SERVICE CORPORATION INTERNATIONAL
Form 10-K/A
May 13, 2005

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K/A
(Amendment No. 1)

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

For the fiscal year ended December 31, 2003

Or

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

For the transition period from to

Commission file number 1-6402-1

Service Corporation International
(Exact name of registrant as specified in its charter)

Texas (State or other jurisdiction of incorporation or organization)	**74-1488375** (I.R.S. employer identification no.)
1929 Allen Parkway **Houston, Texas** (Address of principal executive offices)	**77019** (Zip code)

Registrant s telephone number, including area code: **713/522-5141**

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

Title of each class	Name of each exchange on which registered
Common Stock ($1 par value)	New York Stock Exchange
Preferred Share Purchase Rights	New York Stock Exchange
6 3/4% Convertible Subordinated Notes Due 2008	New York Stock Exchange

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

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 þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is an accelerated filer (as defined in the Securities Exchange Act of 1934 Rule 12b-2). Yes þ No o

The aggregate market value of the common stock held by non-affiliates of the registrant (assuming that the registrant s only affiliates are its officers and directors) was $1,142,008,087 based upon a closing market price of $3.87 on June 30, 2003 of a share of common stock as reported on the New York Stock Exchange Composite Transactions Tape.

The number of shares outstanding of the registrant s common stock as of February 27, 2004 was 303,571,052 (net of treasury shares).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s Proxy Statement in connection with its 2004 Annual Meeting of Shareholders (Part III)

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Explanatory Note

The Company is amending and restating in its entirety its Form 10-K for the year ended December 31, 2003, to reflect operations that have been classified as discontinued operations and to reflect certain accounting changes surrounding the Company s insurance funded preneed funeral contracts. The Company is also including additional disclosures that were not provided in its original Form 10-K.

In addition, the Company has changed its method of accounting for insurance funded preneed funeral contracts as the Company has concluded that its insurance funded preneed funeral contracts are not assets and liabilities as defined by Statement of Financial Accounting Concepts No. 6, *Elements in Financial Statements*. Therefore, the Company has removed from its consolidated balance sheet amounts relating to insurance funded preneed funeral contracts previously recorded in Preneed funeral contracts, net and Deferred preneed funeral revenues. The removal of these amounts did not have an impact on the Company s consolidated shareholders equity, results of operations or cash flows.

Discontinued Operations

In 1999, the Company began an initiative to identify and address non-strategic or underperforming businesses. As a result of this assessment, the Company committed to a plan in June 2004 to divest the existing funeral and cemetery operations in Argentina and Uruguay. The Company is actively marketing these operations and plans to have no continuing interest in these operations subsequent to the disposal of the Argentina and Uruguay businesses. As a result, the Company has classified these operations as discontinued operations for all periods presented.

SERVICE CORPORATION INTERNATIONAL

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PART I

ITEM 1. *Business.*

(Dollars in millions)

We restated our previously issued financial statements for the fiscal years ended December 31, 2002, 2001 and 2000, the interim quarters of 2002, 2001, 2000 and the first three quarters of 2003. All applicable amounts relating to these restatements have been reflected in this Form 10-K. See Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and notes two and twenty-one to the consolidated financial statements in Item 8 of this Form 10-K for details of the restatement.

General

Service Corporation International (SCI or the Company) is the world s largest provider of funeral and cemetery services. At December 31, 2003, we operated 2,225 funeral service locations, 417 cemeteries and 183 crematoria located in eight countries. We also had a minority interest equity investment in funeral and cemetery operations in the United Kingdom and Australia. In the fourth quarter of 2003, we sold our minority interest equity investment in our Australia operations. We expect to sell our minority interest investment in the United Kingdom in the second quarter of 2004, pending a successful public offering transaction. On March 11, 2004, we sold our funeral operations in France and subsequently purchased a 25% equity interest in the acquiring entity. The French operations consisted of 963 funeral service locations and 39 crematoria at December 31, 2003. For additional information regarding this transaction, see note twenty to the consolidated financial statements in Item 8 of this Form 10-K.

Our funeral service and cemetery operations consist of funeral service locations, cemeteries, crematoria and related businesses. Personnel at the funeral service locations provide all professional services relating to funerals, including the use of funeral facilities, motor vehicles, and preparation and embalming services. Funeral related merchandise (including caskets, coffins, burial vaults, cremation receptacles, flowers and other ancillary products and services) is sold at funeral service locations. Certain funeral service locations contain crematoria. We sell prearranged funeral services whereby a customer contractually agrees to the terms of a funeral to be performed in the future. Our cemeteries provide cemetery property interment rights (including mausoleum spaces, lots and lawn crypts) and sell cemetery related merchandise (including stone and bronze memorials, burial vaults, casket and cremation memorialization products) and services (primarily merchandise installation fees and burial opening and closing fees). Cemetery items are sold on an atneed or preneed basis. Personnel at cemeteries perform interment services and provide management and maintenance of cemetery grounds. Certain cemeteries operate crematoria and certain cemeteries contain gardens specifically for the purpose of cremation memorialization. There are 185 combination locations that contain a funeral service location within or adjacent to an SCI owned cemetery.

SCI was incorporated in Texas in July of 1962. Our principal corporate offices are located at 1929 Allen Parkway, Houston, Texas 77019 and our telephone number is (713) 522-5141. Our website is http://www.sci-corp.com. We make available free of charge, on or through our website, our annual, quarterly and current reports and any amendments to those reports, as soon as reasonably practicable after electronically filing such reports with the Securities and Exchange Commission. Information contained on our website is not part of this report.

Funeral and Cemetery Operations

General

The funeral and cemetery operations consist of our funeral service locations, cemeteries, crematoria and related businesses. As of December 31, 2003, our operations were organized into a North America division, which represents the United States and Canada, a European division primarily consisting of operations in France and an Other Foreign division relating to operations managed in South America and Singapore. In March 2004, we joint ventured our funeral operations in France. (For additional information regarding this transaction, see note twenty to the consolidated financial statements in Item 8 of this Form 10-K.)

During the fourth quarter of 2003, we realigned our funeral and cemetery operations in North America to better meet the needs of different market types. As a result, the funeral and cemetery operations in North America are organized into 32 major markets and 44 middle markets. Each market is led by a market director with responsibility for funeral and cemetery operations as well as preneed sales. Within each market, the operational facilities realize efficiencies by sharing common resources such as personnel, preparation services and vehicles. There are three market support centers in North America to assist market directors with financial, administrative and human resource needs. These support centers, commonly referred to as hubs , are located in Houston, New York and Los Angeles. The primary functions of the market support centers are to help facilitate the execution of corporate strategies, coordinate communication between the field and corporate offices and serve as liaisons for implementation of policies and procedures.

The death care industry in North America is characterized by a large number of locally owned, independent operations. In order to be successful, we believe our funeral service locations and cemeteries must maintain good reputations and high professional standards in the industry, as well as offer attractive products and services at competitive prices. We believe we have an unparalleled network of funeral service locations and cemeteries that offer high quality products and services at prices that are competitive with local competing funeral homes, cemeteries and retail locations.

We have multiple funeral service locations and cemeteries in a number of metropolitan areas. Within individual metropolitan areas, the funeral service locations and cemeteries operate under various names because most operations were acquired as existing businesses. Some of our international funeral service locations operate under certain brand names specific for a general area or country. We have branded our funeral operations in North America under the name Dignity Memorial®. A national brand name is unique to the death care industry in North America and we believe this gives us a strategic advantage in the industry. While this branding process is intended to emphasize our seamless national network of funeral service locations and cemeteries, the original names associated with acquired operations, and their inherent goodwill and heritage, will generally remain the same. For example, Geo. H. Lewis & Sons Funeral Directors is now Geo. H. Lewis & Sons Funeral Directors, a Dignity Memorial® provider.

In the death care industry, there has been a growing trend in the number of cremations performed in North America as an alternative to traditional funeral service dispositions. The west coast of the United States, Florida and Arizona have the highest concentration of cremation consumers in North America. Cremations usually result in lower revenue and gross profit dollars than traditional funeral services. In North America during 2003, 39.0% of all funeral services we performed were cremation cases, compared to 37.9% performed in 2002. We have expanded our cremation memorialization products and services in several North America markets, which has resulted in higher average sales for cremation cases compared to historical levels. During 2003, we continued to expand our nationally branded cremation service locations called National Cremation® Service (NCS). At December 31, 2003, NCS operated in eighteen states and Canada. NCS plans to expand its presence in existing states by adding locations where there is a business need.

Historically, we focused on the acquisition and consolidation of independent funeral homes and cemeteries in the fragmented death care industry in North America. During the 1990 s, we also expanded our operations through acquisitions in Europe, Australia, South America and the Pacific Rim. At one time, our network consisted of more than 4,500 businesses in 20 countries on 5 continents. During the mid to late 1990 s, the acquisition market became extremely competitive resulting in increased prices for acquisitions and substantially reduced returns on invested capital. In 1999, we significantly reduced the level of acquisition activity and focused on identifying and addressing non-strategic or underperforming businesses. This focus resulted in the divestiture of several North America and international operations. During 2002 and 2001, we completed joint ventures of operations in Australia, United Kingdom, Spain and Portugal; and divested of operations in the Netherlands, Norway, Italy and Belgium. In 2003, we sold our equity investment in our operations in Australia, Spain and Portugal. During the first quarter of 2004, we completed a joint venture of our funeral operations in France. We expect to sell our minority interest equity investment in the United Kingdom in the second quarter of 2004, pending a successful public offering transaction. We will pursue discussions with various third parties concerning the sale or joint venture of our remaining international operations (primarily in South America) as we intend to focus our efforts on operating a core business of high quality funeral service locations and cemeteries in North America.

Funeral Service Locations

Our 2,225 funeral service locations provide all professional services relating to funerals, including the use of funeral facilities, motor vehicles, and preparation and embalming services. Funeral service locations sell caskets, coffins, burial vaults, cremation receptacles, flowers, burial garments, and other ancillary products and services. Our funeral service locations generally experience a greater demand for services in the winter months primarily related to higher incidents of deaths from pneumonia and influenza.

In addition to selling products and services to client families at the time of need, we also sell preneed funeral services in most of our service markets. A funeral preneed arrangement is a means through which a customer contractually agrees to the terms of a funeral to be performed in the future. All or a portion of the funds collected from preneed funeral contracts are placed into trust accounts, pursuant to applicable law. Alternatively, where allowed, customers may choose to purchase a life insurance or annuity policy from third party insurance companies to fund their preneed funeral. In certain situations and pursuant to applicable laws, we will post a surety bond as financial assurance for a certain amount of the preneed funeral contract in lieu of placing certain funds in trust accounts. See the *Financial Assurances* section included in Financial Condition, Liquidity and Capital Resources in Item 7 of this Form 10-K for further details on our practice of posting such surety bonds. For additional information regarding preneed funeral activities, see the *Preneed Funeral and Cemetery Activities* section in Financial Condition, Liquidity and Capital Resources in Item 7 and notes three, four and five to the consolidated financial statements in Item 8 of this Form 10-K.

Cemeteries

Our cemeteries sell interment rights associated with cemetery property such as mausoleum spaces, lots and lawn crypts, and sell cemetery merchandise such as stone and bronze memorials, burial vaults, caskets and cremation memorialization products. Our cemeteries perform interment services and provide management and maintenance of cemetery grounds. Certain cemeteries operate crematoria and certain cemeteries contain gardens specifically for the purpose of cremation memorialization.

Cemetery sales are often made on a preneed basis pursuant to installment contracts providing for monthly payments. A portion of the proceeds from cemetery contracts is generally required by law to be paid into perpetual care trust funds. Earnings from perpetual care trust funds are used to defray the maintenance costs of cemeteries. Additionally, all or a portion of the proceeds from the sale of preneed cemetery merchandise and services may be required by various state laws to be paid into merchandise and services trusts until the merchandise is delivered or the service is provided. In certain situations and pursuant to applicable laws, we will post a surety bond as financial assurance for a certain amount of the preneed cemetery contract in lieu of placing certain funds into trust accounts. See the *Financial Assurances* section included in Financial Condition, Liquidity and Capital Resources in Item 7 of this Form 10-K for further details on the practice of posting such surety bonds. For additional information regarding cemetery preneed activities, see the *Prearranged Funeral and Cemetery Activities* section in Financial Condition, Liquidity and Capital Resources in Item 7 of this Form 10-K and notes three, four and six to the consolidated financial statements in Item 8 of this Form 10-K.

Combined Funeral Service Locations and Cemeteries

At December 31, 2003, we owned 185 funeral service/cemetery combination locations in which a funeral service location is physically located within or adjoining an SCI owned cemetery. Combination locations allow certain facility, personnel and equipment costs to be shared between the funeral service location and cemetery and typically have a higher gross margin than if the funeral and cemetery operations were operated separately. Combination locations also create synergies between funeral and cemetery sales force personnel and give consumers added convenience to purchase both funeral and cemetery products and services at a single location.

Employees

At December 31, 2003, we employed 20,471 (13,461 in North America) individuals on a full time basis and 7,342 (6,788 in North America) individuals on a part time basis. Of the full time employees, 19,949 were employed in the funeral and cemetery operations and 522 were employed in corporate or other overhead activities and services. All eligible employees in the United States who so elect are covered by SCI s group health and life insurance plans. Eligible employees in the United States are participants in retirement plans of SCI or various subsidiaries, while international employees are covered by other SCI (or SCI subsidiary) defined or government mandated benefit plans. Approximately 3% of our employees in North America are represented by unions. Although labor disputes are experienced from time to time, relations with employees are generally considered favorable.

Regulation

Our operations are subject to regulations, supervision and licensing under numerous foreign, federal, state and local laws, ordinances and regulations, including extensive regulations concerning trust funds, preneed sales of funeral and cemetery products and services and various other aspects of our business. We comply in all material respects with the provisions of such laws, ordinances and regulations. Since 1984, we have operated in the United States under the Federal Trade Commission (FTC) comprehensive trade regulation rule for the funeral industry. The rule contains requirements for funeral industry practices, including extensive price and other affirmative disclosures and imposes mandatory itemization of funeral goods and services. From time to time in connection with our former strategy of growth through acquisitions, we entered into consent orders with the FTC that required us to dispose of certain operations in order to proceed with such acquisitions, or limited our ability to make acquisitions in specified areas. The trade regulation rule and the various consent orders have not had a material adverse effect on our operations.

As previously mentioned, we sold our funeral operations in France in March 2004. The French funeral services industry has undergone significant regulatory change in recent years. Historically, the French funeral services industry had been controlled, as provided by national legislation, either (i) directly by municipalities through municipality-operated funeral establishments (Municipal

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Monopoly), or (ii) indirectly by the remaining municipalities that have contracted for funeral service activities with third party providers, such as our French funeral operations (Exclusive Municipal Authority). Legislation was passed that has generally ended municipal control of the French funeral service business and has allowed free competition among funeral service providers. Under such legislation, the Exclusive Municipal Authority was abolished in January 1996, and the Municipal Monopoly was eliminated in January 1998. Cemeteries in France are currently controlled by municipalities and religious organizations. We previously sold cemetery merchandise such as markers and monuments to consumers for use in these cemeteries.

ITEM 2. *Properties.*

Our corporate headquarters are located at 1929 Allen Parkway, Houston, Texas 77019. A wholly-owned subsidiary of SCI owns an undivided one-half interest in the building and parking garage. The other undivided one-half interest is owned by an unrelated third party. We plan to acquire the other one-half interest in the building at the end of the lease in July 2005 for $2 million. The property consists of approximately 127,000 square feet of office space and 185,000 square feet of parking space. We lease all of the office space in the building for $59 thousand per month and pay all operating expenses. One half of the rent is paid to the wholly-owned subsidiary and the other half is paid to the owners of the remaining undivided one-half interest. We own and utilize two additional buildings located in Houston, Texas for corporate activities containing a total of approximately 207,000 square feet of office space.

At December 31, 2003, we owned approximately 68% of the real estate and buildings used by our 2,225 funeral service locations, cemeteries and 183 crematoria, and 32% of such facilities are leased. In addition, we leased two aircraft pursuant to cancelable operating leases. At December 31, 2003, we operated 10,032 vehicles, of which 29% were owned and 71% were leased. For additional information regarding leases, see the *Contractual, Commercial and Contingent Commitments* section in Financial Condition, Liquidity and Capital Resources in Item 7 and note twelve to the consolidated financial statements in Item 8 of this Form 10-K.

At December 31, 2003, our 417 cemeteries contained a total of approximately 28,254 acres, of which approximately 57% was developed.

The specialized nature of our businesses requires that our facilities be well-maintained and kept in good condition and we believe that these standards are being met.

ITEM 3. *Legal Proceedings.*

Information regarding legal proceedings is set forth in note twelve to the consolidated financial statements in Item 8 of this Form 10-K.

ITEM 4. *Submission of Matters to a Vote of Security Holders.*

None.

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EXECUTIVE OFFICERS OF THE COMPANY

Pursuant to General Instruction G to Form 10-K, the information regarding executive officers of the Company called for by Item 401 of Regulation S-K is hereby included in Part I of this report.

The following table sets forth as of March 15, 2004 the name and age of each executive officer of the Company, the office held, and the date first elected an officer.

Officer Name	Age	Position	Year First Became Officer(1)
R. L. Waltrip	73	Chairman of the Board and Chief Executive Officer	1962
B. D. Hunter	74	Vice Chairman of the Board	1986
Thomas L. Ryan	38	President and Chief Operating Officer	1999
Michael R. Webb	45	Executive Vice President	1998
Jeffrey E. Curtiss	55	Senior Vice President Chief Financial Officer and Treasurer	2000
Stephen M. Mack	52	Senior Vice President Middle Market Operations	1998
James M. Shelger	54	Senior Vice President General Counsel and Secretary	1987
J. Daniel Garrison	52	Vice President Operations Services	1998
W. Cardon Gerner	49	Vice President Accounting	1999
Eric D. Tanzberger	35	Vice President and Corporate Controller	2000
Stephen J. Uthoff	52	Vice President Chief Information Officer	2000
Sumner J. Waring, III	35	Vice President Major Market Operations	2002

(1) Indicates the year a person was first elected as an officer although there were subsequent periods when certain persons ceased being officers of the Company.

Unless otherwise indicated below, the persons listed above have been executive officers or employees for more than five years.

Mr. Waltrip is the founder, Chairman and Chief Executive Officer of the Company and a licensed funeral director. He grew up in his family s funeral business and assumed management of the firm in the 1950s after earning a Bachelor s degree in Business Administration from the University of Houston. He began buying additional funeral homes in the 1960s, achieving cost efficiencies by pooling their resources. At the end of 2003, the network he began had grown to include more than 2,800 funeral service locations, cemeteries and crematoria in eight countries. Mr. Waltrip took the Company public in 1969. He has provided leadership to the Company for over 40 years.

Mr. Hunter was appointed Vice Chairman of the Board in January 2000. For more than five years, prior to February 2002, Mr. Hunter had been the Chairman of Huntco, Inc., an intermediate steel processor, and was also its Chief Executive Officer prior to May 2000. In February 2002, Huntco, Inc., filed a petition for bankruptcy under Chapter 11 of the United States Bankruptcy Code during a severe downturn in the steel industry. Mr. Hunter has been a director since 1986 and also served as Vice Chairman of the Board from September 1986 to May 1989. He is a graduate of Truman State University, formerly known as Northeast Missouri State University, in Kirksville, Missouri.

Mr. Ryan joined the Company in June 1996 and served in a variety of financial management roles within the Company. In February 1999, Mr. Ryan was promoted to Vice President International Finance. In November 2000, he was promoted to Chief Executive Officer of European Operations based in Paris, France. In July 2002, Mr. Ryan was appointed President and Chief Operating Officer. Prior to joining the Company, Mr. Ryan was a certified public accountant with Coopers & Lybrand L.L.P. for more than five years. Mr. Ryan holds a Bachelor of Business Administration degree from the University of Texas-Austin.

Mr. Webb joined the Company in 1991 when it acquired Arlington Corporation, a regional funeral and cemetery consolidator, where he was then Chief Financial Officer. Prior to joining Arlington Corporation, Mr. Webb held various executive financial and development roles at Days Inns of America and Telemundo Group, Inc. In 1993, Mr. Webb joined the Company s corporate development group, which he later led on a global basis before accepting operational responsibility for the Company s Australian and Hispanic businesses. Most recently, Mr. Webb has led the efforts to reduce overhead costs and improve business and financial processes. Mr. Webb was named Executive Vice President in July 2002. He is a graduate of the University of Georgia, where he earned a Bachelor of Business Administration degree.

Mr. Curtiss joined the Company as Senior Vice President and Chief Financial Officer in January 2000. In August 2002, Mr. Curtiss responsibilities changed to include the responsibilities of Treasurer of the Company. From January 1992 until July 1999, Mr. Curtiss served as Senior Vice President and Chief Financial Officer of Browning-Ferris Industries, a waste services company. Mr. Curtiss attended the University of Nebraska, Lincoln, where he earned Bachelor of Science in Business Administration and Doctor of Jurisprudence degrees. He also holds a Master of Legal Letters degree in taxation from Washington University in St. Louis, Missouri.

