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**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 July 2, 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 000-11917**



**THE DAVEY TREE EXPERT COMPANY**

(Exact name of registrant as specified in its charter)

**Ohio**

**34-0176110**

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification Number)

**1500 North Mantua Street**

**P.O. Box 5193**

**Kent, Ohio 44240**

(Address of principal executive offices) (Zip code)

**(330) 673-9511**

(Registrant's telephone number, including area code)

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

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

There were 12,729,277 Common Shares, \$1.00 par value, outstanding as of July 29, 2016.

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**The Davey Tree Expert Company**  
**Quarterly Report on Form 10-Q**  
**July 2, 2016**  
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**We,” “Us,” “Our,” “Davey” and “Davey Tree,” unless the context otherwise requires, means The Davey Tree Expert Company and its subsidiaries.**

**THE DAVEY TREE EXPERT COMPANY**  
**CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)**  
(In thousands, except per share data dollar amounts)

	<u>July 2, 2016</u>	<u>December 31, 2015</u>
<b>Assets</b>		
Current assets:		
Cash	\$ 13,366	\$ 16,030
Accounts receivable, net	140,817	120,001
Operating supplies	7,495	7,171
Other current assets	10,141	17,732
Total current assets	<u>171,819</u>	<u>160,934</u>
Property and equipment	594,857	557,194
Less accumulated depreciation	409,398	390,772
	<u>185,459</u>	<u>166,422</u>
Other assets	33,996	31,949
Identified intangible assets and goodwill, net	34,870	34,281
	<u>\$ 426,144</u>	<u>\$ 393,586</u>
<b>Liabilities and shareholders' equity</b>		
Current liabilities:		
Accounts payable	\$ 34,765	\$ 37,750
Accrued expenses	32,854	36,146
Other current liabilities	34,346	38,054
Total current liabilities	<u>101,965</u>	<u>111,950</u>
Long-term debt	115,708	84,633
Self-insurance accruals	42,158	37,786
Other noncurrent liabilities	17,251	17,678
	<u>277,082</u>	<u>252,047</u>
Common shareholders' equity:		
Common shares, \$1.00 par value, per share; 48,000 shares authorized; 21,457 shares issued and outstanding before deducting treasury shares as of July 2, 2016 and December 31, 2015	21,457	21,457
Additional paid-in capital	20,868	17,815
Common shares subscribed, unissued	8,350	8,591
Retained earnings	278,410	270,605
Accumulated other comprehensive loss	(10,889)	(13,394)
	<u>318,196</u>	<u>305,074</u>
Less: Cost of common shares held in treasury; 8,731 shares at July 2, 2016 and 8,714 shares at December 31, 2015	165,399	159,429
Common shares subscription receivable	3,735	4,106
	<u>149,062</u>	<u>141,539</u>
	<u>\$ 426,144</u>	<u>\$ 393,586</u>

*See notes to condensed consolidated financial statements.*

**THE DAVEY TREE EXPERT COMPANY**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS** *(Unaudited)*  
(In thousands, except per share dollar amounts)

	Three Months Ended		Six Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
<b>Revenues</b>	\$ 224,763	\$ 224,773	\$ 405,596	\$ 399,065
Costs and expenses:				
Operating	137,132	137,341	260,305	257,199
Selling	36,859	34,914	71,189	67,570
General and administrative	14,675	13,534	31,814	28,666
Depreciation and amortization	12,290	11,607	23,631	22,268
Gain on sale of assets, net	(479)	(419)	(509)	(449)
	200,477	196,977	386,430	375,254
<b>Income from operations</b>	24,286	27,796	19,166	23,811
Other income (expense):				
Interest expense	(1,062)	(900)	(2,027)	(1,690)
Interest income	60	59	128	122
Other, net	(1,156)	(881)	(1,755)	(1,708)
<b>Income before income taxes</b>	22,128	26,074	15,512	20,535
Income taxes	8,819	10,142	6,391	8,131
<b>Net income</b>	\$ 13,309	\$ 15,932	\$ 9,121	\$ 12,404
<b>Net income per share:</b>				
Basic	\$ 1.03	\$ 1.21	\$ .70	\$ .93
Diluted	\$ 1.00	\$ 1.17	\$ .68	\$ .90
<b>Weighted-average shares outstanding:</b>				
Basic	12,870	13,214	12,979	13,375
Diluted	13,349	13,665	13,484	13,835
<b>Dividends declared per share</b>	\$ .05	\$ .05	\$ .10	\$ .10

See notes to condensed consolidated financial statements.

**THE DAVEY TREE EXPERT COMPANY**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)**  
**(In thousands)**

	Three Months Ended		Six Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
<b>Net income</b>	\$ 13,309	\$ 15,932	\$ 9,121	\$ 12,404
Components of other comprehensive income/(loss), net of tax:				
Foreign currency translation adjustments	245	(84)	1,997	(2,267)
Adjustments to defined benefit pension plans:				
Reclassification to results of operations:				
Amortization of defined benefit pension items:				
Net actuarial loss	146	215	508	455
Prior service cost	—	—	—	2
Defined benefit pension plan adjustments	<u>146</u>	<u>215</u>	<u>508</u>	<u>457</u>
<b>Other comprehensive income/(loss), net of tax</b>	<u>391</u>	<u>131</u>	<u>2,505</u>	<u>(1,810)</u>
<b>Comprehensive income</b>	<u>\$ 13,700</u>	<u>\$ 16,063</u>	<u>\$ 11,626</u>	<u>\$ 10,594</u>

*See notes to condensed consolidated financial statements.*

**THE DAVEY TREE EXPERT COMPANY**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**  
**(In thousands)**

	Six Months Ended	
	July 2, 2016	July 4, 2015
<b>Operating activities</b>		
Net income	\$ 9,121	\$ 12,404
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	23,631	22,268
Other	1,135	(1,303)
Changes in operating assets and liabilities:		
Accounts receivable	(20,816)	(18,897)
Operating liabilities	570	(3,699)
Other, net	4,993	7,919
	<u>9,513</u>	<u>6,288</u>
<b>Net cash provided by operating activities</b>	<b>18,634</b>	<b>18,692</b>
<b>Investing activities</b>		
Capital expenditures:		
Equipment	(36,373)	(44,545)
Land and building	(1,463)	(1,013)
Purchases of businesses	(3,497)	(1,549)
Other	671	607
	<u>(40,662)</u>	<u>(46,500)</u>
<b>Net cash used in investing activities</b>	<b>(40,662)</b>	<b>(46,500)</b>
<b>Financing activities</b>		
Revolving credit facility proceeds, net	31,500	40,500
Purchase of common shares for treasury	(11,627)	(11,614)
Sale of common shares from treasury	8,155	6,887
Dividends	(1,314)	(1,348)
Payments of notes payable	(7,350)	(6,806)
	<u>19,364</u>	<u>27,619</u>
<b>Net cash provided by financing activities</b>	<b>19,364</b>	<b>27,619</b>
<b>Decrease in cash</b>	<b>(2,664)</b>	<b>(189)</b>
Cash, beginning of period	16,030	18,415
<b>Cash, end of period</b>	<b>\$ <u>13,366</u></b>	<b>\$ <u>18,226</u></b>
Supplemental cash flow information follows:		
Interest paid	\$ 1,035	\$ 909
Income taxes paid	<u>505</u>	<u>9,143</u>

*See notes to condensed consolidated financial statements.*

**The Davey Tree Expert Company**  
**Notes to Condensed Consolidated Financial Statements (Unaudited)**  
**July 2, 2016**  
**(Amounts in thousands, except share data)**

**A. Basis of Financial Statement Preparation**

The condensed consolidated financial statements present the financial position, results of operations and cash flows of The Davey Tree Expert Company and its subsidiaries. When we refer to “we,” “us,” “our,” “Davey,” or “Davey Tree”, we mean The Davey Tree Expert Company and its subsidiaries, unless otherwise expressly stated or the context indicates otherwise.

We have prepared the accompanying unaudited condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”), as codified in the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”), and with the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial information. The consolidated financial statements include all adjustments which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. All such adjustments are of a normal, recurring nature. All significant intercompany accounts and transactions have been eliminated.

Certain information and disclosures required by U.S. GAAP for complete financial statements have been omitted in accordance with the rules and regulations of the SEC. We suggest that these condensed consolidated financial statements be read in conjunction with the financial statements included in our annual report on Form 10-K for the year ended December 31, 2015 (the “2015 Annual Report”).

***Use of Estimates in Financial Statement Preparation***--The preparation of financial statements in accordance with U.S. GAAP requires the use of estimates and assumptions that affect reported amounts. Our consolidated financial statements include amounts that are based on management’s best estimates and judgments. Estimates are used for, but not limited to, accounts receivable valuation, depreciable lives of fixed assets, self-insurance accruals, income taxes and revenue recognition. Actual results could differ from those estimates.

***Interim Results of Operations***--Interim results may not be indicative of calendar year performance because of seasonal and short-term variations.

**Recent Accounting Guidance**

**Accounting Standards Adopted in 2016**

***Accounting Standards Update 2015-16, Business Combinations: Simplifying the Accounting for Measurement-Period Adjustments***--In September 2015, the FASB issued Accounting Standards Update (“ASU”) 2015-16, “Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments.” ASU 2015-16 simplifies the reporting of adjustments to the provisional amounts recorded for a business combination during the measurement period by eliminating the requirement to retrospectively account for those adjustments. Companies are required to present separately, on the face of the income statement, or disclose in the notes to the financial statements, the impact on current period earnings by line item that would have been recorded in previous periods if the adjustment to the provisional amounts were recognized as of the acquisition date. The amendments in ASU 2015-16 became effective January 1, 2016 and require prospective application to qualifying business combinations.

**Accounting Standards Not Yet Adopted**

***Accounting Standards Update 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting***--In March 2016, the FASB issued ASU 2016-09, “Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting,” with the objective to simplify several aspects of the accounting for share-based payment transactions, including: the income tax

**The Davey Tree Expert Company**  
**Notes to Condensed Consolidated Financial Statements (Unaudited)**  
**July 2, 2016**  
**(Amounts in thousands, except share data)**

**A. Basis of Financial Statement Preparation (continued)**

consequences; classification of awards as either equity or liabilities; classification of certain items on the statement of cash flows; and, accounting for forfeitures. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, which for Davey Tree would be January 1, 2017. Early adoption is permitted. Management has not yet completed its assessment of the impact of the new standard on the Company's consolidated financial statements.

**Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606)**--In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)," which will replace all current U.S. GAAP guidance on revenue recognition and eliminate all industry-specific guidance.

The new revenue recognition guidance provides a unified model to determine when and how revenue is recognized. The underlying principle is that an entity should recognize revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration for which the entity expects in exchange for those goods and services. The guidance provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include capitalization of certain contract costs, consideration of the time value of money in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. The guidance also requires enhanced information to be presented in the financial statements regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers.

In August 2015, the FASB issued ASU No. 2015-14, "Revenue from Contracts with Customers (Topic 606) ('Update 2015-14'): Deferral of the Effective Date," which responded to stakeholders' requests to defer the effective date of the guidance in ASU 2014-09. In March 2016, the FASB issued ASU 2016-08, "Revenue from Contracts with Customers (Topic 606)--Principal versus Agent Considerations (Reporting Revenue Gross versus Net) ('Update 2016-08')," which clarifies the implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU 2016-10, "Revenue from Contracts with Customers (Topic 606) ('Update 2016-10') Identifying Performance Obligations and Licensing," which clarifies multiple aspects of Topic 606. In May 2016, the FASB issued ASU No. 2016-12, "Revenue from Contracts with Customers (Topic 606) - Narrow-Scope Improvements and Practical Expedients ('Update 2016-12')," which provides clarifying guidance in a few narrow areas and adds some practical expedients to the guidance.

The effective date and the transition requirements for the Updates are the same as the effective date of Topic 606 ASU 2015-14, which becomes effective for Davey Tree beginning with the first quarter 2018 and can be adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption. The FASB also affirmed its proposal to permit all entities to apply the new revenue standard early, but not before the original effective date, which for Davey Tree would be first quarter 2017. The new revenue guidance will supersede existing revenue guidance affecting our Company, and may also affect our business processes and our information technology systems. As a result, our evaluation of the effect of the new revenue guidance will extend over future periods.

