

SERVICE CORPORATION INTERNATIONAL

Form 10-Q

July 28, 2016

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2016

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 1-6402-1

SERVICE CORPORATION INTERNATIONAL

(Exact name of registrant as specified in its charter)

Texas

(State or other jurisdiction of incorporation or organization)

74-1488375

(I. R. S. employer identification number)

1929 Allen Parkway, Houston, Texas

(Address of principal executive offices)

77019

(Zip code)

713-522-5141

(Registrant's telephone number, including area code)

None

(Former name, former address, or former fiscal year, if changed since last report)

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 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 of 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 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 Smaller reporting company

(Do not check if smaller reporting company)

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

YES NO

The number of shares outstanding of the registrant's common stock as of July 26, 2016 was 193,630,022 (net of treasury shares).

Table of Contents

SERVICE CORPORATION INTERNATIONAL
INDEX

	Page
<u>Glossary</u>	<u>3</u>
<u>Part I. Financial Information</u>	<u>5</u>
<u>Item 1. Financial Statements</u>	<u>5</u>
<u>Unaudited Condensed Consolidated Statement of Operations — Three and Six Months Ended June 30, 2016 and 2015</u>	<u>5</u>
<u>Unaudited Condensed Consolidated Statement of Comprehensive Income — Three and Six Months Ended June 30, 2016 and 2015</u>	<u>6</u>
<u>Unaudited Condensed Consolidated Balance Sheet — June 30, 2016 and December 31, 2015</u>	<u>7</u>
<u>Unaudited Condensed Consolidated Statement of Cash Flows — Six Months Ended June 30, 2016 and 2015</u>	<u>8</u>
<u>Unaudited Condensed Consolidated Statement of Equity — Six Months Ended June 30, 2016 and 2015</u>	<u>9</u>
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	<u>10</u>
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>41</u>
<u>The Company</u>	<u>41</u>
<u>Financial Condition, Liquidity, and Capital Resources</u>	<u>41</u>
<u>Results of Operations - Three and Six Months Ended June 30, 2016 and 2015</u>	<u>48</u>
<u>Critical Accounting Policies</u>	<u>54</u>
<u>Cautionary Statement on Forward-Looking Statements</u>	<u>54</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>55</u>
<u>Item 4. Controls and Procedures</u>	<u>55</u>
<u>Part II. Other Information</u>	<u>56</u>
<u>Item 1. Legal Proceedings</u>	<u>56</u>
<u>Item 1A. Risk Factors</u>	<u>56</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>56</u>
<u>Item 6. Exhibits</u>	<u>56</u>
<u>Signature</u>	<u>57</u>

Table of Contents

GLOSSARY

The following terms are common to the deathcare industry, are used throughout this report, and have the following meanings:

Atneed — Funeral, including cremation, and cemetery arrangements sold once death has occurred.

Burial Vault — A reinforced container intended to inhibit the subsidence of the earth and house the casket after it is placed in the ground, also known as outer burial containers.

Cancellation — Termination of a preneed contract, which relieves us of the obligation to provide the goods and services included in the contract. Cancellations may be requested by the customer or be initiated by us for failure to comply with the contractual terms of payment. State or provincial laws govern the amount of refund, if any, owed to the customer.

Care Trust Corpus — The deposits and net realized capital gains and losses included in a perpetual care trust that cannot be withdrawn. In certain states, some or all of the net realized capital gains can be distributed, so they are not included in the corpus.

Cemetery Perpetual Care or Endowment Care Fund (ECF) — A trust fund established for the purpose of maintaining cemetery grounds and property into perpetuity, also referred to as a cemetery perpetual care trust. For these trusts, the corpus remains in the trust in perpetuity and the net ordinary investment earnings are distributed to us regularly and are intended to defray our expenses incurred to maintain the cemetery. In certain states, some or all of the net realized capital gains can also be distributed.

Cemetery Property — Developed lots, lawn crypts, mausoleum spaces, niches and cremation memorialization property items (constructed and ready to accept interments) and undeveloped land we intend to develop for the sale of interment rights. Includes the construction-in-progress balance during the pre-construction and construction phases of projects creating new property inventory.

Cemetery Property Amortization — The non-cash recognized expenses of cemetery property interment rights, which are recorded by specific identification with the cemetery property revenue for each contract.

Cemetery Property Revenue — Recognized sales of interment rights in cemetery property when a minimum of 10% of the sales price has been collected and the property has been constructed and is available for interment.

Cemetery Merchandise and Services — Stone and bronze memorials, markers, burial vaults, floral placement, graveside services, merchandise installations, urns, outer burial containers, and burial openings and closings.

Cremation — The reduction of human remains to bone fragments by intense heat.

Cremation Memorialization — Products specifically designed to commemorate and honor the life of an individual that has been cremated. These products include cemetery property inventory types that provide for the disposition of cremated remains within our cemeteries such as benches, boulders, statues, etc. They also include memorial walls and books where the name of the individual is inscribed but the remains have been scattered or kept by the family.

