately $5.5 million in cash. We also incurred transaction costs of $233,419 for a total purchase price of $5.7 million. On January 9, 2006, Middleton acquired substantially all of the assets of Paragon, a pest control and termite services company headquartered in Port St. Lucie, Florida, for approximately $1.1 million, consisting of $800,000 cash, $100,000 in the form of a subordinated promissory note, approximately $50,000 in transaction costs and 17,036 shares of our common stock valued at $100,000. On February 28, 2006, Middleton acquired substantially all of the assets of Pestec, a pest control and lawn care services company headquartered in Sarasota, Florida, for approximately $800,000, consisting of $600,000 cash, $175,000 in the form of a subordinated promissory note and approximately $25,000 in transaction costs. On March 31, 2006, Middleton acquired Ron Fee, a pest control and termite services company located in Central Florida, for approximately $5.2 million, consisting of $4.0 million in cash and $1.2 million in the form of a subordinated promissory note. We also incurred transaction costs of approximately $325,000 for a total purchase price of $5,525,000.

In fiscal 2007, Middleton acquired 6 pest control service and lawn care service companies. On November 30, 2006, Middleton acquired substantially all of the assets of Archer, a pest control services company located in Orlando, Florida, for $3.3 million, consisting of $1.5 million in cash, $1.5 million in the form of a subordinated promissory note and 73,529 shares of the Company s common stock valued at $300,000. We also incurred approximately $150,400 of transactions costs related to this acquisition. On February 8, 2007, Middleton acquired substantially all the assets of Valentine, headquartered in St. Cloud, Florida for approximately $43,400, consisting of $18,432 in cash and $25,000 in the form of a promissory note. On April 30, 2007, Middleton acquired substantially all the assets of Florida Exterminating, a pest control company headquartered in Tampa, Florida for approximately $815,000 consisting of $580,000 in cash and $235,000 in the form of a promissory note. We also incurred approximately $55,000 of transactions costs related to this acquisition. On May 31, 2007, Middleton acquired substantially all the assets of Summer Rain, a lawn care services company headquartered in Margate, Florida for approximately $1.0 million, consisting of $500,000 in cash and $500,000 in the form of a promissory note. We also incurred approximately $161,400 of transactions costs related to this acquisition. On August 27, 2007, Middleton acquired substantially all the assets of Howell, a lawn care and pest control services company located in West Palm Beach, Florida, for approximately $2.3 million, consisting of $925,000 in cash and $1.4 million in the form of a subordinated promissory note with $1.0 million secured by a letter of credit. We also incurred approximately $161,500 of transactions costs related to this acquisition. On September 20, 2007, Middleton acquired substantially all of the assets of Longboat Key, a lawn care and pest control services company located in Longboat, Florida for $1.7 million, consisting of $1.0 million in cash, $542,000 in the form of a promissory note and $158,000 to be paid over a two year period at a rate equal to 50% of the collections received by Longboat Key from a large commercial customer. We also incurred approximately $165,700 of transactions costs related to this acquisition.

In fiscal 2008, Middleton acquired substantially all of the assets of Marshall, a lawn care and pest control services company located in Naples, Florida for $1.6 million, consisting of $1.0 million in cash and $600,000 in the form of a promissory note. In addition, the Company incurred working capital adjustments and transaction costs of approximately $0.3 million.

In fiscal 2009, we focused on the organic growth of our core business within the Company s existing market area. We did not make any acquisitions of lawn and pest control companies in fiscal 2009, however we did enter into an Agreement and Plan of Merger with Massey and Merger Sub, as described above.

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Business of Middleton

Overview

Middleton, with headquarters located in Orlando, Florida, provides lawn care services and pest control services to both residential and commercial customers. Middleton provides essential pest control services and protection against termite damage, rodents and insects to homes and businesses. In addition, Middleton supplies essential lawn care services to homes and businesses, which includes fertilization treatments and protection against disease, weeds and insects for lawns and shrubs. Middleton operates under Middleton Lawn and Pest Control and Middleton Pest Control, Inc.

Middleton was founded in 1952 as a single location in Orlando, Florida... Middleton has since grown to a network of 24 branches throughout Florida, from which it serves approximately 67,500 customers as of September 30, 2009.

Seasonality

The lawn and pest control business is seasonal in nature. The termite swarm season, which generally occurs in early spring but varies by region depending on climate, leads to the highest demand for termite control services and therefore the highest level of revenues. Weather conditions, such as hurricanes, affect the demand for lawn care services and may result in a decrease in revenues or an increase in costs.

Customers

As of September 30, 2009, approximately 89% of Middleton s accounts were residential representing approximately 84% of Middleton s revenues and approximately 11% of Middleton s accounts were commercial representing approximately 16% of Middleton s revenues.

The following table provides information regarding the services utilized by Middleton s revenue:

Service	**% of Revenue**
Lawn Care	53.4%
General Pest Control	22.6%
Termite	24.0%
Total	100.00%

Inventories

Middleton has relationships with multiple vendors for lawn and pest control treatment products and maintains a sufficient level of chemicals, materials and other supplies to fulfill its immediate servicing needs and to alleviate any potential short-term shortage in availability from its national network of suppliers.

Competition

The lawn and pest control services industry, a highly fragmented industry which is actively consolidating, is made up of approximately 20,000 pest control firms nationally and approximately 2,300 in Florida.. The top five firms account for approximately 30% of revenues in the national market and the top 100 firms account for approximately 50% of the revenues. The principal methods of competition include quality of service, name recognition, pricing, assurance of customer satisfaction and reputation.

Lawn Care Services. Competition in the market for lawn care services is strong, coming mainly from large national companies including TruGreen/Chemlawn and, to a lesser extent, from regional and local, independently owned firms and from homeowners who care for their own lawns.

