

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C.  
20549

FILE COPY

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 1986

Commission file number: 0-11917

THE DAVEY TREE EXPERT COMPANY  
(Exact name of Registrant as specified in its charter)

Ohio  
(State of Incorporation)

34-0176110  
(IRS Employer Identification No.)

1500 North Mantua Street  
Kent, Ohio  
(Address of principal executive offices)

44240  
(Zip Code)

Registrant's telephone number, including area code: (216) 673-9511

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

None

(Title of class)

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

Common Shares, \$1 par value

(Title of class)

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, and (2) has been subject to such filing requirements for the past 90 days.

Documents incorporated by reference: Portions of the Registrant's definitive Proxy Statement for its 1987 Annual Meeting of Shareholders (Part III).

The aggregate "market value" (See Item 5 hereof) of voting stock held by non-affiliates of the Registrant at March 15, 1987 (based upon excluding the total number of Common Shares reported in Item 12 hereof), was \$35,618,011.

Common Shares outstanding at March 15, 1987: 689,203

Index to Exhibits is located on sequential page 16.

FORM 10-K

THE DAVEY TREE EXPERT COMPANY

Year Ended December 31, 1986

PART I

Item 1. Business.

General. The Davey Tree Expert Company, which was incorporated in 1909, and its subsidiaries (the "Registrant") are in the business of providing horticultural services to a variety of residential, corporate, institutional and governmental customers. Horticultural services include the treatment, preservation, maintenance, cultivation, planting and removal of trees, shrubs and other plant life and also include the practices of landscaping, tree surgery, tree feeding, tree spraying and line clearing for public utilities. Horticultural services also involve the application of scientifically formulated fertilizers, herbicides and insecticides with hydraulic spray equipment on residential and commercial lawns.

Competition and Customers. The Registrant is one of the largest national organizations in the private horticultural services industry. The Registrant competes with other national and local firms with respect to its services, although the Registrant believes that no other firm, whether national or local, offers the range of services that it offers.

Competition in private horticultural services is generally localized but very active and widespread. The principal methods of competition are advertising, customer service, image, performance and reputation. The Registrant's program to meet its competition stresses the necessity for its employees to have and to project to customers a thorough knowledge of horticulture and utilization of modern, well-maintained equipment and also stresses the Registrant's ability to render technical and diagnostic support for its private horticultural services. Pricing is not always a critical factor in a customer's decision. Pricing is, however, the principal method of competition in providing horticultural services to utility customers, although in most instances consideration is given to reputation and past production performance.

The Registrant provides a wide range of horticultural services to private companies, public utilities, local, state and Federal agencies, and a variety of industrial, commercial and residential customers. During the fiscal year ended December 31, 1986, the Registrant had sales of approximately \$32,000,000 (24% of total sales) to Pacific Gas & Electric Company.

Regulation and Environment. The Registrant's facilities and operations, in common with those of the industry generally, are subject to governmental regulations designed to protect the environment. This is particularly important with respect to the Registrant's services regarding insect and disease control, because these services involve to a considerable degree the blending and application of spray materials, which require formal licensing in most areas. The Registrant believes that it is in compliance with existing Federal, state and local laws regulating the use of materials in its spraying operations as well as the other aspects of its business that are subject to any such regulation.

Marketing. The Registrant solicits business from residential and commercial customers principally through direct mail programs and to a lesser extent through the placement of advertisements in national magazines and trade journals and in local newspapers and "yellow pages" telephone directories. Business from utility customers is obtained principally through negotiated contracts and competitive bidding. All sales and services are carried out through personnel who are direct employees. The Registrant does not use agents and does not franchise its name or business.

Seasonality. The Registrant's business is highly seasonal. Sales and earnings are generally highest in the second and third quarters of the calendar year, and historically the Registrant has incurred losses in the first quarter. This seasonality has historically created heavy demands for additional working capital in the first four to six calendar months ranging from \$2,000,000 to \$8,000,000, and the Registrant borrows against bank commitments for short-term loans in the form of lines of credit and a revolving credit agreement to provide the necessary funds. Services to utility customers show only small fluctuations in volume throughout the year. Extreme fluctuations do exist, however, in horticultural services to private customers.

Other Factors. The constant changes in environmental conditions, environmental awareness, technology and social attitudes make it necessary for the Registrant to maintain a high degree of awareness of the impact such changes have on the market for its services. Environmental controls inhibit the economic disposal of debris, which directly affects the Registrant's profitability. The Registrant believes, however, that the opportunities resulting from the environmental consciousness of the general public more than offset most of the environmental controls by which it is affected.

Rapid changes in equipment technology require a constant updating of equipment and processes to ensure competitive services to the Registrant's clients. Also, the Registrant must continue to assure its compliance with the Occupational Health and Safety Act. In keeping with

these requirements, capital expenditures in 1985 and 1986 were approximately \$14,350,000 and \$10,595,000 respectively. These expenditures included \$3,017,000 related to the completion of the Registrant's new headquarters in 1985, and \$1,933,000 related to the acquisition of a subsidiary in 1986.

Employees. The Registrant employs between 3,500 and 3,800 persons, depending upon the season, and considers its employee relations to be good.

Foreign and Domestic Operations. The Registrant and its Canadian subsidiaries sell the Registrant's services to customers in the United States and Canada, respectively.

The Registrant does not consider its foreign operations to be material and considers the risks attendant to its business with foreign customers, other than currency translation risks, to be not materially different from those attendant to business with its domestic customers.

Item 2. Properties.

The following table lists certain information with respect to major properties owned by the Registrant and used in connection with its operations.

<u>Location</u>	<u>Acreage</u>	<u>Building Sq. Ft</u>
Cincinnati, Ohio	2.5	7,200
Livermore, California	10.0	27,737
Winter Park, Florida	1.0	2,500
Chamblee, Georgia	1.9	7,000
East Dundee, Illinois	4.0	7,500
Indianapolis, Indiana	1.5	5,000
Grand Rapids, Michigan	4.0	2,300
Troy, Michigan	2.0	10,200
Cheektowaga, New York	6.9	3,200
Bayport, New York	2.0	7,000
Charlotte, North Carolina	3.1	4,900
Kent, Ohio (multiple)	124.5	111,608
Toledo, Ohio	.5	4,300
Wooster, Ohio	228.0	7,800
Pittsburgh, Pennsylvania	2.5	2,000
Ninety-Six, South Carolina	6.2	6,150
Houston, Texas	1.6	8,200
Chantilly, Virginia	2.0	8,900
Downsview, Ontario, Canada	.5	2,800
Baltimore, Maryland	3.3	22,500
Lancaster, New York	3.0	6,600
Bettendorf, Iowa	.5	320
Richmond, Virginia	.5	1,200
Mecklenburg, North Carolina	15.6	-0-
Penn. Twp., Pennsylvania	5.7	-0-
Soco Gap, North Carolina	17.0	-0-

The Registrant also rents approximately 60 other premises ranging from desk space with parking to disposal and storage use. The Registrant believes that all of these properties have been adequately maintained and are suitable and adequate for its business as presently conducted.

Item 3. Legal Proceedings.

There are no material legal proceedings, other than ordinary routine litigation incidental to the business, to which the Registrant or any of its subsidiaries is a party or of which any of their property is the subject.

Item 4. Submission of Matters to a Vote of Security Holders.

No matter was submitted during the fourth quarter of 1986 to a vote of security holders, through the solicitation of proxies or otherwise.

Executive Officers of the Registrant (included pursuant to Instruction 3 to paragraph (b) of Item 401 of Regulation S-K). The executive officers of the Registrant and their present positions and ages are as follows:

<u>Name</u>	<u>Position</u>	<u>Age</u>
John W. Joy	Chairman of the Board and Chief Executive Officer	64
R. Douglas Cowan	President and Chief Operating Officer	46
Eugene W. Haupt	Executive Vice President, and President of Davey Tree Surgery Company	64
David E. Adante	Secretary-Treasurer and Chief Financial Officer	35
Paul E. Daniel	Vice President, and Senior Vice President of Davey Tree Surgery Company	58
Dr. Roger C. Funk	Vice President-Human and Technical Resources	42
William F. Heim	Vice President and General Manager-Utility Services	59
James J. Reed	Vice President and Controller	58
Donald J. Shope	Vice President and General Manager-Residential and Commercial Services	53

<u>Name</u>	<u>Position</u>	<u>Age</u>
Gordon L. Ober	Vice President, New Ventures	37
Rosemary T. Nicholas	Assistant Secretary	43

Mr. Joy was elected Chairman of the Board and Chief Executive Officer in July 1985. From January, 1984, he had served as Chairman of the Board, President and Chief Executive Officer and prior to 1984 had served as President and Chief Executive Officer since before 1982.