**Accounting Standards Update 2016-02, Leases (Topic 842)**--In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)." ASU 2016-02 establishes a comprehensive new lease accounting model. The new standard: (a) clarifies the definition of a lease; (b) requires a dual approach to lease classification similar to current lease classifications; and, (c) causes lessees to recognize leases on the balance sheet as a lease liability with a corresponding right-of-use asset for leases with a lease-term of more than twelve months. The new standard is effective for interim and annual periods beginning after December 15, 2018, which for Davey Tree would be January 1, 2019. Early adoption is permitted. The new standard requires a modified retrospective transition for



**The Davey Tree Expert Company**  
**Notes to Condensed Consolidated Financial Statements (Unaudited)**  
**July 2, 2016**  
(Amounts in thousands, except share data)

**A. Basis of Financial Statement Preparation (continued)**

capital or operating leases existing at or entered into after the beginning of the earliest comparative period presented in the financial statements, but it does not require transition accounting for leases that expire prior to the date of initial application. We are currently evaluating the impact of the new standard on our consolidated financial statements.

**B. Seasonality of Business**

Due to the seasonality of our business, our operating results for the six months ended July 2, 2016 are not indicative of results that may be expected for any other interim period or for the year ending December 31, 2016. Business seasonality traditionally results in higher revenues during the second and third quarters as compared with the first and fourth quarters of the year, while the methods of accounting for fixed costs, such as depreciation expense, amortization, rent and interest expense, are not significantly impacted by business seasonality.

**C. Accounts Receivable, Net and Supplemental Balance-Sheet Information**

Accounts receivable, net, consisted of the following:

<b>Accounts receivable, net</b>	<b>July 2, 2016</b>	<b>December 31, 2015</b>
Accounts receivable	\$ 116,888	\$ 104,567
Receivables under contractual arrangements	27,404	19,142
	<u>144,292</u>	<u>123,709</u>
Less allowances for doubtful accounts	3,475	3,708
Accounts receivable, net	<u>\$ 140,817</u>	<u>\$ 120,001</u>

Receivables under contractual arrangements consist of work-in-process in accordance with the terms of contracts, primarily with utility services customers.

The following items comprise the amounts included in the balance sheets:

<b>Other current assets</b>	<b>July 2, 2016</b>	<b>December 31, 2015</b>
Refundable income taxes	\$ —	\$ 2,952
Prepaid expenses	9,371	13,862
Other	770	918
Total	<u>\$ 10,141</u>	<u>\$ 17,732</u>

**The Davey Tree Expert Company**  
**Notes to Condensed Consolidated Financial Statements (Unaudited)**  
**July 2, 2016**  
(Amounts in thousands, except share data)

**C. Accounts Receivable, Net and Supplemental Balance-Sheet Information (continued)**

<b>Accrued expenses</b>	<b>July 2, 2016</b>	<b>December 31, 2015</b>
Employee compensation	\$ 14,479	\$ 18,176
Accrued compensated absences	9,230	8,607
Self-insured medical claims	3,701	2,347
Customer advances, deposits	758	2,564
Taxes, other than income	2,904	3,517
Other	1,782	935
<b>Total</b>	<b>\$ 32,854</b>	<b>\$ 36,146</b>

**D. Business Combinations**

Our investment in businesses during the first six months of 2016 was \$4,170, with liabilities assumed of \$98 and debt issued of \$575. Measurement-period adjustments are not complete. The measurement period for purchase price allocations ends as soon as information of the facts and circumstances becomes available, but does not exceed one year from the acquisition date. During the six months ended July 4, 2015, our investment in businesses was \$2,449, with no liabilities assumed and debt issued of \$900.

The results of operations of acquired businesses have been included in the consolidated statements of operations beginning as of the effective dates of acquisition. The effect of these acquisitions on our consolidated revenues and results of operations was not significant.

**The Davey Tree Expert Company**  
**Notes to Condensed Consolidated Financial Statements (Unaudited)**  
**July 2, 2016**  
(Amounts in thousands, except share data)

**E. Identified Intangible Assets and Goodwill, Net**

The carrying amounts of the identified intangibles and goodwill acquired in connection with our historical investments in businesses were as follows:

Identified Intangible Assets and Goodwill, Net	July 2, 2016		December 31, 2015	
	Carrying Amount	Accumulated Amortization	Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Customer lists/relationships	\$ 17,626	\$ 14,426	\$ 16,805	\$ 13,764
Employment-related	6,934	6,171	6,811	6,008
Tradenames	5,575	4,739	5,502	4,539
Amortized intangible assets	\$ 30,135	\$ 25,336	\$ 29,118	\$ 24,311
Less accumulated amortization	25,336		24,311	
Identified intangibles, net	4,799		4,807	
Unamortized intangible assets:				
Goodwill	30,071		29,474	
	\$ 34,870		\$ 34,281	

**F. Long-Term Debt and Commitments Related to Letters of Credit**

Our long-term debt consisted of the following:

	July 2, 2016	December 31, 2015
Revolving credit facility		
Swing-line borrowings	\$ —	\$ 2,500
LIBOR borrowings	86,000	52,000
	86,000	54,500
Senior unsecured notes	30,000	30,000
Term loans	8,769	16,105
Capital leases	561	—
	125,330	100,605
Less debt issuance costs	402	471
Less current portion	9,220	15,501
	\$ 115,708	\$ 84,633

**Revolving Credit Facility** --We have a \$175,000 revolving credit facility with a group of banks, which will expire in November 2018 and permits borrowings, as defined, up to \$175,000, including a letter of credit sublimit of

**The Davey Tree Expert Company**  
**Notes to Condensed Consolidated Financial Statements (Unaudited)**  
**July 2, 2016**  
**(Amounts in thousands, except share data)**

**F. Long-Term Debt and Commitments Related to Letters of Credit (continued)**

\$100,000 and a swing-line commitment of \$15,000. Under certain circumstances, the amount available under the revolving credit facility may be increased to \$210,000. The revolving credit facility contains certain affirmative and negative covenants customary for this type of facility and includes financial covenant ratios with respect to a maximum leverage ratio and a maximum balance-sheet leverage ratio.

As of July 2, 2016, we had unused commitments under the facility approximating \$84,939, with \$90,061 committed, consisting of borrowings of \$86,000 and issued letters of credit of \$4,061.

Borrowings outstanding bear interest, at Davey Tree's option, of either (a) a base rate or (b) LIBOR plus a margin adjustment ranging from .75% to 1.50%--with the margin adjustments in both instances based on the Company's leverage ratio at the time of borrowing. The base rate is the greater of (i) the agent bank's prime rate, (ii) LIBOR plus 1.50%, or (iii) the federal funds rate plus .50%. A commitment fee ranging from .10% to .25% is also required based on the average daily unborrowed commitment.

**5.09% Senior Unsecured Notes**--The \$30,000 senior unsecured notes are due July 22, 2020 and were issued during July 2010 as 5.09% Senior Unsecured Notes, Series A (the "5.09% Senior Notes"), pursuant to a Master Note Purchase Agreement (the "Purchase Agreement") between the Company and the purchasers of the 5.09% Senior Notes.

The 5.09% Senior Notes are equal in right of payment with our revolving credit facility and all other senior unsecured obligations of the Company. Interest is payable semiannually and five equal, annual principal payments commenced on July 22, 2016 (the sixth anniversary of issuance). The Purchase Agreement contains customary events of default and covenants related to limitations on indebtedness and transactions with affiliates and the maintenance of certain financial ratios.

**Accounts Receivable Securitization Facility**--On May 9, 2016, Davey Tree entered into a one-year agreement with a bank, for an accounts receivable securitization facility (the "AR securitization program"), whereby Davey Tree has pledged a first priority security interest in certain trade receivables in exchange for the bank issuing letters of credit ("LCs") with a committed facility limit of \$60,000.

As of July 2, 2016, we had issued letters of credit of \$53,250 under the terms of the AR securitization program.

Under the AR securitization program, Davey Tree transfers by selling or contributing current and future trade receivables to a wholly-owned, bankruptcy-remote financing subsidiary which pledges a perfected first priority security interest in the trade receivables--equal to the issued letters of credit as of July 2, 2016--to the bank in exchange for the bank issuing LCs.

Fees payable to the bank include: (a) an LC issuance fee, payable on each settlement date, in the amount of .90% per annum on the aggregate amount of all LCs outstanding plus outstanding reimbursement obligations (e.g., arising from drawn LCs), if any, and (b) an unused LC fee, payable monthly, equal to (i) .35% per annum for each day on which the sum of the total LCs outstanding plus any outstanding reimbursement obligations is greater than or equal to 50% of the facility limit and (ii) .45% per annum for each day on which the sum of the total LCs outstanding plus any outstanding reimbursement obligations is less than 50% of the facility limit. If an LC is drawn and the bank is not immediately reimbursed in full for the drawn amount, any outstanding reimbursement obligation will accrue interest at a per annum rate equal to a reserve-adjusted LIBOR or, in certain circumstances, a base rate equal to the higher of (i) the bank's prime rate and (ii) the federal funds rate plus .50% and, following

**The Davey Tree Expert Company**  
**Notes to Condensed Consolidated Financial Statements (Unaudited)**  
**July 2, 2016**  
**(Amounts in thousands, except share data)**

**F. Long-Term Debt and Commitments Related to Letters of Credit (continued)**

any default, 2.00% plus the greater of (a) adjusted LIBOR and (b) a base rate equal to the higher of (i) the bank's prime rate and (ii) the federal funds rate plus .50%.

The agreements underlying the AR securitization program contains various customary representations and warranties, covenants, and default provisions which provide for the termination and acceleration of the commitments under the AR securitization program in circumstances including, but not limited to, failure to make payments when due, breach of a representation, warranty or covenant, certain insolvency events or failure to maintain the security interest in the trade receivables, and defaults under other material indebtedness.

**Total Commitments Related to Issued Letters of Credit**--As of July 2, 2016, total commitments related to issued letters of credit were \$59,315, of which \$4,061 were issued under the Revolving Credit Facility, \$53,250 were issued under the Accounts Receivable Securitization Facility and, \$2,004 were issued under short-term lines of credit. As of December 31, 2015, total commitments related to issued letters of credit were \$59,350, of which \$57,347 were issued under the Revolving Credit Facility and \$2,003 were issued under short-term lines of credit.

**G. Stock-Based Compensation**

Our shareholders approved the 2014 Omnibus Stock Plan (the "2014 Stock Plan") at our annual meeting of shareholders on May 20, 2014. The 2014 Stock Plan replaced the expired 2004 Omnibus Stock Plan (the "2004 plan") previously approved by the shareholders in 2004. The 2014 Stock Plan is administered by the Compensation Committee of the Board of Directors and will remain in effect for ten years. All directors of the Company and employees of the Company and its subsidiaries are eligible to participate in the 2014 Stock Plan. The 2014 Stock Plan (similar to the 2004 plan) continues the maintenance of the Employee Stock Purchase Plan, as well as provisions for the grant of stock options and other stock-based incentives. The 2014 Stock Plan provides for the grant of five percent of the number of the Company's common shares outstanding as of the first day of each fiscal year plus the number of common shares that were available for grant of awards, but not granted, in prior years. In no event, however, may the number of common shares available for the grant of awards in any fiscal year exceed ten percent of the common shares outstanding as of the first day of that fiscal year. Common shares subject to an award that is forfeited, terminated, or canceled without having been exercised are generally added back to the number of shares available for grant under the 2014 Stock Plan.

Stock-based compensation expense under all share-based payment plans -- our Employee Stock Purchase Plan, stock option plans, stock-settled stock appreciation rights and performance-based restricted stock units -- included in the results of operations follows:

	Three months ended		Six Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Compensation expense, all share-based payment plans	\$ 678	\$ 557	\$ 1,324	\$ 1,055

Stock-based compensation consisted of the following:

**Employee Stock Purchase Plan**--Under the Employee Stock Purchase Plan, all full-time employees with one year of service are eligible to purchase, through payroll deduction, common shares. Employee purchases under the

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**G. Stock-Based Compensation (continued)**

Employee Stock Purchase Plan are at 85% of the fair market value of the common shares--a 15% discount. We recognize compensation costs as payroll deductions are made. The 15% discount of total shares purchased under the plan resulted in compensation cost of \$337 being recognized for the six months ended July 2, 2016 and \$263 for the six months ended July 4, 2015.