Pest Control Services. Competition in the Florida market for pest control services is strong, coming mainly from regional and local, independently owned firms, and, to a lesser extent, from large national companies including Orkin and Terminix, and from homeowners who treat their own pest control problems.

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Marketing and Distribution

Middleton markets its services through an integrated marketing communications strategy which includes television advertisement, yellow pages and local print advertising, direct mail, local events and tradeshows, telemarketing and email marketing targeted at reaching both prospective and current customers. Public relation initiatives are also used in targeting key external audiences, including trade, local and consumer media.

Services are sold through two main distribution channels, field sales representatives and the internet. Sales representatives use the point of sale data and targeted collateral materials to conduct door-to door solicitations. Middleton s website enables customers to order, pay, schedule and request information about services online.

Environmental and Regulatory Considerations

Middleton is subject to various legislative and regulatory enactments that are designed to protect the environment, public health and consumer protection. Middleton believes that it is in substantial compliance with all such legislative and regulatory requirements. Compliance with these requirements has not had a material negative effect on its financial position, results of operations or liquidity.

The Federal Insecticide Fungicide and Rodentcide Act (as amended) is a federal law that grants the responsibility of the states to be the primary agent in enforcement and conditions under which pest control companies operate. Each state must meet certain guidelines of the Environmental Protection Agency in regulating the following: licensing, record keeping, contracts, standards of application, training and registration of products. This allows each state to institute certain features that set their regulatory programs in keeping with special interests of the citizens and the pest control companies wishes in each state. Florida has enacted such guidelines which regulate and license the pest control industry in Florida. The pest control industry is impacted by these federal and state regulations.

Employees

The number of persons employed by Middleton as of September 28, 2009 was 539, which includes 149 salespersons, 233 technicians, 60 branch and district managers, 37 office associates, 5 telemarketers, and 55 persons in Middleton s corporate office.

Subsequent Event

On September 28, 2009, the Company, Massey Services, Inc. (Massey), and Buyer Acquisition Company, Inc. (Merger Sub) entered into an Agreement and Plan of Merger (the Merger Agreement) pursuant to which Merger Sub, would merge with and into the Company, the Company would become a wholly-owned subsidiary of Massey, and all outstanding shares of common stock of the Company (other than shares held by the Massey, Merger Sub or their affiliates) would be converted into the right to receive an amount per share in cash of $2.75. Buyer Acquisition Company, Inc., a Florida corporation and a wholly owned subsidiary of Massey, was formed solely for the purpose of entering into the Merger Agreement with Sunair and completing the Merger, and has not conducted any business operations. Further information about the Merger is included on Form 8-K as filed with the Securities and Exchange Commission (SEC) on October 1, 2009, which information is incorporated herein by reference. We completed the Merger with Massey and Merger Sub on December 16, 2009.

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ITEM 1A. RISK FACTORS
Not applicable.

ITEM 2. DESCRIPTION OF PROPERTY
Middleton s corporate headquarters are located at 1736 33rd Street, Orlando, Florida 32839. Middleton leases the building where its corporate headquarters are located, which contains approximately 12,000 sq. ft. of floor space. The lease expires on June 1, 2015. In addition, Middleton leases 23 other branch offices in its business which operates in space held primarily under three to five year leases providing for fixed monthly rental payments. The following is a list of the branch locations:

East Region	West Region
Orlando, Florida	Tampa, Florida
Kissimmee, Florida	Clearwater, Florida
Longwood, Florida	Sarasota, Florida
Daytona Beach, Florida	Naples, Florida
Cocoa, Florida	Groveland, Florida
Orange City, Florida	Lakeland, Florida
Palm Coast, Florida	Odessa, Florida
New Smyrna Beach, Florida	Brooksville, Florida
Melbourne, Florida	Gainesville, Florida
Vero Beach, Florida	Ocala, Florida
West Palm Beach, Florida	
Jacksonville, Florida	
St. Augustine, Florida	

We believe that these facilities are well maintained, in compliance with environmental laws and regulations, in all material respects and adequately covered by insurance. We also believe that these leased facilities are not unique and could be replaced, if necessary, at the end of the term of the existing leases.

ITEM 3. LEGAL PROCEEDINGS
We are involved in litigation from time to time in the ordinary course of our business. We do not believe that any litigation in which we are currently involved, individually or in the aggregate, is material to our financial condition or results of operations.

Lawsuit filed by the Dissident Group against the Company

On February 19, 2009, Michael Brauser, Dru Schmitt and Michael Herman (the Dissident Group) filed a complaint in the Fifteenth Judicial Circuit Court (Court or the Palm Beach Court) in Palm Beach County, Florida against the Company, Coconut Palm Capital Investors II, Ltd. (Coconut Palm) and Coconut Palm Capital Investors II, Inc. (Coconut Palm Inc.). The claims relate to the Dissident Group s action to take control of the Company by replacing the Company s current Board and replacing it with their six nominees and a claim that certain proxies granted to Coconut Palm Inc. by Mr. Brauser and Mr. Schmitt are not valid.

In the complaint, the Dissident Group demanded that (i) we provide it with a copy of our shareholder list as of January 28, 2009, the record date for the Annual Meeting of Shareholders, and pre-addressed mailing labels for our shareholders as of the record date, (ii) the Court issue a declaratory judgment relating to the validity of proxies granted to Coconut Palm Inc. by Mr. Brauser and Mr. Schmitt and (iii) that the Court enjoin our Annual Meeting to be held on March 18, 2009 because our proxy materials contain misrepresentations and omissions of material facts. On March 17, 2009, we, Coconut Palm and Coconut Palm Inc. filed a motion to remove the lawsuit to the United States District Court, the Southern District of Florida (Federal Court), which the Palm Beach Court granted two days later. On April 16, 2009, the Dissident Group filed a Motion to Remand the lawsuit to the state court, the Palm Beach Court. On July 6, 2009, the Federal Court entered an Order Denying Motion to Remand. On March 24, 2009, the Company, Coconut Palm and Coconut Palm Inc. filed a motion to dismiss the lawsuit and the Dissident Group filed a response to this motion on May 18, 2009. The Company, Coconut Palm and Coconut Palm, Inc. filed a Reply to the Dissident Group s response to the motion to dismiss on May 29, 2009. The Federal Court has not ruled on the Motion to Dismiss. The Company believes this lawsuit is without merit and intends to continue to vigorously defend itself.