Mr. Cowan was elected President and Chief Operating Officer in July, 1985. From January, 1984 until July, 1985 he served as Executive Vice President-Finance and Administration, Corporate Group, and prior to holding that position had served as Vice President, Finance, since before 1982.

Mr. Haupt was elected Executive Vice President, and President of Davey Tree Surgery Company in July, 1985. From January, 1984 to July 1985 he served as Executive Vice President-General Manager of Davey Tree Surgery Company, and had served as Vice President-General Manager of Davey Tree Surgery Company for more than 5 years prior to January, 1984.

Mr. Adante was elected Secretary-Treasurer and Chief Financial Officer in July, 1985, and had served as Treasurer since January, 1984. He served as Assistant Treasurer beginning in May, 1982, and from prior to May, 1982, Mr. Adante was Internal Auditor of the Registrant.

Mr. Daniel was elected Vice President in May, 1984 and has served as Senior Vice President-Operations, Davey Tree Surgery Company for more than five years.

Dr. Funk was elected Vice President-Human and Technical Resources in January 1984 and had served as Vice President, Research and Development since prior to 1982.

Mr. Heim has been Vice President and General Manager-Utility Services for more than five years.

Mr. Reed was elected Vice President-Controller in December 1986. He served as Vice President-Operations Administration from September 1985 through December 1986, and as Controller from March 1984 through September 1985. Mr. Reed served as Executive Vice President of King Musical Instruments, Inc. from January, 1982 through September, 1983 and served as Vice President and Chief Financial Officer of King Musical Instruments, Inc. for a number of years prior to 1982.

Mr. Shope was elected Vice President and General Manager-Residential and Commercial Services in January, 1984, and had served as Vice President and General Manager-Tree Care Services since prior to 1982.

Mr. Ober was elected Vice President-New Ventures in March, 1986. He served as Vice President and Operations Manager-Residential and Commercial Services from January 1984 to March 1986 and as Vice President-Lawnscape Services from prior to 1982 to January 1984.

Mrs. Nicholas was elected Assistant Secretary in May, 1982 and has been employed as an executive secretary with the Registrant for more than five years.

Officers of the Registrant serve for a term of office from the date of their election to the next organizational meeting of the Board of Directors and until their respective successors are elected.

## PART II

### Item 5. Market for Registrant's Common Shares and Related Security Holder Matters.

There is no established public trading market for the Registrant's Common Shares. As of March 15, 1987 there were 725 record holders of the Registrant's Common Shares. During the year ended December 31, 1985, the Registrant paid a dividend of \$.19 per share in each of the first three quarters and \$.21 per share in the fourth quarter. During the year ended December 31, 1986, the Registrant paid a dividend of \$.21 per share in each of the first three quarters and \$.23 per share in the fourth quarter. The Registrant's agreements with its lenders provide that the payment of cash dividends during any year may not exceed the lesser of (a) 30% of the average of annual net earnings (as defined) for the prior three years or (b) 10% of consolidated net worth (as defined) as at the first day of that year. See Note D to Consolidated Financial Statements beginning on page F-11 of the Annual Report on Form 10-K.



Item 6. Selected Financial Data.

	Years Ended December 31				
	<u>1986</u>	<u>1985</u>	<u>1984</u>	<u>1983</u>	<u>1982</u>
	(000's omitted, except per share data)				
<b>Operating Results:</b>					
Revenues	\$133,156	\$129,221	\$118,915	\$104,557	\$ 84,618
Net Earnings	\$ 3,007	\$ 4,256	\$ 4,623	\$ 4,422	\$ 2,682
New Earnings Per Common Share	\$ 4.02	\$ 5.18	\$ 5.38	\$ 5.19	\$ 3.24
<b>At Year End:</b>					
Total Assets	\$ 52,630	\$ 50,609	\$ 46,769	\$ 36,967	\$ 29,335
Total Long-Term Debt	\$ 8,972	\$ 7,499	\$ 8,892	\$ 3,471	\$ 2,998
Cash Dividends Per Common Share	\$ .86	\$ .78	\$ .70	\$ .60	\$ .43

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The Registrant's management uses a number of measurements and ratios to gauge the Registrant's financial condition and to monitor trends in key performance areas in operations.

FINANCIAL CONDITION

Liquidity Measurements. Management believes that the following measurements are useful in evaluating the Registrant's ability to meet short-term obligations, in evaluating liquidity, and in evaluating the extent to which capital expenditures can be financed from internal cash flow.

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Working Capital (in 000's)	\$ 2,318	\$ 1,483	\$ 3,069
Current Ratio	1.1:1	1.1:1	1.2:1
Cash Flow from Operations (in 000's)	\$13,454	\$14,015	\$13,037
Capital Expenditures (in 000's)	\$10,595	\$14,350	\$13,592
Cash Flow to Capital Expenditures Ratio	1.3:1	1.0:1	1.0:1
Cash Flow as % of Revenues	10.1%	10.8%	11.0%



At year end 1986, working capital (current assets less current liabilities) increased compared to the prior year, and was \$835,000 higher than 1985 and \$751,000 lower than 1984. The increase in 1986 was due to higher levels of cash, inventories, and prepaid expenses. The increase in cash arose from a high level of receipts from customers late in 1986. The increase in inventories resulted from increased buying to take advantage of favorable purchase terms in late 1986. Prepaid expenses increased due to higher prepaid insurance premiums.

Management believes that cash flow is the best measure of the Registrant's liquidity, particularly when related to capital expenditures. In 1986, cash flow decreased \$561,000 from 1985, and increased \$417,000 from 1984. The decrease in cash flow in 1986 was primarily due to lower net income. As a percentage of revenues, cash flow was at 10.1%, compared to levels of 10.8% and 11.0% for the previous two years. However, capital expenditures for 1986 were reduced to \$10,595,000 from levels of \$14,350,000 and \$13,592,000 for 1985 and 1984 respectively. In 1986, cash flow in excess of capital expenditures was \$2,859,000, compared to capital expenditures in excess of cash flow of \$335,000 in 1985 and \$555,000 in 1984. It continues to be management's objective to finance capital expenditures from internally generated funds (cash flow) as much as possible, so long as that posture does not prevent the Registrant from maximizing growth opportunities.

Leverage Measurements. These ratios measure the extent to which the Registrant has been financed by debt, or, put another way, the proportion of the total assets employed in the business that have been provided by creditors as compared to shareholders. Debt is defined as total liabilities.

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Equity to Debt Ratio	.9:1	1.0:1	1.0:1
Debt as % of Assets	52.9%	49.7%	49.1%
Equity as % of Assets	47.1%	50.3%	50.9%

At the end of 1986, the relationship of equity to debt declined slightly to .9:1, compared to 1.0:1 in 1984 and 1985. The decline in the ratio for the past three years was caused by the debt incurred in connection with the construction of the Corporate Center and by the Registrant's redemption of common stock. Redemptions in 1986, 1985 and 1984 were \$3,838,000, \$2,815,000, and \$1,503,000, respectively. Since a significant number of the shares redeemed in recent years were due to retirees and employees nearing retirement, management believes that the current level of redemptions will not continue in the near term, and that the impact of redemptions on the debt to equity ratio will tend to diminish. Management believes that a ratio of less than 1.0:1 is not necessarily unhealthy, and continues to evaluate opportunities which could require additional debt financing.

The Registrant will continue to finance its operations needs with borrowing under a Revolving Credit Agreement and short-term lines of credit. At March 15, 1987, the Registrant had available \$12,700,000 in credit commitments under all revolving credit and line of credit arrangements. Management believes those arrangements to be sufficient for the Registrant's borrowing needs for operations.