**Stock Option Plans**--The stock options outstanding were awarded under a graded vesting schedule, measured at fair value, and have a term of ten years. Compensation costs for stock options are recognized over the requisite service period on the straight-line recognition method. Compensation cost recognized for stock options was \$270 for the six months ended July 2, 2016 and \$223 for the six months ended July 4, 2015.

**Stock-Settled Stock Appreciation Rights**--During the six months ended July 2, 2016, the Compensation Committee awarded 150,100 stock-settled stock appreciation rights ("SSARs") to certain management employees, which vest ratably over five years. A SSAR is an award that allows the recipient to receive common stock equal to the appreciation in the fair market value of our common stock between the date the award was granted and the conversion date of the shares vested.

The following table summarizes our SSARs as of July 2, 2016.

Stock-Settled Stock Appreciation Rights	Number of Rights	Weighted- Average Award Date Value	Weighted- Average Remaining Contractual Life	Unrecognized Compensation Cost	Aggregate Intrinsic Value
Unvested, January 1, 2016	330,707	\$ 4.65			
Granted	150,100	6.38			
Forfeited	—	—			
Vested	(92,556)	4.25			
Unvested, July 2, 2016	<u>388,251</u>	<u>\$ 5.41</u>	<u>3.1 years</u>	<u>\$ 1,814</u>	<u>\$ 12,696</u>
Employee SSARs	<u>385,252</u>	<u>\$ 5.43</u>	<u>3.2 years</u>	<u>\$ 1,809</u>	<u>\$ 12,598</u>
Nonemployee Director SSARs	<u>2,999</u>	<u>\$ 2.03</u>	<u>0.9 years</u>	<u>\$ 5</u>	<u>\$ 98</u>

Compensation costs for stock appreciation rights are determined using a fair-value method and amortized over the requisite service period. Compensation expense for stock appreciation rights was \$292 for the six months ended July 2, 2016 and \$229 for the six months ended July 4, 2015.

**Performance-Based Restricted Stock Units**--During the six months ended July 2, 2016, the Compensation Committee awarded 33,915 performance-based restricted stock units to certain directors and management employees. The Compensation Committee made similar awards in prior periods. The awards vest over specified periods. The following table summarizes performance-based restricted stock units as of July 2, 2016.

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**G. Stock-Based Compensation (continued)**

Performance-Based Restricted Stock Units	Number of Stock Units	Weighted- Average Grant Date Value	Weighted- Average Remaining Contractual Life	Unrecognized Compensation Cost	Aggregate Intrinsic Value
Unvested, January 1, 2016	141,985	\$ 23.98			
Granted	33,915	31.59			
Forfeited	—	—			
Vested	(19,488)	19.12			
Unvested, July 2, 2016	<u>156,412</u>	<u>\$ 26.24</u>	<u>3.0 years</u>	<u>\$ 2,555</u>	<u>\$ 5,115</u>

Compensation cost for restricted stock awards is determined using a fair-value method and amortized on the straight-line recognition method over the requisite service period. Compensation expense on restricted stock awards totaled \$425 for the six months ended July 2, 2016 and \$340 for the six months ended July 4, 2015.

We estimated the fair value of each stock-based award on the date of grant using a binomial option-pricing model. The binomial model considers a range of assumptions related to volatility, risk-free interest rate and employee exercise behavior. Expected volatilities utilized in the binomial model are based on historical volatility of our stock prices and other factors. Similarly, the dividend yield is based on historical experience and expected future changes. The binomial model also incorporates exercise and forfeiture assumptions based on an analysis of historical data. The expected life of the stock-based awards is derived from the output of the binomial model and represents the period of time that awards granted are expected to be outstanding.

The fair values of stock-based awards granted were estimated at the dates of grant with the following weighted-average assumption.

	Six Months Ended	
	July 2, 2016	July 4, 2015
Volatility rate	10.6%	10.9%
Risk-free interest rate	1.8%	2.1%
Expected dividend yield	.7%	.7%
Expected life of awards (years)	9.5	9.3

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**G. Stock-Based Compensation (continued)**

**General Stock Option Information**--The following table summarizes activity under the stock option plans for the six months ended July 2, 2016.

Stock Options	Number of Options Outstanding	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Life	Aggregate Intrinsic Value
Outstanding, January 1, 2016	816,744	\$ 21.58		
Granted	148,000	32.70		
Exercised	(130,821)	11.93		
Forfeited	(6,900)	17.20		
Outstanding, July 2, 2016	<u>827,023</u>	<u>\$ 25.13</u>	7.3 years	<u>\$ 6,261</u>
Exercisable, July 2, 2016	<u>382,323</u>	<u>\$ 20.85</u>	5.8 years	<u>\$ 4,531</u>

As of July 2, 2016, there was approximately \$1,561 of unrecognized compensation cost related to stock options outstanding. The cost is expected to be recognized over a weighted-average period of 3.1 years. "Intrinsic value" is defined as the amount by which the market price of a common share exceeds the exercise price of an option.

Common shares are issued from treasury upon the exercise of stock options, stock-settled stock appreciation rights, restricted stock units or purchases under the Employee Stock Purchase Plan.

**H. Net Periodic Benefit Cost--Defined Benefit Pension Plans**

The results of operations included the following net periodic benefit cost recognized related to our defined-benefit pension plans.

	Three Months Ended		Six Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
<b>Components of pension cost</b>				
Service costs--increase in benefit obligation earned	\$ 90	\$ 5	\$ 190	\$ 26
Interest cost on projected benefit obligation	310	376	627	755
Expected return on plan assets	(276)	(406)	(553)	(811)
Curtailement cost	—	49	—	49
Settlement loss	—	—	453	—
Amortization of net actuarial loss	237	346	480	733
Amortization of prior service cost	—	1	—	4
Net pension cost of defined benefit pension plans	<u>\$ 361</u>	<u>\$ 371</u>	<u>\$ 1,197</u>	<u>\$ 756</u>

During March 2016, we entered into an agreement to purchase a guaranteed group annuity contract from a third-party insurance company which unconditionally and irrevocably guarantees the full-payment of all annuity



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**H. Net Periodic Benefit Cost--Defined Benefit Pension Plans (continued)**

payments to the participants of our plan for bargaining employees not covered by union pension plans (the "SPP"), for which future benefits were frozen effective December 31, 2013. A similar group annuity contract was purchased in December 2015 on behalf of certain SPP participants.

The March 2016 agreement transferred the remaining SPP benefit obligations to the third-party insurance company, resulting in an actuarial settlement loss of \$453.

**I. Income Taxes**

Our income tax provision for interim periods is determined using an estimate of our annual effective tax rate adjusted for discrete items, if any, that are taken into account in the relevant period. Each quarter we update our estimate of the annual effective tax rate and, if our estimated annual tax rate changes, we make a cumulative adjustment. The 2016 annual effective tax rate is estimated to approximate 40.1%. Our annual effective tax rate for 2015 was 38.2%.

At December 31, 2015, we had unrecognized tax benefits of \$2,557, of which \$1,981 would affect our effective rate if recognized, and accrued interest expense related to unrecognized benefits of \$115. At July 2, 2016, there were no significant changes in the unrecognized tax benefits, including the amount that would affect our effective rate if recognized, or the accrued interest expense related to the unrecognized benefits. Unrecognized tax benefits are the differences between a tax position taken, or expected to be taken in a tax return, and the benefit recognized for financial reporting purposes.

The Company is routinely under audit by federal, state, local and Canadian authorities in the area of income tax. These audits include questioning the timing and the amount of income and deductions and the allocation of income and deductions among various tax jurisdictions. During the fourth quarter 2013, the U.S. Internal Revenue Service completed its audit of the Company's U.S. income tax returns for 2010 and 2011 and, during 2010, Canada Revenue Agency completed its audit of the Company's Canadian operations for 2006, 2007 and 2008. With the exception of U.S. state jurisdictions, the Company is no longer subject to examination by tax authorities for the years through 2010. As of July 2, 2016, we believe it is reasonably possible that the total amount of unrecognized tax benefits will not significantly increase or decrease.

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**J. Accumulated Other Comprehensive Income (Loss)**

Comprehensive income (or loss) is comprised of net income (or net loss) and other components, including currency translation adjustments and defined-benefit pension plan adjustments.

The following summarizes the components of other comprehensive income (loss) accumulated in shareholders' equity for the six months ended July 2, 2016 and six months ended July 4, 2015:

	Foreign Currency Translation Adjustments	Defined Benefit Pension Plans	Accumulated Other Comprehensive Income (Loss)
<b>Balance at January 1, 2016</b>	\$ (6,244)	\$ (7,150)	\$ (13,394)
Other comprehensive income (loss) before reclassifications			
Unrealized gains	\$ 1,997	\$ —	\$ 1,997
Amounts reclassified from accumulated other comprehensive income (loss)	—	829	829
Tax effect	—	(321)	(321)
Net of tax amount	1,997	508	2,505
<b>Balance at July 2, 2016</b>	\$ (4,247)	\$ (6,642)	\$ (10,889)

	Foreign Currency Translation Adjustments	Defined Benefit Pension Plans	Accumulated Other Comprehensive Income (Loss)
<b>Balance at January 1, 2015</b>	\$ (1,151)	\$ (10,372)	\$ (11,523)
Other comprehensive income (loss) before reclassifications			
Unrealized losses	\$ (2,267)	\$ —	\$ (2,267)
Amounts reclassified from accumulated other comprehensive income (loss)	—	737	737
Tax effect	—	(280)	(280)
Net of tax amount	(2,267)	457	(1,810)
<b>Balance at July 4, 2015</b>	\$ (3,418)	\$ (9,915)	\$ (13,333)

The change in defined benefit pension plans of \$829 for the six months ended July 2, 2016 and the \$737 for the six months ended July 4, 2015 is included in net periodic pension expense and is classified in the condensed statement of operations as costs and expenses, general and administrative.

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**K. Per Share Amounts and Common Shares Outstanding**

We calculate our basic earnings per share by dividing net income or net loss by the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated in a similar manner, but include the effect of dilutive securities. To the extent these securities are antidilutive, they are excluded from the calculation of earnings per share. The per share amounts were computed as follows:

	Three Months Ended		Six Months Ended	
	July 2, 2016	July 4, 2015	July 2, 2016	July 4, 2015
Income available to common shareholders:				
Net income	\$ 13,309	\$ 15,932	\$ 9,121	\$ 12,404
Weighted-average shares:				
Basic:				
Outstanding	12,764	13,099	12,767	13,146
Partially-paid share subscriptions	106	115	212	229
Basic weighted-average shares	<u>12,870</u>	<u>13,214</u>	<u>12,979</u>	<u>13,375</u>
Diluted:				
Basic from above	12,870	13,214	12,979	13,375
Incremental shares from assumed:				
Exercise of stock subscription purchase rights	68	61	68	62
Exercise of stock options and awards	411	390	437	398
Diluted weighted-average shares	<u>13,349</u>	<u>13,665</u>	<u>13,484</u>	<u>13,835</u>
Net income per share:				
Basic	\$ 1.03	\$ 1.21	\$ .70	\$ .93
Diluted	<u>\$ 1.00</u>	<u>\$ 1.17</u>	<u>\$ .68</u>	<u>\$ .90</u>

**Common Shares Outstanding**--A summary of the activity of the common shares outstanding for the six months ended July 2, 2016 follows:

Shares outstanding at January 1, 2016	12,743,314
Shares purchased	(343,622)
Shares sold	207,952
Stock subscription offering -- cash purchases	12,046
Options and awards exercised	106,485
	<u>(17,139)</u>
Shares outstanding at July 2, 2016	<u>12,726,175</u>

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**K. Per Share Amounts and Common Shares Outstanding (continued)**

On May 19, 2015, at the Annual Meeting of Shareholders, the Company's shareholders approved an increase in the number of the Company's authorized common shares, par value \$1.00, to 48 million from 24 million. The number of authorized preferred shares of the Company remains at four million preferred shares, no par value, of which none were issued.

On July 2, 2016, we had 12,726,175 common shares outstanding, employee options exercisable to purchase 382,323 common shares, partially-paid subscriptions for 423,837 common shares and purchase rights outstanding for 174,388 common shares.