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Complaint filed by the Company against the Dissident Group

On March 12, 2009, the Company filed a complaint in the Federal Court against the Dissident Group and certain other co-defendants for violations of federal securities laws. The complaint relates to actions that have arisen in connection with the information statement that the Dissident Group filed with the SEC on January 28, 2009, as amended on February 25th, March 6th and March 9, 2009 (collectively, the Information Statement), in which the Dissident Group sought to remove the Company s current Board of Directors and replace it with their nominees.

The complaint alleges that the Dissident Group and certain other co-defendants unlawfully solicited proxies from the Company s shareholders in violation of Section 14(a) and 14(c) of the Exchange Act in connection with their actions to take control of the Company and replace the Company s current Board of Directors with their six nominees. It also alleges that the Information Statement filed by the Dissident Group omits material information relating to Mr. Brauser s background, including civil fraud litigation and a bankruptcy proceeding involving a company owned by Mr. Brauser.

With its lawsuit, the Company seeking injunctive relief against the Dissident Group to prevent them from voting any proxies obtained in the unlawful proxy solicitation, requiring corrective disclosure in the Information Statement and establishing a 90-day cooling off period before the Dissident Group can commence any further activity relating to a change of control. The Dissident Group has filed motions for extension of time to respond to the Complaint. On July 30, 2009, the Federal Court granted an extension of time through August 31, 2009, for the Dissident Group to file an Answer to the Complaint.

Settlement Agreement

Massey reached a settlement agreement with the Dissident Group that provides that at the closing of the Merger (i) the Dissident Group will dismiss its lawsuit against Sunair, (ii) Massey will cause Sunair to dismiss its lawsuit against the Dissident Group and (iii) the Dissident Group will grant a general release to Sunair and Massey and their respective officers, directors and employees as to all potential claims by the Dissident Group. As of the filing of this report, the parties were waiting for approval of the settlement agreement by the parties respective counsel and had not yet filed the Joint Stipulation of Dismissal with the court.

Class Action Lawsuits Filed

On October 9, 2009, a putative class action lawsuit was filed in the Circuit Court of the Seventeenth Judicial Circuit for Broward County, State of Florida, Civil Division regarding the proposed Merger between our company and Massey. The complaint was purportedly filed on behalf of the public holders of Sunair s common stock, and names as defendants, Sunair, each of Sunair s directors, Massey and Merger Sub. The complaint alleges, among other things, that Sunair s directors breached their fiduciary duties by adopting the Agreement and Plan of Merger (Merger Agreement) dated September 28, 2009, between Sunair, Massey and Merger Sub, and by approving the Merger described therein. The complaint further alleges that the proposed Merger provides Sunair s public shareholders with inadequate consideration for their shares of Sunair s common stock and that Sunair and Massey aided and abetted the alleged breaches by Sunair s directors. The plaintiff seeks, among other things, class action status, an injunction preventing the completion of the Merger (or rescinding the Merger if it is completed), rescissory damages and the payment of attorneys fees and expenses. On December 3, 2009, Plaintiff, individually and on behalf of others similarly situated, served an emergency motion for a temporary injunction in the Circuit Court of the Seventeenth Judicial Circuit for Broward County, State of Florida (Court). On December 11, 2009, the Court denied the plaintiff s motion for a temporary injunction. Plaintiff has objected to the court s Order denying plaintiff s motion for a temporary injunction and defendants have filed a response to the same. We believe the lawsuit is without merit and intend to continue to vigorously defend ourselves.

On November 17, 2009, a putative class action lawsuit was filed in the United States District Court, Southern District of Florida regarding the proposed Merger between our company and Massey. The complaint was purportedly filed on behalf of the public holders of Sunair s common stock, and names as defendants, Sunair, each of Sunair s directors, Massey and Merger Sub. The Complaint alleges, among other things, that Sunair s directors breached their fiduciary duties by adopting the Merger Agreement between Sunair, Massey and Merger Sub, and by approving the Merger described therein. The Complaint further alleges that Sunair and Massey knowingly aided and abetted the alleged breaches by Sunair s directors. Additionally, the Complaint alleges that Defendants violated Sections 14(a) and 20(a) of the Securities Exchange Act of 1934 and Rule 14a-9 promulgated thereunder by the Securities and Exchange Commission. The Plaintiff seeks, among other things, class action status, an injunction preventing the completion of the merger (or rescinding the merger if it is completed), rescissory damages and the payment of attorneys fees and expenses. A motion to stay the proceedings was filed on November 25, 2009. An Order staying the proceedings in this case was entered staying the case until February 2009 pending the resolution of the first class action filed. We believe this class action lawsuit is without merit and will be resolved in our favor.

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

There were no matters submitted to a vote of our security holders either through solicitation of proxies or otherwise in the fourth quarter of the fiscal year ended September 30, 2009.

PART II

ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES

The following table sets forth the high and low sale price of the Company s common stock as traded on the American Stock Exchange under the symbol SNR.

	High	Low
Year ended September 30, 2009		
First quarter	2.30	1.20
Second quarter	1.96	1.32
Third quarter	2.55	1.63
Fourth quarter	2.69	1.71
Year ended September 30, 2008		
First quarter	3.12	1.66
Second quarter	2.55	1.58
Third quarter	3.03	2.21
Fourth quarter	2.60	1.61

As of December 16, 2009, there was one shareholder of record. See Subsequent Event under Part I-Item I Description of Business.