Common Share Measurements. With these measurements, shareholders can assess the Registrant's earnings performance, dividend payout, and equity position as related to their shareholdings.

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Earnings Per Share	\$ 4.02	\$ 5.18	\$ 5.38
Dividends Per Share	\$ .86	.78	\$ .70
Book Value Per Share	\$35.54	\$33.12	\$29.31
ESOT Market Valuation Per Share	\$51.68	\$35.40	\$32.20

The earnings per share measurements are shown as if all outstanding stock options had been exercised at December 31 of the years presented. The lower number of shares outstanding at December 31, 1986, due to the redemptions of stock have favorably affected the per share measurement.

The lower earnings in 1986 are reflected in the per share measurements in the table above. Earnings per share in 1986 declined to \$4.02 per share, down \$1.16 from 1985, and \$1.36 from 1984. The market value per share increased to \$51.68 per share, up 46% from 1985, and 61% from 1984. The increase in the Registrant's market valuation per share for 1986 was affected by the lower number of shares outstanding, which had a favorable impact on the Registrant's earnings per share and, the increase in the price earnings multiples of publicly traded stocks and stock indexes. These two factors combined to effect the increase in the valuation of the Registrant's stock.

Dividends paid per share were again increased in 1986. In 1986, they were increased \$.08 per share, or 10% over 1985, compared to an increase in 1985 of \$.08 per share, or 11% over 1984. Total dividends paid to shareholders in 1986 were \$630,000, compared to \$616,000 in 1985 and \$567,000 in 1984. It is the Registrant's objective to provide a fair return on investment to its shareholders through improved dividends, so long as the Registrant can financially justify such a policy. The increases in each of the last five years reflect this objective.

The Registrant's Common Shares are not listed or traded on an active stock market and market prices are, therefore, not available. Each year, an independent consultant is retained by the Registrant's Employee Stock Ownership Trust (ESOT) to evaluate the Registrant's performance and financial condition and determine a fair market value, as of the end of the year, for the shares owned by the ESOT. The valuations are presented due to the absence of other market data.

## RESULTS OF OPERATIONS

Profitability Measurements. Management uses these measurements to evaluate its overall effectiveness in increasing revenues and generating returns on revenues.

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Increase in Revenues	3.0%	8.7%	13.7%
Operating Earnings as % of Revenues	5.5%	6.1%	7.2%
Pre-Tax Earnings as % of Revenues	4.3%	5.4%	6.4%
Net Earnings as % of Revenue	2.3%	3.3%	3.9%

Revenues for 1986 of \$133,156,000 set a new record and increased \$3,935,000, or 3.0%, over 1985, compared to an 8.7% increase in revenues in 1985 and 13.7% in 1984. Revenues increased in both the Kent Operating Company and Davey Tree Surgery Company, and in most of the Registrant's major service lines.

Operating costs increased 3.5% over 1985, and as a percentage of revenues, increased to 68.3% as compared with 68.0% in 1985, and 65.8% in 1984. The increases in 1986 and 1985 were primarily due to higher insurance costs and unfavorable results from the Registrant's retrospective insurance programs.

Selling, General and Administrative ("S, G&A") costs increased 3.2% in 1986, and at a slightly higher rate than the revenue increase of 3.0%. As a percentage of revenues, these costs were 19.0% in 1986, compared to 19.0% in 1985, and 20.3% in 1984. Management is committed to continuing the control of S,G&A expenses, and believes that these expenses will remain at or below current levels in the short term.

Depreciation expense in 1986 increased 6.9% over 1985, compared to an increase of 11.7% in 1985, and an increase of 22.8% in 1984. As a percentage of revenues, depreciation expense was 7.2% in 1986, compared to 6.9% in 1985, and 6.7% in 1984. The Registrant records its depreciation expense on a double-declining balance method, which provides a higher depreciation expense in the early years of asset life. Each year's expense, therefore, is significantly affected by the level of capital expenditures in the current and immediately preceding years. Capital expenditures, exclusive of the investment in a subsidiary in 1986, and Corporate Center expenditure in 1985 and 1984, were \$8,662,000, \$11,333,000 and \$10,902,000, respectively. Capital expenditures for 1986 were reduced due to the leveling of the growth pattern of the previous three years, and by improved utilization of existing equipment.

Interest expense in 1986 increased to \$1,363,000 compared to \$1,191,000 in 1985 and \$1,087,000 in 1984. Interest expense for 1986 and 1985 included \$363,000 and \$232,000, respectively, related to the financing of the Corporate Center. Excluding the effect of the Corporate Center financing in 1985, interest expense increased in 1986 by \$41,000, or 4.3% over the 1985 level. Management believes that interest expense will remain at or below current levels in the short term.

As a result of the above factors, earnings before income taxes decreased, and as a percentage of revenues, declined to 4.3%. In addition, the effect of the Tax Reform Act of 1986 in limiting the investment tax credit caused an increase in the effective income tax rate to 47.1% compared to effective tax rates of 38.6% for 1985 and 39.0% for 1984, contributing to a decline in net earnings to 2.3% of revenues. Management believes that both pre-tax and net earnings will improve in the short term from efforts to reduce operating costs and from lower effective tax rates as provided in the Tax Reform Act for 1987 and beyond.

Asset Utilization Measurements. Management uses these measurements to evaluate its efficiency in employing assets to generate revenues and returns.

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Average Assets Employed (in 000's)	\$51,620	\$48,689	\$41,868
Asset Turnover (Revenues to Average Assets)	2.6	2.7	2.8
Return on Average Assets	5.8%	8.7%	11.0%

Due to capital expenditures for the Corporate Center of \$3,017,000 and \$2,478,000 in 1985 and 1984, respectively, the average assets employed and the asset turnover ratio for those years as well as for 1986 are somewhat distorted as compared to prior years. Excluding the effect of the Corporate Center from the above table, the turnover rate would have been 2.9 in each of the three years, and the return on average assets would have been 6.7%, 9.5% and 11.4%, respectively. Notwithstanding the effect of the Corporate Center on these measurements, the deterioration in the 1986 return on assets was due to the lower net earnings percentage (2.3%), which resulted primarily from higher insurance costs, and higher than normal income taxes.

Management believes that high insurance costs will continue to adversely affect return on assets for the short-term but is steadfast in its goal to achieve a turnover rate of at least 3.0 and to improve the net earnings percentage to provide a return on assets of 15%.

Item 8. Consolidated Financial Statements and Supplementary Data.

The opinion of independent certified public accountants, the audited consolidated financial statements, and the notes to the audited consolidated financial statements required by this Item 8 appear on pages F-1 through F-19 of this Annual Report on Form 10-K.

Item 9. Disagreements on Accounting and Financial Disclosure.

Within the 24 months prior to the date of the most recent financial statements, no Form 8-K under the Exchange Act has been filed to report a change of accountants and a disagreement on any matter of accounting principles or practices or financial statement disclosure.

PART III

Item 10. Directors and Executive Officers of the Registrant.

The information regarding directors of the Registrant appearing under the heading "Proposal 1 - Election of Directors" in the Registrant's definitive Proxy Statement for its 1987 Annual Meeting of Shareholders is hereby incorporated by reference.

Item 11. Executive Compensation.

The information regarding compensation of the Registrant's executive officers appearing under the heading "Compensation of Executive Officers" in the Registrant's definitive Proxy Statement for its 1987 Annual Meeting of Shareholders is hereby incorporated by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management.

The information regarding the security ownership of certain beneficial owners and management appearing under the heading "Beneficial Ownership of Voting Stock" in the Registrant's definitive Proxy Statement for its 1987 Annual Meeting of Shareholders is hereby incorporated by reference.

Item 13. Certain Relationships and Related Transactions.

The information regarding certain relationships and related transactions appearing under the headings "Proposal 1 - Election of Directors" and "Compensation of Executive Officers" in the Registrant's definitive Proxy Statement for its 1987 Annual Meeting of Shareholders is hereby incorporated by reference.

PART IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K.