**Stock Subscription Offering**--Beginning May 2012, the Company offered to eligible employees and nonemployee directors the right to subscribe to common shares of the Company at \$19.70 per share in accordance with the provisions of The Davey Tree Expert Company 2004 Omnibus Stock Plan and the rules of the Compensation Committee of the Company's Board of Directors (collectively, the "plan"). The offering period ended on August 1, 2012 and resulted in the subscription of 637,714 common shares for \$12,563 at \$19.70 per share.

Under the plan, a participant in the offering purchasing common shares for an aggregate purchase price of less than \$5 had to pay with cash. All participants (excluding Company directors and officers) purchasing \$5 or more of the common shares had an option to finance their purchase through a down-payment of at least 10% of the total purchase price and a seven-year promissory note for the balance due with interest at 2%. Payments on the promissory note can be made either by payroll deductions or annual lump-sum payments of both principal and interest.

Common shares purchased under the plan have been pledged as security for the payment of the promissory note and the common shares will not be issued until the promissory note is paid-in-full. Dividends will be paid on all subscribed shares, subject to forfeiture to the extent that payment is not ultimately made for the shares.

All participants in the offering purchasing in excess of \$5 of common shares were granted a "right" to purchase one additional common share at a price of \$19.70 per share for every three common shares purchased under the plan. As a result of the stock subscription, employees were granted rights to purchase 211,800 common shares. Each right may be exercised at the rate of one-seventh per year and will expire seven years after the date that the right was granted. Employees may not exercise a right should they cease to be employed by the Company.

**L. Operations by Business Segment**

We provide a wide range of arboriculture, horticulture, environmental and consulting services to residential, utility, commercial and government entities throughout the United States and Canada. We have two reportable operating segments organized by type or class of customer: Residential and Commercial, and Utility.

**Residential and Commercial**--Residential and Commercial provides services to our residential and commercial customers including: the treatment, preservation, maintenance, removal and planting of trees, shrubs and other plant life; the practice of landscaping, grounds maintenance, tree surgery, tree feeding and tree spraying; the

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**L. Operations by Business Segment (continued)**

application of fertilizer, herbicides and insecticides; and, natural resource management and consulting, forestry research and development, and environmental planning.

**Utility**--Utility is principally engaged in providing services to our utility customers--investor-owned, municipal utilities, and rural electric cooperatives--including: the practice of line-clearing and vegetation management around power lines, rights-of-way and chemical brush control; and, natural resource management and consulting, forestry research and development, and environmental planning.

All other operating activities, including research, technical support and laboratory diagnostic facilities, are included in "All Other."

**Measurement of Segment Profit and Loss and Segment Assets**--We evaluate performance and allocate resources based primarily on operating income and also actively manage business unit operating assets. Segment information, including reconciling adjustments, is presented consistent with the basis described in our 2015 Annual Report.

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**L. Operations by Business Segment (continued)**

Segment information reconciled to consolidated external reporting information follows:

	<u>Utility</u>	<u>Residential and Commercial</u>	<u>All Other</u>	<u>Reconciling Adjustments</u>	<u>Consolidated</u>
<b>Three Months Ended July 2, 2016</b>					
Revenues	\$ 105,285	\$ 118,945	\$ 533	\$ —	\$ 224,763
Income (loss) from operations	<u>5,587</u>	<u>21,226</u>	<u>(980)</u>	(1,547) (a)	24,286
Interest expense				(1,062)	(1,062)
Interest income				60	60
Other income (expense), net				<u>(1,156)</u>	<u>(1,156)</u>
Income before income taxes					<u>\$ 22,128</u>
Segment assets, total	<u>\$ 159,824</u>	<u>\$ 181,945</u>	<u>\$ —</u>	<u>\$ 84,375</u> (b)	<u>\$ 426,144</u>
<b>Three Months Ended July 4, 2015</b>					
Revenues	\$ 108,537	\$ 115,635	\$ 601	\$ —	\$ 224,773
Income (loss) from operations	<u>7,478</u>	<u>22,712</u>	<u>(923)</u>	(1,471) (a)	27,796
Interest expense				(900)	(900)
Interest income				59	59
Other income (expense), net				<u>(881)</u>	<u>(881)</u>
Income before income taxes					<u>\$ 26,074</u>
Segment assets, total	<u>\$ 164,250</u>	<u>\$ 165,587</u>	<u>\$ —</u>	<u>\$ 78,358</u> (b)	<u>\$ 408,195</u>
<b>Six Months Ended July 2, 2016</b>					
Revenues	\$ 205,313	\$ 199,279	\$ 1,004	\$ —	\$ 405,596
Income (loss) from operations	<u>7,061</u>	<u>19,790</u>	<u>(4,086)</u>	(3,599) (a)	19,166
Interest expense				(2,027)	(2,027)
Interest income				128	128
Other income (expense), net				<u>(1,755)</u>	<u>(1,755)</u>
Income before income taxes					<u>\$ 15,512</u>
Segment assets, total	<u>\$ 159,824</u>	<u>\$ 181,945</u>	<u>\$ —</u>	<u>\$ 84,375</u> (b)	<u>\$ 426,144</u>
<b>Six Months Ended July 4, 2015</b>					
Revenues	\$ 208,920	\$ 189,092	\$ 1,053	\$ —	\$ 399,065
Income (loss) from operations	<u>11,363</u>	<u>18,823</u>	<u>(3,538)</u>	(2,837) (a)	23,811
Interest expense				(1,690)	(1,690)
Interest income				122	122
Other income (expense), net				<u>(1,708)</u>	<u>(1,708)</u>
Income before income taxes					<u>\$ 20,535</u>
Segment assets, total	<u>\$ 164,250</u>	<u>\$ 165,587</u>	<u>\$ —</u>	<u>\$ 78,358</u> (b)	<u>\$ 408,195</u>

Reconciling adjustments from segment reporting to consolidated external financial reporting include unallocated corporate items:

- (a) Reclassification of depreciation expense and allocation of corporate expenses.
- (b) Corporate assets include cash, prepaid expenses, corporate facilities, enterprise-wide information systems and other nonoperating assets.

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**M. Fair Value Measurements and Financial Instruments**

Financial Accounting Standards Board Accounting Standard Codification 820, “Fair Value of Measurements and Disclosures (“Topic 820”)” defines fair value based on the price that would be received to sell an asset or the exit price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date. Market participants are defined as buyers or sellers in the principal or most advantageous market for the asset or liability that are independent of the reporting entity, knowledgeable and able and willing to transact for the asset or liability.

**Valuation Hierarchy**--Topic 820 establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value. The hierarchy prioritizes the inputs into three broad levels:

Level 1 inputs are quoted prices in active markets for identical assets or liabilities that the entity has the ability to access.

Level 2 inputs are observable inputs other than prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated with observable market data.

Level 3 inputs are unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

Our assets and liabilities measured at fair value on a recurring basis at July 2, 2016 were as follows:

<b>Assets and Liabilities Recorded at Fair Value on a Recurring Basis</b>	<b>Total Carrying Value at July 2, 2016</b>	<b>Fair Value Measurements at July 2, 2016 Using:</b>		
		<b>Quoted Prices in Active Markets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
<b>Assets:</b>				
Assets invested for self-insurance, classified as other assets, noncurrent	\$ 19,659	\$ 19,659	\$ —	\$ —
<b>Liabilities:</b>				
Deferred compensation	\$ 1,696	\$ —	\$ 1,696	\$ —

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**M. Fair Value Measurements and Financial Instruments (continued)**

Our assets and liabilities measured at fair value on a recurring basis at December 31, 2015 were as follows:

<b>Assets and Liabilities Recorded at Fair Value on a Recurring Basis</b>	<b>Total Carrying Value at December 31, 2015</b>	<b>Fair Value Measurements at December 31, 2015 Using:</b>		
		<b>Quoted Prices in Active Markets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
<b>Assets:</b>				
Assets invested for self-insurance, classified as other assets, noncurrent	\$ 17,167	\$ 17,167	\$ —	\$ —
<b>Liabilities:</b>				
Deferred compensation	\$ 1,574	\$ —	\$ 1,574	\$ —

The assets invested for self-insurance are money market funds--classified as Level 1--based on quoted market prices of the identical underlying securities in active markets. The estimated fair value of the deferred compensation--classified as Level 2--is based on the value of the Company's common shares, determined by independent valuation.

**Fair Value of Financial Instruments**--The fair values of our current financial assets and current liabilities, including cash, accounts receivable, accounts payable, and accrued expenses, among others, approximate their reported carrying values because of their short-term nature. Financial instruments classified as noncurrent liabilities and their carrying values and fair values were as follows:

	<b>July 2, 2016</b>		<b>December 31, 2015</b>	
	<b>Carrying Value</b>	<b>Fair Value</b>	<b>Carrying Value</b>	<b>Fair Value</b>
Revolving credit facility, noncurrent	\$ 86,000	\$ 86,000	\$ 54,500	\$ 54,500
Senior unsecured notes	24,000	25,447	24,000	24,837
Term loans, noncurrent	6,108	7,034	6,604	7,008
Total	<u>\$ 116,108</u>	<u>\$ 118,481</u>	<u>\$ 85,104</u>	<u>\$ 86,345</u>

The carrying value of our revolving credit facility approximates fair value--classified as Level 2--as the interest rates on the amounts outstanding are variable. The fair value of our senior unsecured notes and term loans--classified as Level 2--is determined based on expected future weighted-average interest rates with the same remaining maturities.

**Market Risk**--In the normal course of business, we are exposed to market risk related to changes in foreign currency exchange rates, changes in interest rates and changes in fuel prices. We do not hold or issue derivative financial instruments for trading or speculative purposes. In prior years, we have used derivative financial instruments to manage risk, in part, associated with changes in interest rates and changes in fuel prices. Presently, we are not engaged in any hedging or derivative activities.



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**N. Contingencies**

We are 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 reflected in the self-insurance accruals, and would not be material in relation to the financial position or results of operations.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**  
*(Amounts in thousands, except share data)*

Management's Discussion and Analysis of Financial Condition and Results of Operations is provided as a supplement to the accompanying condensed consolidated financial statements and notes to help provide an understanding of our financial condition, cash flows and results of operations.

We provide a wide range of arboriculture, horticultural, environmental and consulting services to residential, utility, commercial and government entities throughout the United States and Canada.

**Our Business**--Our operating results are reported in two segments: Residential and Commercial, and Utility. Residential and Commercial provides services to our residential and commercial customers including: the treatment, preservation, maintenance, removal and planting of trees, shrubs and other plant life; the practice of landscaping, grounds maintenance, tree surgery, tree feeding and tree spraying; the application of fertilizer, herbicides and insecticides; and, natural resource management and consulting, forestry research and development, and environmental planning. Utility is principally engaged in providing services to our utility customers--investor-owned, municipal utilities, and rural electric cooperatives--including: the practice of line-clearing and vegetation management around power lines, rights-of-way and chemical brush control; and, natural resource management and consulting, forestry research and development, and environmental planning. All other operating activities, including research, technical support and laboratory diagnostic facilities, are included in "All Other."

**RESULTS OF OPERATIONS**

The following table sets forth our consolidated results of operations as a percentage of revenues and the percentage change in dollar amounts of the results of operations for the periods presented.