Mr. Mack joined the Company in 1973 as a resident director after graduating from Farmingdale State University of New York. He became Vice President of the Eastern Region in 1987 and Regional President in 1992. Mr. Mack was appointed Corporate Vice President in 1998 and then promoted to Senior Vice President in 2002. Mr. Mack was promoted to Senior Vice President Eastern Operations in August 2002 and assumed the office of Senior Vice President Middle Market Operations in November 2003.

Mr. Shelger joined the Company in 1981 when it acquired IFS Industries, a regional funeral and cemetery consolidator, where he was then General Counsel. Mr. Shelger subsequently served as counsel for the Cemetery Division until 1991, when he was appointed General Counsel. Mr. Shelger earned a Bachelor of Science degree in business administration from the University of Southern California in Los Angeles and a Juris Doctor from the California Western School of Law in San Diego.

Mr. Garrison joined the Company in 1978 and worked in a series of management positions until he was promoted to President of the Southeastern Region in 1992. In 1998, Mr. Garrison was promoted to Corporate Vice President in charge of operations outside North America. In 2000, Mr. Garrison was promoted to Vice President North American Cemetery Operations. He served in this position until assuming his current position as Vice President Operations Services in August 2002. Mr. Garrison is an Administrative Management graduate of Clemson University.

Mr. Gerner joined the Company in January 1999 in connection with the acquisition of Equity Corporation International (ECI) and in March 1999 was promoted to Vice President Corporate Controller. In August 2002, Mr. Gerner s responsibilities and position changed to Vice President Accounting. Before the acquisition, Mr. Gerner had been Senior Vice President and Chief Financial Officer of ECI since March 1995. Prior thereto, Mr. Gerner was a partner with Ernst & Young LLP. Mr. Gerner graduated with honors from the University of Texas-Austin, with a Bachelor of Business Administration in Accounting.

Mr. Tanzberger joined the Company in August 1996 as Manager of Budgets & Financial Analysis. Since then, Mr. Tanzberger has served as Vice President of Operations/Western Division, Director of Investor Relations and Assistant Corporate Controller. Mr. Tanzberger was promoted to Vice President Investor Relations and Assistant Corporate Controller in January 2000, and to Corporate Controller in August 2002. Prior to joining the Company, Mr. Tanzberger was Assistant Corporate Controller at Kirby Marine Transportation Corporation, an inland waterway barge and tanker company, from January through August 1996. Prior thereto, he was a certified public accountant with Coopers & Lybrand L.L.P. for more than five years. Mr. Tanzberger is a graduate of the University of Notre Dame, where he earned a Bachelor of Business Administration degree.

Mr. Uthoff joined the Company as Vice President Chief Information Officer in January 2000. From June 1994 through July 1999, Mr. Uthoff served as Vice President Planning & Analysis of Browning-Ferris Industries, a waste services company. Mr. Uthoff attended Oklahoma State University, where he earned a Bachelor of Science degree in Engineering and a Master of Science degree in Accounting.

Mr. Waring, a licensed funeral director, joined the Company as an Area Vice President in 1996 when the Company merged with his family s funeral business. Mr. Waring was appointed Regional President of the Northeast Region in 1999 and was promoted to Regional President of the Pacific Region in September 2001. Mr. Waring was promoted to

Vice President Western Operations in August 2002 and assumed the office of Vice President Major Market Operations in November 2003. Mr. Waring holds a Bachelor s degree in Business Administration from Stetson University in Deland, Florida, a degree in Mortuary Science from Mt. Ida College and a Masters of Business Administration degree from the University of Massachusetts Dartmouth.

Each officer of the Company is elected by the Board of Directors and holds his office until his successor is elected and qualified or until his earlier death, resignation or removal in the manner prescribed in the Bylaws of the Company. Each officer of a subsidiary of the Company is elected by the subsidiary s board of directors and holds his office until his successor is elected and qualified or until his earlier death, resignation or removal in the manner prescribed in the bylaws of the subsidiary.

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PART II

ITEM 5. ***Market for the Company s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.***

The Company s common stock has been traded on the New York Stock Exchange since May 14, 1974. On December 31, 2003, there were 6,609 holders of record of the Company s common stock.

In October 1999, the Company suspended payment of regular quarterly cash dividends on its outstanding common stock in order to focus on improving cash flow and reducing existing debt. Under the Company s bank credit agreement, the Company is restricted from paying dividends and making other distributions.

The table below shows the Company s quarterly high and low common stock prices for the two years ended December 31, 2003:

	2003		2002	
	High	**Low**	**High**	**Low**
First quarter.	$ 3.82	$ 2.78	$ 5.50	$ 4.55
Second quarter	4.24	2.67	5.15	3.60
Third quarter.	4.95	3.75	4.64	2.25
Fourth quarter	5.58	4.45	3.71	2.42

SRV is the New York Stock Exchange ticker symbol for the common stock of the Company. Options in the Company s common stock are traded on the Philadelphia Stock Exchange under the symbol SRV.

For equity compensation plan information, see Part III of this report on page 99.

ITEM 6. ***Selected Financial Data.***

The following selected consolidated financial data for the years ended December 31, 1999 through December 31, 2003 is derived from our audited consolidated financial statements as restated. The operating data includes reclassifications to conform to current period presentations with no impact on net income. In the second quarter of 2004, we committed to a plan to divest our existing funeral and cemetery operations in Argentina and Uruguay. Therefore, these operations are classified as discontinued for all periods presented. In the first quarter of 2004, we changed our method of accounting for insurance funded preneed contracts as we have concluded that our insurance funded preneed funeral contracts are not assets and liabilities as defined by Statement of Financial Accounting Concepts No. 6, *Elements in Financial Statements* . Therefore, we have removed from our balance sheet amounts relating to insurance funded preneed funeral contracts for periods presented. The data set forth should be read in conjunction with our consolidated financial statements and accompanying notes to the consolidated financial statements included in this Form 10-K. The historical information is not necessarily indicative of the results to be expected in the future.

The financial statements for the fiscal years ended December 31, 2002, 2001 and 2000, the interim quarters of 2002, 2001, 2000 and the first three quarters of 2003 have been restated. All applicable amounts relating to these restatements have been reflected in the following selected financial data.

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SELECTED CONSOLIDATED FINANCIAL DATA

(Dollars in millions except per share amounts)	Year ended December 31,				
	2003	2002 (Restated)	2001 (Restated)	2000 (Restated)	1999
Selected Consolidated Statement of Operations Data:					
Revenue	$ 2,328.4	$ 2,312.4	$ 2,489.0	$ 2,569.5	$ 2,979.0
Income (loss) from continuing operations before cumulative effects of accounting changes	$ 82.6	$ (82.2)	$ (464.0)	$ (388.4)	$ (55.8)
Net income (loss)	$ 85.1	$ (232.5)	$ (623.4)	$ (1,294.1)	$ (32.4)
Earnings per share:					
Income (loss) from continuing operations before cumulative effects of accounting changes					
Basic	$ 0.28	$ (0.28)	$ (1.63)	$ (1.43)	$ (0.21)
Diluted	$ 0.28	$ (0.28)	$ (1.63)	$ (1.43)	$ (0.21)
Net income (loss)					
Basic	$ 0.28	$ (0.79)	$ (2.19)	$ (4.75)	$ (0.12)
Diluted	$ 0.28	$ (0.79)	$ (2.19)	$ (4.75)	$ (0.12)
Dividends per share					$ 0.27
Selected Consolidated Balance Sheet Data:					
Total assets	$ 7,725.2	$ 7,798.2	$ 9,025.0	$ 10,525.0	$ 10,779.7
Long-term debt, less current maturities	$ 1,519.2	$ 1,874.1	$ 2,301.4	$ 3,078.7	$ 3,622.2
Stockholders equity	$ 1,527.0	$ 1,326.7	$ 1,456.4	$ 2,025.0	$ 3,495.3

ITEM 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations.***
(Dollars in millions, except average sales prices and per share data)

Restatement of Historical Financial Statements

We restated our previously issued financial statements for the fiscal years ended December 31, 2002, 2001 and 2000, the interim quarters of 2002, 2001 and 2000, and the first three quarters of 2003, primarily related to adjustments to Deferred preneed cemetery contract revenues. All applicable amounts relating to these restatements have been reflected in the consolidated financial statements and notes to the consolidated financial statements.

Prior to the implementation of Staff Accounting Bulletin No. 101, *Revenue Recognition in Financial Statements* (SAB 101), the Company recorded revenues for cemetery merchandise or services at the time the contract was signed by the customer. The estimated costs to deliver merchandise and perform services were charged to expense at the time the contract was signed and a corresponding liability was recorded on the Company s consolidated balance sheet. This liability was periodically adjusted to reflect changes in the estimated costs of merchandise and services. When the Company delivered merchandise or performed services under a customer s cemetery contract, our policy required cemetery personnel to record such delivery or performance into the accounting system. This entry reduced the corresponding liability as the obligation was satisfied.

Effective January 1, 2000, we adopted SAB 101. We determined that the accounting policy for recognition of preneed cemetery merchandise or service revenue should be changed from the time of sale to the time of delivery or performance. Undelivered merchandise and services would be recorded as deferred revenue at the contract sale price and revenue from such merchandise and services would be recognized when delivered or performed.

In the latter part of 2001, we identified preneed cemetery merchandise and services that had been previously delivered, but the delivery had not been input into our accounting system in a timely manner. When identified, these items were recognized as revenues and disclosed as changes in estimates in the period identified. Deliveries made in a period other than when they were ultimately recognized as a change in estimate are referred to as out-of-period deliveries .

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During 2000 through September 2003, we identified approximately $109.4 million of preneed cemetery contract items that were out-of-period deliveries, which means that these items had been delivered or performed, but the revenue had not been recognized in the appropriate period of delivery. These items were originally recognized as revenues and disclosed as changes in estimates in the periods from 2000 through 2003. Offsetting the $109.4 million, we recorded $43.6 million of cemetery revenue from 2000 through September 2003, which represents the effects of subsequent years being restated into the appropriate earlier period as detailed in the table below.

(Dollars in millions)	2000	2001	2002	First Three Quarters of 2003	Total
Reductions in cemetery revenues for out-of-period deliveries	$ (12.8)	$ (68.5)	$ (23.4)	$ (4.7)	$ (109.4)
Effects of subsequent years being restated into the appropriate period	$ 27.7	$ 11.0	$ 4.9	$	$ 43.6
Net restatement of cemetery revenues for out-of-period deliveries	$ 14.9	$ (57.5)	$ (18.5)	$ (4.7)	$ (65.8)

Additionally, during the fourth quarter of 2003, we recorded adjustments to prior periods totaling $40.7 million to report additional cemetery merchandise and service revenue in the period that such items were delivered or performed. The difference between the $40.7 million and the $109.4 million described above is that the cemetery contract items within the $109.4 million were previously identified by the Company and were recognized as revenue and disclosed as a change in estimate in the period identified. The cemetery contract items within the $40.7 million were not previously identified or recognized as revenue by the Company prior to the fourth quarter of 2003. The distribution of the $40.7 million was restated as follows:

(Dollars in millions)	2000	2001	2002	2003	Total
Increased revenues for items for which delivery or performance occurred, but no revenue was recognized	$ 4.9	$ 8.3	$ 8.7	$ 8.7	$ 30.6
Cumulative effect (pretax)	$ 10.1	$	$	$	$ 10.1
Total revenues for items for which delivery or performance occurred, but no revenue was recognized.	$ 15.0	$ 8.3	$ 8.7	$ 8.7	$ 40.7

We also reviewed our accounting policy for amortizing preneed funeral deferred selling costs and have changed the methodology for amortizing these costs from a straight line basis to a method more in proportion to when the associated revenues are recognized. We included this change in amortization in our restated results.

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The effect of the restatement of our previously reported consolidated statement of operations and consolidated balance sheet for the periods described above is as follows:

	Year ended December 31, 2002		Year ended December 31, 2001		Year ended December 31 2000	
	As reported	As Restated	As Reported	As Restated	As Reported	As Restated
Selected consolidated statement of operations data:						
Revenues	$ 2,322.2	$ 2,312.4	$ 2,538.1	$ 2,489.0	$ 2,549.8	$ 2,569.5
Costs and expenses	$ (1,959.3)	$ (1,950.4)	$ (2,173.5)	$ (2,166.2)	$ (2,216.4)	$ (2,226.5)
Gross profits	$ 362.9	$ 362.0	$ 364.6	$ 322.8	$ 333.4	$ 343.0
Operating income (loss)	$ 16.8	$ 15.8	$ (189.0)	$ (230.9)	$ (247.2)	$ (237.5)
Loss from continuing operations before income taxes and cumulative effects of accounting changes	$ (118.9)	$ (119.9)	$ (376.7)	$ (418.6)	$ (475.6)	$ (465.9)
Benefit (provision) for income taxes	$ 37.3	$ 37.7	$ (61.6)	$ (45.3)	$ 81.3	$ 77.6
Cumulative effects of accounting changes (net of income taxes)	$ (135.6)	$ (135.6)	$ (7.6)	$ (7.6)	$ (913.6)	$ (870.4)
Net loss	$ (231.9)	$ (232.5)	$ (597.8)	$ (623.4)	$ (1,343.3)	$ (1,294.1)
Basic and diluted earnings per share:						
Loss from continuing operations before cumulative effects of accounting changes	$ (.28)	$ (.28)	$ (1.54)	$ (1.63)	$ (1.45)	$ (1.43)
Net loss	$ (.79)	$ (.79)	$ (2.10)	$ (2.19)	$ (4.93)	$ (4.75)

(Dollars in thousands, except per share data)

	As of December 31, 2002	
	As Reported	As Restated
Selected consolidated balance sheet data:		
Inventories	$ 135,263	$ 136,666
Total current assets	$ 612,874	$ 614,277
Deferred charges and other assets	$ 719,180	$ 712,030
Total assets	$ 8,253,993	$ 7,798,246
Deferred cemetery contract revenues, net	$ 1,672,661	$ 1,629,540
Deferred income taxes	$ 420,658	$ 435,148
Accumulated deficit	$ (1,046,029)	$ (1,023,145)
Total stockholders equity	$ 1,303,771	$ 1,326,655
Total liabilities and stockholders equity	$ 8,253,993	$ 7,798,246

See note twenty-one to the consolidated financial statements for the effect of the restatement upon quarterly unaudited financial data.

We have changed our method of accounting for insurance funded preneed contracts as we have concluded that our insurance funded preneed funeral contracts are not assets and liabilities as defined by Statement of Financial Accounting Concepts No. 6, *Elements in Financial Statements.* Therefore, we have removed from our consolidated balance sheet amounts relating to insurance funded preneed funeral contracts previously recorded in *Preneed funeral receivables and trust investments and Deferred preneed funeral revenues,* which at December 31, 2003 and 2002, were $3,505,094 and $2,948,100, respectively. The removal of these amounts did not have an impact on our consolidated stockholders equity, results of operations or cash flows.

Overview

Service Corporation International (SCI), headquartered in Houston, Texas, is the world s largest funeral and cemetery company. At December 31, 2003, we operated 2,225 funeral service locations, 417 cemeteries, and 183 crematoria in eight countries. North America operations represented 56% of funeral service locations, 97% of cemeteries and 77% of crematoria owned at December 31, 2003, and approximately 73% of consolidated revenues and 79% of consolidated gross profits.

North America Operations

To meet the needs of different markets, the funeral and cemetery operations in North America are organized into 32 major markets and 44 middle markets. Each market is led by a market director with responsibility for both funeral and cemetery operations as well as preneed sales in their particular market. Within each market, the businesses realize efficiencies by sharing common resources such as personnel, preparation services, and vehicles. To assist market directors with financial and administrative needs as well as human resource issues, there are three market support centers in North America. These support centers, commonly referred to as hubs are located in Houston, New York and Los Angeles. The market support centers help to facilitate the execution of corporate strategies, coordinate the communication between corporate office and the field, and act as liaisons for implementation of policies and procedures.

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International Operations

On March 11, 2004, we sold our funeral operations in France and then purchased a 25% equity interest in the acquiring company. We also have a minority interest equity investment in the United Kingdom. Remaining international operations outside of North America consist of funeral businesses in Singapore and primarily cemetery businesses in Argentina, Chile and Uruguay. It is our intention to exit these remaining international businesses when market values and economic conditions are conducive to a sale or joint venture. At this time, we believe our focus is best spent in North America where significant opportunities for growth exist. Subsequent to December 31, 2003, management committed to a plan to sell its Argentina and Uruguay operations. For additional information, see note nineteen to the consolidated financial statements included in this Form 10-K.

Strengths and Challenges

SCI is the dominant industry leader in North America. While there are three other publicly-traded companies that operate in our industry, we have more physical locations and serve more consumers than the rest of the public peer group combined. With that said, the industry remains highly fragmented with these three public companies and SCI combined representing approximately 20% of the total industry, and the other 80% of the industry is represented by independent funeral and cemetery operators. In 2000, we launched the first national branding strategy in the funeral service industry in North America under the name Dignity Memorial®. While this branding process is intended to emphasize our seamless national network of funeral service locations and cemeteries, the original names associated with acquired locations generally remain the same. For example, Geo. H. Lewis & Sons Funeral Directors is now Geo. H. Lewis & Sons Funeral Directors, a Dignity Memorial® provider. We believe SCI is the only company in our industry to successfully implement a national brand. We believe that a national brand gives us a competitive advantage and is discussed further in our strategies for growth described below.

Our core business can be characterized as stable, reflective of favorable demographics and relatively predictable revenue and cash flow streams that are further enhanced by more than $3,100 million of deferred revenues associated with North America preneed funeral and cemetery sales. This backlog of future revenues is primarily supported by investments in trust funds or third party insurance policies.

We and others in the industry face certain challenges in growing revenues. The primary external factors impacting revenue growth are a lack of near-term growth in the number of deaths and an increasing trend toward cremation. Although the United States Census Bureau projects that the numbers of deaths will grow between 0.7% and 0.8% annually through 2010, modern advances in medicine and healthier lifestyles could reduce the numbers of deaths during this time. Our comparable (same store) funeral services performed declined 1.6% in 2003 which we believe is consistent with, or in certain instances less than, the declines experienced by other companies in the funeral service and casket manufacturing industries as well as mortality data reported by the Centers for Disease Control and Prevention (CDC). Preliminary mortality statistics reported by the CDC reflect a decline in the number of deaths in the United States of more than 2.0% in 2003 versus 2002.

In North America, social trends, religious changes, environmental issues and cultural preferences are driving an increasing preference for cremation. SCI is the largest provider of cremation services in North America where approximately 39% of the total funeral services we perform are cremation services as compared to the national average of approximately 30%. Our cremation mix is greater due to the high concentration of properties we own along the west coast of the United States, Florida, and Arizona where cremation rates exceed 45%. The rate of cremation in North America has been increasing approximately 100 to 150 basis points each year and we expect this trend to continue in the near term. A cremation service historically has generated less revenues and gross profit dollars than a traditional funeral service. Additionally, the cremation consumer may choose not to purchase cemetery property or merchandise. We believe we are well positioned to address this growing trend and have experienced initial success through the use of contemporary marketing strategies and unique product and service offerings that specifically appeal to cremation consumers. See further information regarding initiatives to address cremation as part of our overall revenue growth strategy described below.

The Path to Growth

With the significant progress made in reducing debt and increasing cash flow since 1999, we believe our current capital structure affords us improved financial flexibility. Our primary focus has shifted to initiatives that will grow revenues and earnings. In the near term, we believe that cost reduction efforts will be the main means to improve earnings. We believe strategies centered on our national brand, Dignity Memorial®, and other revenue growth initiatives will provide the framework that will drive sustainable growth over the longer term.

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Improving the Infrastructure

We have historically had an infrastructure that did not fully realize the inherent efficiencies in our large organization. As a result, we did not fully capitalize on the benefits of standardization, technology, process improvement and outsourcing programs. Some of the key actions taken to improve the infrastructure while reducing costs include redesigning our sales organization, improving business and financial processes, implementing new information systems, and changing the management structure.

In late 2002 and early 2003, we made significant changes to the structure and processes of the sales organization. These changes included eliminating certain lead generation programs, incentive travel programs and other inefficient sales activities and shifting to a sales model based on personal referrals and standardized professional certification, redesigning sales management compensation programs to profit-based measures from revenue-based measures and reducing sales management positions. We are also in the final stages of shifting to a compensation model for sales counselors that is variable and directly related to the production of new business. Historically, sales counselors compensation was based solely on commissions. These changes made to the sales organization were a significant driver of improved cemetery margins in 2003.

In 2003, we began to focus on improving business and financial processes and systems that support our North American funeral and cemetery operations. The information systems used by us in the field were proprietary systems developed by us internally. There were three separate systems (funeral, cemetery and trust administration) and the systems operated independent of each other. These systems were costly to maintain. In 2003, we began to implement a new information system in the field that would replace the three separate contract entry systems and integrate these functions into one system. In addition, process improvement reviews resulted in our decision to outsource certain accounting functions, including accounts payable and payroll, and to change outsourcers for trust administration.