(a)(1) and (a)(2) Financial Statements and Schedules. See the Index to Financial Statements and Financial Statement Schedules on page F-1 of this Annual Report on Form 10-K.

(a)(3) Exhibits. See the Index to Exhibits on sequentially numbered page 16 of this Annual Report on Form 10-K.

(b) Reports on Form 8-K. No reports on Form 8-K were filed during the last quarter of the period covered by this Annual Report on Form 10-K.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Annual Report on Form 10-K to be signed on its behalf by the undersigned thereunto duly authorized.

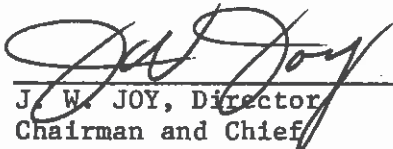
THE DAVEY TREE EXPERT COMPANY



By: J. W. Joy, Chairman and Chief  
Executive Officer

March 6, 1987

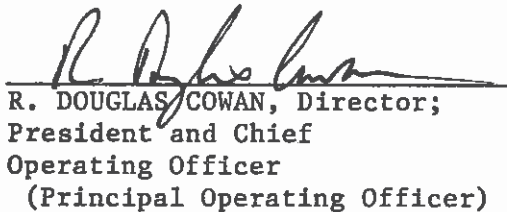
Pursuant to the requirements of the Securities Exchange Act of 1934, this Annual Report on Form 10-K has been signed below by the following persons on behalf of the Registrant and in the capacities indicated on March 6, 1987.



J. W. JOY, Director  
Chairman and Chief  
Executive Officer  
(Principal Executive Officer)



WILLIAM D. GINN, Director



R. DOUGLAS COWAN, Director;  
President and Chief  
Operating Officer  
(Principal Operating Officer)



EUGENE W. HAUPT, Director



THOMAS W. BLAZEY, Director



J MAURICE STRUCHEN, Director

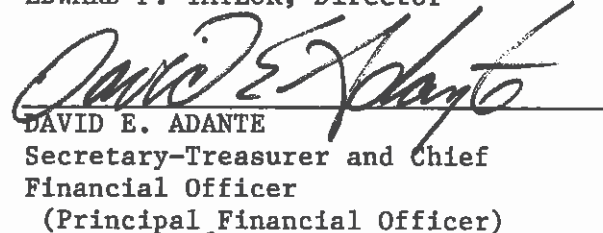
JAMES H. MILLER, Director



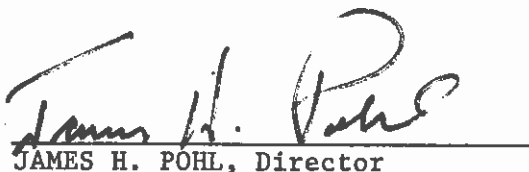
EDWARD P. TAYLOR, Director



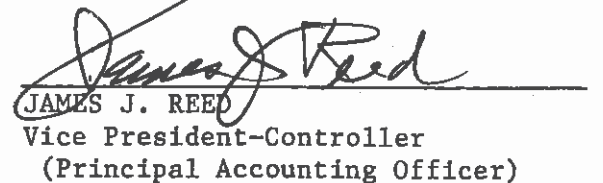
RICHARD E. DUNN, Director



DAVID E. ADANTE  
Secretary-Treasurer and Chief  
Financial Officer  
(Principal Financial Officer)



JAMES H. POHL, Director



JAMES J. REED  
Vice President-Controller  
(Principal Accounting Officer)



INDEX TO EXHIBITS

[Item 14(a)(3)]

<u>Exhibit No.</u>	<u>Description</u>	<u>Location or Sequential Page</u>
(3)(a)	1983 Amended Articles of Incorporation	Incorporated by reference to Exhibit 3(a) to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1983.
(3)(b)	1984 Amended Regulations of The Davey Tree Expert Company	Incorporated by reference to Exhibit 3(b) to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1984.
(4)	The Company is a party to certain instruments, copies of which will be furnished to the Securities and Exchange Commission upon request, defining the rights of holders of long-term debt identified in Note D of Notes to Consolidated Financial Statements.	
(9)	Voting Trust Agreement	Not applicable
(10)(a)	1980 Employee Stock Option Plan, as amended	Incorporated by reference to Exhibit 10 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1983
(10)(b)	1985 Incentive Stock Option Plan	Incorporated by reference to Exhibit 10(b) to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1985

<u>Exhibit No.</u>	<u>Description</u>	<u>Location or Sequential Page</u>
(11)	Statement re computation of per share earnings	Not applicable
(12)	Statement re computation ratios	Not applicable
(13)	Annual report to security holders, Form 10-Q or quarterly report to security holders	Not applicable
(18)	Letter re change in accounting principles	Not applicable
(19)	Previously unfiled documents	Not applicable
(22)	Subsidiaries of the Company	Incorporated by reference to Exhibit 22 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1983
(24)	Consent of independent auditors to incorporation of their opinion in Registrant's Statements on Form S-8 (File Nos. 2-73052, 2-77353 and 33-5755)	19
(25)	Power of Attorney	Not applicable
(28)	Additional Exhibits	Not applicable

INDEX TO FINANCIAL STATEMENTS  
AND FINANCIAL STATEMENT SCHEDULES  
[Item 14(a)(1) and (2)]

<u>Description</u>	<u>Page</u>
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OPINION OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors  
The Davey Tree Expert Company  
Kent, Ohio

We have examined the consolidated balance sheets of The Davey Tree Expert Company and subsidiary companies as of December 31, 1986, 1985 and 1984, and the related consolidated statements of earnings, shareholders' equity and changes in financial position for each of the three years in the period ended December 31, 1986. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of The Davey Tree Expert Company and subsidiary companies at December 31, 1986, 1985 and 1984 and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1986, in conformity with generally accepted accounting principles applied on a consistent basis.

Our examination also comprehended the schedules listed in the index at Item 14(a)(2). In our opinion, such schedules, when considered in relation to the basic financial statements, present fairly in all material respects the information shown therein.

*Touche Ross & Co*

TOUCHE ROSS & CO.

Akron, Ohio  
February 24, 1987

THE DAVEY TREE EXPERT COMPANY  
AND SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEETS

(Dollars in Thousands)

ASSETS

	December 31		
	<u>1986</u>	<u>1985</u>	<u>1984</u>
<b>CURRENT ASSETS:</b>			
Cash and short-term investments	\$ 1,210	\$ 399	\$ 771
Accounts receivable, less allowance for uncollectible accounts of \$315,000, \$184,000 and -0-	13,945	13,970	13,276
Operating supplies	1,335	886	812
Prepaid expenses	1,319	769	419
Deferred income taxes	66	52	36
Refundable income taxes	<u>82</u>	<u>748</u>	<u>389</u>
TOTAL CURRENT ASSETS	17,957	16,824	15,703
<b>OTHER ASSETS</b>	401	282	245
<b>PROPERTY AND EQUIPMENT:</b>			
Land and land improvements	1,906	1,738	1,307
Buildings and leasehold improvements	8,999	8,971	4,186
Equipment, principally revenue producing	68,300	61,467	52,969
Corporate Center under construction			2,569
Short-term investments of funds restricted for construction			<u>2,308</u>
	<u>79,205</u>	<u>72,176</u>	<u>63,339</u>
Less accumulated depreciation	<u>44,933</u>	<u>38,673</u>	<u>32,518</u>
NET PROPERTY AND EQUIPMENT	34,272	33,503	30,821
	<hr/>	<hr/>	<hr/>
TOTAL ASSETS	<u>\$52,630</u>	<u>\$50,609</u>	<u>\$46,769</u>

See notes to consolidated financial statements.