Dividends

We paid no dividends on our common stock in fiscal 2009 or fiscal 2008. The payment of cash dividends will depend upon our earnings, consolidated financial position and cash requirements, our compliance with loan agreements and other relevant factors. Management does not presently intend to pay cash dividends on our common stock.

Equity Compensation Plan Information

The following table sets forth information, as of September 30, 2009, with respect to the Company s compensation plans under which the Company s common stock is authorized for issuance:

Equity Compensation Plan Information

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding

			securities reflected in column (a)) (c)
Equity compensation plans approved by stockholders	539,950	$ 4.23	260,050
Equity compensation plans not approved by stockholders	0	0	0

Recent Sales of Unregistered Securities

None.

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Issuer Repurchases

None.

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION
The following Management s Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our consolidated financial statements and related notes contained in Item 8 of this report Form 10-K. The following Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) includes the following sections:

Company Overview

Results of Operations

Liquidity and Capital Resources

Off-Balance Sheet Arrangements

Critical Accounting Policies

Recent Accounting Pronouncements

You should note that this MD&A discussion contains forward-looking statements that involve risks and uncertainties. You should read this MD&A in conjunction with the Company s financial statements and related notes included in Item 8.

Company Overview

Sunair Services Corporation is a Florida corporation organized in 1956. We changed our corporate name from Sunair Electronics, Inc. to Sunair Services Corporation in November of 2005. Previously, we operated through two business segments: Telephone Communications and High Frequency Radio. In June 2005 with the acquisition of Middleton we embarked on a new strategy to become a leading regional provider of lawn and pest control services focusing mainly on residential customers.

We have completed the execution of our strategy which was to focus on growing our core business, Lawn and Pest Control Services, and to divest our legacy businesses (Telephone Communications and High Frequency Radio).

The acquisitions and divestitures for the years ended September 30, 2009 and 2008 are as follows:

Acquisitions:

In October 2007, we acquired substantially all the assets of Marshall Pest Control of SW FL, Inc.

All acquisitions of lawn care and pest control companies have been made by Middleton, our platform company, and have been integrated into its operations.

Dispositions:

In September 2008, we sold all the issued and outstanding stock of Telecom FM Limited, (Telecom FM), a wholly-owned subsidiary operating in our Telephone Communications business segment.

We have completed the execution of our strategy to divest our legacy businesses (Telephone Communications and High Frequency Radio) and will continue to focus on growing our core business, Lawn and Pest Control Services.

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Results of Operations

Fiscal Year Ended September 30, 2009 (fiscal 2009) compared to the Fiscal Year ended September 30, 2008 (fiscal 2008)

Revenue, Cost of Sales, and Gross Profit:

	(dollars in thousands) For the Year Ended September 30, 2009	2008
Revenue	$ 51,162	$ 56,613
Cost of sales	18,861	22,121
Gross Profit	$ 32,301	$ 34,492

Revenue

Revenue is comprised of lawn and ornamental, pest control and termite services. Revenue decreased by $5.5 million or 9.6% for the year ended September 30, 2009 as compared to the year ended September 30, 2008. This decrease was primarily from lawn and ornamental services which began to decline in the latter part of our fiscal 2008 year due to the overall economic downturn and continued through 2009. Despite the downturn, revenue for pest control and termite services remained at levels similar to those achieved in 2008.

Cost of Sales

Cost of sales decreased as a percentage of revenue from 39.1% to 36.9%, or $3.3 million due to the following factors:

Payroll costs decreased $1.3 million primarily due to the reduction in services rendered, and the transition of our compensation structure in our acquired branches to mirror the rest of the Company.

Chemical costs decreased $0.7 million which is proportionate to the decline in revenue.

Vehicle costs decreased $1.2 million. Fuel purchases decreased $0.7 million due to the reduction in fuel prices and the decrease in gallons purchased due to lower activity. Repair and maintenance costs decreased $0.3 million and vehicle lease costs decreased $0.2 million. The Company reduced its fleet size by 97 vehicles from September 30, 2008 to September 30, 2009 as part of a rightsizing initiative to better manage our costs which also included the discontinuation of our third party vehicle maintenance program which was brought in house.

Gross Profit

The gross profit increased from 60.9% of revenue to 63.1% of revenue for the years ended September 30, 2008 and 2009, respectively.

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Operating Expenses:

Selling, General and Administrative Expenses:

	(dollars in thousands) For the Year Ended September 30, 2009	2008
Selling	$ 5,047	$ 5,921
General and administrative	24,491	27,650
Depreciation and amortization	4,464	4,425
Total operating expenses	$ 34,002	$ 37,996

Total operating expenses decreased by $4.0 million or 10.5%. As a percentage of revenue, operating expenses decreased from 67.1% to 66.5% for the year ended September 30, 2008 and 2009 respectively.

Selling expenses decreased by $0.9 million primarily due to the decline in sales commissions paid as a result of a decrease in new sales activity.

General and administrative expenses decreased as a percentage of revenue from 48.8% to 47.9%, or 3.2 million primarily due to the following factors:

Payroll expenses decreased by $0.9 million primarily due to a reduction in headcount.

Vehicle expenses decreased $0.7 million due to lower fuel costs and a reduced fleet size.

Office and printing expenses decreased by $0.3 million primarily due to tighter controls on office supply inventory and print expenditures.

Health insurance expenses decreased by $0.5 million due to a reduction in headcount and the renegotiation of our health and dental insurance rates with our provider, along with adjustments to our employee contribution levels.

Outsourcing costs decreased by $0.3 million, primarily due to a decrease in professional fees.