Having simplified our sales approach and redesigned our financial, technical and administrative infrastructure, we were able to make significant changes to the field management structure in late 2003. The old management structure consisted of multiple layers and two organizations (sales and operations). The new management structure is based on a major market and middle market concept with the understanding that our markets and businesses are not all the same and can benefit from different management approaches. We eliminated the dual management organizations and now have one person responsible for each market who has the ability to lead in a multi-segment environment, who is focused on growing our business and who is committed to the Dignity Memorial® standards and brand. This single line management structure is expected to increase accountability and execution, improve communication and reduce overhead costs. To assist market directors with financial and administrative needs as well as human resource issues, there are three market support centers, commonly referred to as hubs . The market support centers help facilitate the execution of corporate strategies, coordinate the communication between the corporate office and our operating locations, and act as liaisons for implementation of policies and procedures, including monitoring and enhancing our internal control policies and procedures.

Building the Brand

SCI has implemented the first national brand in the funeral service industry called Dignity Memorial®. Internally, we are focused on ensuring that we have consistency in service standards and processes across our network of businesses. We want every customer interaction to be the standard Dignity interaction, which is based upon values of integrity, respect, enduring relationships and service excellence. All of our employees who interact with consumers must complete a Dignity certification process. Additionally, we are developing a comprehensive training program under the name Dignity University that incorporates required specific curriculum for each job type within SCI using a combination of traditional classroom, web-based courses, virtual classroom and on-the-job training for the more than 20,000 individuals that we employ in North America.

Externally, we continue to enhance signage and local advertising efforts using the Dignity® name and logo. Through our national brand we are the sponsor of several nationally recognized community programs including Dignity Memorial Escape School® (www.escapeschool.com), which provides parents and their children with critical abduction prevention and escape techniques, Dignity Memorial Smart and Safe Seniors® (www.smartandsafe.com), which educates seniors about consumer fraud, cons and scams, home break-ins, travel safety and other topics, and The Vietnam Wall Experience (www.vietnamwallexperience.com), which is a traveling, three-quarter-scale replica of the Vietnam Veterans Memorial in Washington, D.C. We are also currently testing new television, radio and print advertising, which if successful, will be launched on a national basis. This new media advertising focuses on the unique products and services exclusive to Dignity Memorial® providers.

It is our belief that today s funeral consumers preferences are changing. The focus in this industry historically has been on selling caskets, flowers and interment rights. Based on our market studies, we believe customers are less interested in buying products and more interested in creating a meaningful experience and receiving professional help to deal with the aspects of what occurs when a loved one dies. Through our Dignity® brand we are developing more contemporary and comprehensive products and services that we believe will help the consumer through the entire experience. Some of the exclusive items offered through Dignity providers include grief counseling services through a 24-hour Compassion Helpline, legal services membership, internet memorial archive capabilities through Making Everlasting Memories (www.mem.com) and the Aftercare® Planner a comprehensive organizing system that helps families manage the many business details that arise after a death occurs. Dignity benefits also include the Bereavement Travel Program, a unique feature through which customers can obtain special rates on airfare, car rentals and hotel accommodations for family and friends who must travel from out of town to attend memorial services. Depending on the number of visitors and the cities from which their travel originates, the cumulative savings in connection with one funeral can be in the hundreds even thousands of dollars. Importantly, these products and services appeal to both burial and cremation consumers. We are also focusing on programs that offer consumers new ways to personalize funeral services and create meaning in the experience.

Growing Our Revenues

As described earlier, we believe improvements in our cost structure will drive near term earnings growth; however, we realize to achieve sustainable long-term growth that we must grow our revenues. We believe we can be successful in this regard by developing the Dignity brand, listening to our consumers and developing an approach that takes our Company to new levels.

Enhancing Sales Opportunities

We believe we can grow core revenues by utilizing technology and contemporary marketing strategies to enhance our sales opportunities and strengthen the competitive advantage of our national brand, Dignity Memorial®. In this regard, particular focus is being placed on selling Dignity Memorial® packaged funeral and cremation plans, developing product differentiation within our cemeteries, and enhancing our cremation strategies.

Our national brand name, Dignity Memorial®, also represents a unique set of packaged funeral and cremation plans offered exclusively through our network on an atneed and preneed basis. These packages are designed to simplify customer decision-making and include the unique value-added products and services described earlier which have traditionally been unavailable through funeral service locations. Our customer satisfaction index, as measured by independent surveys completed by consumers three weeks following a funeral, continues to reach record levels which we believe is largely attributable to the value and savings consumers receive when they select a Dignity package. When Dignity packages are sold, it results in significant incremental revenue and gross profit margin per funeral service compared to non-Dignity sales due to the comprehensive product and service offerings they provide. On a burial funeral, Dignity packaged sales generate on average approximately $2,800 more than non-Dignity sales. On a cremation service, Dignity packaged sales generate approximately $1,700 more than non-Dignity sales. In 2003, approximately 16% of the total funeral consumers we served selected a Dignity package. On a preneed basis, approximately 20% of funeral prearrangement contracts sold were Dignity plans. A key initiative to help drive increases in the selection rate of Dignity packaged plans is through improved merchandising techniques. In a limited number of test locations, modifications are being made to casket selection rooms that will place less emphasis on traditional funeral merchandise and more focus on the comprehensive product and service offerings unique to Dignity Memorial providers. These new displays and other presentation models also offer a special emphasis on personalization options. We will continue to enhance and make modifications to these new displays in the test locations in early 2004. As we finalize a model of what works best, these new modifications will be launched nationally in late 2004 and 2005.

We are also beginning to use more contemporary marketing strategies within our cemetery segment. Initiatives are underway to employ a tiered-product strategy that emphasizes a wide range of product offerings versus only grave spaces. Special emphasis is being placed on the development of high-end cemetery property projects such as private family estates. As of December 31, 2003, this tiered-product strategy had been implemented in less than 15% of the more than 400 cemeteries that we own and we believe this initiative will be a key driver of cemetery revenue growth in 2004 and 2005.

To grow core revenues and profits, we believe we must address the growing trend toward cremation. We believe a successful cremation strategy is built on product differentiation, personalization and simplicity. The sale of Dignity Memorial® cremation plans can have a meaningful impact in the near term as these sales on average result in more than $1,700 of incremental revenue per service to us compared to non-Dignity cremation sales. We are also developing new displays to be used in the arrangement process that clearly explain the products and services available to cremation consumers. Within the cemetery segment, we are promoting cremation gardens, which are separate sections located within certain of our cemeteries where cremated remains can be permanently placed and that contain other unique memorialization products. We continue to develop and expand our national brand, National Cremation®, which targets the direct cremation consumer. And finally, comprehensive training programs are being developed to support and drive these key initiatives, as well as to focus on creating a personal and meaningful experience for the cremation consumer.

Increasing Market Share

We believe that SCI has unique opportunities to grow market share due to its size and geographic diversity. We believe that a national brand will provide us access to new customers over the long term due to an increasingly mobile society in North America. We think consumers today are less likely to know a funeral director personally or live in the same area as past generations who may have used funeral home services before. A favorable experience with Dignity Memorial® through one of our community outreach programs, attending a funeral service at a Dignity location, or through previous use of a Dignity provider may influence a consumer to choose one of our funeral homes. Our centralized marketing effort will utilize information from our broad customer databases to determine geographic, demographic and lifestyle information about our consumers in order to promote awareness of the Dignity Memorial® brand name, our local names, and our provider network in the most efficient and effective manner. In addition, we will continue to capitalize on our nationwide network of providers to develop affinity relationships with large groups of individuals to whom we could market our products and services including employers, social organizations and insurance companies. Our most strategic affinity partnership today is with the Veterans of Foreign Wars and Ladies Auxiliary whose membership exceeds two million. Over the longer term, we believe these types of groups can be key influencers in the funeral home selection process.

In addition to reducing costs, our new management structure is intended to have our strongest business leaders driving results in each of our markets. Under the new structure, many of the administrative and financial functions are now handled by support centers and the geographical scope of responsibility and accountability for business leaders has been narrowed. We believe this allows our market leaders to have a greater focus on developing people, growing market share and improving profitability in their respective markets. In addition, we continue to use market action plans as a measurement tool to drive accountability and improved results. Market leaders identify the strengths, weaknesses, opportunities and threats of their local area and develop supporting action plans in response that include measurable objectives, necessary resources and a timetable for completion.

We are also targeting expansion through acquisition or construction in the top 150 markets in North America where probable investment returns will exceed our cost of capital. We will focus future growth capital deployment in the major metropolitan markets where there are large population bases and where multiple businesses are more conducive to clustering and contemporary marketing strategies and it is easier to attract quality management. Over the longer term, the potential for a franchise opportunity exists for further expansion in the smaller markets. In a franchise relationship we could recruit independent funeral providers to join the Dignity Memorial® network and earn fees for a comprehensive range of services that we could provide to the franchisee all at very little or no capital cost to us.

Outlook for Fiscal 2004

Our outlook for 2004 demonstrates continued strength in cash flows and further improvements to the capital structure. We expect growth in operating margins in 2004 largely as a result of infrastructure improvements and cost reduction programs that began in 2003. As discussed earlier in this section, initiatives centered on our Dignity Memorial® brand are being further developed to increase revenues and profits while addressing the consumers increasing preference for value-added products and services that assist them through the entire experience when a death occurs. In 2004, we anticipate increases in the selection rate of Dignity Memorial packaged funeral and cremation plans. We are continuing to focus on the development of strategic high-end cemetery inventory and implementation of a tiered-product approach and standard pricing model in each of our cemeteries.

The outlook below provides ranges for certain operating measures on the income statement that could be used to calculate a broad range of expected diluted earnings per share; however, we believe it is more appropriate to use the range of expected diluted earnings per share provided because of the uncertainty of developments described below.

Highlights of Fiscal 2004 Outlook

(In millions)

Operating Measures	
North America Comparable Operations Funeral Revenues	$ 1,120 - $1,170
Funeral Gross Margin Percentage	20% - 24%
Cemetery Revenues	$ 500 - $550
Cemetery Gross Margin Percentage	13% - 17%
General and Administrative Expense	$ 65 - $70
Interest Expense	$ 127 - $130
Consolidated Effective Tax Rate	15% - 18%
Diluted Earnings Per Share	$ .42 - $.50
Cash Flow and Other Measures	
Cash Flows from Operating Activities	$ 270 - $310
Capital Expenditures	$ 100 - $120
Depreciation and Amortization	$ 125 - $135

Diluted earnings per share guidance and all other outlook provided above specifically exclude the following:

§ Any impact from the implementation of Financial Accounting Standards Board (FASB) Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin (ARB) 51* . This standard was originally required to be implemented in the third quarter of 2003. In December 2003, the FASB issued a revision (FIN 46R) which allows companies to defer implementation. We will implement FIN 46R as of March 31, 2004. For a complete discussion of the effect that the implementation of FIN 46R could have on our financial statements, see Critical Accounting Policies, New Accounting Pronouncements and Accounting Changes within this Management s Discussion and Analysis of Financial Condition and Results of Operations and note four to the consolidated financial statements included in this Form 10-K.

§ The recognition of a charge of approximately $55 million (pretax) for the cumulative effect of an accounting change associated with pension plan accounting. Effective January 1, 2004, we changed the accounting for gains and losses on our pension plan assets and obligations to recognize these gains and losses as they occur. In our outlook for 2004, we anticipate this change will reduce pension expenses in 2004 compared to 2003; however, because gains and losses will be recognized currently, market conditions could cause an adverse affect on results of operations as these gains and losses will be recognized currently. See note four to the consolidated financial statements included in this Form 10-K.

§ Any impact from potential changes to our accounting for insurance funded preneed funeral contracts and other accounting changes.

§ The recognition of costs associated with settlements of litigation and the recognition of receivables for insurance recoveries associated with litigation.

§ The possibility of gains or losses associated with early extinguishments of debt.

§ The possibility of gains or losses associated with asset dispositions or joint ventures.

§ The possibility of changes in the capital structure, including new debt issuances and new credit facility.

§

The possibility of the recognition of a cumulative effect of an accounting change under generally accepted accounting principles (other than FIN 46R and the change in pension accounting described above).

The following commentary describes our assumptions, estimates and beliefs supporting our 2004 outlook:

Operating Measures

§ Comparable financial information as used in our 2004 outlook is intended to be reflective of same store results and excludes the effects of acquisition or construction as well as divestitures or joint ventures.

§ The outlook for North America comparable funeral revenues assumes the number of funeral services performed will be flat to slightly down with an increase in cremation services performed offset by a 1% to 3% increase in the overall average revenue per funeral service compared to 2003 levels.

§ North America comparable cemetery revenues are expected to be lower than 2003 levels due to a decline in cemetery construction revenues to more normalized levels. Revenues associated with cemetery property development projects in 2003 were approximately $60 million. Normalized levels of construction revenues in 2004 are expected to be $25 to $30 million. Offsetting this decline in revenues are anticipated increases in preneed sales as our sales structure becomes more stabilized following the significant changes that occurred in late 2002 and 2003.

§ North America funeral and cemetery gross margin percentages are expected to improve in 2004 compared to 2003 primarily due to the recent business process and operating management structure changes and expected reductions in pension plan expenses.

§ General and administrative expenses in 2003 were $178.1 million and included $95.2 million of net costs associated with various litigation-related matters. Also included in 2003 were accelerated systems amortization costs of $13.8 million that ceased in the third quarter of 2003. Excluding these litigation expenses and accelerated system amortization costs, general and administrative expenses in 2003 would have been $69.1 million. For 2004, we are estimating general and administrative expenses to be $65 to $70 million (excluding the possibility of the recognition of costs associated with settlements of litigation or receivables for insurance recoveries). Reductions in system costs will be somewhat offset by increased expenses associated with Sarbanes-Oxley compliance and compensation programs.

§ Interest expense is expected to decrease $13 to $16 million in 2004 compared to 2003 as a result of retiring debt that is scheduled to mature in 2004. Interest expense expected in 2004 of $127 to $130 million includes approximately $10 million associated with amortization of deferred loan costs. The outlook for interest expense does not take into consideration any additional debt reduction that could occur with proceeds from asset sales or joint ventures or from cash flows from operating activities.

§ The consolidated effective tax rate is expected to be 15% to 18% in 2004 compared to 25.6% in 2003. These unusually low rates are attributable to tax benefits received from certain international transactions. The 2004 expected effective tax rate on an annual basis for 2004 includes approximately $30 million of tax benefits associated with the joint venture of our France operations which will be realized in first quarter of 2004. The consolidated effective tax rate in the remaining quarterly periods is expected to be 32% to 35%.

§ The range for expected diluted earnings per share assumes dilution from shares associated with the 6.75% convertible notes due 2008.

International Operations

§ On March 11, 2004, we sold our funeral operations in France. In addition to maintaining a 25% share of the total equity capital of the newly formed entity, we received net cash proceeds of approximately $300 million and a note receivable in the amount of 10 million euros. As a result of the transaction, we expect to recognize a pretax gain on the sale of approximately $10 to $20 million in the first quarter of 2004. We also anticipate receiving tax benefits of approximately $30 million in 2004 related to the transaction. Our consolidated reported results for the year 2003 included $584.6 million in revenues and $68.3 million in gross profits that were associated with France.

§ Remaining international operations consist primarily of cemetery businesses in South America, where we anticipate modest improvement, net of currency fluctuations.

§ We own a 20% minority equity investment in funeral and cemetery operations in the United Kingdom. Pending a successful public offering transaction, we expect to receive proceeds of approximately $50 to $60 million in the second quarter of 2004 associated with the sale of our holdings in stock and notes in these operations.

Cash Flow and Other Measures

§ Cash flows from operating activities in 2003 were $374.1 million and included a tax refund of $94.5 million and payments of $27.1 million, net of insurance recoveries, made during 2003 to resolve certain litigation matters. Had we not received the tax refund or incurred these net litigation payments, cash flows from operating activities in 2003 would have been $306.7 million. Cash flows from operating activities are expected to be $270 to $310 million. This amount includes our ownership of France through March 11, 2004, and excludes the $100 million payment related to the proposed settlement of certain Florida litigation and any possible payments that could be made associated with other litigation matters. It also excludes any receipts from insurance recoveries related to litigation matters and any cash contributions to our frozen pension plan as discussed below.

Anticipated improvements in North America funeral and cemetery margins and reduced interest expense are expected to offset the loss of cash flows from operating activities in 2004 due to the sale of our funeral operations in France, the discontinued use of surety bonding in Florida as discussed below.

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§ Excluded from our 2004 outlook for cash flows from operating activities are payments made related to litigation matters. In February 2004, we paid $100 million into escrow to settle certain litigation matters in Florida. We expect this payment to be partially offset by the receipt of $25 million in recoveries under the first layer of our insurance coverage in 2004.

§ On March 11, 2004, we completed the joint venture of our funeral operations in France. In 2003, cash flows from operating activities were approximately $33 million associated with these businesses in France.

§ In the first quarter of 2004, we made a voluntary cash contribution of $20 million to our frozen pension plan to increase the fair value of the plan assets. This contribution is excluded from our 2004 outlook for cash flows from operating activities.

§ In February 2004, we discontinued the use of surety bonding as a means to provide financial assurance to customers for the prospective sale of preneed contracts in Florida. Beginning with contracts written in early 2004, we have elected to deposit customer receipts from the sale of preneed contracts into trust funds in accordance with state requirements. As a result of this change, our cash flows from operating activities will decline by $15 to $20 million, net of prospective trust receipts, in 2004 over 2003 levels. In subsequent periods, the impact to cash flows is expected to be immaterial. Not included in the outlook for 2004 are other potential changes regarding the use of surety bonding. We are currently evaluating our surety bonding program and may elect to discontinue the use of bonding in other states or cancel certain outstanding bonds and replace with funds in trusts in accordance with state regulations.

§ Payments on restructuring charges are expected to increase by approximately $7 million in 2004 compared to 2003 primarily due to severance costs associated with the reorganization of our operating management structure in the fourth quarter of 2003.

§ Similar to 2003, we do not expect to pay U.S. federal income taxes in 2004 due to significant tax loss carry-forwards. Because of these tax loss carry-forwards, we believe we will not pay cash taxes until 2006. In 2004, we expect to pay approximately $5 million for various state and Canadian province taxes.

§ Capital expenditures in 2004 are expected to be $100 to $120 million compared to $116 million in 2003. Increases in North America capital spending will be offset by reductions related to the joint venture of France. In 2003, $34.3 million of our total capital expenditures were associated with operations in France. Of the total projected capital expenditures in 2004, we expect to spend approximately $65 to $70 million on capital improvements that we believe are necessary to maintain our existing facilities in a condition consistent with company standards and extend their useful lives. This includes approximately $5 million related to our partial year ownership of France in 2004. Growth-oriented capital spending in North America is expected to increase due to investments in new funeral service facilities, Dignity® product displays in our funeral homes, and in developing strategic high-end cemetery property inventory.

§ Depreciation and amortization expense is expected to decline in 2004 compared to 2003 primarily due to the elimination of accelerated systems amortization costs and a reduction in cemetery deferred selling amortization costs due to expected lower levels of preneed revenues in 2004.

Critical Accounting Policies, New Accounting Pronouncements and Accounting Changes

Our consolidated financial statements are impacted by the accounting policies used and the estimates and assumptions made by management during their preparation. The following is a discussion of our critical accounting policies pertaining to revenue recognition, the impairment or disposal of long-lived assets, and the use of estimates.

Revenue Recognition

Funeral revenue is recognized when funeral services are performed. Our trade receivables primarily consist of amounts due for funeral services already performed. We sell price guaranteed preneed funeral contracts through various programs providing for future funeral services at prices prevailing when the agreements are signed. Revenues associated with sales of preneed funeral contracts, including accumulated trust earnings, are deferred until such time that the funeral services are performed (see notes three and five to the consolidated financial statements included in this Form 10-K).

Revenue associated with cemetery merchandise and services is recognized when the service is performed or merchandise is delivered. Revenue associated with preneed cemetery property interment rights is recognized in accordance with the retail land sales provision of SFAS No. 66, *Accounting for the Sales of Real Estate* (SFAS 66). Under SFAS 66, revenue from constructed cemetery property is not recognized until a minimum percentage (10%) of the sales price has been collected. Revenue related to the preneed sale of unconstructed cemetery property is deferred until it is constructed and 10% of the sales price is collected. Revenue associated with sales of preneed merchandise and services is not recognized until the merchandise is delivered or the services are performed (see notes three and six to the consolidated financial statements included in this Form 10-K).

Impairment or Disposal of Long-Lived Assets

We test for impairment of goodwill using a two-step approach as prescribed in SFAS No. 142, *Goodwill and Other Intangible Assets* (SFAS 142). The first step of our goodwill impairment test compares the fair value of a reporting unit with its carrying amount, including goodwill. We do not record an impairment of goodwill in instances where the fair value of a reporting unit exceeds its carrying amount. The second step of our goodwill impairment test is required only in situations where the carrying amount of the reporting unit exceeds its fair value as determined in the first step. In such instances, we compare the implied fair value of goodwill (as defined in SFAS 142) to its carrying amount of goodwill. If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. Fair market value of a reporting unit is determined using a calculation based on multiples of revenue and multiples of EBITDA of both SCI and its competitors.