LIABILITIES AND SHAREHOLDERS' EQUITY

	December 31		
	<u>1986</u>	<u>1985</u>	<u>1984</u>
<b>CURRENT LIABILITIES:</b>			
Accounts payable	\$ 5,297	\$ 6,460	\$ 4,736
Accrued liabilities	8,461	8,010	6,946
Income taxes payable	312	87	67
Notes payable, bank	606		
Current maturities on long-term debt	<u>963</u>	<u>784</u>	<u>885</u>
<b>TOTAL CURRENT LIABILITIES</b>	<b>15,639</b>	<b>15,341</b>	<b>12,634</b>
<b>LONG-TERM DEBT</b>	<b>8,972</b>	<b>7,499</b>	<b>8,892</b>
<b>DEFERRED INCOME TAXES</b>	<b>2,920</b>	<b>2,017</b>	<b>1,186</b>
<b>OTHER LIABILITIES</b>	<u>317</u>	<u>297</u>	<u>283</u>
<b>TOTAL LIABILITIES</b>	<b>27,848</b>	<b>25,154</b>	<b>22,995</b>
<b>SHAREHOLDERS' EQUITY:</b>			
Common shares	1,091	1,091	1,084
Additional paid-in capital	1,285	974	557
Retained earnings	<u>33,019</u>	<u>30,632</u>	<u>27,075</u>
	<b>35,395</b>	<b>32,697</b>	<b>28,716</b>
<b>Less:</b>			
Treasury shares, at cost	9,695	6,209	3,676
Subscriptions receivable from employees			118
Future contributions to ESOT	<u>918</u>	<u>1,033</u>	<u>1,148</u>
<b>TOTAL SHAREHOLDERS' EQUITY</b>	<b>24,782</b>	<b>25,455</b>	<b>23,774</b>
<b>TOTAL LIABILITIES AND SHARE- HOLDERS' EQUITY</b>	<b><u>\$52,630</u></b>	<b><u>\$50,609</u></b>	<b><u>\$46,769</u></b>

THE DAVEY TREE EXPERT COMPANY  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF EARNINGS

(Dollars in Thousands)

	Year Ended December 31					
	1986		1985		1984	
REVENUES	\$133,156	100.0%	\$129,221	100.0%	\$118,915	100.0%
COSTS AND EXPENSES:						
Operating costs	90,981	68.3	87,908	68.0	78,252	65.8
Selling, general and administrative	25,278	19.0	24,493	19.0	24,181	20.3
Depreciation	9,526	7.2	8,908	6.9	7,973	6.7
	<u>125,785</u>	<u>94.5</u>	<u>121,309</u>	<u>93.9</u>	<u>110,406</u>	<u>92.8</u>
EARNINGS FROM OPERA- TIONS	7,371	5.5	7,912	6.1	8,509	7.2
INTEREST EXPENSE	(1,363)	(.7)	(1,191)	(.9)	(1,087)	(.9)
OTHER INCOME (EXPENSE) - NET	<u>(321)</u>	<u>(.5)</u>	<u>212</u>	<u>.2</u>	<u>160</u>	<u>.1</u>
EARNINGS BEFORE INCOME TAXES	5,687	4.3	6,933	5.4	7,582	6.4
INCOME TAXES	<u>2,680</u>	<u>2.0</u>	<u>2,677</u>	<u>2.1</u>	<u>2,959</u>	<u>2.5</u>
NET EARNINGS	<u>\$ 3,007</u>	<u>2.3%</u>	<u>\$ 4,256</u>	<u>3.3%</u>	<u>\$ 4,623</u>	<u>3.9%</u>
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING INCLUDING COMMON STOCK EQUIVALENTS	<u>748,449</u>		<u>821,139</u>		<u>859,067</u>	
NET EARNINGS PER COMMON SHARE	<u>\$ 4.02</u>		<u>\$ 5.18</u>		<u>\$ 5.38</u>	

See notes to consolidated financial statements.



THE DAVEY TREE EXPERT COMPANY  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF  
SHAREHOLDERS' EQUITY

YEARS ENDED DECEMBER 31, 1986, 1985 AND 1984

(Dollars in Thousands)

	<u>Par Value Common Shares</u>	<u>Additional Paid-In Capital</u>
BALANCE, JANUARY 1, 1984	\$1,075	\$ 161
Shares purchased		
Shares sold to employees		304
Options exercised	9	92
Receipts on subscriptions		
Contributions to ESOT		
Net earnings		
Dividends, \$.70 per share		
Net adjustment for foreign currency translation		
	<hr/>	<hr/>
BALANCE, DECEMBER 31, 1984	1,084	557
Shares purchased		
Shares sold to employees		319
Options exercised	7	98
Receipts on subscriptions		
Contributions to ESOT		
Net earnings		
Dividends, \$.78 per share		
Net adjustment for foreign currency translation		
	<hr/>	<hr/>
BALANCE, DECEMBER 31, 1985	1,091	974
Shares purchased		
Shares sold to employees		292
Options exercised		19
Contributions to ESOT		
Net earnings		
Dividends, \$.86 per share		
Net adjustment for foreign currency translation		
	<hr/>	<hr/>
BALANCE, DECEMBER 31, 1986	<u>\$1,091</u>	<u>\$1,285</u>

See notes to consolidated financial statements.

<u>Retained Earnings</u>	<u>Treasury Shares</u>	<u>Subscriptions Receivable From Employees</u>	<u>Future Contributions to ESOT</u>	<u>Total</u>
\$23,051	\$(2,433)	\$(291)	\$(1,418)	\$20,145
	(1,503)			(1,503)
	120			424
	140			241
		173		173
			270	270
4,623				4,623
(567)				(567)
(32)				(32)
27,075	\$(3,676)	\$(118)	\$(1,148)	23,774
	(2,815)			(2,815)
	116			435
	166			271
		118		118
			115	115
4,256				4,256
(616)				(616)
(83)				(83)
30,632	\$(6,209)		\$(1,033)	25,455
	(3,838)			(3,838)
	135			427
	217			236
			115	115
3,007				3,007
(630)				(630)
10				10
<u>\$33,019</u>	<u>\$(9,695)</u>	<u>\$ -0-</u>	<u>\$(918)</u>	<u>\$24,782</u>

**THE DAVEY TREE EXPERT COMPANY  
AND SUBSIDIARY COMPANIES**

**CONSOLIDATED STATEMENTS OF  
CHANGES IN FINANCIAL POSITION**

(Dollars in Thousands)

	<u>Year Ended December 31</u>		
	<u>1986</u>	<u>1985</u>	<u>1984</u>
<b>CASH PROVIDED FROM OPERATIONS:</b>			
Net earnings	\$ 3,007	\$ 4,256	\$ 4,623
Items not affecting cash:			
Depreciation and amortization	9,558	8,944	8,013
Deferred income taxes	889	815	401
	<u>13,454</u>	<u>14,015</u>	<u>13,037</u>
 Net book value of property and equipment disposals	 300	 452	 129
 Cash provided (used) by major components of working capital:			
Accounts receivable	25	(694)	(1,627)
Accounts payable and accrued liabilities	(712)	2,788	1,258
	<u>(687)</u>	<u>2,094</u>	<u>(369)</u>
 <b>TOTAL CASH PROVIDED FROM OPERATIONS</b>	 13,067	 16,561	 12,797
 <b>CASH PROVIDED (USED) FROM FINANCING ACTIVITIES:</b>			
Proceeds of long-term borrowings	2,267	491	6,305
Short-term financing - net	606		
Short-term investments of funds restricted for construction		2,308	(2,308)
ESOT payment of debt guaranteed by the Company	115	115	270
Sale of treasury shares:			
Receipts on subscriptions receivable		118	173
Proceeds from stock options exercised	236	271	241
Employee stock purchase plan	427	404	355
Other		31	69
	<u>3,651</u>	<u>3,738</u>	<u>5,105</u>
 <b>TOTAL CASH PROVIDED FROM FINANCING ACTIVITIES</b>	 3,651	 3,738	 5,105
 <b>TOTAL CASH PROVIDED</b>	 16,718	 20,299	 17,902

THE DAVEY TREE EXPERT COMPANY  
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENTS OF  
CHANGES IN FINANCIAL POSITION (Continued)

(Dollars in Thousands)

	<u>Year Ended December 31</u>		
	<u>1986</u>	<u>1985</u>	<u>1984</u>
<b>USES OF CASH:</b>			
Additions to property and equipment	\$ 8,604	\$11,333	\$11,114
Investment in subsidiary	1,933		
Additions to corporate center	58	3,017	2,478
Purchase of treasury shares	3,838	2,815	1,503
Reduction of long-term debt	615	1,985	1,028
Reduction of notes payable, bank			700
Other	229	905	594
Dividends	630	616	567
	<u>15,907</u>	<u>20,671</u>	<u>17,984</u>
INCREASE (DECREASE) IN CASH	811	(372)	(82)
CASH, BEGINNING OF YEAR	<u>399</u>	<u>771</u>	<u>853</u>
CASH, END OF YEAR	<u>\$ 1,210</u>	<u>\$ 399</u>	<u>\$ 771</u>

See notes to consolidated financial statements.