	Three Months Ended			Six Months Ended		
	July 2, 2016	July 4, 2015	Percentage Change	July 2, 2016	July 4, 2015	Percentage Change
<b>Revenues</b>	100.0%	100.0%	— %	100.0%	100.0%	— %
Costs and expenses:						
Operating	61.0	61.1	(.1)	64.2	64.5	(.3)
Selling	16.4	15.5	.9	17.6	16.9	.7
General and administrative	6.5	6.0	.5	7.8	7.2	.6
Depreciation and amortization	5.5	5.2	.3	5.8	5.6	.2
Gain on sale of assets, net	(.2)	(.2)	—	(.1)	(.1)	—
<b>Income from operations</b>	10.8	12.4	(1.6)	4.7	5.9	(1.2)
Other income (expense):						
Interest expense	(.5)	(.4)	(.1)	(.5)	(.4)	(.1)
Interest income	—	—	—	—	—	—
Other, net	(.5)	(.4)	(.1)	(.4)	(.4)	—
<b>Income before income taxes</b>	9.8	11.6	(1.8)	3.8	5.1	(1.3)
Income taxes	3.9	4.5	(.6)	1.6	2.0	(.4)
<b>Net income</b>	5.9%	7.1%	(1.2)%	2.2%	3.1%	(.9)%

## Second Quarter—Three Months Ended July 2, 2016 Compared to Three Months Ended July 4, 2015

Our results of operations for the three months ended July 2, 2016 compared to the three months ended July 4, 2015 follows:

	Three Months Ended			
	July 2, 2016	July 4, 2015	Change	Percentage Change
<b>Revenues</b>	\$ 224,763	\$ 224,773	\$ (10)	— %
<b>Costs and expenses:</b>				
Operating	137,132	137,341	(209)	(.2)
Selling	36,859	34,914	1,945	5.6
General and administrative	14,675	13,534	1,141	8.4
Depreciation and amortization	12,290	11,607	683	5.9
Gain on sale of assets, net	(479)	(419)	(60)	14.3
	<u>200,477</u>	<u>196,977</u>	<u>3,500</u>	<u>1.8</u>
<b>Income from operations</b>	24,286	27,796	(3,510)	(12.6)
<b>Other income (expense):</b>				
Interest expense	(1,062)	(900)	(162)	18.0
Interest income	60	59	1	1.7
Other, net	(1,156)	(881)	(275)	nm
<b>Income before income taxes</b>	22,128	26,074	(3,946)	(15.1)
Income taxes	8,819	10,142	(1,323)	(13.0)
<b>Net income</b>	<u>\$ 13,309</u>	<u>\$ 15,932</u>	<u>\$ (2,623)</u>	<u>(16.5)%</u>

nm--not meaningful

**Revenues**--Revenues of \$224,763 decreased \$10 compared with \$224,773 in the second quarter 2015. Utility decreased \$3,252 or 3.0% compared with the second quarter 2015. Contracts lost and significant reductions in contract scope with two utility providers were partially offset by new contracts obtained and increases in rates and productivity on other contracts within both our U.S. and Canadian operations. Residential and Commercial increased \$3,310 or 2.9% compared with the second quarter 2015. Increases in productivity and contract rates on our tree pruning, tree removal and liquid service applications as well as additional revenue from the purchases of businesses account for the increase. Total revenues of \$224,763 include production incentive revenue, recognized under the completed-performance method, of \$804 during the second quarter 2016 compared with \$1,007 during the second quarter 2015.

**Operating Expenses**--Operating expenses of \$137,132 decreased \$209 compared with the second quarter 2015 and, as a percentage of revenues, decreased .1% to 61.0%. Utility decreased \$1,780 or 2.3% compared with the second quarter 2015 but, as a percentage of revenues, increased .5% to 73.3%. Decreases in labor expense, equipment maintenance expense, fuel expense and material expense were partially offset by increases in subcontractor expense, tool and saw expense, disposal expense and crew expenses. Residential and Commercial increased \$2,134 or 3.7% compared with the second quarter 2015 and, as a percentage of revenues, increased .5% to 49.8%. Increases in employee labor, equipment repair and maintenance expense, material expense, subcontractor expense and tool and saw expense were partially offset by a decrease in fuel expense, disposal expense and crew expenses.

Fuel costs of \$5,774 decreased \$1,374, or 19.2%, from the \$7,148 incurred in the second quarter 2015 and impacted operating expenses within all segments. The \$1,374 decrease included price decreases approximating \$1,098 and usage decreases approximating \$276.

**Selling Expenses**--Selling expenses of \$36,859 increased \$1,945 compared with the second quarter 2015 and as a percentage of revenues increased .9% to 16.4%. Utility decreased \$216 or 2.0% over the second quarter 2015 but as a percentage of revenues increased .1% to 10.2%. Decreases in field management wages and incentive expense, office expense and professional service expense were partially offset by increases in field management auto expense, travel and living expense, rent expense, communication expense and computer expense. Residential and Commercial increased \$2,071 or 8.3% over the second quarter 2015 and, as a percentage of revenues increased 1.1% to 22.7%. Increases in field management wages and incentive expense, office support wages, field management travel expense, rent expense, computer expense, communication expense and employee development expense were partially offset by a decrease in field management auto expense and sales and marketing expense.

**General and Administrative Expenses**--General and administrative expenses of \$14,675 increased \$1,141 from \$13,534 in the second quarter 2015. Increases in salary and incentive expense, stock compensation expense, pension expense and computer expense were partially offset by decreases in professional services expense, personnel development expense, communication expense, office rent and utilities expense and office expense.

**Depreciation and Amortization Expense**--Depreciation and amortization expense of \$12,290 increased \$683 from \$11,607 in the second quarter of 2015. The increase is attributable to higher capital expenditures related to increased business volume and purchases of businesses.

**Gain on the Sale of Assets, Net**--Gain on the sale of assets was \$479 for the second quarter 2016 and remained level with the gain in the second quarter 2015 due to higher average sales prices on fewer units sold as compared to the second quarter 2015.

**Interest Expense**--Interest expense of \$1,062 increased \$162 from the \$900 incurred in the second quarter 2015. The increase is attributable to higher-average debt levels necessary to fund operations and capital expenditures during the second quarter of 2016, as compared with the second quarter of 2015.

**Other, Net**--Other, net, of \$1,156 increased \$275 from the \$881 incurred in the second quarter 2015 and consisted of nonoperating income and expense, including foreign currency gains/losses on the intercompany account balances of our Canadian operations.

**Income Taxes**--Income taxes for the second quarter 2016 was \$8,819, as compared to \$10,142 for the second quarter 2015. Our tax provision for interim periods is determined using an estimate of our annual effective tax rate adjusted for discrete items, if any, that are taken into account in the relevant period. The 2016 annual effective tax rate is estimated to approximate 40.1%. Our annual effective tax rate for 2015 was 38.2%.

**Net Income**--Net income of \$13,309 for the second quarter 2016 was \$2,623 less than the \$15,932 experienced in the second quarter 2015.

## First Half—Six Months Ended July 2, 2016 Compared to Six Months Ended July 4, 2015

Our results of operations for the six months ended July 2, 2016 compared to the six months ended July 4, 2015 follows:

	Six Months Ended			Percentage Change
	July 2, 2016	July 4, 2015	Change	
<b>Revenues</b>	\$ 405,596	\$ 399,065	\$ 6,531	1.6 %
<b>Costs and expenses:</b>				
Operating	260,305	257,199	3,106	1.2
Selling	71,189	67,570	3,619	5.4
General and administrative	31,814	28,666	3,148	11.0
Depreciation and amortization	23,631	22,268	1,363	6.1
Gain on sale of assets, net	(509)	(449)	(60)	13.4
	<u>386,430</u>	<u>375,254</u>	<u>11,176</u>	<u>3.0</u>
<b>Income from operations</b>	19,166	23,811	(4,645)	(19.5)
<b>Other income (expense):</b>				
Interest expense	(2,027)	(1,690)	(337)	19.9
Interest income	128	122	6	4.9
Other, net	(1,755)	(1,708)	(47)	2.8
<b>Income before income taxes</b>	<u>15,512</u>	<u>20,535</u>	<u>(5,023)</u>	<u>(24.5)</u>
Income taxes	<u>6,391</u>	<u>8,131</u>	<u>(1,740)</u>	<u>(21.4)</u>
<b>Net income</b>	<u>\$ 9,121</u>	<u>\$ 12,404</u>	<u>\$ (3,283)</u>	<u>(26.5)%</u>

**Revenues**--Revenues of \$405,596 increased \$6,531 compared with \$399,065 in the first half 2015. Utility Services decreased \$3,607 or 1.7% compared with the first half 2015. Contracts lost and significant reductions in contract scope with two utility providers within our U.S. Utility operations were partially offset by new contracts obtained and increases in rates and productivity on other contracts within both our U.S. and Canadian operations. Residential and Commercial Services increased \$10,187 or 5.4% from the first half 2015. Higher contract rates on our tree pruning, tree removal and liquid services, increased productivity and additional revenue from the purchases of businesses account for the increase. Total revenues of \$405,596 include production incentive revenue, recognized under the completed-performance method, of \$1,095 during the first half 2016 compared with \$2,161 during the first half 2015.

**Operating Expenses**--Operating expenses of \$260,305 increased \$3,106 compared with the first half 2015 but, as a percentage of revenues, decreased .3% to 64.2%. Utility Services decreased \$1,133 or .7% compared with the first half 2015 but, as a percentage of revenue increased .6% to 74.6%. Decreases in labor expense, fuel expense and material expense were partially offset by increases in subcontractor expense, equipment maintenance expense, tool and saw expense and disposal expense. Residential and Commercial Services increased \$4,926 or 4.9% compared with the first half 2015 but, as a percentage of revenue decreased .3% to 53.1%. Increases in labor expense, equipment maintenance expense, materials expense, subcontractor expense and disposal expense were partially offset by a reductions in crew expenses and fuel expense.

Fuel costs of \$10,135 decreased \$2,717, or 21.1%, from the \$12,852 incurred in the first half 2015 and impacted operating expenses within all segments. The \$2,717 decrease included price decreases approximating \$2,508 and usage decreases approximating \$209.

**Selling Expenses**--Selling expenses of \$71,189 increased \$3,619 compared with the first half 2015 and, as a percentage of revenues increased .7% to 17.6%. Utility Services increased \$460 or 2.1% over the first half 2015. Increases in field management travel expense, field management auto expense, rent expense and employee development expense were partially offset by a decrease in field management wages and incentive expense, office expense, computer expense and professional service expense. Residential and Commercial Services experienced an increase of \$3,061 or 6.4% over the first half 2015 and as a percentage of revenue increased .3% to 25.4%. Increases in field management wages and incentive expense, office rent expense, employee development expense, field management travel expense, and office support wages were partially offset by a reduction in field management auto expense, communication expense and professional services expense.

**General and Administrative Expenses**--General and administrative expenses of \$31,814 increased \$3,148 from \$28,666 in the first half 2015. Increases in salary and incentive expense, stock compensation expense, travel and living expenses, computer expense and pension expense were partially offset by decreases in professional service expense, employee development expense and advertising expense.

**Depreciation and Amortization Expense**--Depreciation and amortization expense of \$23,631 increased \$1,363 from \$22,268 incurred in the first half of 2015. The increase is attributable to higher capital expenditures related to increased business volume and purchases of businesses.

**Gain on the Sale of Assets, Net**--Gain on the sale of assets was \$509 for the first half 2016 and remained level with the gain in the first half 2015 due to higher average sales prices on fewer units sold in the first half 2016 as compared with the first half 2015.

**Interest Expense**--Interest expense of \$2,027 increased \$337 from the \$1,690 incurred in the first half 2015. The increase is attributable to higher-average debt levels necessary to fund operations and capital expenditures during the first half of 2016, as compared with the first half of 2015.

**Other, Net**--Other, net, of \$1,755 increased \$47 from the \$1,708 incurred in the first half 2015 and consisted of nonoperating income and expense, including foreign currency gains/losses on the intercompany account balances of our Canadian operations.

**Income Taxes**--Income tax expense for the first half 2016 was \$6,391, as compared to \$8,131 for the first half 2015. Our tax provision for interim periods is determined using an estimate of our annual effective tax rate adjusted for discrete items, if any, that are taken into account in the relevant period. The 2016 annual effective tax rate is estimated to approximate 40.1%. Our annual effective tax rate for 2015 was 38.2%.

**Net Income**--Net income of \$9,121 for the first half 2016 was \$3,283 less than the \$12,404 experienced in the first half 2015.

## LIQUIDITY AND CAPITAL RESOURCES

Our principal financial requirements are for capital spending, working capital and business acquisitions.

### Cash Flow Summary

Our cash flows from operating, investing and financing activities for the six months ended July 2, 2016 and July 4, 2015 follow:

	<u>2016</u>	<u>2015</u>
<b>Cash provided by (used in):</b>		
Operating activities	\$ 18,634	\$ 18,692
Investing activities	(40,662)	(46,500)
Financing activities	19,364	27,619
Decrease in cash	<u>\$ (2,664)</u>	<u>\$ (189)</u>

**Cash Provided By Operating Activities**--Cash provided by operating activities was \$18,634 for the first six months of 2016, or \$58 less than the \$18,692 provided in the first six months of 2015. The \$58 decrease in operating cash flow was primarily attributable to an increase of \$1,363 in depreciation and amortization, \$576 more cash used from operating assets and liabilities and a \$3,283 decrease in net income.