We apply the requirements of SFAS No. 60 *Accounting and Reporting by Insurance Enterprises* (SFAS 60) to test for impairment of our deferred selling costs as prescribed by the AICPA Industry Guide, *Life and Health Insurance Entities* . Accordingly, when circumstances indicate that actual experience for a portfolio of contracts, regardless of the year of origin, may result in losses, we assess whether the expected gross contract revenues for each portfolio of preneed funeral contracts or preneed cemetery contracts less all related expected contract costs is sufficient to cover the current unamortized deferred selling costs associated with each portfolio. For purposes of applying this policy, a portfolio of preneed funeral contracts or preneed cemetery contracts is comprised of all such contracts executed within a given market (i.e. an area of operation). If deferred selling costs for a portfolio of contracts exceeds the related gross contract revenue less expected contract costs, the excess is charged to expense. We believe this is the most appropriate way to evaluate impairment because it is consistent with the manner in which we acquire, service, and measure the profitability of our preneed funeral and cemetery contracts. Our sales organization is organized by market, and the selling costs incurred and deferred specifically related to the preneed funeral and cemetery deferred revenues recorded in the operating market. The Company is addressing loss contracts in its impairment review of deferred selling costs because we are including all related expected costs in the contract analysis. The application of the requirements under SFAS No. 5 *Accounting for Contingencies* is comparable with the Company s current application of the requirements under SFAS 60.

Our systems do not allow us to track cash flow at the individual contract level for preneed funeral and cemetery contracts. Further, we do not believe that evaluation for impairment at the individual contract level is required by SFAS 60 or SFAS 5. We believe the lowest level of identifiable cash flows associated with our preneed funeral and cemetery activities is at our market level of operations. The contracts are homogenous at this level. Therefore, the assumptions at this level would be the same as on an individual contract level.

We review our remaining long-lived assets for impairment when changes in circumstances indicate that the carrying amount of the asset may not be recoverable, in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144). SFAS 144 requires that long-lived assets to be held and used be reported at the lower of their carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to us are recorded at the lower of their carrying amount or fair value less estimated cost to sell.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make certain estimates and assumptions. These estimates and assumptions affect the carrying values of assets and liabilities and disclosures of contingent assets and liabilities at the balance sheet date. Actual results could differ from such estimates due to uncertainties associated with the methods and assumptions underlying our critical accounting measurements. Key estimates used by management, among others, include:

Allowances We provide various allowances and/or cancellation reserves for our funeral and cemetery preneed and atneed receivables, our preneed funeral and preneed cemetery deferred revenues, as well as for our funeral and cemetery deferred selling costs. These allowances are based on an analysis of historical trends and include, where applicable, collection and cancellation activity. These estimates are impacted by a number of factors, including changes in economy, relocation, and demographic or competitive changes in our areas of operation.

Depreciation of long-lived assets We depreciate our long-lived assets over their estimated useful lives. These estimates of useful lives may be affected by such factors as changing market conditions or changes in regulatory requirements. In 2002, we changed the estimated useful life of our existing information technology systems as a result of the decision to implement a new North America point of sale system and an upgraded general ledger system. We recognized approximately $13.8 and $13.5 million of additional amortization expense related to this change in estimate in 2003 and 2002, respectively.

Deferred Selling Costs Our policy is to defer selling costs that vary with and are primarily related to the acquisition of preneed funeral (trust funded only) and preneed cemetery contracts, and to expense such costs in proportion to the revenue recognized. This deferral, which is calculated based on deferral rates discussed below, and amortization model follows the provisions of SFAS 60, *Accounting and Reporting by Insurance Enterprises* (SFAS 60). The selling costs subject to deferral are the pool of compensation expense and related fringe costs incurred by the Company s sales counselors and sales managers. Other selling costs associated with the sales and marketing of preneed funeral and cemetery contracts (e.g., lead procurement costs, brochures and marketing materials, advertising and general administrative costs) are expensed as incurred.

Deferral rates are determined for the following:

- Preneed funeral contracts
- Preneed cemetery contract items:
  - interment rights (burial property)
  - merchandise
  - services

These deferral rates are based on the ratio of the selling compensation and fringe costs to preneed funeral and cemetery production (in dollars) weighted accordingly in the manner for which the counselor is compensated (with interment rights, or burial property, being the highest and preneed cemetery services being the lowest compensation to the counselor). In developing the deferral rates, the Company reviews various rate scenarios to ensure the finalized rates, when applied to forecasted production dollars, are reasonable compared to forecasted selling compensation. Additionally, the developed deferral rates are reviewed annually for reasonableness compared to current and historical commission rates used by the Company.

Taxes Our ability to realize the benefit of deferred tax assets requires us to achieve certain future earnings levels. We have established a valuation allowance against a portion of deferred tax assets and could be required to further adjust that valuation allowance if market conditions change materially and future earnings are, or are projected to be, significantly different from current estimates. We intend to permanently reinvest the unremitted earnings of certain of our foreign subsidiaries in those businesses outside the United States and, therefore, have not provided for deferred federal income taxes on such unremitted foreign earnings.

Pension cost Our pension costs and liabilities are actuarially determined based on certain assumptions, including expected long-term rates of return on plan assets and the discount rate used to compute future benefit obligations. It is our policy to use a discount rate comparable to rates of return on high-quality fixed income investments available and expected to be available during the period to maturity of the Company s pension benefits. In 2003 and in prior years, actuarial gains and losses resulting from changes in the assumptions, or experience differences from those assumptions, are amortized over the remaining service period of active employees expected to receive benefits under the plans.

Since 2002, we have used a 9.0% assumed rate of return on plan assets as a result of a high allocation of equity securities within the plan assets. At December 31, 2003, 74% of the plan assets were equity securities with the remaining 26% of plan assets being represented by fixed income securities. As of December 31, 2003, the equity securities were invested approximately 40% in U.S. Large Cap investments, 15% in international equities, 10% in U.S. Small Cap investments and 9% in the Company s stock. Our actuaries estimate the expected performance over a ten year period of each class of security. The 9.0% rate of return on plan assets was determined by allocating these expected long-term returns to the different components of the assets.

Pursuant to the previously mentioned $20 million infusion of funds into the plan in early 2004, we expect to rebalance the plan assets to have a lower percentage invested in traditional equity securities and fixed income securities and instead

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incorporate investments in hedge funds. We believe that this reallocation will reduce the volatility with limited reduction of returns.

Furthermore, we are changing our method of accounting for gains and losses on pension assets and obligations in 2004 to recognize such gains and losses during the year in which they occur. In addition to the change in our investment strategy described above, we expect to record net pension expense reflecting estimated returns on plan assets and obligations for our interim financial statements. Under the new accounting policy, upon completion of our annual remeasurement during the fourth quarter, we will recognize actual gains and losses on plan assets and obligations. Therefore, pension expense during the fourth quarter could be different than amounts recorded in interim periods. Additionally, the rate of return on pension plan assets could be lower in 2004 due to the accounting change to immediately recognize gains and losses and due to the reallocation of plan assets as discussed above. See accounting changes and note four to the consolidated financial statements in Item 8 of this Form 10-K for details of this accounting change.

Insurance loss reserves   We purchase comprehensive general liability, morticians and cemetery professional liability, automobile liability and workers compensation insurance coverages structured with high deductibles. This high deductible insurance program results in the Company being primarily self-insured for claims and associated costs and losses covered by these policies. Historical insurance industry experience indicates a high degree of inherent variability in assessing the ultimate amount of losses associated with casualty insurance claims. This is especially true with respect to liability and workers compensation exposures due to the extended period of time that transpires between when the claim might occur and the full settlement of such claim, often many years. We continually evaluate loss estimates associated with claims and losses related to these insurance coverages and falling within the deductible of each coverage through the use of qualified and independent actuaries. A variety of actuarial methodologies are applied to the underlying loss data by the actuary in arriving at an estimate of the reasonably possible loss range. Assumptions based on factors such as claim settlement patterns, claim development trends, claim frequency and severity patterns, inflationary trends and data reasonableness will generally effect the analysis and determination of the best estimate of the projected ultimate claim losses. The results of these actuarial evaluations are used to both analyze and adjust our insurance loss reserves.

Our independent actuaries used five actuarial methods generally accepted by the Casualty Actuarial Society to arrive at an estimate of a range that we refer to as reasonably possible . The Actuarial Standard of Practice No. 36 (ASOP 36 published by the American Academy of Actuaries) states: A range of reasonable estimates is a range of estimates that could be produced by appropriate actuarial methods or alternative sets of assumptions that the actuary judges to be reasonable. Methods used to determine the Company s reasonably possible range are: paid and incurred loss development methods; frequency-severity methods; and paid and incurred Bornhuetter-Ferguson methods. All of these methods were used to determine the Company s reasonably possible range of insurance loss reserves for the years ended December 31, 2003, 2002 and 2001.

The Company has not changed its methodologies for determining the reasonably possible range; however, there are changes made to the assumptions as the loss development factors are updated. These loss development factors are determined based on the Company s historical loss development data[1] and are updated annually as new data becomes available. As a result, the loss development factors used in the December 31, 2002 analysis could be different from the loss development factors used in the December 31, 2003 analysis. The Company considers these changes in loss development factors synonymous to changes in assumptions . The final loss estimate is not determined by weighting the methodologies, but instead is subjectively arrived at by our independent actuary considering the relative merits of the various methods and the truncated average of the various methods.

For each loss type (workers compensation, general liability, and auto liability) loss triangles are generated, which show the cumulative valuation of each loss period over time. The loss components evaluated include incurred losses, paid losses, reported claim counts, and average incurred loss. The actuarial analysis of losses uses this data to estimate future loss development or settlement value of the losses. Since these loss development factors are an estimate about future loss development, the calculation of ultimate losses is also an estimate. The actual ultimate loss value may not be known for many years, and may differ significantly from the estimated value of the ultimate losses.

As of December 31, 2003, reported losses within the Company s retention for workers compensation, general liability and auto liability incurred during the period May 1, 1987 through December 31, 2003 were approximately $167 million. The selected fully developed ultimate settlement value estimated by our independent actuary was $199.4 million. Paid losses were $155.1 million indicating a reserve requirement of $44.3 million. After considering matters discussed between our independent actuary, related to this calculation, the Company estimated the reserve to be $46.8 million as of December 31, 2003.

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At December 31, 2003 and 2002, the balances in the reserve and the related activity were as follows:

(Dollars in millions)	
Balance at December 31, 2001	$ (42.6)
Additions	(22.7)
Payments	26.3
Balance at December 31, 2002	$ (39.0)
Additions	(31.6)
Payments	23.8
Balance at December 31, 2003	$ (46.8)

Our independent actuary performed a sensitivity analysis that was modeled to assess the impact of changes to the reserve pertaining to workers compensation, general liability, and auto liability. The sensitivity analysis assumes an instantaneous 10% adverse change to the loss development factors as summarized below.

(Dollars in millions)	**Sensitivity Analysis**
Workers Compensation	$ 2.3
General Liability	$ 0.4
Auto Liability	$ 1.6
Total Sensitivity	$ 4.3

(1) The loss development factors used in the December 31, 2003 calculation are based on the Company s actual claim history by policy year for the period beginning May 1, 1991 May 1, 2003.

New Accounting Pronouncements

In January 2003, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin (ARB) No. 51* . This interpretation clarifies the application of ARB 51, *Consolidated Financial Statements* , to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity and risk for the entity to finance its activities without additional subordinated financial support from other parties. In December 2003, the FASB revised FASB Interpretation No. 46 (FIN 46R) which allows companies with certain types of variable interest entities to defer implementation until March 31, 2004.

We are currently in discussions with the Staff of the Securities and Exchange Commission related to our implementation of FIN 46R. The discussion relates to (i) the consolidation under FIN 46R of our preneed funeral and preneed cemetery merchandise and service trusts; (ii) the potential consolidation of our cemetery perpetual care trust funds; and (iii) the policies of recognition of the associated investment earnings of the trust funds.

We believe, at this time, that we will consolidate the preneed funeral and preneed cemetery merchandise and service trust funds upon implementation of FIN 46R. Upon consolidation, the large majority of the trust assets will be recorded at fair value. We are unclear at this time whether we will consolidate the cemetery perpetual care trust funds upon implementation of FIN 46R. Currently, the perpetual care trust funds are not recognized on our consolidated balance sheet. If the cemetery perpetual care trust funds are consolidated, we believe we will recognize an asset and a corresponding liability in our consolidated balance sheet of approximately $650 million. The large majority of the assets of cemetery perpetual care trust funds will be recorded at fair value.

Currently, we defer investment earnings associated with preneed funeral and preneed cemetery merchandise and service trust funds until the corresponding merchandise is delivered or the service is performed. It is unclear at this time whether this revenue recognition policy will continue upon implementation of FIN 46R, or if we will have to recognize these trust fund earnings in a revised manner, such as at the time the trusts funds themselves earn such investment earnings.

Realized investment earnings from cemetery perpetual care trust funds are recognized in current cemetery revenues as they are intended to defray cemetery maintenance costs. We expect to continue recognizing these investment earnings under this new accounting policy.

We believe the consolidation of the preneed funeral and preneed cemetery merchandise and service trust funds (and possibly the cemetery perpetual care trust funds) will have an effect on certain components within our consolidated statement of cash flows. Upon such consolidation, proceeds from sales of trust fund investments and disbursements for purchases of trust fund investments will be shown as separate components of cash flows from investing activities. Currently, the cash flows described above are reported within cash flows from operations as they are receivables collected from third parties.

In addition to potentially consolidating our trust funds, we also believe we will consolidate certain cemeteries managed by us upon implementation of FIN 46R. We expect to recognize a charge of approximately $10 to $20 million, representing the cumulative effect of an accounting change, as a result of consolidating these cemeteries as of March 31, 2004. The results of operations and cash flows of these cemeteries will be included in our consolidated financial statements upon implementation of FIN 46R, although no material impact is anticipated.

We have changed our method of accounting for insurance funded preneed contracts as we have concluded that our insurance funded preneed funeral contracts are not assets and liabilities as defined by Statement of Financial Accounting Concepts No. 6, *Elements in Financial Statements*. Therefore, we have removed from our consolidated balance sheets amounts relating to insurance funded preneed funeral contracts previously recorded in Preneed funeral contracts, net and Deferred preneed funeral revenues for all periods presented. The amounts relating to insurance contracts removed were approximately $3.5 billion and $2.9 billion at December 31, 2003 and December 31, 2002, respectively. The removal of these amounts did not have an impact on our consolidated stockholders equity, results of operations or cash flows. See note five to the consolidated financial statements included in this Form 10-K for additional information on insurance related preneed funeral balances.

Effective January 1, 2004, we changed the accounting for gains and losses on our pension plan assets and liabilities. We will recognize such gains and losses in our consolidated statement of operations as such gains and losses are incurred under pension accounting. Prior to January 1, 2004, we amortized the difference between actual and expected investment returns and actuarial gains and losses over seven years (except to the extent that settlements with employees required earlier recognition). We believe the change is preferable as the new method of accounting better reflects the economic nature of our pension plan and recognizes gains and losses on the pension plan assets and liabilities in the year the gains and losses occur. As a result of this accounting change, we expect to recognize a charge for the cumulative effect of an accounting change of approximately $55 million (on a pretax basis) as of January 1, 2004. This amount represents accumulated unrecognized net losses related to the pension plan assets and liabilities.

Results of Operations

Our results for the fiscal years ended 2002 and 2001 and the first three quarters of 2003 have been restated. The financial data below reflects the effects of the restatement for all periods affected. For details relating to this restatement, see notes two and twenty-one to the consolidated financial statements.

Additionally, we have reclassified certain prior year amounts to conform to the current period financial presentation with no effect on previously reported net income, financial condition or cash flows.

Net income in 2003 totaled $85.1 million compared to net losses in 2002 and 2001 of $232.5 million and $623.4 million, respectively. Net income in 2003 included a pretax gain on the sale of our equity investment in Australia and the collection of an associated note receivable of $45.7 million. Net income in 2003 was negatively impacted by litigation related expenses, net of estimated insurance recoveries, of $95.2 million. Included in these net litigation expenses was the recognition of a $25 million receivable during the fourth quarter of 2003 for expected insurance recoveries under the first layer of our insurance coverage related to the previously announced $100 million proposed settlement of certain Florida litigation. Net losses reported in 2002 and 2001 were impacted by impairment losses on dispositions, expenses related to market value adjustments of certain options associated with our 6.3% notes due in 2003, severance costs of former employees and expenses related to the termination of certain consulting and non-compete contractual obligations.

Total consolidated revenues were $2,328.4 million in 2003 compared to $2,312.4 million in 2002 and $2,489.0 million in 2001. The growth in revenues in 2003 over 2002 is largely attributable to increases in our funeral operations in France which benefited from positive currency fluctuations. The decrease in revenues in 2002 compared to 2001 is primarily the result of the sale of several foreign businesses, including our funeral and cemetery operations in the United Kingdom in February 2002 which previously generated annual revenues of approximately $165 million, and several businesses in North America. Although revenues have declined from 2001 levels, gross profits improved to $362.0 million in 2003 and 2002, which in turn were 12.2% higher than 2001. The gross profit margin was 15.5% in 2003 and 15.7% in 2002, which was substantially above 12.6% in 2001 largely as a result of successful ongoing cost reduction initiatives.

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General and Administrative Expenses

General and administrative expenses in 2003 were $178.1 million compared to $89.8 million in 2002. This increase of $88.3 million is primarily a result of an increase in litigation expenses of $85.2 million. We recognized expenses, net of estimated insurance recoveries, of $95.2 million in 2003 compared to $10 million in 2002. These expenses were primarily associated with litigation matters in Florida. Excluding these litigation related expenses in 2003 and 2002, general and administrative expenses increased $3.1 million. Decreases in technology and other overhead costs were offset by $6.0 million of accrued expenses associated with our long-term incentive compensation program. This new plan is based upon our total shareholder return (share price appreciation including reinvested dividends) during the period 2003 to 2005 relative to a peer group of companies. This new compensation plan is expensed currently in contrast to our historical stock option plan in 2002 that was not expensed. Amounts accrued in 2003 related to this compensation plan are not expected to be paid until 2006 and only if earned.

General and administrative expenses increased $19.4 million in 2002 compared to 2001. Included in 2002 is $10 million of expenses associated with litigation related matters and $13.5 million of accelerated non-cash amortization expense related to our decision to implement new information systems that was not included in 2001. In 2002, we made the decision to implement new information systems and, therefore, accelerated the existing systems amortization costs which ceased in the third quarter of 2003.

In addition to general and administrative expenses, there are two other components of overhead costs in North America: home office overhead and field overhead. These overhead costs are allocated to funeral and cemetery operations in North America. Home office and field overhead costs totaled $152.7 million in 2003 compared to $162.9 million in 2002 representing a decline of more than $10 million or 6.3%. This decline is primarily attributable to reductions in preneed sales overhead costs as a result of significant changes made to our sales organization in late 2002 and early 2003.

Other

In 2003, we recognized a net pretax gain of $49.4 million in gains and impairment (losses) on dispositions, net, primarily related to the sale of certain equity investments during the year. In December 2003, we sold our equity investment in Australia and collected an associated note receivable that generated a gain and net cash proceeds of $45.7 million. During the second quarter of 2003, we sold our equity investment in Spain for net cash proceeds of $26.0 million and recognized a gain of $8.1 million. These gains helped to offset net losses related to sales of various North America businesses. In 2002, we recognized net gains and impairment losses on dispositions of $161.5 million primarily related to an impairment charge for several funeral and cemetery operations held for sale in North America. In 2001, we recognized a net loss of $482.5 million primarily related to the loss on joint venturing our Australian operations, losses from the disposition of operations in the Netherlands, Norway and Belgium and the impairment of certain international operations held for sale.

Other operating expenses of $9.0 million recognized in 2003 are largely due to severance costs associated with the reorganization of our operating management structure in the fourth quarter of 2003. In November 2003, we moved to a major market and middle market concept with the understanding that our markets and businesses are not all the same and require different management approaches. We eliminated the dual management organizations of sales and operations and now have one leader responsible for each market that has the ability to lead in a multi-segment environment, who is focused on growing our business and who is committed to the Dignity Memorial® standards and brand. Other operating expenses recognized in 2002 of $94.9 million related to market value adjustments of certain options associated with our 6.3% notes due 2003, severance costs of former employees, and expenses related to the termination of certain consulting and non-compete contractual obligations.

Interest expense decreased to $142.7 million in 2003 compared to $160.9 million and $210.9 million in 2002 and 2001, respectively. The decrease in interest expense reflects the success we have had in reducing outstanding debt.

Other income, net was $29.7 million in 2003 compared to $25.2 million in 2002 and $23.2 million in 2001. Other income, net primarily consists of income from various notes receivable and cash investments, gains from early extinguishments of debt, equity earnings of investments in certain companies and cash overrides associated with preneed funeral sales with third party insurance companies. Other income, net increased in 2003 over 2002 and 2001 primarily associated with increases in interest income and transactional foreign currency exchange gains which helped to offset declines in gains from early extinguishments of debt and lower levels of cash overrides received from third party insurance companies associated with the sale of preneed funeral contracts.

In the twelve months ended December 31, 2002, we recognized an after tax charge of $135.6 million as a result of the adoption of Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets"*. This standard required goodwill to no longer be amortized, but instead tested for impairment annually. This charge related to impairment of goodwill in our North America cemetery segment.