Facility costs decreased by $0.1 million.

Corporate general and administrative expenses were increased by $0.5 million. Legal and professional fees increased by $1.0 million, primarily due to a shareholders dispute and the Merger with Massey and Merger Sub. The increase was offset by decreases in management fees and compensation expense. Management fees decreased by $0.3 million, a result of the Amended Management Services Agreement between the Company and RPC Financial Advisors, LLC, (a related party), which was effective as of February 8, 2008, which resulted in lower management fees. Compensation expenses decreased by $0.3 million. During the fourth quarter of 2008, the Company incurred $0.4 million in severance payments related to the termination of the employment agreement of our Chief Executive Officer and President.

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Other Income (Expense):

	(dollars in thousands) For the Year Ended September 30, 2009	2008
Interest expense	$ (857)	$ (1,340)
Interest income	2	143
Gain (loss) on disposal of assets	6	(11)
Gain on extinguishment of debt	55	
Loss on impairment of goodwill	(15,705)	
Other income	31	75
Total other expenses	$ (16,468)	$ (1,133)

Other expenses increased $15.3 million for the year ended September 30, 2009 as compared to the year ended September 30, 2008 primarily due to the impairment of goodwill. See Note 1 Business Activity and Summary of Significant Accounting Policies. The increase was partially offset by a decrease in interest expense from lower interest rates and the overall reduction of our debt in the amount of $5.2 million. In connection with the closing of the Merger, this revolving line of credit was paid in full. See Note 20 Subsequent Events. The interest rate on the revolving line of credit was 5.25% at September 30, 2009 compared to 8.93% at September 30, 2008.

Income Tax (Expense) Benefit from Continuing Operations:

	(dollars in thousands) For the Year Ended September 30, 2009	2008
Income tax (provision) benefit	$	$

The income tax provision from continuing operations for the year ended September 30, 2009 and 2008 was zero. The Company did not recognize an income tax benefit for the year ended September 30, 2009 as the Company has $19.9 million of net operating losses carryforwards which expire in 2029 and which are fully reserved. In addition, the Company does not have any operating loss carrybacks. The Company also has $1.7 million of capital loss carryforwards which expire in 2014 and which are fully reserved. As a result the Company was unable to recognize an income tax benefit for year ended September 30, 2009 and 2008.

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Discontinued Operations:

As indicated earlier, the divestitures of our legacy businesses have been recorded as discontinued operations:

	For the Year Ended September 30, 2009	2008
Income from discontinued operations	$ 211,694	$ (1,876,039)
Pre-tax income from discontinued operations	211,694	(1,876,039)
Income tax benefit		
Income from discontinued operations, net of income tax	$ 211,694	$ (1,876,039)

Our significant divestitures have been recorded as discontinued operations:

On September 30, 2008 we completed the sale of all the issued and outstanding stock of Telecom FM, a wholly owned subsidiary operating in our Telephone Communications business segment. The effective date of the sale was September 1, 2008. The aggregate purchase price paid to the Company for Telecom FM was $3.6 million, which included the payment of outstanding inter-company debt in the amount of $1.2 million. The gain on the sale of Telecom FM amounted to $0.4 million. The activity for the year ended September 30, 2008 represents the operations of Telecom FM for that period.

As of September 30, 2008 a reserve was set up for the entire amount of a $2.0 million note receivable due from Sunair Electronics LLC, relating to the sale of our legacy high frequency radio business, as collection of this note is doubtful due to recent adverse developments at Sunair Electronics LLC. In February 2009 a payment of $275,000 was received from Sunair Electronics LLC as settlement of the note receivable. This amount was recorded as income from discontinued operations in the accompanying condensed consolidated statements of operations for the year ended September 30, 2009.

Net Income (Loss)

As a result of the foregoing, the Company s net loss was ($18.0) million for the year ended September 30, 2009 compared to a net loss of ($6.5) million for the year ended September 30, 2008.

Liquidity and Capital Resources

Generally our working capital needs are funded from operations and advances under our revolving line of credit. In the lawn care and pest control business segment customers are billed when service is rendered and payment is usually received in less than thirty (30) days.

As of September 30, 2009, our liquidity and capital resources included cash and cash equivalents of $1.5 million, working capital deficit of $17.0 million and $0.3 million was available under our revolving line of credit. As of September 30, 2008, our liquidity and capital resources included cash and cash equivalents of $3.0 million, a working capital deficit of $5.7 million and there was $1.4 million available under our revolving line of credit.

Cash provided by operating activities for fiscal 2009 was $4.3 million compared to cash used in operating activities of $0.1 million for fiscal 2008. In 2009 the cash flows from operating activities included a $15.7 million loss on impairment of goodwill.

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In fiscal 2009 the primary uses of cash from operating activities were a decrease in accounts payable and accrued expenses of $0.4 million, a decrease in customer deposits of $0.3 million and a decrease in unearned revenue of approximately $0.4 million. The primary sources of cash from operating activities for fiscal year 2009 were a decrease in prepaid expenses and other current assets of $2.2 million, a decrease in accounts receivable of $0.2 million, and a decrease in inventory of $0.4 million.

Net cash used in investing activities for fiscal 2009 and 2008 was $0.6 million and $1.9 million, respectively. The primary uses of cash from investing activities in fiscal 2009 were $0.3 million for the purchase of property, plant and equipment and $0.4 million for the purchase of software and other related costs.

Net cash used in financing activities for fiscal 2009 was $5.2 million. In fiscal 2008 cash provided from financing activities was $2.5 million. The primary uses of cash from financing activities in 2009 were $4.6 million for the repayment of the revolving line of credit and $0.6 million for the repayment of notes payable.

Cash flows from discontinued operations are included in the consolidated statement of cash flows within operating, investing and financing activities. The absence of cash flows from discontinued operations is not expected to impact future liquidity or capital resources.