Overall, accounts receivable increased \$20,816 during the first six months of 2016, as compared to the increase of \$18,897 during the first six months of 2015. With respect to the change in accounts receivable arising from business levels, the “days-sales-outstanding” in accounts receivable (sometimes referred to as “DSO”) at the end of the first six months of 2016 increased four days to 57 days, as compared to the end of the first six months of 2015. The DSO at July 4, 2015 was 53 days.

Operating liabilities increased \$570 in the first six months of 2016, or \$4,269 more than the \$3,699 decrease in the first six months of 2015. Accounts payable and accrued expenses decreased \$6,375 during the first six months of 2016 as compared with a decrease of \$6,061 for the first six months of 2015. Decreases in employee compensation accruals, trade payables and 401K/SOP liabilities were partially offset by increases in advance payments from customers, compensated-absence accruals, group insurance accruals and employee savings withholdings. Self-insurance accruals increased \$6,945 in the first six months of 2016, which was \$4,583 more than the increase of \$2,362 experienced in the first six months of 2015. The increase occurred in our workers’ compensation, general liability and vehicle liability classifications and resulted primarily from an overall increase in deductible amounts under commercial insurance and the self-insured risk retention.

The change in operating assets and liabilities other, net, increased \$4,993 for the first six months of 2016 as compared with an increase of \$7,919 for the first six months of 2015, with the \$2,926 net change related primarily to a decrease in prepaid expenses and tax deposits.

**Cash Used In Investing Activities**--Cash used in investing activities for the first six months of 2016 was \$40,662, or \$5,838 less than the \$46,500 used during the first six months of 2015. Reductions in the purchase of equipment were partially offset by an increase in the purchase of land and buildings and businesses.

**Cash Provided By Financing Activities**--Cash provided by financing activities of \$19,364 decreased \$8,255 during the first six months of 2016 as compared with \$27,619 of cash provided during the first six months of 2015. During the first six months of 2016, our revolving credit facility provided \$31,500 in cash as compared with the \$40,500 provided during the first six months of 2015. We use the credit facility primarily for capital expenditures and payments of notes payable related to acquisitions. Payments of notes payable used \$7,350 during the first six months of 2016, \$544 more than the \$6,806 used in the first six months of 2015. Treasury share transactions (purchases and sales) used \$3,472 for the first six months of 2016, \$1,255 less than the \$4,727 used in the first six months of 2015, and included \$371 of cash received from our common share subscriptions. Dividends paid of \$1,314 during the first six months of 2016 decreased \$34, as compared with \$1,348 paid in the first six months of 2015.

**Revolving Credit Facility** --We have a \$175,000 revolving credit facility with a group of banks, which will expire in November 2018 and permits borrowings, as defined, up to \$175,000, including a letter of credit sublimit of \$100,000 and a swing-line commitment of \$15,000. Under certain circumstances, the amount available under the revolving credit facility may be increased to \$210,000. The revolving credit facility contains certain affirmative and negative covenants customary for this type of facility and includes financial covenant ratios with respect to a maximum leverage ratio and a maximum balance-sheet leverage ratio.

As of July 2, 2016, we had unused commitments under the facility approximating \$84,939, with \$90,061 committed, consisting of borrowings of \$86,000 and issued letters of credit of \$4,061.

Borrowings outstanding bear interest, at Davey Tree’s option, of either (a) a base rate or (b) LIBOR plus a margin adjustment ranging from .75% to 1.50%--with the margin adjustments in both instances based on the Company’s leverage ratio at the time of borrowing. The base rate is the greater of (i) the agent bank’s prime rate, (ii) LIBOR

plus 1.50%, or (iii) the federal funds rate plus .50%. A commitment fee ranging from .10% to .25% is also required based on the average daily unborrowed commitment.

**5.09% Senior Unsecured Notes**--The \$30,000 senior unsecured notes are due July 22, 2020 and were issued during July 2010 as 5.09% Senior Unsecured Notes, Series A (the "5.09% Senior Notes"), pursuant to a Master Note Purchase Agreement (the "Purchase Agreement") between the Company and the purchasers of the 5.09% Senior Notes.

The 5.09% Senior Notes are equal in right of payment with our revolving credit facility and all other senior unsecured obligations of the Company. Interest is payable semiannually and five equal, annual principal payments commenced on July 22, 2016 (the sixth anniversary of issuance). The Purchase Agreement contains customary events of default and covenants related to limitations on indebtedness and transactions with affiliates and the maintenance of certain financial ratios.

**Accounts Receivable Securitization Facility**--On May 9, 2016, Davey Tree entered into a one-year agreement with a bank, for an accounts receivable securitization facility (the "AR securitization program"), whereby Davey Tree has pledged a first priority security interest in certain trade receivables in exchange for the bank issuing letters of credit ("LCs") with a committed facility limit of \$60,000.

As of July 2, 2016, we had issued letters of credit of \$53,250 under the terms of the AR securitization program.

Under the AR securitization program, Davey Tree transfers by selling or contributing current and future trade receivables to a wholly-owned, bankruptcy-remote financing subsidiary which pledges a perfected first priority security interest in the trade receivables--equal to the issued letters of credit as of July 2, 2016--to the bank in exchange for the bank issuing LCs.

Fees payable to the bank include: (a) an LC issuance fee, payable on each settlement date, in the amount of .90% per annum on the aggregate amount of all LCs outstanding plus outstanding reimbursement obligations (e.g., arising from drawn LCs), if any, and (b) an unused LC fee, payable monthly, equal to (i) .35% per annum for each day on which the sum of the total LCs outstanding plus any outstanding reimbursement obligations is greater than or equal to 50% of the facility limit and (ii) .45% per annum for each day on which the sum of the total LCs outstanding plus any outstanding reimbursement obligations is less than 50% of the facility limit. If an LC is drawn and the bank is not immediately reimbursed in full for the drawn amount, any outstanding reimbursement obligation will accrue interest at a per annum rate equal to a reserve-adjusted LIBOR or, in certain circumstances, a base rate equal to the higher of (i) the bank's prime rate and (ii) the federal funds rate plus .50% and, following any default, 2.00% plus the greater of (a) adjusted LIBOR and (b) a base rate equal to the higher of (i) the bank's prime rate and (ii) the federal funds rate plus .50%.

The agreements underlying the AR securitization program contains various customary representations and warranties, covenants, and default provisions which provide for the termination and acceleration of the commitments under the AR securitization program in circumstances including, but not limited to, failure to make payments when due, breach of a representation, warranty or covenant, certain insolvency events or failure to maintain the security interest in the trade receivables, and defaults under other material indebtedness.



### ***Contractual Obligations Summary and Commercial Commitments***

The following summarizes our long-term contractual obligations, as of July 2, 2016, to make future payments for the periods indicated

<b>Description</b>	<b>Total</b>	<b>Six</b>	<b>Year Ending December 31,</b>					<b>Thereafter</b>
		<b>Months Ending</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>		
		<b>December 31,</b>						
		<b>2016</b>						
Revolving credit facility	\$ 86,000	\$ —	\$ —	\$ 86,000	\$ —	\$ —	\$ —	\$ —
Senior unsecured notes	30,000	6,000	6,000	6,000	6,000	6,000	6,000	—
Term loans	8,769	1,893	1,801	533	164	4,378	—	—
Capital lease obligations	561	65	130	130	130	106	—	—
Operating lease obligations	21,036	1,395	4,302	3,348	2,463	1,980	7,548	—
Self-insurance accruals	64,674	13,558	17,805	12,328	7,489	3,902	9,592	—
Purchase obligations	9,700	9,700	—	—	—	—	—	—
Other liabilities	17,251	1,399	1,890	2,240	1,749	1,409	8,564	—
	<u>\$ 237,991</u>	<u>\$ 34,010</u>	<u>\$ 31,928</u>	<u>\$110,579</u>	<u>\$ 17,995</u>	<u>\$ 17,775</u>	<u>\$ 25,704</u>	

The self-insurance accruals in the summary above reflect the total of the undiscounted amount accrued, for which amounts estimated to be due each year may differ from actual payments required to fund claims. Purchase obligations in the summary above represent open purchase-order amounts we anticipate will become payable for goods and services we have negotiated for delivery as of July 2, 2016. Other liabilities include estimates of future expected funding requirements related to retirement plans and other sundry items. Because their future cash outflows are uncertain, accrued income tax liabilities for uncertain tax positions, as of July 2, 2016, have not been included in the summary above. Noncurrent deferred taxes and payments related to defined benefit pension plans are also not included in the summary.

As of July 2, 2016, total commitments related to issued letters of credit were \$59,315, of which \$4,061 were issued under the Revolving Credit Facility, \$53,250 were issued under the Accounts Receivable Securitization Facility and, \$2,004 were issued under short-term lines of credit. As of December 31, 2015, total commitments related to issued letters of credit were \$59,350, of which \$57,347 were issued under the Revolving Credit Facility and \$2,003 were issued under short-term lines of credit.

Also, as is common in our industry, we have performance obligations that are supported by surety bonds, which expire during 2016 through 2020. We intend to renew the surety bonds where appropriate and as necessary.

### ***Capital Resources***

Cash generated from operations and our revolving credit facility are our primary sources of capital.

Business seasonality results in higher revenues during the second and third quarters as compared with the first and fourth quarters of the year, while our methods of accounting for fixed costs, such as depreciation and amortization expense, rent and interest expense, are not significantly impacted by business seasonality. Capital resources during these periods are equally affected. We satisfy seasonal working capital needs and other financing requirements with the revolving credit facility and other short-term lines of credit. We are continually reviewing our existing sources of financing and evaluating alternatives. At July 2, 2016, we had working capital of \$69,854, short-term lines of credit approximating \$7,156 and \$84,939 available under our revolving credit facility.

We believe our sources of capital, at this time, provide us with the financial flexibility to meet our capital-spending plans and to continue to complete business acquisitions for at least the next twelve months and for the reasonably foreseeable future.

## Recent Accounting Guidance

### Accounting Standards Adopted in 2016

***Accounting Standards Update 2015-16, Business Combinations: Simplifying the Accounting for Measurement-Period Adjustments***--In September 2015, the FASB issued Accounting Standards Update (“ASU”) 2015-16, “Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments.” ASU 2015-16 simplifies the reporting of adjustments to the provisional amounts recorded for a business combination during the measurement period by eliminating the requirement to retrospectively account for those adjustments. Companies are required to present separately, on the face of the income statement, or disclose in the notes to the financial statements, the impact on current period earnings by line item that would have been recorded in previous periods if the adjustment to the provisional amounts were recognized as of the acquisition date. The amendments in ASU 2015-16 became effective January 1, 2016 and require prospective application to qualifying business combinations.

### Accounting Standards Not Yet Adopted

***Accounting Standards Update 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting***--In March 2016, the FASB issued ASU 2016-09, “Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting,” with the objective to simplify several aspects of the accounting for share-based payment transactions, including: the income tax consequences; classification of awards as either equity or liabilities; classification of certain items on the statement of cash flows; and, accounting for forfeitures. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, which for Davey Tree would be January 1, 2017. Early adoption is permitted. Management has not yet completed its assessment of the impact of the new standard on the Company’s consolidated financial statements.

***Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606)***--In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers (Topic 606),” which will replace all current U.S. GAAP guidance on revenue recognition and eliminate all industry-specific guidance.

The new revenue recognition guidance provides a unified model to determine when and how revenue is recognized. The underlying principle is that an entity should recognize revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration for which the entity expects in exchange for those goods and services. The guidance provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include capitalization of certain contract costs, consideration of the time value of money in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. The guidance also requires enhanced information to be presented in the financial statements regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity’s contracts with customers.

In August 2015, the FASB issued ASU No. 2015-14, “Revenue from Contracts with Customers (Topic 606) (‘Update 2015-14’): Deferral of the Effective Date,” which responded to stakeholders’ requests to defer the effective date of the guidance in ASU 2014-09. In March 2016, the FASB issued ASU 2016-08, “Revenue from Contracts with Customers (Topic 606)--Principal versus Agent Considerations (Reporting Revenue Gross versus Net) (‘Update 2016-08’),” which clarifies the implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU 2016-10, “Revenue from Contracts with Customers (Topic 606) (‘Update 2016-10’) Identifying Performance Obligations and Licensing,” which clarifies multiple aspects of Topic 606. In May 2016, the FASB issued ASU No. 2016-12, “Revenue from Contracts with Customers (Topic

606) - Narrow-Scope Improvements and Practical Expedients ('Update 2016-12')," which provides clarifying guidance in a few narrow areas and adds some practical expedients to the guidance.