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The effective tax rate was 25.8% in 2003 compared to 31.4% in 2002. The decline in the effective tax rate is due primarily to income tax benefits associated with certain international transactions. We expect the annual effective tax rate in 2004 to be 15% to 18% due to income tax benefits of approximately $30 million related to our joint venture of France which will be realized in the first quarter of 2004.

Actual Versus Comparable Results of Operations Twelve Months Ended December 31, 2003, 2002 and 2001

The table below reconciles our actual results to our comparable or same store results for the periods ended December 31, 2003, 2002 and 2001. We regard same store results of operations as analogous to our comparable results of operations. We consider comparable operations as operations that were not acquired or constructed after January 1, 2001 or divested prior to December 31, 2003. Therefore, in the following three-year presentation, we are providing results of operations for the same funeral and cemetery locations in each of the three year periods presented.

In 2002, we ceased amortization of goodwill as required by SFAS 142; changed the allocation methodology of overhead costs in North America to be based on funeral and cemetery reporting unit revenues; began recognizing revenues associated with delivered caskets previously preneed on cemetery contracts as part of funeral operations instead of cemetery operations; and ceased depreciation of operating assets held for sale during 2002. In 2002, we determined transactions to sell or joint venture certain assets would be delayed until after 2002. As a result, we resumed normal depreciation of those assets held in France and Chile in the third quarter of 2002. In January 2003, the Company once again ceased depreciation of France operating assets held for sale. For purposes of the following discussion, we have presented the financial information for 2001 on a pro forma basis as if these changes had been implemented as of January 1, 2001.

(Dollars in thousands)	Actual	Activity Associated with Acquisition / New Construction	Activity Associated with Dispositions	Comparable	% Variance
2003					
North America					
Funeral Revenue	$ 1,145,016	$ 3,807	$ 8,427	$ 1,132,782	1.1%
Cemetery Revenue	561,397		4,421	556,976	0.8%
	$ 1,706,413	$ 3,807	$ 12,848	$ 1,689,758	1.0%
Other Foreign					
Funeral Revenue	$ 595,938	$	$ 1	$ 595,937	0.0%
Cemetery Revenue	26,074			26,074	0.0%
	$ 622,012	$	$ 1	$ 622,011	0.0%
Total Revenues	$ 2,328,425	$ 3,807	$ 12,849	$ 2,311,769	0.8%

North America									
Funeral Gross Profits	$	210,708	$	895	$	(4,582)	$	214,395	-1.7%
Cemetery Gross Profits		74,262				(1,005)		75,267	-1.4%
	$	284,970	$	895	$	(5,587)	$	289,662	-1.6%
Other Foreign									
Funeral Gross Profits	$	71,167	$		$	2	$	71,165	0.0%
Cemetery Gross Profits		5,828				(1)		5,829	0.0%
	$	76,995	$		$	1	$	76,994	0.00%
Total Gross Profit	$	361,965	$	895	$	(5,586)	$	366,656	1.30%

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2002	Actual	Activity Associated with Acquisition / New Construction	Activity Associated with Dispositions	Comparable	% Variance
North America					
Funeral Revenue	$ 1,181,425	$ 3,761	$ 38,680	$ 1,138,984	3.6%
Cemetery Revenue	611,153		18,866	592,287	3.1%
	$ 1,792,578	$ 3,761	$ 57,546	$ 1,731,271	3.4%
Other Foreign					
Funeral Revenue	$ 498,670	$	$ 14,282	$ 484,388	2.9%
Cemetery Revenue	21,191		2,191	19,000	10.3%
	$ 519,861	$	$ 16,473	$ 503,388	3.2%
Total Revenues	$ 2,312,439	$ 3,761	$ 74,019	$ 2,234,659	3.4%
North America					
Funeral Gross Profits	$ 231,089	$ 1,662	$ (3,205)	$ 232,632	-0.7%
Cemetery Gross Profits	72,779		2,421	70,358	3.3%
	$ 303,868	$ 1,662	$ (784)	$ 302,990	0.3%
Other Foreign					
Funeral Gross Profits	$ 52,954	$	$ 3,356	$ 49,598	6.3%
Cemetery Gross Profits	5,187		1,785	3,402	34.4%
	$ 58,141	$	$ 5,141	$ 53,000	8.8%
Total Gross Profit	$ 362,009	$ 1,662	$ 4,357	$ 355,990	1.7%

	Actual	Activity Associated with Acquisition / New Construction	Activity Associated with Dispositions	Comparable	% Variance

2001

North America					
Funeral Revenue	$ 1,217,840	$ 127	$ 103,027	$ 1,114,686	8.5%
Cemetery Revenue	571,270		31,653	539,617	5.5%
	$ 1,789,110	$ 127	$ 134,680	$ 1,654,303	7.5%
Other Foreign Funeral Revenue	$ 640,180	$	$ 204,310	$ 435,870	31.9%
Cemetery Revenue	59,715		32,354	27,361	54.2%
	$ 699,895	$	$ 236,664	$ 463,231	33.8%
Total Revenues	$ 2,489,005	$ 127	$ 371,344	$ 2,117,534	14.9%
North America					
Funeral Gross Profits.	$ 214,751	$ 105	$ (24,172)	$ 238,818	-11.2%
Cemetery Gross Profits	37,854		(11,357)	49,211	-30.0%
	$ 252,605	$ 105	$ (35,529)	$ 288,029	-14.0%
Other Foreign					
Funeral Gross Profits.	$ 48,571	$	$ 2,706	$ 45,865	5.6%
Cemetery Gross Profits	21,609		10,946	10,663	50.7%
	$ 70,180	$	$ 13,652	$ 56,528	19.5%
Total Gross Profit	$ 322,785	$ 105	$ (21,877)	$ 344,557	6.7%

The following table provides the components to calculate our comparable average revenue per funeral service in North America for the periods ended December 31, 2003, 2002 and 2001. We calculate average revenue per funeral service as adjusted comparable North America funeral revenue divided by the comparable number of funeral services performed in North America during the applicable period. In the calculation of average revenue per funeral service, General Agency (GA) revenues and Kenyon revenues are excluded from comparable North America funeral revenue to avoid distorting our averages of normal funeral case volume.

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(Dollars in thousands)	2003	2002	2001
Comparable North America funeral revenue	$ 1,132,782	$ 1,138,984	$ 1,114,686
Less: GA revenues (1)	27,995	46,256	42,770
Kenyon revenue (2)	11,945	4,996	5,269
Adjusted comparable North America funeral revenue	$ 1,092,842	$ 1,087,732	$ 1,066,647
Comparable North America funeral services performed	263,952	268,326	268,197
Average North America revenue per funeral service	$ 4,140	$ 4,054	$ 3,977

(1) General Agency (GA) revenues are commissions we receive from third party insurance companies when customers purchase insurance contracts from such third-party insurance companies to fund funeral services and merchandise at a future date.

(2) Kenyon International Emergency Services is our disaster response subsidiary that engages in mass fatality and emergency response services.

Consolidated Funeral Segment Analysis

Consolidated funeral revenues increased $60.9 million in 2003 compared to 2002 as a result of a $97.3 million increase in foreign revenues, partially offset by a decline of $36.4 million in North America funeral revenues. The increase in foreign revenues is predominantly related to our French operations and is due to increases in funeral services performed and in the average revenue per funeral, as well as favorable currency effects. North America funeral revenues declined primarily as a result of divestitures and declines in GA revenues. GA revenues are commissions we receive from third-party insurance companies when customers purchase insurance contracts from such third-party insurance companies to fund funeral services and merchandise at a future date.

Consolidated funeral gross profits declined $2.2 million in 2003 compared to 2002. Declines in North America funeral operations due to decreased revenues described above and increases in employee benefit and insurance costs were partially offset by improvements in French funeral operations which benefited from increased revenues described above and reduced depreciation expense.

Consolidated funeral revenues decreased $177.9 million in 2002 compared to 2001 mainly due to a decrease of $141.5 million in foreign funeral revenues primarily as a result of the sale of our funeral operations in the United Kingdom in February 2002. In 2002, funeral operations in the United Kingdom generated $13.2 million of revenues compared to $140.4 million in 2001. The remaining decrease in foreign funeral revenues is primarily due other foreign divestitures which was partially offset by increased revenues from funeral operations in France. North America funeral revenues declined $36.4 million due to dispositions.

Despite the decline in revenues in 2002, consolidated funeral gross profits increased $20.7 million in 2002 compared to 2001. North America funeral gross profits increased $16.3 million primarily due to the sale of certain underperforming businesses. Foreign funeral gross profits improved $4.4 million primarily due to improvements in French funeral operations which benefited from increased revenues, positive currency effects, and reduced depreciation expense. These increases in funeral operations in France helped to offset the loss of gross profits from the sale of certain foreign operations, including funeral operations in the United Kingdom. In 2002, gross profits from funeral operations in the United Kingdom were $3.3 million compared to $14.1 million in 2001.

Comparable Funeral Segment Analysis

Comparable North America funeral revenues in 2003 were $1,132.8 million and on the upper end of our guidance range of $1,090 million to $1,150 million. Comparable North America funeral revenues decreased slightly in 2003 from 2002. A decline of 1.6% in the number of funeral services performed and lower levels of general agency revenues associated with the sale of insurance funded preneed funeral contracts were partially offset by an increase of 2.1% in the average revenue per funeral service. We believe the declines in funeral services performed are consistent with, and in certain instances less than, the declines reported by others in the funeral service and casket manufacturing industries. We also track weekly mortality data published by the Centers for Disease Control (CDC). We believe that the decline in our funeral services performed in 2003 is less than the declines in numbers of deaths reported by the CDC. General agency revenues declined in 2003 versus 2002 due to the anticipated decrease in sales of insurance funded preneed funeral contracts as a result of the significant changes made to the sales organization. Comparable North America funeral revenues increased 2.2% in 2002 compared to 2001 led by a slight increase in comparable funeral services performed and a 1.9% increase in the average revenue per funeral service.

The average revenue per funeral service increased 2.1% in 2003 over 2002 and increased 1.9% in 2002 over 2001. The fourth quarter of 2003 represents the fourteenth consecutive quarter in which we have increased our average revenue per funeral service. This consistent growth in average revenue is largely a result of the success of the nationally branded Dignity Memorial® packaged funeral and cremation plan initiative. Dignity Memorial packaged plans are designed to simplify the customer decision-making process, provide savings and enhance the value to consumers through unique products and services which have traditionally been unavailable through funeral service locations. In addition to improving customer satisfaction levels as measured by independent surveys, Dignity Memorial burial and cremation packaged plans generate significant incremental revenue per funeral service compared to non-Dignity sales due to the comprehensive product and service offerings they provide. On a burial funeral, Dignity Memorial packaged sales generate on average approximately $2,800 more than non-Dignity sales. On a cremation service, Dignity Memorial packaged sales generate approximately $1,700 more than non-Dignity sales. During 2003, approximately 16% of the total funeral consumers served selected a Dignity packaged plan compared to approximately 14% in 2002 and approximately 7% in 2001. On a preneed basis, approximately 20% of funeral preneed arrangements contracts sold in 2003 were Dignity plans compared to approximately 18% in 2002 and approximately 7% in 2001.

We achieved increases in average revenue during 2001 through 2003 despite an increase in cremation services. In the death care industry, there has been a growing trend in the number of cremations performed in North America as an alternative to traditional funeral service dispositions. While cremations performed by us in North America typically have higher gross profit margins than traditional funeral services, cremations usually result in lower revenue and gross profit dollars compared to traditional burial funeral services. Of the total comparable funeral services performed in North America during 2003, 39.0% were cremation services compared to 37.9% in 2002 and 36.7% in 2001. Our ability to offer the cremation consumer a broad array of products and services through Dignity packaged plans resulted in increases in the average revenue per cremation service in 2003 compared to 2002.

The North America funeral gross margin percentage for the twelve months ended December 31, 2003 was 18.9% and on the lower end of our targeted range of 18% to 22%. The North America funeral gross profits and gross margin percentage declined in 2003 compared to 2002 and 2001 primarily due to volume declines experienced by us and others in the industry and increased employee benefit costs and insurance costs. These increases in employee benefit and insurance costs were somewhat offset by reductions in selling and other overhead costs.

Comparable foreign funeral revenues and gross profits, which predominantly are associated with our businesses in France, increased in 2003 compared to 2002 and 2001. Subsequent to December 31, 2003, these businesses were sold in a joint venture transaction on March 11, 2004 and we retained a 25% minority equity interest. In 2003, France s reported revenues and gross profits were $584.6 million and $68.3 million, respectively. Included in 2003 results are positive effects of foreign currency translation of $93.2 million in revenues and $9.2 million in gross profits compared to 2002. Excluding favorable currency effects, France s revenues grew 3.1% and the gross margin percentage improved to 11.7% compared to 9.9%. These improved results were driven by a 2.6% increase in funeral services performed and a 4.5% increase in the average revenue per funeral service. Also, 2002 results included $8.9 million of depreciation expense that was not included in 2003 under accounting rules once we began to actively pursue a joint venture with respect to the French funeral operations. Revenues and gross profits for France also improved in 2002 over 2001 despite a 0.5% decline in funeral services. The effect of foreign currency translations positively benefited 2002 revenues by $24.9 million and gross profits by $2.5 million. Included in results for 2001 is approximately $10 million more of depreciation expense as discussed above. Excluding favorable currency effects and the impact of depreciation expense, France s revenues grew by 5.5% and gross profits improved by approximately $10 million. These improved results were due to a 4.3% increase in the average revenue per funeral and increases in burial monument sales, along with successful cost reduction initiatives.

Consolidated Cemetery Segment Analysis

Consolidated cemetery revenues declined $44.9 million in 2003 compared to 2002 primarily as a result of a $49.8 million decrease in North America cemetery revenues, partially offset by improvements in foreign cemetery revenues. This decline in North America cemetery revenues was due to divestitures and also due to the significant changes made to the sales organization in 2003. Although we expected cemetery revenues to decline in 2003 from these strategic changes, we also anticipated, and realized, higher gross margins as a result. Cemetery gross profits in 2003 improved $2.1 million from 2002 due primarily to reductions in preneed selling costs from a number of changes made to the sales organization to increase our effectiveness.

Consolidated cemetery revenues improved $1.4 million in 2002 compared to 2001. Increased revenues in North America of $39.9 million due primarily to increases in completed cemetery property development projects helped to offset a decline in foreign cemetery revenues of $38.5 million as a result of the sale of certain foreign cemetery operations, including cemetery operations in the United Kingdom in February 2002, and unfavorable currency effects in South America cemetery operations. In 2002, cemetery operations in the United Kingdom generated $2.2 million of revenues compared to $24.4 in 2001. Consolidated cemetery gross profits grew $18.5 million in 2002 compared to 2001. Improvements in North America cemetery operations of $34.9 million due to increases in revenue described above helped to offset a decline of $16.4 million in foreign cemetery gross profits due to the sale of certain foreign cemetery businesses, including businesses in the United Kingdom, and unfavorable currency effects in South America cemetery operations. In 2002, gross profits from cemetery operations in the United Kingdom were $0.7 million compared to $7.7 million in 2001.

Comparable Cemetery Segment Analysis

Comparable North America cemetery revenues for the twelve months ended December 31, 2003 were $557.0 million. Comparable North America cemetery revenues decreased in 2003 compared to 2002 associated with the anticipated decrease in preneed revenues due to significant changes in the sales organization and lower levels of revenues associated with completed cemetery property development projects. As a result of redesigning sales compensation programs, eliminating certain lead generation programs, incentive travel programs and other sales activities and shifting to a sales model based on personal referrals, we expected revenues in 2003 to be negatively impacted. We also expected, and realized, higher gross margins as a result of these strategic changes. Comparable North America cemetery revenues increased in 2002 compared to 2001 as a result of increases in completed cemetery property development projects and increases in the amount of cash receipts and down payments received from preneed property sales. Preneed cemetery property revenues are recognized when development of the property is completed and customer payments are at least 10% of the total contract amount.

The comparable North America cemetery gross margin percentage for the twelve months ended December 31, 2003 was 13.5%, which exceeded the 2002 gross margin percentage of 11.9%. A significant decline in preneed selling costs as described above helped to overcome increased employee benefit and insurance costs and increased maintenance expenses to bring certain cemeteries in line with Company standards. Comparable North America cemetery gross profit and margin percentage increased in 2002 compared to 2001 primarily as a result of increases in completed cemetery property development projects.

Comparable foreign cemetery operations represent our businesses in Chile and Uruguay. In 2003, revenues from these operations were $26.1 million compared to $19.0 million in 2002 and $27.4 million in 2001. Gross profits from these operations were $5.8 million in 2003 compared to $3.4 million in 2002 and $10.7 million in 2001. The increase in revenues and gross profits in 2003 compared to 2002 is reflective of an improved economy following a difficult year in 2002. Revenues and gross profits declined in 2002 compared to 2001 primarily as a result of unfavorable currency effects.

Financial Condition, Liquidity and Capital Resources

Our primary financial objectives are to continue to improve our financial flexibility by generating strong cash flows, completing remaining asset sales or joint ventures, and further reducing debt. We have a goal of achieving specific ratings with the credit rating agencies. At December 31, 2003, our long-term debt was rated BB- by Standard and Poor s and B1 by Moody s Investors Service. Our targeted rating from Standard and Poor s is BB and from Moody Investors Service a Ba2 . Our balance sheet continues to improve. We have made significant progress in reducing debt since 2001.

	December 31,		
	2003	2002	2001
Cash and cash equivalents	$ 239.4	$ 200.6	$ 29.3
Total debt	$ 1,701.9	$ 1,974.4	$ 2,522.0
Net debt (total debt less cash)	$ 1,462.5	$ 1,773.8	$ 2,492.7

Cash and cash equivalents were $239.4 million at the end of 2003 as compared with $200.6 million at the end of 2002 and $29.3 million at the end of 2001. Total debt less cash and cash equivalents at December 31, 2003, was $1,462.5 million, representing the lowest levels in our company since 1994. Total debt has been reduced by $820.1 million or 32.5% since December 31, 2001. This reduction since December 31, 2001, is a result of strong cash flows from operating activities including the receipt of tax refunds of approximately $152 million and a successful asset divestiture and joint venture program that produced more than $500 million of net cash proceeds.

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Cash Flow

We believe our ability to generate cash from operations to reinvest in our business is one of our fundamental financial strengths. Cash flows from operating activities were $374.1 million in 2003 and included payments of $27.1 million, net of insurance recoveries, to resolve certain litigation matters. Excluding these litigation payments, cash flows from operating activities were $401.2 million, ahead of our guidance range of $350 to $400 million (our target range specifically excluded any potential impact from litigation matters). Also included in our actual and projected 2003 amounts and our 2003 guidance range was the receipt of a $94.5 million tax refund. Cash flows from operating activities in 2002 were $352.2 million and included a $57.1 million tax refund and a $10.1 million escrow receipt from the sale of our French insurance company. Had we not incurred these net litigation payments or received the tax refunds and escrow receipt, cash flows from operating activities in 2003 would have been $306.7 million compared to $285.0 million in 2002, representing an increase of $21.7 million or 7.6%. The increase is primarily attributable to reductions in cash interest paid. We also had improvements in working capital in North America associated with reduced preneed selling costs which helped to offset reduced operating cash flows from our French operations.

Our investing activities resulted in a net cash outflow of $37.4 million in 2003 compared to a net cash inflow of $326.9 million in 2002. The change is primarily due to a reduction in proceeds from asset sales and joint ventures, increases in capital expenditures and additional deposits to restricted cash as we decided to replace certain letters of credit with cash collateral.

Net cash used in financing activities was $300.1 million in 2003 compared to $505.5 million in 2002. The net cash used in both periods is primarily due to our continued focus on debt reduction. Repayments of long term debt were $291.3 million in 2003 and $383.1 million in 2002. Included in 2002 was a use of cash of $57 million related to the final settlement of certain options associated with our 6.3% notes due 2003.

Cash flows from operating activities in 2004 are expected to be $270 to $310 million, excluding the $100 million payment related to the proposed settlement of certain Florida litigation matters in February 2004 and the possibility of payments that could be made associated with other litigation related matters. It also excludes any receipts from insurance recoveries related to litigation matters and any cash contributions to our frozen pension plan. Anticipated improvements in North America funeral and cemetery margins and reduced interest expense are expected to offset the loss of cash flows from operating activities in 2004 as a result of the joint venture of France, the discontinued use of surety bonding in Florida prospectively.

Capital Expenditures

For 2003, capital expenditures totaled $115.6 million compared to $99.9 million in 2002 and $74.9 million in 2001. Of the total capital expenditures in 2003, $34.3 million was associated with our funeral operations in France, which was divested in a joint venture on March 11, 2004. Capital spending for items that we believe are necessary to maintain our existing facilities in a condition consistent with Company standards and extend their useful lives amounted to $87.2 million in 2003 as compared to $72.9 million in 2002 and $74.0 million in 2001. The increase in capital improvement spending at our existing facilities in 2003 was planned as we continue to focus on the quality of our facilities to ensure that they are consistent with standards that we have established related to our national branding strategy and that we are competitive in our respective markets. Capital spending associated with new growth initiatives was $29.2 million in 2003 compared to $27.1 million in 2002. Included in these amounts are approximately $10 million in 2003 and 2002 associated with your operations in France. These expenditures are intended to grow revenues and profits and are primarily related to the construction of cemetery property inventory and the construction of funeral home facilities on SCI-owned cemeteries.