Funeral Merchandise and Services — Merchandise such as burial caskets and related accessories, burial vaults, urns and other cremation receptacles, casket and cremation memorialization products, and flowers and professional services relating to funerals including arranging and directing services, use of funeral facilities and motor vehicles, removal, preparation, embalming, cremations, memorialization, visitations, and catering.

Funeral Recognized Preneed Revenue — Funeral merchandise and travel protection sold on a preneed contract and delivered before a death has occurred.

Funeral Services Performed — The number of funeral services, including cremations, provided after the date of death, sometimes referred to as funeral volume.

General agency (GA) revenue — Commissions we receive from third-party life insurance companies for life insurance policies sold to preneed customers for the purpose of funding preneed funeral arrangements. The commission rate paid is determined based on the product type sold, the length of payment terms, and the age of the insured/annuitant.

Interment — The burial or final placement of human remains in the ground, in mausoleums, in niches, or in cremation memorialization property.

Lawn Crypt — An underground outer burial receptacle constructed of concrete and reinforced steel, which is usually pre-installed in predetermined designated areas.

Marker — A method of identifying a deceased person in a particular burial space, crypt, niche, or cremation memorialization property. Permanent burial and cremation memorialization markers are usually made of bronze or stone.

3

Table of Contents

Maturity — When the underlying contracted merchandise is delivered or service is performed, typically at death. This is the point at which preneed contracts are converted to atneed contracts (note — delivery of certain merchandise and services can occur prior to death).

Mausoleum — An above ground structure that is designed to house caskets and cremation urns.

Merchandise and Service Trust — A trust account established in accordance with state or provincial law into which we deposit the required percentage of customers' payments for preneed funeral, cremation, or cemetery merchandise and services to be delivered or performed by us in the future. The amounts deposited can be withdrawn only after we have completed our obligations under the preneed contract or the cancellation of the contract.

Preneed — Purchase of cemetery property interment rights and merchandise and services prior to death occurring.

Preneed Backlog — Future revenue from unfulfilled preneed funeral, cremation, and cemetery contractual arrangements.

Preneed Cemetery Production — Sales of preneed or atneed cemetery contracts. These sales are recorded in Deferred preneed cemetery revenue until the merchandise is delivered, the service is performed, or when a minimum of 10% of the sales price has been collected and the property has been constructed and is available for interment.

Preneed Funeral Production — Sales of preneed funeral trust-funded and insurance-funded contracts. Preneed funeral trust-funded contracts are recorded in Deferred preneed funeral revenue until the merchandise is delivered or the service is performed. We do not reflect the unfulfilled insurance-funded preneed funeral contract amounts in our Consolidated Balance Sheet. The proceeds of the life insurance policies will be reflected in revenue as these funerals are performed by us in the future.

Sales Average — Average revenue per funeral service performed, excluding the impact of funeral recognized preneed revenue, GA revenue, and certain other revenue.

Trust Fund Income — Recognized investment earnings from our merchandise and service and perpetual care trust investments.

As used herein, "SCI", "Company", "we", "our", and "us" refer to Service Corporation International and companies owned directly or indirectly by Service Corporation International, unless the context requires otherwise.

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SERVICE CORPORATION INTERNATIONAL
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS
(UNAUDITED)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2016	2015	2016	2015
	(In thousands, except per share amounts)			
Revenue	\$751,710	\$754,354	\$1,500,981	\$1,502,471
Costs and expenses	(590,339)	(588,097)	(1,178,114)	(1,158,770)
Gross profit	161,371	166,257	322,867	343,701
General and administrative expenses	(36,260)	(33,095)	(73,768)	(67,645)
Losses on divestitures and impairment charges, net	(30,641)	(5,582)	(30,988)	(7,361)
Operating income	94,470	127,580	218,111	268,695
Interest expense	(39,398)	(42,982)	(82,480)	(85,921)
Loss on early extinguishment of debt	(21,898)	—	(22,479)	—
Other expense, net	(535)	(109)	(746)	(167)
Income before income taxes	32,639	84,489	112,406	182,607
Provision for income taxes	(16,746)	(31,007)	(49,059)	(67,660)
Net income from continuing operations	15,893	53,482	63,347	114,947
Net loss from discontinued operations, net of tax	—	(390)	—	(390)
Net income	15,893	53,092	63,347	114,557
Net income attributable to noncontrolling interests	(273)	(497)	(282)	(587)
Net income attributable to common stockholders	\$15,620	\$52,595	\$63,065	\$113,970
Basic earnings per share:				
Net income attributable to common stockholders	\$0.08	\$0.26	\$0.32	\$0.56
Basic weighted average number of shares	193,806	202,466	194,366	202,966
Diluted earnings per share:				
Net income attributable to common stockholders	\$0.08	\$0.25	\$0.32	\$0.55
Diluted weighted average number of shares	196,718	206,746	197,463	207,221
Dividends declared per share	\$0.13	\$0.10	\$0.25	\$0.20

(See notes to unaudited condensed consolidated financial statements)