The effective date and the transition requirements for the Updates are the same as the effective date of Topic 606 ASU 2015-14, which becomes effective for Davey Tree beginning with the first quarter 2018 and can be adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption. The FASB also affirmed its proposal to permit all entities to apply the new revenue standard early, but not before the original effective date, which for Davey Tree would be first quarter 2017. The new revenue guidance will supersede existing revenue guidance affecting our Company, and may also affect our business processes and our information technology systems. As a result, our evaluation of the effect of the new revenue guidance will extend over future periods.

**Accounting Standards Update 2016-02, Leases (Topic 842)**--In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)." ASU 2016-02 establishes a comprehensive new lease accounting model. The new standard: (a) clarifies the definition of a lease; (b) requires a dual approach to lease classification similar to current lease classifications; and, (c) causes lessees to recognize leases on the balance sheet as a lease liability with a corresponding right-of-use asset for leases with a lease-term of more than twelve months. The new standard is effective for interim and annual periods beginning after December 15, 2018, which for Davey Tree would be January 1, 2019. Early adoption is permitted. The new standard requires a modified retrospective transition for capital or operating leases existing at or entered into after the beginning of the earliest comparative period presented in the financial statements, but it does not require transition accounting for leases that expire prior to the date of initial application. We are currently evaluating the impact of the new standard on our consolidated financial statements.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the use of estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented.

As discussed in our annual report on Form 10-K for the year ended December 31, 2015, we believe that our policies related to revenue recognition, the allowance for doubtful accounts and self-insurance accruals are our "critical accounting policies and estimates"--those most important to the financial presentations and those that require the most difficult, subjective or complex judgments.

On an ongoing basis, we evaluate our estimates and assumptions, including those related to accounts receivable, specifically those receivables under contractual arrangements primarily with Utility customers; allowance for doubtful accounts; and self-insurance accruals. We base our estimates on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates.

## **NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. These statements relate to future events or our future financial performance. In some cases, forward-looking statements may be identified by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "potential," "continue" or the negative of these terms or other comparable terminology. These statements are only predictions

and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's actual results, levels of activity, performance or achievements to differ materially from what is expressed or implied in these forward-looking statements. Some important factors that could cause actual results to differ materially from those in the forward-looking statements include:

- Our business, other than tree services to utility customers, is highly seasonal and weather dependent.
- The effects of the uneven economic recovery and the continuing financial and credit uncertainties may adversely impact our customers' spending and pricing for our services, and impede our collection of accounts receivable.
- Significant customers, particularly utilities, may experience financial difficulties, resulting in payment delays or delinquencies.
- The seasonal nature of our business and changes in general and local economic conditions, among other factors, may cause our quarterly results to fluctuate, and our prior performance is not necessarily indicative of future results.
- The uncertainties in the credit and financial markets may limit our access to capital.
- Significant increases in fuel prices for extended periods of time will increase our operating expenses.
- Fluctuations in foreign currency exchange rates may have a material adverse impact on our operating results.
- We have significant contracts with our utility, commercial and government customers that include liability risk exposure as part of those contracts. Consequently, we have substantial excess-umbrella liability insurance, and increases in the cost of obtaining adequate insurance, or the inadequacy of our self-insurance accruals or insurance coverages, could negatively impact our liquidity and financial condition.
- Because no public market exists for our common shares, the ability of shareholders to sell their common shares is limited.
- Significant increases in health care costs could negatively impact our results of operations or financial position.
- We are subject to intense competition.
- Our failure to comply with environmental laws could result in significant liabilities, fines and/or penalties.
- The impact of regulations initiated as a response to possible changing climate conditions could have a negative effect on our results of operations or our financial condition.
- We may encounter difficulties obtaining surety bonds or letters of credit necessary to support our operations.
- We are dependent, in part, on our reputation of quality, integrity and performance. If our reputation is damaged, we may be adversely affected.
- We may be unable to attract and retain a sufficient number of qualified employees for our field operations, and we may be unable to attract and retain qualified management personnel.
- Our facilities could be damaged or our operations could be disrupted, or our customers or vendors may be adversely affected, by events such as natural disasters, pandemics, terrorist attacks or other external events.
- A disruption in our information technology systems, including a disruption related to cybersecurity, could adversely affect our financial performance.
- We are subject to third-party and governmental regulatory claims and litigation that may have an adverse effect on us.
- We may misjudge a competitive bid and be contractually bound to an unprofitable contract.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We are under no duty to update any of the forward-looking statements after the date of this quarterly report on Form 10-Q to conform these statements to actual future results.

The factors described above, as well as other factors that may adversely impact our actual results, are discussed in "Part II - Item 1A. Risk Factors." of this quarterly report on Form 10-Q and in our annual report on Form 10-K for the year ended December 31, 2015 in "Part I - Item 1A. Risk Factors."

**Item 3. *Quantitative and Qualitative Disclosures about Market Risk.***

During the quarter ended July 2, 2016, there have been no material changes in the market risk previously presented in our annual report on Form 10-K for the year ended December 31, 2015.

**Item 4. *Controls and Procedures.***

**(a) Management's Evaluation of Disclosure Controls and Procedures**

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that the design and operation of our disclosure controls and procedures were effective at the reasonable assurance level as of the end of the period covered by this report in ensuring that information required to be disclosed in the reports that we file or submit under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

**(b) Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting during the fiscal quarter ended July 2, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **The Davey Tree Expert Company**

### **Part II. Other Information**

Items 1, 3, 4 and 5 are not applicable.

#### **Item 1A. Risk Factors.**

The factors described below represent the principal risks we face. Except as otherwise indicated, these factors may or may not occur and we are not in a position to express a view on the likelihood of any such factor occurring. Other factors may exist that we do not consider to be significant based on information that is currently available or that we are not currently able to anticipate.

#### **Our business is highly seasonal and weather dependent.**

Our business, other than tree services to utility customers, is highly seasonal and weather dependent, primarily due to fluctuations in horticultural services provided to Residential and Commercial customers. We have historically incurred losses in the first quarter, while revenue and operating income are generally highest in the second and third quarters of the calendar year. Inclement weather, such as uncharacteristically low or high (drought) temperatures, in the second and third quarters could dampen the demand for our horticultural services, resulting in reduced revenues that would have an adverse effect on our results of operations.

#### **The effects of the uneven economic recovery and the continuing financial and credit uncertainties may adversely impact our customers' future spending as well as pricing and payment for our services, thus negatively impacting our operations and growth.**

While the economy has shown signs of improvement, sustainability of economic recovery remains uncertain. A slowing or stoppage in economic recovery may adversely impact the demand for our services and potentially result in depressed prices for our services and the delay or cancellation of projects. This makes it difficult to estimate our customers' requirements for our services and, therefore, adds uncertainty to customer demand. Increased uncertainty about the economy may cause a reduction in our customers' spending for our services and may also impact the ability of our customers to pay amounts owed, which could reduce our cash flow and adversely impact our debt or equity financing. These events could have a material adverse effect on our operations and our ability to grow at historical levels.

#### **Financial difficulties or the bankruptcy of one or more of our major customers could adversely affect our results.**

Our ability to collect our accounts receivable and future sales depends, in part, on the financial strength of our customers. We grant credit, generally without collateral, to our customers. Consequently, we are subject to credit risk related to changes in business and economic factors throughout the United States and Canada. In the event customers experience financial difficulty, and particularly if bankruptcy results, our profitability may be adversely impacted by our failure to collect our accounts receivable in excess of our estimated allowance for uncollectible accounts. Additionally, our future revenues could be reduced by the loss of a customer due to bankruptcy. Our failure to collect accounts receivable and/or the loss of one or more major customers could have an adverse effect on our net income and financial condition.

#### **Our business is dependent upon service to our utility customers and we may be affected by developments in the utility industry.**

We derive approximately 53% of our total revenues from our Utility segment, including approximately 11% of our total revenues from Pacific Gas & Electric Company. Significant adverse developments in the utility industry generally, or specifically for our major utility customers, could result in pressure to reduce costs by utility industry service providers (such as us), delays in payments of our accounts receivable, or increases in uncollectible

accounts receivable, among other things. As a result, such developments could have an adverse effect on our results of operations.

**Our quarterly results may fluctuate.**

We have experienced and expect to continue to experience quarterly variations in revenues and operating income as a result of many factors, including:

- the seasonality of our business;
- the timing and volume of customers' projects;
- budgetary spending patterns of customers;
- the commencement or termination of service agreements;
- costs incurred to support growth internally or through acquisitions;
- changes in our mix of customers, contracts and business activities;
- fluctuations in insurance expense due to changes in claims experience and actuarial assumptions; and
- general and local economic conditions.

Accordingly, our operating results in any particular quarter may not be indicative of the results that you can expect for any other quarter or for the entire year.

**We may not have access to capital in the future due to continuing uncertainties in the financial and credit markets.**

We may need new or additional financing in the future to conduct our operations, expand our business or refinance existing indebtedness. Future changes in the general economic conditions and/or financial markets in the United States or globally could affect adversely our ability to raise capital on favorable terms or at all. From time-to-time we have relied, and may also rely in the future, on access to financial markets as a source of liquidity for working capital requirements, acquisitions and general corporate purposes. Our access to funds under our revolving credit facility is dependent on the ability of the financial institutions that are parties to the facility to meet their funding commitments. Those financial institutions may not be able to meet their funding commitments if they experience shortages of capital and liquidity or if they experience excessive volumes of borrowing requests within a short period of time. The continuation of economic disruptions and any resulting limitations on future funding, including any restrictions on access to funds under our revolving credit facility, could have a material adverse effect on us.

**We are subject to the risk of changes in fuel costs.**

The cost of fuel is a major operating expense of our business. Significant increases in fuel prices for extended periods of time will cause our operating expenses to fluctuate. An increase in cost with partial or no corresponding compensation from customers would lead to lower margins that would have an adverse effect on our results of operations.

**We are subject to the effect of foreign currency exchange rate fluctuations, which may have a material adverse impact on us.**

We are exposed to foreign currency exchange rate risk resulting from our operations in Canada, where we provide a comprehensive range of horticultural services. Fluctuations in foreign currency exchange rates may make our services more expensive for others to purchase or increase our operating costs, affecting our competitiveness and our profitability. Our financial results could be affected by factors such as changes in the foreign currency exchange rate or differing economic conditions in the Canadian markets as compared with the markets for our services in the United States. Our earnings are affected by translation exposures from currency fluctuations in the value of the U.S. dollar as compared to the Canadian dollar.

Revenues from customers in Canada are subject to foreign currency exchange. Thus, certain revenues and expenses have been, and are expected to be subject to the effect of foreign currency fluctuations, and these fluctuations may have a material adverse impact on our operating results, asset values and could reduce shareholders' equity. In addition, if we expand our Canadian operations, exposures to gains and losses on foreign currency transactions may increase.

**We could be negatively impacted if our self-insurance accruals or our insurance coverages prove to be inadequate.**

We are generally self-insured for losses and liabilities related to workers' compensation, vehicle liability and general liability claims (including any wildfire-suppression claims, up to certain retained coverage limits). A liability for unpaid claims and associated expenses, including incurred but not reported losses, is actuarially determined and reflected in our consolidated balance sheet as an accrued liability. The determination of such claims and expenses, and the extent of the need for accrued liabilities, are continually reviewed and updated. If we were to experience insurance claims or costs above our estimates and were unable to offset such increases with earnings, our business could be adversely affected. Also, where we self-insure, a deterioration in claims management, whether by our management or by a third-party claims administrator, could lead to delays in settling claims, thereby increasing claim costs, particularly as it relates to workers' compensation. In addition, catastrophic uninsured claims filed against us or the inability of our insurance carriers to pay otherwise-insured claims would have an adverse effect on our financial condition.

Furthermore, many customers, particularly utilities, prefer to do business with contractors with significant financial resources, who can provide substantial insurance coverage. Should we be unable to renew our excess liability insurance and other commercial insurance policies at competitive rates, this loss would have an adverse effect on our financial condition and results of operations.