THE DAVEY TREE EXPERT COMPANY  
AND SUBSIDIARY COMPANIES

NOTES TO CONSOLIDATED  
FINANCIAL STATEMENTS

THREE YEARS ENDED DECEMBER 31, 1986

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation - The consolidated financial statements include the accounts of The Davey Tree Expert Company and its wholly-owned subsidiary companies, Davey Tree Surgery Company and Davey Tree Expert Co. of Canada, Limited. All significant intercompany transactions, accounts and profits have been eliminated.

Property and equipment are recorded at cost. Generally, the Company depreciates its land improvements, leasehold improvements and buildings by the straight-line method while using the double declining balance method for equipment. The estimated useful lives used in computing depreciation are: land improvements, 5-20 years; buildings and leasehold improvements, 5-40 years; equipment, 3-10 years.

Income Taxes - Deferred income taxes are provided to recognize the effect of timing differences between financial statement and income tax reporting for depreciation and other items. Investment tax credits are used to reduce the income tax provision in the year in which they are earned.

B. COMMON SHARES

At December 31, 1986 there were 3,000,000 shares of \$1.00 par value common stock authorized. There were 1,091,055, 1,091,055 and 1,083,685 shares issued and 393,758, 322,522 and 272,475 shares in the treasury at December 31, 1986, 1985 and 1984, respectively.

The Company's stock is not listed or traded on an active stock market and market prices are, therefore, not available. Semi-annually, the fair value based upon the Company's performance and financial condition is determined by an investment banking firm.

C. ACCRUED LIABILITIES

Accrued liabilities consisted of:

	December 31		
	1986	1985	1984
	(000's omitted)		
Workers' compensation	\$3,574	\$3,504	\$2,516
Wages, salaries, etc.	2,435	2,317	2,274
Taxes, other than taxes on income	1,276	1,056	1,002
Accrued vacation	951	963	877
Other	225	170	277
<b>TOTAL</b>	<b><u>\$8,461</u></b>	<b><u>\$8,010</u></b>	<b><u>\$6,946</u></b>

D. SHORT-TERM AND LONG-TERM DEBT

Short-Term Debt

At December 31, 1986, the Company had unused short-term lines of credit with four banks totalling \$3,050,000, generally at the banks' prime rate. Within the total commitment, the Company has the option to borrow specific amounts for periods of 30, 60 or 90 days at the London Interbank Offered Rate (LIBOR), which is generally less than the U.S. prime rate.

Long-Term Debt

Long-term debt consists of:

	December 31		
	1986	1985	1984
	(000's omitted)		
8.95% Industrial Development Bonds	\$3,625	\$4,125	\$4,500
Revolving credit agreement	3,600	2,000	3,100
Long-term debt of ESOT	918	1,033	1,148
Subordinated notes - stock redemption	1,380	775	355
3% Community Development Block Grant	350	350	350
Other	62		324
	<u>9,935</u>	<u>8,283</u>	<u>9,777</u>
Less current maturities	963	784	885
<b>TOTAL LONG-TERM DEBT</b>	<b><u>\$8,972</u></b>	<b><u>\$7,499</u></b>	<b><u>\$8,892</u></b>

D. SHORT-TERM AND LONG-TERM DEBT (Continued)

Long-Term Debt (Continued)

As of December 31, 1986, the total annual installments required to be paid on long-term debt in the years 1987 to 1991 are as follows: 1987, \$963,000; 1988, \$963,000; 1989, \$1,618,000; 1990, \$758,000; 1991, \$658,000.

Corporate Center Financing

The Company completed construction of its new corporate center during 1985. Financing for the construction of the center was provided by the issuance of 8.95% Industrial Development Bonds, and a 3% Community Development Block Grant in the amounts of \$4,500,000 and \$350,000, respectively.

Interest expense incurred on the Industrial Development Bonds during the period of construction, net of interest earned on the investment of these funds prior to their use for construction, was capitalized and included in the cost of the corporate center. The net interest capitalized was \$122,000 and \$56,000 in 1985 and 1984, respectively.

The Industrial Development Bonds are to be repaid in equal quarterly principal payments of \$125,000 commencing on May 1, 1985 and ending on February 1, 1994. The Community Development Block Grant is to be repaid by principal payments of \$100,000 on August 1, 1989 and \$250,000 on August 1, 1994.

Revolving Credit Agreement

On March 21, 1985, a new Revolving Credit Agreement was executed to permit the Company to borrow, repay and reborrow up to \$9,000,000. The Agreement provides for interest on any borrowings on the "Revolver" at prime, plus a commitment fee of 3/8 of 1% on the unborrowed commitment. In accordance with an informal arrangement, the banks expect the Company to maintain compensating balances equal to approximately 3% of the Revolving Credit Agreement commitment. Borrowings under the "Revolver" may be converted at the Company's option to a 5-year term loan payable in equal quarterly installments plus interest at a floating rate of 1/2 of 1% over the banks' prime rate.



D. SHORT-TERM AND LONG-TERM DEBT (Continued)

Revolving Credit Agreement (Continued)

Under the most restrictive covenants of the Agreement, there is a restriction on dividend payments (\$1,330,000 of retained earnings were unrestricted at December 31, 1986), and the Company is obligated to maintain a minimum shareholders' equity, as defined, of \$15,000,000; a minimum ratio of shareholders' equity to total liabilities, as defined, of .8 to 1 at June 30 of each year and 1 to 1 at December 31 of each year; and a minimum current ratio of 1 to 1. At December 31, 1986, the Company did not meet the minimum debt to equity ratio requirement but has been granted a waiver by the banks.

Long-Term Debt of ESOT

On March 21, 1985, the loan balance of \$1,147,500 was converted to a 5-year term loan at an interest rate of 1/2% over prime. Effective April 17, 1985 the interest rate was fixed at 12.5%. The loan agreement provides for equal quarterly principal payments of \$28,688, commencing March 31, 1985, with a final installment on December 31, 1989, of the remaining unpaid principal balance.

Subordinated Notes

In 1986, 1985 and 1984, the Company redeemed shares of its common stock from shareholders for cash and 5-year subordinated promissory notes bearing interest at a rate equal to the average of the prime rate and the prevailing local basic bank savings rate. There were 33,948 shares redeemed in 1986 for cash of \$429,300 and notes of \$774,778. In 1985 and 1984, 24,000 and 15,000 shares were redeemed for cash of \$293,000 and \$88,800, and notes of \$490,700 and \$355,200, respectively.

E. EMPLOYEE STOCK OWNERSHIP PLAN

On March 15, 1979, the Company consummated a plan which transferred control of the Company to its employees. As a part of this plan, the Company sold 360,000 Common Shares to the Company's new Employee Stock Ownership Trust (ESOT) for \$2,700,000.

The Employee Stock Ownership Plan, in conjunction with the related trust (ESOT), provides for the grant to certain employees of certain ownership rights in, but not possession of, the Common Shares held by the trustee of the Trust. Annual allocations of shares are made to individual accounts established for the benefit of the participants.