Total capital expenditures in 2004 are expected to be $100 million to $120 million. Of the total projected capital expenditures in 2004, we expect to spend approximately $65 to $70 million on capital improvements to maintain our existing facilities. Growth-oriented capital spending in North America is expected to increase due to investments in new funeral home facilities, Dignity ® product displays in our funeral homes, and in developing strategic high-end cemetery property.

Liquidity

We believe we have sufficient liquidity and that our financial position is sound. As of December 31, 2003, we had a cash balance of approximately $240 million plus approximately $115 million of availability under a $185 million bank credit facility. We have no cash borrowings under this credit facility, but we have issued approximately $70 million of letters of credit under the facility. In February 2004, we paid $100 million into escrow to settle certain litigation matters in Florida. We expect this payment to be partially offset by the receipt of $25 million from recoveries under the first layer of our insurance coverage in 2004. On March 11, 2004, we

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successfully completed a joint venture of our funeral operations in France and received approximately $300 million in net cash proceeds while retaining a 25% minority interest in the acquiring company. In the first quarter of 2004, we made a voluntary cash contribution of $20 million to our frozen pension plan to increase the fair value of plan assets. For further details regarding this pension plan, see note fourteen to the consolidated financial statements in Item 8 of this Form 10-K. Beginning in early 2004, we discontinued the use of surety bonding for the prospective sale of preneed cemetery contracts in the state of Florida and have elected to deposit customer receipts from the sale of preneed contracts into trust funds. As a result of this change, we expect our cash flows from operations to decline by $15 to $20 million in 2004. Pending a successful public offering transaction, we expect to receive proceeds of approximately $50 to $60 million in the second quarter of 2004 associated with the sale of our holdings in stock and notes in operations in the United Kingdom.

At December 31, 2003, the maturity schedule for outstanding public notes due in the near and intermediate term was as follows:

	Outstanding at December 31, 2003
7.375% notes due April 2004	$ 111.2
8.375% notes due December 2004	$ 50.8
6.0% notes due December 2005	$ 272.5
7.2% notes due June 2006	$ 150.0

Based on our cash balance and credit availability, expectations of future cash flows from operating activities and asset sales, and proceeds received from the joint venture of France, we believe that we have adequate means to meet the near and intermediate term debt obligations as well as our operating needs.

Contractual, Commercial and Contingent Commitments

We have assumed various financial obligations and commitments in the ordinary course of conducting our business. We have contractual obligations requiring future cash payments under existing contractual arrangements, such as management, consulting and non-competition agreements. We also have commercial and contingent obligations which result in cash payments only if certain contingent events occur requiring our performance pursuant to a funding commitment.

The following table details our known future cash payments (on an undiscounted basis) related to various contractual obligations as of December 31, 2003.

	Payments Due By Period				
Contractual Obligations	**2004**	**2005 - 2006**	**2007 - 2008**	**Thereafter**	**Total**
Current maturities of long-term debt [1]	$ 182,682	$	$	$	$ 182,682
Long-term debt [1]		477,958	668,376	422,449	1,568,783
Interest payments on long-term debt	110,537	150,937	109,995	41,248	412,717
Casket purchase agreement [2]	100,000	187,000			287,000
Operating lease agreements [3]	50,138	65,978	29,873	27,986	173,975
Contingent purchase obligation [4]		53,000			53,000
	50,110	43,889	13,597	7,361	114,957

Management, consulting and non-competition agreements (5)					
Total contractual obligations	$ 493,467	$ 978,762	$ 821,841	$ 499,044	$ 2,793,114

(1) Our outstanding indebtedness contains standard provisions, such as payment delinquency default clauses and change of control clauses. In addition, our bank credit agreement contains a maximum leverage ratio and a minimum interest coverage ratio. Our outstanding indebtedness includes $25.4 million principal balance of capital lease obligations of which $24.2 million was associated with capital leases of our French operations. For further information see note nine to the consolidated financial statements included in this Form 10-K.

(2) We have executed a purchase agreement with a major casket manufacturer for our North America operations with an original minimum commitment of $750 million, covering a six-year period, which will expire in 2004. The agreement contains provisions for annual price adjustments and provides for a one-year extension to December 31, 2005 in which we are allowed to satisfy any remaining commitment that exists at the end of the original term. At December 31, 2003, our remaining maximum commitment under the purchase agreement was $287 million. Based on our historical purchases, we expect to exercise our option to extend the terms of the agreement for one year and expect to fulfill our commitment without any economic loss.

(3) The majority of our operating leases contain options to (i) purchase the property at fair value on the exercise date, (ii) purchase the property for a value determined at the inception of the leases, or (iii) renew for the fair rental value at the end of the primary lease term. Our operating leases primarily relate to funeral service locations, automobiles, limousines, hearses, cemetery operating and maintenance equipment and two aircraft. Approximately $28 million of our operating leases are associated with facilities in our France operations. We have residual value exposures related to certain operating leases of approximately $7.6 million. We believe it is unlikely that we will have to make future cash payments related to these residual value exposures.

(4) In connection with certain acquisitions related to our South America operations, we entered into contingent purchase obligations with certain former owners of those businesses, which require us to pay additional consideration in any one year between 2003 and 2005, at the option of the former owners, based on the results of operations, as defined. The additional consideration may be partially paid in common stock at the discretion of the former owners. Presently, we expect the former owners to request the additional consideration in 2005 and estimate it to be a $53 million liability, which is recorded in Other liabilities in the consolidated balance sheet.

(5) We have entered into management employment, consulting and non-competition agreements which contractually require us to make cash payments over the contractual period. The agreements have been primarily entered into with certain officers and employees of the Company and former owners of businesses acquired. The contractual obligation amounts pertain to the total commitment outstanding under these agreements and may not be indicative of future expenses to be incurred related to these agreements due to cost rationalization programs completed by the Company.

We have not included amounts in this table for payments of pension contributions and payments for various postretirement welfare plans and postemployment benefit plans, as such amounts have not been determined beyond 2004. Furthermore, we have not presented the amounts associated with these obligations for 2004 since we are not required to make any payments to the plans. Still, as previously disclosed, we have voluntarily elected to contribute $20 million to our frozen pension plans in the first quarter of 2004.

The following table details our known potential or possible future cash payments (on an undiscounted basis) related to various commercial and contingent obligations as of December 31, 2003.

	Expiration By Period				
Commercial and Contingent Obligations	**2004**	**2005 - 2006**	**2007 - 2008**	**Thereafter**	**Total**
Surety obligations [1]	$ 241,856	$	$	$	$ 241,856
Letters of credit [2]	69,815				69,815
Representations and warranties [3]	7,194	13,543		18,386	39,123
Total commercial and contingent obligations	$ 318,865	$ 13,543	$	$ 18,386	$ 350,794

(1) To support our operations, we have engaged certain surety companies to issue surety bonds on behalf of the Company for customer financial assurance or as required by state and local regulations. The surety bonds are primarily obtained to provide assurance for our preneed funeral and cemetery obligations, which are appropriately presented as liabilities in the consolidated balance sheet as Deferred preneed funeral contract revenues and Deferred cemetery contract revenues. The total outstanding surety bonds at December 31, 2003, were $333 million. Of this amount, $310 million was related to preneed funeral and preneed cemetery obligations. When we obtain surety bonds, we are required to obtain 100% of our liability amount to perform

the services. When we deposit funds into state-mandated trust funds, however, we are often not required to deposit 100% of the liability amount. Therefore, in the event all of the surety companies canceled or did not renew our outstanding surety bonds, which are generally renewed for twelve-month periods, we would be required to either obtain replacement assurance or fund approximately $242 million, as of December 31, 2003, primarily into state-mandated trust accounts. At this time, we do not believe we will be required to fund material future amounts related to these surety bonds. We are currently evaluating our surety bonding program and may elect to discontinue the use of bonding in other states or cancel certain outstanding bonds and replace with funds in trusts in accordance with state regulations.

(2) We are occasionally required to post letters of credit, issued by a financial institution, to secure certain insurance programs or other obligations. Letters of credit generally authorize the financial institution to make a payment to the beneficiary upon the satisfaction of a certain event or the failure to satisfy an obligation. The letters of credit are generally posted for 1-year terms and are usually automatically renewed upon maturity until such time as we have satisfied the commitment secured by the letter of credit. We are obligated to reimburse the issuer only if the beneficiary collects on the letter of credit. We believe that it is unlikely we will be required to fund a claim under our outstanding letters of credit. In 2003, the full amount of the letters of credit

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were supported by our credit facility which expires July 2005.

(3) In addition to the letters of credit described above, we currently have contingent obligations of $39.1 million related to our asset sale and joint venture transactions. We have agreed to guarantee certain representations and warranties associated with such disposition transactions with letters of credit or interest bearing cash investments. We have interest bearing cash investments of $13.8 million included in Deferred charges and other assets pledged as collateral for certain of these contingent obligations. We do not believe we will ultimately be required to fund to third parties any claims against these representations and warranties.

Subsequent to December 31, 2003, we agreed to certain representations and warranties associated with the disposition of our investment in France. The undiscounted amount of the representations and warranties associated with the sale is approximately $36 million and includes indemnifications related to taxes and other obligations. This amount will be recorded in Other liabilities in our consolidated balance sheet.

Preneed Funeral and Cemetery Activities

In addition to selling our products and services to client families at the time of need, we believe an active funeral and cemetery preneed arrangement program, which complements our framework for long-term growth, can increase future market share in our service markets. Preneed arrangement is a means through which a customer contractually agrees to the terms of a funeral service, cremation service, and/or cemetery burial interment right, merchandise or cemetery service to be performed or provided in the future (that is, in advance of when needed or preneed).

Preneed Funeral Activities

When customers contractually prearrange their funeral services, we record an asset, Preneed funeral contracts, net, and a corresponding liability, Deferred preneed funeral contract revenues, net in our consolidated balance sheet for the contract price. The funeral revenues are deferred and will not be recognized in the consolidated statement of operations until the funeral services are performed or the merchandise is delivered. While some customers may pay for their contract in a single payment, most preneed funerals are sold on an installment basis over a period of one to seven years. On these installment contracts, we receive on average a down payment at the time of sale of approximately 11%. Historically, the majority of our preneed funeral trust contracts have not included a finance charge. Because the services or merchandise will not be provided until some time in the future, most states and provinces require that all or a portion of the funds collected from customers on preneed funeral contracts be protected for the benefit of the customer pursuant to applicable law. Some or all of the funds may be required to be placed into trust accounts, or a surety bond may be posted in lieu of trusting (collectively trust funded preneed funeral contracts). Alternatively, where allowed, customers may choose to purchase a life insurance or annuity policy from third party insurance companies to fund their preneed funeral (insurance funded preneed funeral contract). Only certain of these customer funding options may be applicable in any given market we serve.

Trust Funded Preneed Funeral Contracts: Where the applicable law requires that all or a portion of the funds collected from preneed funeral contracts be placed in trust accounts, the funds deposited into trust are invested by the independent trustees in accordance with the investment guidelines established by statute or, where the prudent investor rule is applicable, the guidelines established by our Investment Committee. The trustees utilize professional investment advisors to select and monitor the money managers that make the individual investment decisions in accordance with the guidelines. We retain any funds above the amounts required to be deposited into trust accounts and use them for working capital purposes, generally to offset the selling and administrative costs of the prearrangement programs. Applicable law governs the timing of the required deposits into the trust accounts, which generally ranges from five to 45 days after receipt of the funds from the customer.

The trust investments are expected to generate earnings sufficient to offset the inflationary costs of providing the preneed funeral services and merchandise in the future for the prices that were guaranteed at the time of sale. We believe the market value of the preneed funeral trust investments at December 31, 2003 exceeds the expected cost of meeting our obligations to provide funeral services and merchandise for the unperformed preneed funeral contracts. Investment earnings on funds placed into trust accounts are generally accumulated and deferred until each preneed contract is either utilized upon the death of, or cancelled by, the customer. However, in certain states, the trusts are allowed to distribute a portion of the investment earnings to us prior to that date. Until the preneed contract is utilized or cancelled, any investment earnings are attributed to the individual preneed funeral contract. These attributed investment earnings (whether distributed or undistributed) are recognized in our consolidated statement of operations when the merchandise is delivered and the services are performed following the death of the customer or when the contract is canceled and we are entitled to retain these earnings. Recognition of the investment earnings is independent of the timing of the receipt of the related cash flows.

Direct selling costs incurred pursuant to the sales of trust funded preneed funeral contracts are deferred and included in Deferred charges and other assets in the consolidated balance sheet. The deferred selling costs are expensed in proportion to the corresponding trust funded preneed funeral contract revenues when recognized. Other selling costs associated with the sales and marketing of preneed funeral contracts (e.g., lead procurements costs, brochures and marketing materials, advertising and administrative costs) are expensed as incurred. An allowance for cancellation is recorded for trust funded preneed funeral contract deferred selling costs based on historical contract cancellation experience.

If a customer cancels the trust funded preneed funeral contract, applicable law determines the amount of the refund owed to the customer, including in certain situations the amount of the attributed investment earnings. Upon cancellation, we receive the amount of principal deposited to trust and previously undistributed net investment earnings and pay the customer the required refund. We retain any excess funds and recognize the attributed investment earnings (net of any investment earnings payable to the customer) in our consolidated statement of operations. In certain jurisdictions, we may be obligated to fund any shortfall if the amounts deposited by the customer exceed the funds in trust. As a result, when realized or unrealized losses of a trust result in trust funded preneed funeral contracts being under-funded, we will assess those contracts to determine whether a loss provision should be recorded. We have not been required to recognize any loss amounts.

The cash flow activity over the life of a trust funded preneed funeral contract from the date of sale to its death maturity or cancellation is captured in the line item Net effect of preneed funeral production and maturities in the consolidated statement of cash flows. While the contract is outstanding, cash flow is provided by the amount retained from funds collected from the customer and any distributed investment earnings. This is reduced by the payment of trust funded preneed funeral deferred selling costs. The effect of amortizing trust funded preneed funeral deferred selling costs is reflected in Depreciation and amortization in the consolidated statement of cash flows. At the time of death maturity, we receive the principal and undistributed investment earnings from the trust and any remaining receivable due from the customer. This cash flow at the time of service is generally less than the revenue recognized, thus creating a negative effect on working capital cash flow from operating activities.

In certain situations pursuant to applicable laws, we can post a surety bond as financial assurance for an amount that would otherwise be required to be deposited in trust accounts for trust funded preneed funeral contracts. See the *Financial Assurances* section within this Financial Condition, Liquidity and Capital Resources section for further details on our practice of posting such surety bonds. We believe the deferred revenues associated with preneed funeral bonded contracts exceed the expected cost of meeting our obligations to provide funeral services and merchandise for the outstanding preneed funeral bonded contracts, and our future operating cash flows will be sufficient to fulfill these contracts without use of the surety bonds.

If a customer cancels the trust funded preneed funeral contract that has been bonded prior to death maturity, applicable law determines the amount of the refund owed to the customer. Because the funds have not been held in trust, there are no earnings to be refunded to the customer or us. We pay the customer refund out of our operating funds, which reduces working capital cash flow from operating activities.

The cash flow activity over the life of a trust funded preneed funeral contract that has been bonded from the date of sale to its death maturity or cancellation is captured in the line item Net effect of preneed funeral production and maturities in the consolidated statement of cash flows. The payments received from our customers for their trust funded preneed funeral contracts that have been bonded are a source of working capital cash flow from operating activities until the contracts mature. This is reduced by the payment of deferred selling costs, the premiums to the surety companies for the bond coverage, and refunds on customer cancellations of contracts. When a trust funded preneed funeral contract that has been bonded matures upon the death of the beneficiary, there is no additional cash flow to us unless the customer owed an outstanding balance.

Insurance Funded Preneed Funeral Contracts: Where permitted, customers prearrange their funeral contract by purchasing a life insurance or annuity policy from third party insurance companies, for which we earn a commission for being the general agent for the insurance company. The policy amount of the insurance contract between the customer and the third party insurance company generally equals the amount of the preneed funeral contract. However, we do not reflect the unfulfilled insurance funded preneed funeral contract amounts in our consolidated balance sheet.

The third party insurance company collects funds related to the insurance contract directly from the customer. The life insurance contracts include increasing death benefit provisions, which are expected to offset the inflationary costs of providing the preneed funeral services and merchandise in the future for the prices that were guaranteed at the time of the preneed sale. Increasing insurance benefits or death benefits payable by third party insurance companies increase annually pursuant to the terms of the life insurance policies purchased in advance of need by our customers to fund their funerals. The customer/policy holder assigns the policy benefits to our funeral home to pay for the preneed funeral contract at the time of need. Approximately 63% of our 2003 North America preneed funeral production was insurance funded preneed funeral contracts.

The commission we earn for being the general agent on behalf of the third party insurance companies is based on a percentage per contract sold. These general agency (GA) revenues are recognized as funeral revenues when the insurance purchase transaction between the customer and third party insurance provider is completed. Prior to January 1, 2003, we recognized these GA revenues as reductions to selling expenses in the consolidated statement of operations. In 2003, we began recognizing these amounts as funeral revenues. We have reclassified the prior year amounts to conform to the current period presentation with no effect on previously reported results of operations, financial condition, or cash flows. Direct selling costs incurred pursuant to the sale of insurance funded preneed funeral contracts are expensed as incurred. GA revenues recognized by us totaled approximately $27.7 million, $47.1 million and $43.3 million, and direct selling costs expensed by us totaled approximately $23.9 million, $34.1 million and $37.3 million for the years ended December 31, 2003, 2002 and 2001, respectively, in connection with sales of insurance funded preneed funeral contracts.

Additionally, we may receive cash overrides based on achieving certain dollar volume targets of life insurance policies sold as a result of marketing agreements entered into in connection with the sale of our insurance subsidiaries in 2000. These overrides are recorded in Other income, net, in the consolidated statement of operations.

If a customer cancels the insurance funded preneed funeral contract prior to death maturity, the insurance company pays the cash surrender value under the insurance policy directly to the customer. If the contract was outstanding for less than one year, the insurance company charges back the GA revenues and overrides we received on the contract. An allowance for these chargebacks is included in the consolidated balance sheet based on our historical chargeback experience.

The cash flow activity over the life of an insurance funded preneed funeral contract from the date of sale to its death maturity or cancellation is captured in the consolidated statement of cash flows as cash flows from operating activities within our funeral segment. While the unfulfilled insurance funded preneed funeral contracts are not included in the consolidated balance sheet, they are included in funeral trade accounts receivable and funeral revenues when the funeral service is performed. Proceeds from the life insurance policies are used to satisfy the receivables due. The cash flow activity associated with these contracts generally occurs at the time of sale, where the GA revenues received net of the direct selling costs provide a net source of cash flow, and at death maturity, where the insurance proceeds (including increasing death benefit) less the funds used to provide the funeral goods and services provide a net source of cash flow. If the cancellation occurs within the one year following the date of sale, our cash flow is reduced by the charge-back of GA revenues and overrides.

An allowance for cancellation, based on historical experience, is provided in Preneed funeral contracts, net, and Deferred preneed funeral contract revenues, net, in the consolidated balance sheet.

The table below details the North America results of trust and insurance funded preneed funeral production for the years ended December 31, 2003 and 2002 and the related deferred selling costs incurred to obtain the trust funded preneed arrangements. Additionally, the table reflects revenues and previously deferred trust funded preneed funeral contract selling costs recognized in the consolidated statement of operations associated with death maturities of preneed funeral contracts for the years ended December 31, 2003 and 2002.

(In millions)	**North America Funeral**	
	2003	**2002**

		(Restated)
Preneed Production:		
Trust	$ 99.7	$ 146.4
Insurance (1)	237.7	290.2
Total	$ 337.4	$ 436.6
Trust funded preneed funeral deferred selling costs	$ 13.4	$ 17.0
Death Maturity:		
Previous preneed production included in current period revenues	$ 173.7	$ 147.6
Insurance	165.8	202.6
	$ 339.5	$ 350.2
Amortization/recognition of trust funded preneed funeral deferred selling costs in current period	$ 9.2	$ 9.4

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(1) Amounts are not included in the consolidated balance sheet.

The following table reflects the total North America backlog of deferred preneed funeral contract revenues included in our consolidated balance sheet at December 31, 2003 and 2002. Additionally, we have reflected the North American backlog of unfulfilled insurance funded contracts (not included in our consolidated balance sheet) and total North American backlog of deferred preneed funeral contract revenues at December 31, 2003 and 2002. The backlog amounts presented are reduced by an amount that we believe will cancel before maturity. The preneed funeral deferred selling costs associated with trust funded contracts (net of an estimated allowance for cancellations) are included with preneed cemetery deferred selling costs as a component of Deferred charges and other assets.