**Increases in our health insurance costs could adversely affect our results of operations and cash flows.**

The costs of employee health care insurance have been increasing in recent years due to rising health care costs, legislative changes, and general economic conditions. Additionally, we may incur additional costs because of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, the "Health Care Reform Laws"). Provisions of these laws have become and will become effective at various dates over the next several years. Because of the breadth and complexity of these laws, the lack of regulations and guidance on implementation, and the phased-in nature of the new regulations, as well as other health care reform legislation considered by Congress and state legislatures, we cannot predict with certainty the future effect of these laws on us. A continued increase in health care costs or additional costs incurred as a result of the Health Care Reform Laws or other future health care reform laws imposed by Congress or state legislatures could have a negative impact on our financial position and results of operations.

**The unavailability or cancellation of third-party insurance coverage may have a material adverse effect on our financial condition and results of operations as well as disrupt our operations.**

Any of our existing excess insurance coverage may not be renewed upon the expiration of the coverage period or future coverage may not be available at competitive rates for the required limits. In addition, our third-party insurers could fail, suddenly cancel our coverage or otherwise be unable to provide us with adequate insurance coverage. If any of these events occur, they may have a material adverse effect on our financial condition and results of operations as well as disrupt our operations. For example, we have operations in California, which has an environment prone to wildfires. Should our third-party insurers determine to exclude coverage for wildfires in the future, we could be exposed to significant liabilities, having a material adverse effect on our financial condition and results of operations and potentially disrupting our California operations.



**Because no public market exists for our common shares, your ability to sell your common shares may be limited.**

Our common shares are not traded on any national exchange, market system or over-the-counter bulletin board. Because no public market exists for our common shares, your ability to sell these shares is limited.

**We are subject to intense competition.**

We believe that each aspect of our business is highly competitive. Principal methods of competition in our operating segments are customer service, marketing, image, performance and reputation. Pricing is not always a critical factor in a customer's decision with respect to Residential and Commercial; however, pricing is generally the principal method of competition for Utility, although in most instances consideration is given to reputation and past production performance. On a national level, our competition is primarily landscape construction and maintenance companies as well as residential and commercial lawn care companies. At a local and regional level, our competition comes mainly from small, local companies which are engaged primarily in tree care and lawn services. Our Utility segment competes principally with one major national competitor, as well as several smaller regional firms. Furthermore, competitors may have lower costs because privately-owned companies operating in a limited geographic area may have significantly lower labor and overhead costs. Our competitors may develop the expertise, experience and resources to provide services that are superior in both price and quality to our services. These strong competitive pressures could inhibit our success in bidding for profitable business and may have a material adverse effect on our business, financial condition and results of operations.

**Our failure to comply with environmental laws could result in significant liabilities.**

Our facilities and operations are subject to governmental regulations designed to protect the environment, particularly with respect to our services regarding insect and tree, shrub and lawn disease management, because these services involve to a considerable degree the blending and application of spray materials, which require formal licensing in most areas. Continual changes in environmental laws, regulations and licensing requirements, environmental conditions, environmental awareness, technology and social attitudes make it necessary for us to maintain a high degree of awareness of the impact such changes have on our compliance programs and the market for our services. We are subject to existing federal, state and local laws, regulations and licensing requirements regulating the use of materials in our spraying operations as well as certain other aspects of our business. If we fail to comply with such laws, regulations or licensing requirements, we may become subject to significant liabilities, fines and/or penalties, which could adversely affect our financial condition and results of operations.

**We cannot predict the impact that the debate on changing climate conditions, including legal, regulatory and social responses thereto, may have on our business.**

Many scientists, environmentalists, international organizations, political activists, regulators and other commentators believe that global climate change has added, and will continue to add, to the unpredictability, frequency and severity of natural disasters in certain parts of the world. In response, a number of legal and regulatory measures and social initiatives have been introduced in an effort to reduce greenhouse gas and other carbon emissions that these parties believe may be contributors to global climate change. These proposals, if enacted, could result in a variety of regulatory programs, including potential new regulations, additional charges and taxes to fund energy efficiency activities, or other regulatory actions. Any of these actions could result in increased costs associated with our operations and impact the prices we charge our customers.

We cannot predict the impact, if any, that changing climate conditions will have on us or our customers. However, it is possible that the legal, regulatory and social responses to real or imagined climate change could have a negative effect on our results of operations or our financial condition.

**We may be adversely affected if we are unable to obtain necessary surety bonds or letters of credit.**

Surety market conditions are currently difficult as a result of significant losses incurred by many sureties in recent years, both in the construction industry as well as in certain larger corporate bankruptcies. As a result, less bonding capacity is available in the market and terms have become more expensive and restrictive. Further, under standard terms in the surety market, sureties issue or continue bonds on a project-by-project basis and can decline to issue bonds at any time or require the posting of collateral as a condition to issuing or renewing any bonds. If surety providers were to limit or eliminate our access to bonding, we would need to post other forms of collateral for project performance, such as letters of credit or cash. We may be unable to secure sufficient letters of credit on acceptable terms, or at all. Accordingly, if we were to experience an interruption or reduction in the availability of bonding capacity, our liquidity may be adversely affected.

**We may be adversely affected if our reputation is damaged.**

We are dependent, in part, upon our reputation of quality, integrity and performance. If our reputation were damaged in some way, it may impact our ability to grow or maintain our business.

**We may be unable to employ a sufficient workforce for our field operations.**

Our industry operates in an environment that requires heavy manual labor. We may experience slower growth in the labor force for this type of work than in the past. As a result, we may experience labor shortages or the need to pay more to attract and retain qualified employees.

**We may be unable to attract and retain skilled management.**

Our success depends, in part, on our ability to attract and retain key managers. Competition for the best people can be intense and we may not be able to promote, hire or retain skilled managers. The loss of services of one or more of our key managers could have a material adverse impact on our business because of the loss of the manager's skills, knowledge of our industry and years of industry experience, and the difficulty of promptly finding qualified replacement personnel.

**Natural disasters, pandemics, terrorist attacks and other external events could adversely affect our business.**

Natural disasters, pandemics, terrorist attacks and other adverse external events could materially damage our facilities or disrupt our operations, or damage the facilities or disrupt the operations of our customers or vendors. The occurrence of any such event could adversely affect our business, financial condition and results of operations.

**A disruption in our information technology systems, including a disruption related to cybersecurity, could adversely affect our financial performance.**

We rely on the accuracy, capacity and security of our information technology systems. Despite the security measures that we have implemented, including those measures related to cybersecurity, our systems could be breached or damaged by computer viruses, natural or man-made incidents or disasters or unauthorized physical or electronic access. A breach could result in business disruption, theft of our intellectual property, trade secrets or customer information and unauthorized access to personnel information. To the extent that our business is interrupted or data is lost, destroyed or inappropriately used or disclosed, such disruptions could adversely affect our competitive position, reputation, relationships with our customers, financial condition, operating results and cash flows. In addition, we may be required to incur significant costs to protect against the damage caused by these disruptions or security breaches in the future.

### **We are subject to third-party and governmental regulatory claims and litigation.**

From time-to-time, customers, vendors, employees, governmental regulatory authorities and others may make claims and take legal action against us. Whether these claims and legal actions are founded or unfounded, if such claims and legal actions are not resolved in our favor, they may result in significant financial liability. Any such financial liability could have a material adverse effect on our financial condition and results of operations. Any such claims and legal actions may also require significant management attention and may detract from management's focus on our operations.

### **We may be adversely affected if we enter into a major unprofitable contract.**

Our Residential and Commercial segment and our Utility segment frequently operate in a competitive bid contract environment. As a result, we may misjudge a bid and be contractually bound to an unprofitable contract, which could adversely affect our results of operations.

### **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

The following table provides information on purchases of our common shares outstanding made by us during the first six months of 2016.

<b>Period</b>	<b>Total Number of Shares Purchased</b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs</b>
Fiscal 2016				
January 1 to January 30	804	\$ 31.50	n/a	n/a
January 31 to February 27	270	31.50	n/a	n/a
February 28 to April 2	51,749	32.70	n/a	n/a
Total First Quarter	52,823	32.68		
April 3 to April 30	102,133	32.70	n/a	n/a
May 1 to May 28	109,358	32.70	n/a	n/a
May 29 to July 2	79,308	32.70	n/a	n/a
Total Second Quarter	290,799	32.70		
<b>Total Year-to-Date</b>	<b>343,622</b>	<b>\$ 32.70</b>		

n/a--Not applicable. There are no publicly announced plans or programs to purchase common shares.

Our common shares are not listed or traded on an established public trading market and market prices are, therefore, not available. Semiannually, for purposes of the Davey 401KSOP and ESOP, the fair market value of our common shares is determined by an independent stock valuation firm, based upon our performance and financial condition, using a peer group of comparable companies selected by that firm. The peer group currently consists of: ABM Industries Incorporated; Comfort Systems USA, Inc.; Dycom Industries, Inc.; MYR Group, Inc.; Quanta Services, Inc.; Rollins, Inc.; and Scotts Miracle-Gro Company. The semiannual valuations are effective for a period of six months and the per-share price established by those valuations is the price at which our Board of Directors has determined our common shares will be bought and sold during that six-month period in transactions involving Davey Tree or one of its employee benefit or stock purchase plans. Since 1979, we have

provided a ready market for all shareholders through our direct purchase of their common shares, although we are under no obligation to do so. The purchases described above were added to our treasury stock.

**Item 6. Exhibits.**

See Exhibit Index page below.

### Signatures

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

THE DAVEY TREE EXPERT COMPANY

Date: August 2, 2016      By: /s/ Joseph R. Paul  
Joseph R. Paul  
Executive Vice President, Chief Financial Officer and Secretary  
(Principal Financial Officer)

Date: August 2, 2016      By: /s/ Nicholas R. Sucic  
Nicholas R. Sucic  
Vice President and Controller  
(Principal Accounting Officer)

## Exhibit Index

### **Exhibit No.   Description**

10.1	Receivables Financing Agreement, dated May 9, 2016, between The Davey Tree Expert Company, Davey Receivables LLC, PNC Bank, National Association, and PNC Capital Markets LLC (Incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on May 11, 2016).	
10.2	Receivables Purchase Agreement, dated May 9, 2016, between The Davey Tree Expert Company, Davey Tree Surgery Company, and Davey Receivables LLC (Incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on May 11, 2016).	
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed Herewith
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed Herewith
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.	Furnished Herewith
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.	Furnished Herewith
101	The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended July 2, 2016, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets (unaudited), (ii) the Condensed Consolidated Statements of Operations (unaudited), (iii) the Condensed Consolidated Statements of Comprehensive Income (unaudited), (iv) the Condensed Consolidated Statements of Cash Flows (unaudited), and (v) Notes to Condensed Consolidated Financial Statements (unaudited).	Filed Herewith

**Certification*****Certification of Chief Executive Officer***

I, Karl J. Warnke, certify that:

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

Date: August 2, 2016

/s/ Karl J. Warnke

Karl J. Warnke

Chairman and Chief Executive Officer

## Certification

*Certification of Chief Financial Officer*

I, Joseph R. Paul, certify that:

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

Date: August 2, 2016

/s/ Joseph R. Paul

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Joseph R. Paul

Executive Vice President, Chief Financial Officer and Secretary



**Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

***Certification of Chief Executive Officer***

I, Karl J. Warnke, Chairman and Chief Executive Officer of The Davey Tree Expert Company (the "Company"), do hereby certify in accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1.) The Quarterly Report on Form 10-Q of the Company for the period ended July 2, 2016 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)), as applicable; and
- (2.) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 2, 2016

/s/ Karl J. Warnke

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Karl J. Warnke

Chairman and Chief Executive Officer

**Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

***Certification of Chief Financial Officer***

I, Joseph R. Paul, Executive Vice President, Chief Financial Officer and Secretary of The Davey Tree Expert Company (the "Company"), do hereby certify in accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1.) The Quarterly Report on Form 10-Q of the Company for the period ended July 2, 2016 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)), as applicable; and
- (2.) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 2, 2016

/s/ Joseph R. Paul

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Joseph R. Paul

Executive Vice President, Chief Financial Officer and Secretary