E. EMPLOYEE STOCK OWNERSHIP PLAN (Continued)

The number of shares released from collateral and available for allocation to ESOT participants is determined by dividing the sum of the current year's loan principal and interest payments by the sum of the current and future years' loan principal and interest payments. The Company makes annual cash contributions to the ESOT, net of dividends paid on the shares held as collateral, in order to repay the principal and to pay the interest on the ESOT debt; such contributions are reflected as an expense of the Company. The contributions to the ESOT for 1986, 1985 and 1984 were:

	<u>1986</u>	<u>1985</u>	<u>1984</u>
	(000's omitted)		
Principal repayment	\$115	\$115	\$270
Interest	<u>125</u>	<u>136</u>	<u>154</u>
Total cash contributions required	240	251	424
Less dividends paid on collateral shares	<u>82</u>	<u>88</u>	<u>105</u>
ESOT expense	<u>\$158</u>	<u>\$163</u>	<u>\$319</u>
Annual release of shares from collateral	<u>15,829</u>	<u>16,561</u>	<u>36,536</u>
Cumulative release of shares from collateral	<u>280,774</u>	<u>264,945</u>	<u>248,384</u>
Number of shares remaining in collateral	<u>79,226</u>	<u>95,055</u>	<u>111,616</u>

F. STOCK OPTION AND STOCK PURCHASE PLANS

Stock Option Plans - The Company has two qualified stock option plans available for officers, directors and management employees. The status of the two qualified stock option plans are as follows at December 31, 1986:

Grant date	<u>1980 Option Plan</u>			
	<u>July 22, 1980</u>	<u>May 19, 1981</u>	<u>July 21, 1982</u>	<u>May 22, 1985</u>
Options granted, net of forfeitures	36,000	34,200	18,000	1,800
Exercised in 1982	(2,100)	(600)		
Exercised in 1983	(8,400)	(1,800)		
Exercised in 1984	(11,400)	(6,990)	(300)	
Exercised in 1985	(14,100)	(5,275)	(2,790)	
Exercised in 1986		<u>(19,535)</u>	<u>(2,850)</u>	
Options outstanding, December 31, 1986	<u>-0-</u>	<u>-0-</u>	<u>12,060</u>	<u>1,800</u>
Option purchase price	<u>\$ 8.26</u>	<u>\$ 9.97</u>	<u>\$ 14.83</u>	<u>\$ 32.20</u>

Grant date	<u>1985 Option Plan</u>	
	<u>May 22, 1985</u>	<u>Sept. 10, 1986</u>
Options granted, net of forfeitures	13,900	18,750
Exercised in 1986		
Options outstanding, December 31, 1986	<u>13,900</u>	<u>18,750</u>
Option purchase price	<u>\$ 32.20</u>	<u>\$ 36.60</u>

The option rights granted may be exercised in full one year after grant and expire five years after grant date.

Stock Purchase Plan - The Company has an employee stock purchase plan for which 90,000 shares have been reserved. The Plan provides the opportunity for all full-time employees with two years' service to purchase shares through payroll deductions. The purchase price for the shares offered under the Plan is 85% of the fair market value of the shares. The Plan will terminate when no more shares are available to be offered or December 31, 1991, whichever occurs first.

F. STOCK OPTION AND STOCK PURCHASE PLANS (Continued)

Purchases under the plan have been as follows:

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Number of employees participating	395	352	328
Annual shares purchased	13,722	14,488	13,835
Average price paid	\$30.63	\$27.84	\$25.73
Cumulative shares purchased	62,914	49,192	34,704
Shares available for future purchase	27,086	40,808	55,296

G. PENSION PLANS

The Company has defined benefit pension plans which are available to substantially all of the Company's employees. Two of the plans are contributory. These plans covering salary and hourly employees generally provide benefits at a stated amount for each year of service. The supplemental plan covering salary employees provides benefits under a formula principally based upon compensation levels. The Company's funding policy is to make the annual contributions required by applicable regulations. The annual contributions to all plans were \$315,800, \$352,800 and \$274,900 in 1986, 1985 and 1984, respectively. The plans' assets are principally invested by outside asset managers in marketable debt and equity securities.

Effective January 1, 1986, the Company adopted Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions". The Company is required to adopt this statement no later than January 1, 1987. This change in the method of accounting for pensions does not affect the amounts contributed to the plans by the Company. This change in pension accounting increased earnings before income taxes by \$335,000. Aggregate pension income for 1986 was \$19,000. Pension expense for all plans in 1985 and 1984 as determined under previous accounting principles was the amount contributed.

Pension expense (income) for 1986 was calculated as follows (000's omitted):

Service cost - increase in benefit obligations earned during the period	\$ 202
Interest cost on projected benefit obligation	571
Projected return on plan assets	(693)
Amortization of unrecognized (net assets) at January 1, 1986	<u>(99)</u>
Net pension expense (income)	<u>\$ (19)</u>

G. PENSION PLANS (Continued)

The funded status of pension plans at December 31, 1986 was as follows:

Plan assets at fair market value	\$10,548
Projected benefit obligations	<u>8,420</u>
Excess of assets over projected benefit obligations	2,128
Unrecognized (net assets) at January 1, 1986, less accumulated amortization	(1,857)
Excess contributions	<u>(94)</u>
Prepaid pension cost recognized in the balance sheet	<u>\$ 177</u>

The projected benefit obligation was determined using an assumed discount rate of 7%, and an assumed long-term compensation rate increase of 6%. The assumed long-term rate of return on plan assets was 7%.

The projected benefit obligation is based on an accumulated benefit obligation of \$7,523 which includes vested benefits of \$6,874.

H. INCOME TAXES

The provision for United States Federal, state and local and Canadian income taxes includes:

	<u>1986</u>	<u>1985</u>	<u>1984</u>
	(000's omitted)		
Taxes currently payable before tax credits:			
U.S.	\$1,824	\$2,377	\$3,141
Canadian	(89)	32	(11)
State and local	<u>327</u>	<u>471</u>	<u>388</u>
	2,062	2,880	3,518
Investment tax credits	(199)	(980)	(928)
Other tax credits	<u>(72)</u>	<u>(38)</u>	<u>(32)</u>
	1,791	1,862	2,558
Deferred taxes:			
U.S.	882	816	417
Canadian	<u>7</u>	<u>(1)</u>	<u>(16)</u>
	<u>889</u>	<u>815</u>	<u>401</u>
	<u>\$2,680</u>	<u>\$2,677</u>	<u>\$2,959</u>

H. INCOME TAXES (Continued)

The differences between the U.S. Federal statutory rate and the effective tax rate are as follows:

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Statutory tax rate	46.0%	46.0%	46.0%
State and local income taxes	3.1	3.7	2.8
Investment tax credits	(3.5)	(14.1)	(12.2)
Investment tax credit basis reduction	2.1	3.4	2.9
Miscellaneous	<u>(.6)</u>	<u>(.4)</u>	<u>(.5)</u>
Effective tax rate	<u>47.1%</u>	<u>38.6%</u>	<u>39.0%</u>

The increase in the 1986 effective tax rate is primarily the result of the elimination of the investment tax credit as a result of the Tax Reform Act of 1986.

Deferred income taxes arise because certain income and expense items are recognized on the Company's financial statements in different fiscal years than for tax purposes. The major timing differences and resulting deferred income tax expense are as follows:

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Investment tax credit basis reduction	\$117	\$237	\$217
Capitalized construction interest	23	35	(58)
Accrued vacations	(12)	(6)	7
Accelerated depreciation	611	566	244
Pension contribution	154		
Other	<u>(11)</u>	<u>(16)</u>	<u>7</u>
Total U.S.	882	816	417
Canadian	<u>7</u>	<u>(1)</u>	<u>(16)</u>
	<u>\$889</u>	<u>\$815</u>	<u>\$401</u>

I. SALES TO A MAJOR CUSTOMER

The Davey Tree Expert Company and its subsidiaries are engaged in the business of providing a broad line of horticultural services to corporate, institutional and residential customers throughout most of the United States and in parts of Canada. The Company had revenues from one customer under multiple long-term contracts aggregating approximately \$32,100,000, \$32,000,000 and \$29,500,000 for the years ended December 31, 1986, 1985 and 1984, respectively.

J. OPERATING LEASES

The Company leases certain facilities which are used primarily for district office and warehouse operations, and certain automotive and computer equipment. These leases extend for varying periods of time up to five years and, in some cases, contain renewal options. Total rental expenses under such operating leases amounted to approximately \$988,000, \$1,130,000 and \$1,163,000 for 1986, 1985 and 1984, respectively. As of December 31, 1986, future minimum rental payments, including taxes and other operating costs, for all operating leases having noncancelable lease terms in excess of one year, are as follows: 1987, \$625,000; 1988, \$473,000; 1989, \$268,000; 1990, \$146,000; and 1991, \$17,000.