(In millions)	North America Funeral	
	2003	2002 (Restated)
Backlog of trust funded preneed funeral revenues (1)	$ 1,501.6	$ 1,633.6
Backlog of insurance funded preneed funeral revenues (2)	2,018.4	2,004.7
Total backlog of preneed funeral revenues (total of (1) and (2))	$ 3,520.0	$ 3,638.3
Deferred selling costs associated with trust funded deferred preneed funeral revenues	$ 95.4	$ 91.1

(1) Net of estimated cancellation reserve.

(2) Net of estimated cancellation reserve. Insurance funded preneed funeral contracts are not included in the consolidated balance sheet.

Preneed Cemetery Activities

When purchasing cemetery property interment rights, merchandise, and services on a preneed basis, approximately 30% of our consumers choose to pay 100% of the contract at the time of sale. The remaining customers choose to pay for their contracts on an installment basis generally over a period of one to seven years. On these installment contracts, we receive an average down payment at the time of sale of approximately 14%. Historically, the installment contracts have included a finance charge ranging from 3.5% to 15.7% depending on the date sold, the payment period selected, state laws and the payment method (i.e., monthly statement billing or automated bank draft). Unlike preneed funeral contracts, where the entire purchase price is deferred and the revenue is recognized as one event at the time of death maturity, the revenues associated with a preneed cemetery contract can be recognized as different contract events occur. Preneed sales of cemetery interment rights (cemetery burial property) are recognized when a minimum of 10% of the sales price has been collected and the property has been constructed. With the customer s direction, which is generally obtained at the time of sale, we can choose to order, store, and transfer title to the customer of their personalized marker merchandise. Upon the earlier of vendor storage of these items or delivery in our cemetery, we recognize the associated revenues and record the cost of sale. For services, personalized marker merchandise where the customer chooses not to elect vendor storage or early delivery to our cemetery, and non-personalized merchandise (such as vaults), we defer the revenues until the services are performed and the merchandise is delivered.

Because the services or merchandise will not be provided until some time in the future, all or a portion of the proceeds from the sale of preneed cemetery merchandise and services may be required by law to be paid into merchandise and services trusts until the merchandise is delivered or the service is provided. As with trust funded preneed funeral contracts, the funds deposited into trust are invested by the independent trustees in accordance with the investment guidelines established by statute or, where the prudent investor rule is applicable, the guidelines as established by our Investment Committee. The trustees utilize professional investment advisors to select and monitor the money managers that make the investment decisions in accordance with the guidelines. We retain any funds above the amounts required to be deposited into trust accounts and use them for working capital purposes, generally to defray the selling costs of obtaining the contracts. Applicable law governs the timing of the required deposits into the trust accounts, which generally ranges from five to 45 days after receipt of the funds from the customer. In certain situations pursuant to applicable laws, we post a surety bond as financial assurance for a certain amount of the preneed cemetery contract in lieu of placing funds into trust accounts. See the *Financial Assurances* section within this Financial Condition, Liquidity and Capital Resources section for further details on our practice of posting such surety bonds.

The trust investments are expected to generate earnings sufficient to offset the inflationary costs of providing the preneed cemetery services and merchandise in the future for the prices that were guaranteed at the time of sale. We believe the current market value of the preneed cemetery trust investments at December 31, 2003 exceeds the expected cost of meeting our obligations to provide the cemetery services and merchandise for the outstanding preneed cemetery contracts. Investment earnings on funds placed into trust accounts are generally accumulated and deferred until the delivery of each preneed contract item. However, in certain states, the trustees are allowed to distribute a portion of the investment earnings to us before the preneed cemetery service or merchandise item is delivered (distributable states). Until delivered, any investment earnings are attributed to the individual contract items. Upon delivery, these attributed investment earnings (whether distributed or undistributed) are recognized in our consolidated statement of operations along with the revenues associated with the related contract item. Recognition of the net investment earnings is independent of the timing of the receipt of the related cash flows, but generally will be the same in states that are not distributable states.

We are generally required by law to deposit a portion of the proceeds from the sale of cemetery property interment rights (burial property) into perpetual care trust funds. Earnings, and in some cases realized capital gains, from these perpetual care trust funds are used to defray the maintenance costs of our cemeteries.

Direct selling costs incurred pursuant to the sales of preneed cemetery contracts are deferred and included in Deferred charges and other assets in the consolidated balance sheet. The deferred selling costs are expensed in proportion to the corresponding revenues when recognized. Other selling costs associated with the sales and marketing of preneed cemetery contracts (e.g., lead procurements costs, brochures and marketing materials, advertising and administrative costs) are expensed as incurred. An allowance for cancellation is recorded for cemetery deferred selling costs based on historical contract cancellation experience.

If a preneed cemetery contract is canceled prior to delivery, applicable law determines the amount of the refund owed to the customer, if any, including the amount of the attributed investment earnings. Upon cancellation, we receive the amount of principal deposited to trust and previously undistributed investment earnings and, where required, issue a refund to the customer. We retain any excess funds and recognize the attributed investment earnings (net of any investment earnings payable to the customer) in our consolidated statement of operations. Based on our historical experience, we have included an allowance for cancellation for preneed cemetery contracts in Preneed cemetery contracts, net, and Deferred cemetery contract revenues, net, in our consolidated balance sheet.

As the preneed cemetery contract merchandise and service items for which we were required to deposit funds to trust are delivered and recognized as revenues, we receive the principal and previously undistributed investment earnings from the trust. There is generally no remaining receivable due from the customer, as our policy is to deliver preneed cemetery merchandise and service items only upon payment of the contract balance in full. This cash flow at delivery is generally less than the revenue recognized, thus creating a negative effect on working capital cash flow from operating activities, especially if we posted a surety bond in lieu of trusting for the preneed cemetery contract merchandise and service items, as there are no funds in trust available for withdrawal.

The cash flow activity from the date of sale of a preneed cemetery contract (origination) to the date of the recognition of the deferred revenue upon its delivery or cancellation (maturity) is reported in the Net effect of preneed cemetery production and deliveries line item in the consolidated statement of cash flows. Net effect of preneed cemetery production and deliveries is affected by cash flows provided by the amount retained from funds collected from the customer and distributed trust earnings, reduced by the use of funds for the payment of deferred selling costs when the preneed cemetery contracts are originated. The amortization of the cemetery deferred selling costs is included in Depreciation and amortization in the consolidated statement of cash flows.

The table below details the North America results of preneed cemetery production which has been deferred for the years ended December 31, 2003 and 2002 and the related deferred selling costs incurred to obtain the contract items. Additionally, the table reflects previously deferred revenues and previously deferred selling costs recognized in the consolidated statements of operations associated with deliveries of cemetery contract items for the years ended December 31, 2003 and 2002.

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(In millions)	North America Cemetery 2003	North America Cemetery 2002 (Restated)
Origination:		
Revenue which has been deferred	$ 215.7	$ 303.2
Deferred selling costs, net	$ 42.0	$ 44.2
Recognition:		
Previous deferred revenue included in current period revenues	$ 217.8	$ 288.8
Amortization/recognition of deferred selling costs in current period	$ 35.9	$ 42.2

The following table reflects the total North America backlog of deferred cemetery contract revenues and the related preneed cemetery contract assets included in our consolidated balance sheet at December 31, 2003. Deferred cemetery contract revenues are greater than the related preneed cemetery contract assets primarily due to cash collections allowed to be retained by us in accordance with applicable laws, partially offset by contract amounts where the revenue can be recognized at the date of sale (contracts which include constructed cemetery interment rights where we received at least 10% of the sale price).

(In millions)	North America Cemetery 2003	North America Cemetery 2002 (Restated)
Deferred cemetery contract revenues, net	$ 1,574.2	$ 1,628.5
Deferred selling costs, net	$ 204.9	$ 197.7
Preneed cemetery contracts, net	$ 1,059.2	$ 1,129.4

Deferred preneed cemetery contract revenues, net, and Preneed cemetery contracts, net (which consist of amounts due from trusts and customer receivables, net), are reflected separately in the consolidated balance sheet. The preneed cemetery deferred selling costs (net of an estimated allowance for cancellation) are included with preneed funeral deferred selling costs as a component of Deferred charges and other assets.

Financial Assurances

In support of operations, we have entered into arrangements with certain surety companies whereby such companies agree to issue surety bonds on our behalf as financial assurance and/or as required by existing state and local regulations. The surety bonds are used for various business purposes; however, the majority of the surety bonds issued and outstanding have been used to support our preneed funeral and preneed cemetery sales activities. The underlying obligations these surety bonds assure are recorded on the consolidated balance sheet as Deferred preneed funeral contract revenues, net and Deferred preneed cemetery contract revenues, net (see notes five and six to the consolidated financial statements and *Preneed Funeral and Cemetery Activities* within Financial Condition, Liquidity and Capital Resources of this Form 10-K for further details regarding our preneed funeral and cemetery activities). The breakdown of bonds between funeral and cemetery preneed arrangements, as well as surety bonds for other activities, is as follows:

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(In millions)		**December 31, 2003**
Preneed funeral	$	125.6
Preneed cemetery:		
Merchandise and services		179.6
Preconstruction		18.1
Bonds supporting preneed funeral and cemetery obligations		323.3
Bonds supporting preneed business permits		4.8
Other bonds		4.7
Total bonds outstanding	$	332.8

When selling preneed funeral contract and preneed cemetery contracts, we intend to post surety bonds where allowed by applicable law, except as noted below for Florida. We post the surety bonds in lieu of trusting a certain amount of funds received from the customer. The amount of the bond posted is determined by the total amount of the preneed contract that would otherwise be required to be trusted, in accordance with applicable state law. During 2003 and 2002, we recorded $90.8 million and $95.5 million, respectively, in cash receipts attributable to bonded sales. These amounts do not consider reductions associated with taxes, selling costs or other costs.

Surety bond premiums are paid annually and are automatically renewable until maturity of the underlying preneed contracts, unless we are given prior notice of cancellation. Except for cemetery preconstruction bonds (which are irrevocable), the surety companies generally have the right to cancel the surety bonds at any time with appropriate notice. In the event a surety company was to cancel the surety bond, we are required to obtain replacement assurance from another surety company or fund a trust for an amount generally less than the posted bond amount. A quantitative detail of this subject is discussed in the *Contractual, Commercial and Contingent Commitments* section included within Financial Condition, Liquidity and Capital Resources. We do not believe we will be required to fund any material future amounts related to these surety bonds.

The applicable Florida law that allows posting of surety bonds for preneed contracts expires December 31, 2004; however, it allows for preneed contracts entered into prior to December 31, 2004 to continue to be bonded for the remaining life of those contracts. Thus, we are required to change from bonding to either trust or insurance funding for new preneed funeral and cemetery contracts in Florida by December 31, 2004. We have elected to change to trust funding as of February 1, 2004. Of the total bonding contract proceeds we received from customers for 2003 and 2002, approximately $67.1 million and $70.3 million, respectively, were attributable to Florida contracts. Assuming our preneed funeral and cemetery sales in Florida in 2004 is consistent with production for the full year of 2003, we forecast a negative impact on our cash flow from operations of approximately $15 to $20 million, net of trust receipts in 2004.

Cautionary Statement on Forward-Looking Statements

The statements in this Form 10-K that are not historical facts are forward-looking statements made in reliance on the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995. These statements may be accompanied by words such as believe , estimate , project , expect , anticipate , or predict that indicate th uncertainty of future events or outcomes. These statements are based on assumptions that we believe are reasonable: however, many important factors could cause our actual consolidated results in the future to differ materially from the forward-looking statements made herein and in any other documents or oral presentations made by, or on behalf of, the Company. These factors are discussed below. We assume no obligation to publicly update or revise any forward-looking statements made herein or any other forward-looking statements made by the Company, whether as a result of new information, future events or otherwise.

Our ability to execute our strategic plan depends on many factors, many of which are beyond our control.

Our strategic plan is focused on reducing overhead costs, increasing cash flow, asset redeployment, and reducing debt while at the same time developing key revenue initiatives designed to generate future internal growth in our core funeral and cemetery operations without the outlay of significant additional capital. Many of the factors necessary for the execution of our strategic plan are beyond our control. We cannot give assurance that we will be able to execute any or all of our strategic plan. Failure to execute any or all of the strategic plan could have a material adverse effect on us, our financial condition, results of operations, or cash flows.

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Our indebtedness limits funds available for our operations.

As of December 31, 2003, we had approximately $1.7 billion in indebtedness. Our indebtedness may limit our ability to obtain additional financing and require the dedication of more cash flow to service our debt than we desire. Furthermore, it may require sale of assets or limit our flexibility in planning for, or reacting to, changes in our markets. Our ability to satisfy our indebtedness in a timely manner will be dependent on the successful execution of our long-term strategic plan and the resulting improvements in our operating performance.

Our existing credit agreements and indentures contain covenants that may prevent us from engaging in certain transactions.

Our existing credit agreements and indentures contain, among other things, various affirmative and negative covenants that may prevent us from engaging in certain transactions that might otherwise be considered beneficial to us. These covenants limit, among other things, our and our subsidiaries ability to:

§ Borrow money;

§ Pay dividends or make distributions;

§ Purchase or redeem stock;

§ Make investments;

§ Engage in transactions with affiliates;

§ Engage in sale-leaseback transactions; and

§ Consummate certain liens on assets.

The credit agreement also requires us to maintain certain financial ratios and satisfy other financial condition tests. Although the maturity of our bank credit agreement brings an end to the restrictions created by it, any future credit agreements or indentures may contain terms and conditions that are more or less restrictive than those of the existing bank credit agreement and indentures.

If we lost the ability to use surety bonding to support our prearranged funeral and preneed cemetery activities, we could have to make material cash payments to fund certain trust funds.

We have entered into arrangements with certain surety companies whereby such companies agree to issue surety bonds on our behalf, as financial assurance and/or as required by existing state and local regulations. The surety bonds are used for various business purpose; however, the majority of the surety bonds issued and outstanding have been issued to support our preneed funeral and preneed cemetery activities. The applicable Florida law that allows posting of surety bonds for preneed contracts will expire December 31, 2004. Thus, we are required to change from bonding to either trust or insurance funding for new preneed funeral and cemetery contracts in Florida by December 31, 2004. We have elected to change to trust funding as of February 1, 2004. Of the total bonding contract proceeds we received from customers for 2003 and 2002, approximately $67.1 million and $70.3 million, respectively, were attributable to Florida contracts. Assuming our preneed funeral and cemetery sales in Florida in 2004 is consistent with production for the full year of 2003, we forecast a negative impact on our cash flow from operations of approximately $15 to $20 million, net of prospective trust receipts in 2004. In subsequent years, we do not expect the impact on cash flows from operations to be material. Furthermore, our future cash flows could be materially affected if we lost access to using surety bonds for financial assurance in our normal course of business. We are currently evaluating our surety bonding program and may elect to discontinue the use of bonding in other states or cancel certain outstanding bonds and replace with funds in trusts in accordance with state regulations.

The funeral home and cemetery industry is becoming increasingly competitive.

In North America and most international markets in which we operate, the funeral and cemetery industry is characterized by a large number of locally owned, independent operations. To compete successfully, our funeral service locations and cemeteries must maintain good reputations and high professional standards in the industry, as well as offer attractive products and services at competitive prices. In addition, we must market our company in such a manner as to distinguish us from our competitors. If we are unable to successfully compete, our company, our financial condition, results of operations and cash flows could be materially adversely affected.

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Our affiliated funeral and cemetery trust funds own investments in equity securities and mutual funds, which are affected by financial market conditions that are beyond our control.

In connection with our preneed funeral operations and preneed cemetery merchandise and service sales, affiliated funeral and cemetery trust funds own investments in equity securities and mutual funds. Our earnings and investment gains and losses on these equity securities and mutual funds are affected by financial market conditions that are beyond our control. If our earnings from our trust funds decline, we would likely experience a decline in future revenues. In addition, if the trust funds experienced significant investment losses, there would likely be insufficient funds in the trusts to cover the costs of delivering services and merchandise or maintaining cemeteries in the future. We would have to cover any such shortfall with cash flows, which could have a material adverse effect on us, our financial condition, results of operations, or cash flows.

As of December 31, 2003, net unrealized appreciation in the preneed funeral and cemetery merchandise and services trust funds amounted to $18.8 million and $48.7 million, respectively. The perpetual care trust funds had net unrealized appreciation of $24.8 million as of December 31, 2003. The following table summarizes the investment returns excluding fees on our trust funds for the last three years.

	2003	2002	2001
Prearranged funeral trust funds	17.9%	(7.6)%	1.7%
Cemetery merchandise services trust funds	17.1%	(5.5)%	1.0%
Perpetual care trust funds	12.6%	5.3%	4.3%

Increasing insurance benefits related to preneed funeral contracts funded through life insurance or annuity contracts may not cover future increases in the cost of providing a price guaranteed funeral service.

We sell price guaranteed preneed funeral contracts through various programs providing for future funeral services at prices prevailing when the agreements are signed. For preneed funeral contracts funded through life insurance or annuity contracts, we receive in cash a general agency commission of approximately 14% of the total sale from the third party insurance company. Additionally, we accrue an increasing insurance benefit associated with the contract of approximately 1% per year to be received in cash by us at the time the funeral is performed. There is no guarantee that the increasing insurance benefit will cover future increases in the cost of providing a price guaranteed funeral service, which could materially adversely affect our future cash flows, revenues and profit margins.

We may not be able to joint venture or sell our international operations on acceptable terms or at all.

Our long-term strategic plan includes the joint venture or sale of our remaining international operations outside of North America in order to create cash proceeds to reduce debt. On March 11, 2004, we completed the joint venture of our funeral operations in France having received approximately $300 million in net cash proceeds. However, if we are unable to joint venture or sell our South America or other international operations on acceptable terms or otherwise, it could adversely affect our ability to achieve our strategic plan.

Our foreign operations and investments involve special risks.

Our activities in areas outside the United States are subject to risks inherent in foreign operations, including the following:

§ Loss of revenue, property and equipment as a result of hazards such as expropriation, nationalization, wars, insurrection and other political risks;

- § The effects of currency fluctuations and exchange controls, such as devaluation of foreign currencies and other economic problems; and
- § Changes in laws, regulations, and policies of foreign governments, including those associated with changes in the governing parties.

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We are the subject of lawsuits in Florida that, if not settled in accordance with the agreement in principle with respect thereto, could have a negative effect on our financial condition, results of operations and cash flows and we may be subject to additional class action or other significant lawsuits in the future.

On December 2, 2003, we announced that we entered into an agreement in principle to settle the class action lawsuit and all individual related lawsuits pending against us involving Florida s Menorah Gardens and Funeral Chapels (the Florida litigation), with the exception of two lawsuits pending in Palm Beach County, Florida. All claims under the Florida litigation would be dismissed if final court approval of the settlement is obtained.

The terms of the proposed settlement call for us to make payments totaling approximately $100 million in settlement of these claims. As of December 31, 2003, we have recorded reserves of $100 million related to the Florida litigation. In the fourth quarter of 2003, we recognized a receivable of $25 million for expected recoveries under one primary layer of the Company s insurance coverage related to this litigation. We have a substantial face amount of insurance coverage remaining, although there are various unresolved insurance coverage disputes.

If the settlement is not approved by the court, the proceedings and litigation will continue. We cannot assure you that the results of any such continued proceedings and litigation would be on terms as favorable as those of the current settlement agreement.

In addition, on May 21, 2003, the Special Assistant State Attorney for Palm Beach County, Florida, filed criminal charges against the Company, a Florida subsidiary and certain individuals. The criminal charges involve allegations of misconduct by the Company and its Florida subsidiary, including allegations similar to those in the Florida litigation. In February 2004, the Company negotiated a plea arrangement with the Special Assistant State Attorney for Palm Beach County to resolve the criminal charges; however, the court rejected the plea arrangement.

In addition, we are involved in other litigation proceedings in the ordinary course of business. There is a risk that one of the lawsuits that we do not view as significant at the moment, or an additional lawsuit brought in the future, could have a material adverse effect on us, our financial condition, results of operations, or cash flows.

We are the subject of securities fraud class action lawsuits that, if decided against us, could have a negative effect on our financial condition, results of operations and cash flows.

In January 1999, numerous putative class-action lawsuits were filed in the United States District Courts for the Southern and Eastern Districts of Texas, on behalf of persons and entities who (1) acquired shares of our common stock in the merger with Equity Corporation International (ECI); (2) purchased shares of our common stock in the open market during the period from July 17, 1998 through January 1999 (referred herein as the class period); (3) purchased call options in the open market during the class period; (4) sold put options in the open market during the class period; (5) held employee stock options in ECI that became options to acquire our stock pursuant to the ECI merger; and (6) held employee stock options to purchase our common stock under a plan during the class period. These actions have been consolidated into one lawsuit in the federal court in Houston, Texas. The consolidated complaint alleges that we and three of our current or former executive officers and directors violated federal securities laws by making false and misleading statements and failing to disclose material information concerning our prearranged funeral business and other financial matters, including in connection with the ECI merger. Plaintiffs allege damages based on the market loss, during the class period, of the outstanding shares, including those exchanged in the ECI merger. In October 1999, we filed a motion to dismiss the consolidated complaint that has not been ruled on by the court. The parties have met on at least two occasions to discuss a possible resolution of this case, but no progress has been made. We anticipate that another meeting will be held in mid-April 2004 to discuss a possible resolution of this matter.