Our uses of cash for fiscal 2010 will be principally for working capital needs, capital expenditures and debt service. We are not anticipating significant acquisition activity in fiscal 2010.

Subsequent Event

On September 28, 2009, the Company, Massey Services, Inc. (Massey), and Buyer Acquisition Company, Inc. (Merger Sub) entered into an Agreement and Plan of Merger (the Merger Agreement) pursuant to which Merger Sub, would merge with and into the Company, the Company would become a wholly-owned subsidiary of Massey, and all outstanding shares of common stock of the Company (other than shares held by the Massey, Merger Sub or their affiliates) would be converted into the right to receive an amount per share in cash of $2.75. Buyer Acquisition Company, Inc., a Florida corporation and a wholly owned subsidiary of Massey, was formed solely for the purpose of entering into the Merger Agreement with Sunair and completing the Merger, and has not conducted any business operations. Further information about the Merger is included on Form 8-K as filed with the Securities and Exchange Commission (SEC) on October 1, 2009, which information is incorporated herein by reference. We completed the Merger with Massey and Merger Sub on December 16, 2009.

Off-Balance Sheet Arrangements

We do not have any significant off-balance sheet arrangements.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and the disclosure of contingencies. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be materially different from those estimates. The following policies are those that we consider to be the most critical. See Note 1, Summary of Significant Accounting Policies, for further description of these and all other accounting policies.

Software development costs

We capitalize the costs of acquiring, developing and testing software to meet its internal needs. We capitalize costs associated with software developed or obtained for internal use when both the preliminary project stage is completed and management has authorized further funding for the project which it deems probable will be completed and used to perform the function intended. Capitalized costs include only (1) external direct costs of materials and services consumed in developing or obtaining internal-use software, (2) payroll and payroll-related costs for employees who are directly associated with and devote time to the internal-use software project and (3) interest costs incurred while developing internal-use software. Capitalization of such costs ceases no later than the point at which the project is substantially complete and ready for its intended use. Software development costs are amortized using a straight-line method over a three-year period. We capitalized software costs amounting to $616,461 and $246,979 for Middleton at September 30, 2009 and 2008, respectively.

We also capitalized certain costs associated with software development and amortized software costs for periods of 5 to 10 years, the estimated useful life of the asset. During 2008, we sold the outstanding shares of Telecom FM where these software costs were incurred.

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Customer Lists

Customer lists are stated at fair value based on the discounted cash flows over the estimated life of the customer contracts and relationships. The Company obtained a valuation study at the time of acquisition of Middleton to determine the value and estimated life of customer lists purchased in order to assist management in determining an appropriate method in which to amortize the asset. The amortization life is based on historic analysis of customer relationships combined with estimates of expected future revenues from customer accounts. Middleton has applied the same valuation method on all of the subsequent acquisitions. Customer lists and intangible assets with estimable useful lives are amortized over their respective estimated useful lives to their estimated residual values and reviewed for impairment.

The Company previously amortized customer lists on a straight-line basis over the weighted average expected life of the customer of 8 years. In the fourth quarter of 2007, the Company performed an extensive analysis to reassess the expected life of the customer lists and concluded that the expected life of the customer should be adjusted from 8 years to 5 years. The change in the estimated useful life used to account for customer lists resulted from our ongoing analysis of all pertinent factors, including actual customer attrition data, demand, and competition. The pertinent factors have been influenced by management s ongoing customer retention programs, as well as tactical and strategic initiatives to improve service delivery, customer satisfaction, and the credit worthiness of the subscriber customer base. The change in estimated useful life of customer lists was accounted for prospectively. During fiscal 2008 and fiscal 2009, we continued to assess the expected life of the customer and concluded that a 5 year life remains appropriate. Amortization expense for the years ended September 30, 2009 and 2008 amounted to $3,724,403 and $3,726,734, respectively.

Goodwill and other intangible assets

Goodwill represents the excess of costs over fair value of net assets of businesses acquired. Goodwill acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of Accounting Standards Codification (ASC) Topic 350, Intangibles -Goodwill and Other. The Company tests goodwill for impairment as of September 30th of each year and, more frequently, if a triggering event occurs utilizing a valuation study. Recoverability of goodwill is evaluated using a two-step process. The first step involves a comparison of the fair value of the reporting unit with its carrying amount. If a reporting unit s carrying amount exceeds its fair value, the second step is performed. The second step involves a comparison of the implied fair value and carrying value of that reporting unit s goodwill. To the extent that a reporting unit s carrying amount exceeds the implied fair value of its goodwill, an impairment loss is recognized.

In performing this assessment, we apply a weighting factor to the i) income approach ii) market capitalization approach under the market approach and the (iii) similar transactions method which is the second method under the market approach to develop the fair value of the reporting unit in order to assess its potential impairment of goodwill. The income approach is based on a discounted cash flow model which relies on a number of factors, including operating results, business plans, economic projections and anticipated future cash flows. Developing these future cash flow projections requires management to make significant assumptions and estimates regarding the sales, gross margin and operating expenses of the reporting unit, as well as consideration of future macroeconomic conditions and the impact of planned business or operational strategies, such as cost cutting measures and focusing on enhancing efficiencies. The U.S. economy and specifically the State of Florida experienced downward economic pressure during 2009 and 2008, which has impacted our growth and attrition rates. Over the forecasted period, we presumed a return to a more stable economic environment which would positively impact our overall growth and attrition rates. In addition, the forecasted period presumes a continued focus on enhancing our internal sales capabilities. Rates used to discount future cash flows are dependent upon interest rates and the cost of capital at a point in time.