K. COMMITMENTS AND CONTINGENCIES

The Company is party to a number of lawsuits, threatened lawsuits and other claims arising out of the normal course of business. Management is of the opinion that liabilities which may result are adequately covered by insurance, or to the extent not covered by insurance, would not be material in relation to the financial statements.



THE DAVEY TREE EXPERT COMPANY AND SUBSIDIARY COMPANIES

SCHEDULE V - PROPERTY, PLANT AND EQUIPMENT  
AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

(Dollars in Thousands)

Description	Balance at Beginning of Period	Additions At Cost	Retirements	Other Charges Add/(Deduct)	Balance at End of Period
Year-Ended December 31, 1984:					
Land & Land Improvements	\$ 1,045	\$ 265	\$ 3	\$	\$ 1,307
Buildings & Leaseholds	3,893	294	1		4,186
Equipment, Principally Revenue Producing	45,177	10,555	2,662	(66) (B) (35) (A)	52,969
Corporate Center Under Construction	91	2,478			2,569
Short-Term Investment of Funds		2,308			2,308
Restricted for Construction	<u>\$ 50,206</u>	<u>\$ 15,900</u>	<u>\$ 2,666</u>	<u>\$ (101)</u>	<u>\$ 63,339</u>
Year-Ended December 31, 1985:					
Land & Land Improvements	\$ 1,307	\$ 445	\$ 12	(2)	\$ 1,738
Buildings & Leaseholds	4,186	4,982	192	(5)	8,971
Equipment, Principally Revenue Producing	52,969	11,492	2,954	66 (B) (106) (A)	61,467
Corporate Center Under Construction	2,569	(2,569)			
Short-Term Investment of Funds		(2,308)			
Restricted for Construction	<u>2,308</u>	<u>(2,308)</u>			
	<u>\$ 63,339</u>	<u>\$ 12,042</u>	<u>\$ 3,158</u>	<u>\$ (47)</u>	<u>\$ 72,176</u>
Year-Ended December 31, 1986:					
Land & Land Improvements	\$ 1,738	\$ 167	\$	\$ 1	\$ 1,906
Buildings & Leaseholds	8,971	62	33	(1)	8,999
Equipment, Principally Revenue Producing	61,467	10,366	3,537	4 (A)	68,300
	<u>\$ 72,176</u>	<u>\$ 10,595</u>	<u>\$ 3,570</u>	<u>\$ 4</u>	<u>\$ 79,205</u>

(A) Effect of Compliance with Statement No. 52 of the Financial Accounting Standards Board  
(B) Write-off of Fully Depreciated Equipment & Canadian Subsidiary

THE DAVEY TREE EXPERT COMPANY AND SUBSIDIARY COMPANIES  
 SCHEDULE VI - ACCUMULATED DEPRECIATION, DEPLETION AND  
 AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

(Dollars in Thousands)

Description	Balance at Beginning of Period	Depreciation Expenses	Retirements	Other Charges Add/(Deduct)	Balance at End of Period
Year-Ended December 31, 1984:					
Land & Land Improvements	\$ 65	\$ 15	\$ 1	\$	\$ 79
Buildings & Leaseholds	1,129	219	1	(66) (B)	1,347
Equipment, Principally Revenue Producing	25,989	7,739	2,548	(22) (A)	31,092
	<u>\$ 27,183</u>	<u>\$ 7,973</u>	<u>\$ 2,550</u>	<u>\$ (88)</u>	<u>\$ 32,518</u>
Year-Ended December 31, 1985:					
Land & Land Improvements	\$ 79	\$ 14	\$ 7	\$	\$ 86
Buildings & Leaseholds	1,345	293	178	(4) (A)	1,456
Equipment, Principally Revenue Producing	31,094	8,601	2,572	(58) (A)	37,131
	<u>\$ 32,518</u>	<u>\$ 8,908</u>	<u>\$ 2,757</u>	<u>\$ 4</u>	<u>\$ 38,673</u>
Year-Ended December 31, 1986:					
Land & Land Improvements	\$ 86	\$ 14	\$ 18	\$	\$ 100
Buildings & Leaseholds	1,456	397			1,835
Equipment, Principally Revenue Producing	37,131	9,115	3,257	9 (A)	42,998
	<u>\$ 38,673</u>	<u>\$ 9,526</u>	<u>\$ 3,275</u>	<u>\$ 9</u>	<u>\$ 44,933</u>

(A) Effect of compliance with Statement No. 52 of the Financial Accounting Standards Board

(B) write-off of Fully Depreciated Equipment at Canadian Subsidiary

THE DAVEY TREE EXPERT COMPANY AND SUBSIDIARY COMPANIES

SCHEDULE IX - SHORT-TERM BORROWINGS

(Dollars in Thousands)

<u>Notes Payable to Bank</u>	<u>Balance at End Of Period</u>	<u>Weighted Average Interest Rate</u>	<u>Maximum Amount Outstanding During the Period</u>	<u>Average Amount Outstanding During the Period (1)</u>	<u>Weighted Average Interest Rate During the Period (2)</u>
December 31, 1982	\$ 700	11.0	400	\$ 99	14.52%
December 31, 1983			800	150	10.99%
December 31, 1984			2,807	963	12.36%
December 31, 1985			1,144	201	9.95%
December 31, 1986			1,066	488	9.19%

(1) Average amount outstanding during the period is computed by dividing the total of daily outstanding principal balances by 360.

(2) Weighted average interest rate during the period is computed by multiplying the actual outstanding principal balances by the applicable interest rates and by the actual days outstanding and averaging the resultant totals.

THE DAVEY TREE EXPERT COMPANY AND SUBSIDIARY COMPANIES

SCHEDULE X - SUPPLEMENTARY INCOME STATEMENT DATA

(Dollars in Thousands)

	<u>Charged to Costs &amp; Expenses</u>		
	Year-Ended December 31,		
	<u>1986</u>	<u>1985</u>	<u>1984</u>
Maintenance and Repairs	\$7,133	\$6,138	\$5,549
Amortization of Intangible Assets	(A)	(A)	(A)
Pre-Operating Costs and Similar Deferrals	(A)	(A)	(A)
Taxes, Other Than Payroll & Income Taxes	(A)	(A)	(A)
Royalties	(A)	(A)	(A)
Advertising	(A)	(A)	1,641

(A) Amounts are not presented as such amounts are less than 1% of net sales

3/87

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

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FORM 8

AMENDMENT TO APPLICATION OR REPORT  
Filed pursuant to Section 12, 13 or 15(d) of  
THE SECURITIES EXCHANGE ACT OF 1934

THE DAVEY TREE EXPERT COMPANY  
(Exact name of registrant as specified in charter)

AMENDMENT NO. 1

The undersigned registrant hereby amends the following items, financial statements, exhibits or other portions of its Annual Report for the fiscal year ended December 31, 1986 on Form 10-K as set forth in the pages attached hereto:

The attached Consent of Certified Public Accountants is added to and made a part of Exhibit 24.

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

THE DAVEY TREE EXPERT COMPANY  
(Registrant)

April 3, 1987

By /s/ David E. Adante  
David E. Adante, Secretary-  
Treasurer and Chief  
Financial Officer

CONSENT OF CERTIFIED PUBLIC ACCOUNTANTS

We consent to the incorporation by reference in the Registration Statements on Form S-8 (Nos. 2-73052, 2-77353 and 33-5755) relating to The Davey Tree Expert Company 1980 Employees Stock Option Plan, to The Davey Tree Expert Company 1982 Employee Stock Purchase Plan, and to The Davey Tree Expert Company 1985 Incentive Stock Option Plan, and in the related Prospectuses, of our report, dated February 24, 1987, with respect to the consolidated financial statements of The Davey Tree Expert Company for the year ended December 31, 1986.

*Touche Ross & Co.*  
TOUCHE ROSS & CO.

Akron, Ohio  
March 30, 1987

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TOUCHE ROSS & CO.

Akron, Ohio  
March 30, 1987