The similar transactions method is a market approach methodology in which the fair value of a business is estimated by analyzing the prices at which companies similar to the subject, which are used as guidelines, have sold in controlling interest transactions (mergers and acquisitions). Specific information and prices analyzed were the acquisitions that we completed over the last two years as well as the receipt of an unsolicited offer from a third party to purchase our stock. Target companies are compared to the subject company, and multiples paid in transactions are analyzed and applied to subject company data, resulting in value indications. Comparability can be affected by, among other things, the product or service produced or sold, geographic markets served, competitive position, profitability, growth expectations, size, risk perception, and capital structure. The similar transactions market approach is difficult to apply as there are none to very few similar companies from which comparisons can be derived. There are inherent uncertainties related to these factors and our judgment in applying them to the analysis of goodwill impairment. It is possible that assumptions underlying the impairment analysis will change in such a manner that impairment in value may occur in the future.

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The Company has concluded that in conjunction with the Merger and the agreed upon purchase price a goodwill impairment triggering event occurred in September 2009. As of the date of the Merger Agreement, which was September 28, 2009, our book value per share was approximately $3.81 per share. We used the market approach and the income approach to perform the assessment. After careful consideration of the underlying assumptions and variables utilized in the above methods selected, we concluded that for purposes of valuing the Middleton Unit we would solely use the market approach based on the recent third party transaction of $2.75 per share. Both approaches gave us similar results of approximately $58.9 million in fair value of the Middleton Unit. Based on the results of the first step the carrying amount of the reporting unit exceeded its calculated fair value. If a reporting unit s carrying amount exceeds its fair value, the second step is performed. The second step involves a comparison of the implied fair value and carrying value of that reporting unit s goodwill. To the extent that a reporting unit s carrying amount exceeds the implied fair value of its goodwill, an impairment loss is recognized. Based on the results of the second step an impairment charge to goodwill was determined to be approximately $15.7 million at September 30, 2009.

In addition to our annual testing for impairment, management monitors changes in circumstances and financial results for potential impairment indicators. During each of the quarters in fiscal year 2009, after carefully considering many factors we determined that no indicators of impairment to our goodwill had occurred during the period prior to September 30, 2009, and therefore no impairment charges were recorded in the interim reporting periods.

Customer lists and intangible assets with estimable useful lives are amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment. Customer lists are stated at fair value based on the discounted cash flows over the estimated life of the customer contracts and relationships. We performed a valuation study at the time of acquisition of Middleton to determine the value and estimated life of customer lists purchased in order to assist management in determining an appropriate method in which to amortize the asset. The amortization life is based on historic analysis of customer relationships combined with estimates of expected future revenues from customer accounts. Middleton has applied the same acquisition method on all of the subsequent acquisitions. We previously amortized customer lists on a straight-line basis over the expected life of the customer of 8 years.

In the fourth quarter of 2007, the Company performed an extensive analysis to reassess the expected life of the customer lists and concluded that the expected life of the customer should be adjusted from 8 years to 5 years. The change in the estimated useful life used to account for customer lists resulted from our ongoing analysis of all pertinent factors, including actual customer attrition data, demand, and competition. The pertinent factors have been influenced by management s ongoing customer retention programs, as well as tactical and strategic initiatives to improve service delivery, customer satisfaction, and the credit worthiness of the subscriber customer base. The change in estimated useful life of customer lists was accounted for prospectively.

Impairment of long-lived assets and long-lived assets to be disposed of

We review long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying value of the assets exceeds the estimated fair value. Assets to be disposed of are reported at the lower of the carrying amount or estimated fair value less costs to sell. No asset impairment occurred during the years ended September 30, 2009 and 2008.

Revenue recognition

The Company s revenue recognition policies are designed to recognize revenues at the time services are rendered or when goods change hands.

Lawn and ornamental services are primarily recurring in nature on a bi-monthly basis. In general lawn and ornamental customers sign an initial one year contract, and revenues are recognized when services are rendered. The Company offers a discount to those customers who prepay a full year of services. The Company defers recognition of these advance payments and the related discounts until the underlying services have been rendered.

Pest control services primarily are billed annually with services being rendered on a semi-annual basis. In general pest control customers sign an initial one year contract. The Company recognizes revenue over the life of these contracts in proportion to the direct costs incurred. These costs have a direct relationship to the fulfillment of the Company s obligations under the contracts and are representative of the value provided to the customer.

Termite baiting is primarily billed annually with revenues recognized as services are rendered. At the inception of a new baiting services contract the system is installed. The Company recognizes revenue for the installation of the monitoring stations, initial directed liquid termiticide treatment and rendering of the initial monitoring services. The remaining portion of the annual fees billed are deferred and recognized as the remaining monitoring services are rendered over the annual period. Baiting renewal revenue is deferred and recognized over the annual period when the inspection and monitoring services are actually rendered. Liquid and drywood termite application revenues, both initial and renewal are recognized when the services are rendered.

Stock-based Compensation

Compensation costs recognized include costs related to 1) all share-based payments granted prior to but not yet vested as of January 1, 2006, based on previously estimated grant-date fair values and 2) all share-based payments granted subsequent to December 31, 2005 based on the grant-date estimated fair value. We use the Black-Scholes option pricing model to estimate the fair value of stock options granted See Note 10-Stock Options.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established when necessary to reduce tax assets to the amounts expected to be realized. In assessing the likelihood of realization, we consider estimates of future taxable income.

ASC Topic 740, Income Taxes prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The guidance requires that the Company determine whether the benefits of the Company s tax positions are more likely than not of being sustained upon audit based on the technical merits of the tax position. The Company did not have any unrecognized tax benefits and does not have any interest and penalties in the statement of operations for the year ended September 30, 2009. The tax years 2004-2007 remain subject to examination by major tax jurisdictions.

We currently have provided for a full valuation allowance against our net deferred tax assets. Based on the available objective evidence, management does not believe it is more likely than not that the net deferred tax assets will be realizable in the future. An adjustment to the valuation allowance would benefit net income in the period in which such determination is made if we determine that we would be able to realize our deferred tax assets in the foreseeable future. Our federal and state net operating loss carryforwards, amounting to approximately $19.9 million, which expire in various years through 2029.

Recent Accounting Pronouncements

See Note 1, Summary of Significant Accounting Policies in the Notes to Consolidated Financial Statements for a discussion of recent accounting pronouncements and their effect, if any, on the Company.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements and supplemental data required pursuant to this Item is as follows:

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Audit Committee, Board of Directors

and Stockholders of Sunair Services Corporation

and Subsidiaries

We have audited the consolidated financial statements of Sunair Services Corporation and Subsidiaries as listed in the accompanying index. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sunair Services Corporation and Subsidiaries as of September 30, 2009 and 2008, and the results of their operations and their cash flows for each of the years in the two-year period ended September 30, 2009 in conformity with accounting principles generally accepted in the United States of America.

Berenfeld Spritzer Shechter & Sheer, LLP

Certified Public Accountants

Fort Lauderdale, Florida

January 13, 2010

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SUNAIR SERVICES CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

SEPTEMBER 30,

	2009	2008
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 1,480,146	$ 2,974,382
Accounts receivable, net	2,262,863	2,597,447
Inventories, net	1,019,468	1,403,832
Prepaid and other current assets	651,044	2,829,535
Total Current Assets	5,413,521	9,805,196
PROPERTY, PLANT, AND EQUIPMENT, net	1,324,504	1,907,213
OTHER ASSETS:		
Software costs	616,461	246,979
Customer list, net	3,732,301	7,456,704
Goodwill	46,407,528	62,112,528
Other assets	264,057	254,790
Total Other Assets	51,020,347	70,071,001
TOTAL ASSETS	$ 57,758,372	$ 81,783,410

See accompanying notes to the consolidated financial statements.

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SUNAIR SERVICES CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

SEPTEMBER 30,

	2009	2008
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 1,563,665	$ 1,787,406
Accrued expenses	3,111,534	3,256,342
Unearned revenues	491,839	863,770
Customer deposits	2,847,675	3,149,715
Revolving line of credit, current portion	5,000,000	4,100,000
Note Payable - related party, current portion	5,000,000	
Notes payable and capital leases, current portion	4,427,398	2,306,189
Total Current Liabilities	22,442,111	15,463,422
LONG TERM LIABILITIES:		
Notes payable and capital leases, net of current portion	898,909	3,682,184
Note payable - related party, net of current portion		5,000,000
Revolving line of credit, net of current portion		5,500,000
Total Long Term Liabilities	898,909	14,182,184
TOTAL LIABILITIES	23,341,020	29,645,606
COMMITMENTS & CONTINGENCIES		
STOCKHOLDERS EQUITY:		
Preferred stock, no par value, 8,000,000 shares authorized, none issued and outstanding		
Common stock, $.10 par value, 100,000,000 shares authorized, 13,093,588 and 13,091,088 shares issued and outstanding at September 30, 2009 and September 30, 2008, respectively	1,309,360	1,309,110
Additional paid-in capital	52,993,003	52,756,311
Accumulated deficit	(19,885,011)	(1,927,617)
Total Stockholders Equity	34,417,352	52,137,804
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 57,758,372	$ 81,783,410

See accompanying notes to the consolidated financial statements.

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SUNAIR SERVICES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE TWO YEARS ENDED SEPTEMBER 30,

	2009	2008
SALES	$ 51,162,213	$ 56,612,660
COST OF SALES	18,860,808	22,120,223
GROSS PROFIT	32,301,405	34,492,437
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	34,002,426	37,996,341
LOSS FROM OPERATIONS	(1,701,021)	(3,503,904)
OTHER INCOME (EXPENSES):		
Interest expense	(857,349)	(1,339,721)
Interest income	1,853	142,814
Gain (loss) on disposal of assets	6,477	(10,774)
Gain on extinguishment of debt	55,000	
Loss on impairment of goodwill	(15,705,000)	
Other income	30,952	75,000
Total Other Expenses	(16,468,067)	(1,132,681)
LOSS FROM OPERATIONS BEFORE INCOME TAXES	(18,169,088)	(4,636,585)
INCOME TAX PROVISION		
LOSS FROM CONTINUING OPERATIONS	(18,169,088)	(4,636,585)
INCOME FROM DISCONTINUED OPERATIONS, NET OF INCOME TAX BENEFIT OF $0 and $0 IN 2009 and 2008, RESPECTIVELY	211,694	(1,876,039)
NET LOSS	$ (17,957,394)	$ (6,512,624)
BASIC AND DILUTED (LOSS) INCOME PER SHARE:		
CONTINUING OPERATIONS	$ (1.39)	$ (0.35)
DISCONTINUED OPERATIONS	$ 0.02	$ (0.14)
NET LOSS	$ (1.37)	$ (0.49)
WEIGHTED AVERAGE SHARES OUTSTANDING:		
BASIC and DILUTED	13,091,713	13,091,088

See accompanying notes to the consolidated financial statements.

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SUNAIR SERVICES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDER S EQUITY

AND COMPREHENSIVE (LOSS) INCOME

FOR THE YEARS ENDED SEPTEMBER 30,

	Common Stock		Additional Paid-in	Retained	Accumulated Other Comprehensive	Total Stockholders
	Shares	Amount	Capital	Earnings	Income (Loss)	Equity
Balance at September 30, 2007	13,091,088	$ 1,309,110	$ 52,378,437	$ 4,585,007	$ 88,670	$ 58,361,224
Comprehensive income:						
Net loss				(6,512,624)		(6,512,624)
Currency translation adjustment					(88,670)	(88,670)