The ultimate outcome of the stockholder class-action cannot be determined at this time. The class-action lawsuit seeks to recover an unspecified amount of monetary damages. Certain insurance policies held by us may limit our cash outflows in the event of a decision adverse to us in these matters. If the legal costs or the damages awarded against us exceed the insurance coverage, if the insurance coverage is determined not to apply to these amounts, or if an insurance carrier is unable to pay, we would have to pay them out of our own funds, which could have a material adverse effect on us, our financial condition, results of operations or cash flows.

If the number of deaths in our markets declines, our cash flows and revenues may decrease.

The United States Bureau of the Census estimates that the number of deaths in the United States will increase up to one percent per year from 2000 to 2010. However, longer life spans could reduce the number of deaths. If the number of deaths declines, the number of funeral services and interments performed by us will decrease and our financial condition, results of operations and cash flows may be materially adversely effected.

The growing trend in the number of cremations performed in North America could result in lower revenue and gross profit dollars.

In the death care industry, there has been a growing trend in the number of cremations performed in North America as an alternative to traditional funeral service dispositions. In North America during 2003, 39.0% of the comparable funeral services performed by us were cremation cases compared to 37.9% and 36.7% performed in 2002 and 2001, respectively. In recent years we have continued to expand our cremation memorialization products and services which has resulted in higher average sales for cremation services. If we are unable to successfully expand our cremation memorialization products and services, we, our financial condition, results of operations, and cash flows could be materially adversely affected.

The funeral home and cemetery businesses are high fixed-cost businesses.

The majority of our operations throughout the world are managed in groups called markets . Markets are geographical groups of funeral service locations and cemeteries that share common resources such as operating personnel, preparation services, clerical staff, motor vehicles and preneed sales personnel. Personnel costs, the largest of the operating expenses for the company, are the cost components most beneficially affected by this grouping. We must incur many of these costs regardless of the number of funeral services or interments performed. Because we cannot necessarily decrease these costs when we experience lower sales volumes, the sales decline may cause margins, profits and cash flows to decline at a greater rate than the decline in revenues.

The funeral home and cemetery industry is highly regulated.

Our operations are subject to regulation, supervision, and licensing under numerous foreign, federal, state and local laws, ordinances and regulations, including extensive regulations concerning trust funds, preneed sales of funeral and cemetery products and services, and various other aspects of our business. The impact of such regulations varies depending on the location of our funeral and cemetery operations. Violations of applicable laws could result in fines or their sanctions to us.

In addition, from time to time, governments and agencies propose to amend or add regulations, which would increase costs and decrease cash flows. For example, foreign, federal, state, local and other regulatory agencies have considered and may enact additional legislation or regulations that could affect the death care industry. Some states and regulatory agencies have considered or are considering regulations that could require more liberal refund and cancellation policies for preneed sales of products and services, limit or eliminate our ability to use surety bonding, increase trust requirements and prohibit the common ownership of funeral homes and cemeteries in the same market. If adopted by the regulatory authorities of the jurisdictions in which we operate, these and other possible proposals could have a material adverse effect on us, our financial condition, results of operations and cash flows.

ITEM 7A. *Quantitative and Qualitative Disclosures About Market Risk.*

The information presented below should be read in conjunction with notes eight and nine to the consolidated financial statements in Item 8 of this Form 10-K.

We have historically used derivatives primarily in the form of interest rate swaps, cross-currency interest rate swaps, and forward exchange contracts in combination with local currency borrowings in order to manage our mix of fixed and floating rate debt and to hedge our net investment in foreign assets. We generally do not participate in derivative transactions that are leveraged or considered speculative in nature. We were not a party to any derivative transactions at December 31, 2003. Subsequent to December 31, 2003, we executed certain forward exchange contracts to hedge our net foreign investment in our France operations.

At December 31, 2003 and 2002, 99% of our total debt consisted of fixed rate debt at a weighted average rate of 6.95% and 6.87%, respectively.

Approximately 13% of our net investment and 55% of our operating income, excluding Gains impairment (losses) on dispositions, net, and other operating expenses, are denominated in foreign currencies, primarily the euro, at December 31, 2003. At December 31, 2002, approximately 8% of our net investment and 27% of our operating income excluding Gains and impairment (losses) on dispositions, net, and Other operating expenses were denominated in foreign currencies. We do not have a significant investment in foreign operations that are in highly inflationary economies.

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Marketable Equity and Debt Securities Price Risk

In connection with our preneed funeral operations and preneed cemetery merchandise and service sales, the related funeral and cemetery trust funds own investments in equity securities and mutual funds, which are sensitive to current market prices. Cost and market values as of December 31, 2003 and 2002 are presented in notes four and five to the consolidated financial statements in Item 8 of this Form 10-K.

Market-Rate Sensitive Instruments Interest Rate and Currency Risk

We perform a sensitivity analysis to assess the impact of interest rate and exchange rate risks on earnings. This analysis determines the effect of a hypothetical 10% adverse change in market rates. In actuality, market rate volatility is dependent on many factors that are impossible to forecast. Therefore, the adverse changes described below could differ substantially from the hypothetical 10% change.

A sensitivity analysis of debt instruments with variable interest rate components was modeled to assess the impact that changing interest rates could have on pretax earnings. The sensitivity analysis assumes an instantaneous 10% adverse change to the then prevailing interest rates with all other variables held constant. Given this model, our pretax earnings, on an annual basis, would not change at either December 31, 2003 or 2002. The fair market value of our debt was approximately $127.2 million more than its carrying value at December 31, 2003.

A similar model was used to assess the impact of changes in exchange rates for foreign currencies on interest expense. At December 31, 2003 and 2002, our debt exposure was primarily associated with the euro. A 10% adverse change in the strength of the U.S. dollar would have negatively affected our interest expense, on an annual basis, by approximately $0.2 million on December 31, 2003 and 2002, respectively.

Item 8. Financial Statements and Supplementary Data

INDEX TO FINANCIAL STATEMENTS AND RELATED SCHEDULE

All other schedules have been omitted because the required information is not applicable or is not present in amounts sufficient to require submission or because the information required is included in the consolidated financial statements or the related notes thereto.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and Board of Directors of
Service Corporation International

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Service Corporation International and its subsidiaries at December 31, 2003 and December 31, 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the accompanying index presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note four to the consolidated financial statements, the Company changed its method for accounting for insurance-funded preneed funeral contracts, changed its method of accounting for goodwill on January 1, 2002, and changed its method for accounting for derivative financial instruments and hedging activities on January 1, 2001.

As discussed in note two to the consolidated financial statements, the Company restated its previously issued consolidated financial statements for the years ended December 31, 2002 and 2001.

As discussed in note nineteen to the consolidated financial statements, the Company classified its operations in Argentina and Uruguay as discontinued operations.

PricewaterhouseCoopers LLP
Houston, Texas
March 15, 2004, except as to note nineteen, for which the date is August 27, 2004

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SERVICE CORPORATION INTERNATIONAL

CONSOLIDATED STATEMENT OF OPERATIONS
(In thousands, except per share amounts)

	Years ended December 31, 2003	2002 (Restated) note 2	2001 (Restated) note 2
Revenues	$ 2,328,425	$ 2,312,439	$ 2,489,005
Costs and expenses	(1,966,460)	(1,950,430)	(2,166,220)
Gross profits	361,965	362,009	322,785
General and administrative expenses	(178,105)	(89,752)	(70,309)
Gains and impairment (losses) on dispositions, net	49,366	(161,510)	(482,466)
Other operating expenses	(9,004)	(94,910)	(931)
Operating income (loss)	224,222	15,837	(230,921)
Interest expense	(142,735)	(160,872)	(210,857)
Other income, net	29,732	25,185	23,161
Income (loss) from continuing operations before income taxes and cumulative effects of accounting changes	111,219	(119,850)	(418,617)
(Provision) benefit for income taxes	(28,666)	37,692	(45,333)
Income (loss) from continuing operations before cumulative effects of accounting changes	82,553	(82,158)	(463,950)
Income (loss) from discontinued operations (net of income tax benefit (expense) of $585, $448 and ($1,717), respectively)	2,529	(14,768)	(151,889)
Cumulative effects of accounting changes (net of income tax benefit of $11,234 and $5,318, respectively)		(135,560)	(7,601)
Net income (loss)	$ 85,082	$ (232,486)	$ (623,440)
Basic earnings (loss) per share:			
Income (loss) from continuing operations before cumulative effects of accounting changes	$ .28	$ (.28)	$ (1.63)
Income (loss) from discontinued operations, net of tax		(.05)	(.53)
Cumulative effects of accounting changes, net of tax		(.46)	(.03)
Net income (loss)	$ .28	$ (.79)	$ (2.19)
Basic weighted average shares outstanding	299,801	294,533	285,127

Diluted earnings (loss) per share:						
Income (loss) from continuing operations before cumulative effects of accounting changes	$	.28	$	(.28)	$	(1.63)
Income (loss) from discontinued operations, net of tax				(.05)		(.53)
Cumulative effects of accounting changes, net of tax				(.46)		(.03)
Net income (loss)	$	.28	$	(.79)	$	(2.19)
Diluted weighted average shares outstanding		300,790		294,533		285,127

(See notes to consolidated financial statements)

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SERVICE CORPORATION INTERNATIONAL

CONSOLIDATED BALANCE SHEET
(In thousands, except share amounts)

	December 31, 2003	December 31, 2002
ASSETS		
Current assets:		
Cash and cash equivalents	$ 239,431	$ 200,625
Receivables, net	229,839	150,783
Inventories	136,807	136,666
Other	61,146	126,203
Total current assets	667,223	614,277
Preneed funeral contracts, net	1,229,765	1,333,673
Preneed cemetery contracts, net	1,083,035	1,163,457
Cemetery property, at cost	1,524,847	1,567,716
Property, plant and equipment, at cost, net	1,277,583	1,215,750
Assets of discontinued operations	9,318	7,165
Deferred charges and other assets	738,011	712,030
Goodwill	1,195,422	1,184,178
	$ 7,725,204	$ 7,798,246
LIABILITIES & STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 449,497	$ 356,437
Current maturities of long-term debt	182,682	100,330
Income taxes	29,576	1,225
Total current liabilities	661,755	457,992
Long-term debt	1,519,189	1,874,093
Deferred preneed funeral revenues	1,612,347	1,711,894
Deferred preneed cemetery revenues	1,575,352	1,629,540
Deferred income taxes	418,375	435,148
Liabilities of discontinued operations	61,530	57,388
Other liabilities	349,698	305,536
Commitments and contingencies (note 12)		

Stockholders equity:		
Common stock, $1 per share par value, 500,000,000 shares authorized, 302,039,871 and 297,010,237 issued and outstanding (net of 2,469,445 and 2,516,396 treasury shares at par)	302,040	297,010
Capital in excess of par value	2,274,664	2,259,936
Accumulated deficit	(938,063)	(1,023,145)
Accumulated other comprehensive loss	(111,683)	(207,146)
Total stockholders equity	1,526,958	1,326,655
	$ 7,725,204	$ 7,798,246

(See notes to consolidated financial statements)

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SERVICE CORPORATION INTERNATIONAL

CONSOLIDATED STATEMENT OF CASH FLOWS
(In thousands)

	Years ended December 31,		
	2003	2002 (Restated) note 2	2001 (Restated) note 2
Cash flows from operating activities:			
Net income (loss)	$ 85,082	$ (232,486)	$ (623,440)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
(Income) loss from discontinued operations, net of tax	(2,529)	14,768	151,889
Gains on early extinguishments of debt	(1,315)	(6,660)	(7,755)
Cumulative effects of accounting changes, net of tax		135,560	7,601
Depreciation and amortization	161,058	179,731	236,344
Provision for deferred income taxes	4,084	106,841	55,116
(Gains) and impairment losses on dispositions, net	(49,385)	161,511	475,221
Other operating expenses	9,004	94,910	931
Payments on restructuring charges	(14,155)	(12,806)	(22,794)
Change in assets and liabilities, net of effects from acquisitions and dispositions:			
(Increase) decrease in receivables	(53,630)	3,022	27,451
Decrease (increase) in other assets	67,726	(31,920)	89,906
Increase (decrease) in payables and other liabilities	163,321	(82,670)	(104,773)
Net effect of preneed funeral production and maturities	4,061	26,743	48,329
Net effect of cemetery production and deliveries	986	(7,827)	21,223
Other	(3,163)	2,619	17,755
Net cash provided by continuing operations	371,145	351,336	373,004
Net cash provided by discontinued operations	2,963	836	10,331
Net cash provided by operating activities	374,108	352,172	383,335
Cash flows from investing activities:			
Capital expenditures	(115,563)	(99,875)	(74,931)
Proceeds from divestitures and sales of property and equipment	76,577	76,292	126,686
Proceeds and distributions from joint ventures and equity investments, net of cash retained	73,940	291,794	285,656
Net (deposits) withdrawals of restricted funds and other	(71,939)	58,883	(12,874)
Net cash (used in) provided by investing activities from continuing operations	(36,985)	327,094	324,537
	(437)	(169)	873

Net cash (used in) provided by investing activities from discontinued operations			
Net cash (used in) provided by investing activities	(37,422)	326,925	325,410
Cash flows from financing activities:			
Net decrease in borrowings under credit agreements		(29,061)	(734,187)
Payments of debt	(90,980)	(74,234)	(166,292)
Proceeds from long-term debt issued			345,000
Early extinguishments of debt	(200,349)	(307,232)	(155,545)
Settlement of debt-related options		(57,000)	
Bank overdrafts and other	(8,820)	(36,332)	(16,445)
Net cash used in financing activities from continuing operations	(300,149)	(503,859)	(727,469)
Net cash (used in) provided by financing activities from discontinued operations		(1,623)	31
Net cash used in financing activities	(300,149)	(505,482)	(727,438)
Effect of foreign currency	2,269	(2,282)	76
Net increase (decrease) in cash and cash equivalents	38,806	171,333	(18,617)
Cash and cash equivalents at beginning of period	200,625	29,292	47,909
Cash and cash equivalents at end of period	$ 239,431	$ 200,625	$ 29,292

(See notes to consolidated financial statements)

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SERVICE CORPORATION INTERNATIONAL

CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME
(In thousands)

	Common stock	Capital in excess of par value	Accumulated deficit (Restated) note 2	Accumulated other comprehensive income (loss)	Total (Restated) note 2
Balance at December 31, 2000 as previously reported	$ 272,507	$ 2,156,824	$ (216,353)	$ (237,157)	$ 1,975,821
Restatement (note 2)			49,134		49,134
Balance at December 31, 2000, as restated	$ 272,507	$ 2,156,824	$ (167,219)	$ (237,157)	$ 2,024,955
Comprehensive loss:					
Net loss			(623,440)		(623,440)
Other comprehensive loss:					
Foreign currency translation				(76,403)	(76,403)
Minimum pension liability adjustment, net				(16,629)	(16,629)
Reclassification adjustment for realized loss on foreign currency translation				38,990	38,990
Total other comprehensive loss					(54,042)
Total comprehensive loss:					(677,482)
Common Stock issued:					
Stock option exercises and stock grants	627	2,367			2,994
Contributions to employee 401(k) and cash balance plan	3,576	15,559			19,135
Debenture conversions	244	5,284			5,528
Debenture extinguished using common stock	15,200	66,021			81,221
Balance at December 31, 2001	292,154	2,246,055	(790,659)	(291,199)	1,456,351
Comprehensive loss:					
Net loss			(232,486)		(232,486)
Other comprehensive income:					
Foreign currency translation				43,776	43,776
Minimum pension liability adjustment, net				(7,202)	(7,202)
Reclassification adjustment for realized loss on foreign currency translation				47,479	47,479

Total other comprehensive income					84,053
Total comprehensive loss					(148,433)
Common Stock issued:					
Stock option exercises and stock grants	173	414			587
Contributions to employee 401(k)	4,683	13,467			18,150
Balance at December 31, 2002	297,010	2,259,936	(1,023,145)	(207,146)	1,326,655
Comprehensive income:					
Net income			85,082		85,082
Other comprehensive income:					
Foreign currency translation				92,507	92,507
Minimum pension liability adjustment, net				2,956	2,956
Total other comprehensive income					95,463
Total comprehensive income					180,545
Common stock issued:					
Stock option exercises and other	471	1,909			2,380
Contributions to employee 401(k)	4,559	12,819			17,378
Balance at December 31, 2003	$ 302,040	$ 2,274,664	$ (938,063)	$ (111,683)	$ 1,526,958

(See notes to consolidated financial statements)

SERVICE CORPORATION INTERNATIONAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except per share amounts)

NOTE ONE

Nature of Operations

Service Corporation International (SCI or the Company) is the world s largest provider of funeral and cemetery services. At December 31, 2003, the Company operated 2,225 funeral service locations, 417 cemeteries and 183 crematoria located in eight countries (unaudited). Of these locations, seven funeral homes, five cemeteries and two crematoria were classified as discontinued at December 31, 2003 (unaudited). The Company also had minority interest equity investments in funeral and cemetery operations in the United Kingdom and Australia. In the fourth quarter of 2003, the Company sold its minority interest equity investment in Australia. Subsequent to December 31, 2003, the Company sold its funeral operations in France to a joint venture on March 11, 2004. The French operations consisted of 963 funeral service locations and 39 crematoria at December 31, 2003 (unaudited).

The funeral service and cemetery operations consist of funeral service locations, cemeteries, crematoria and related businesses. Personnel at the funeral service locations provide all professional services relating to funerals, including the use of funeral facilities and motor vehicles, and preparation and embalming services. Funeral related merchandise (including caskets, coffins, burial vaults, cremation receptacles, flowers and other ancillary products and services) is sold at funeral service locations. Certain funeral service locations contain crematoria. The Company sells preneed funeral services whereby a customer contractually agrees to the terms of a funeral to be performed in the future. The Company s cemeteries provide cemetery property interment rights (including mausoleum spaces, lots and lawn crypts) and sell cemetery related merchandise (including stone and bronze memorials, burial vaults, casket and cremation memorialization products) and services (primarily merchandise installation fees and burial opening and closing fees). Cemetery items are sold on an atneed or preneed basis. Personnel at cemeteries perform interment services and provide management and maintenance of cemetery grounds. Certain cemeteries operate crematoria, and certain cemeteries contain gardens specifically for the purpose of cremation memorialization. At December 31, 2003, there were 185 combination locations that contained a funeral service location within a Company owned cemetery (unaudited).

NOTE TWO

Restatement of Financial Statements

The Company restated its previously issued financial statements for the fiscal years ended December 31, 2002, 2001 and 2000, the interim quarters of 2002, 2001 and 2000, and the first three quarters of 2003, primarily due to adjustments to Deferred preneed cemetery contract revenues. All applicable amounts relating to these restatements have been reflected in the consolidated financial statements and notes to the consolidated financial statements.

Prior to the implementation of Staff Accounting Bulletin No. 101, *Revenue Recognition in Financial Statements* (SAB 101), the Company recorded revenues for cemetery merchandise or services at the time the contract was signed by the customer. The estimated costs to deliver merchandise and perform services were charged to expense at the time the contract was signed and a corresponding liability was recorded on the Company s consolidated balance sheet. This liability was periodically adjusted to reflect changes in the estimated costs of merchandise and services. When the Company delivered merchandise or performed services under a customer s cemetery contract, our policy required cemetery personnel to record such delivery or performance into the accounting system. This entry reduced the corresponding liability as the obligation was satisfied.

Effective January 1, 2000, we adopted SAB 101. The Company determined that the accounting policy for recognition of preneed cemetery merchandise or service revenue should be changed from the time of sale to the time of delivery or performance. Undelivered merchandise and services would be recorded as deferred revenue at the contract sale price and revenue from such merchandise and services would be recognized when delivered or performed.

In the latter part of 2001, the Company identified preneed cemetery merchandise and services that had been previously delivered, but the delivery had not been input into our accounting system in a timely manner. When identified, these items were recognized as revenues and disclosed as changes in estimates in the period identified. Deliveries made in a period other than when they were ultimately recognized as a change in estimate are referred to as out-of-period deliveries .

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During 2000 through September 2003, the Company identified approximately $109,399 of preneed cemetery contract items were out-of-period deliveries, which means that these items had been delivered or performed, but the revenue had not been recognized in the appropriate period of delivery. These items were originally recognized as revenues and disclosed as changes in estimates in the periods from 2000 through 2003. Offsetting the $109,399, the Company recorded $43,671 of cemetery revenue from 2000 through September 2003, which represents the effects of subsequent years being restated into the appropriate earlier period as detailed in the table below.

	2000	2001	2002	First Three Quarters of 2003	Total
Reductions in cemetery revenues for out-of-period deliveries	$ (12,773)	$ (68,515)	$ (23,425)	$ (4,686)	$ (109,399)
Effects of subsequent years being restated into the appropriate period	$ 27,682	$ 11,054	$ 4,935	$	$ 43,671
Net restatement of cemetery revenues for out-of-period deliveries	$ 14,909	$ (57,461)	$ (18,490)	$ (4,686)	$ (65,728)

Additionally, during the fourth quarter of 2003, the Company recorded adjustments to prior periods totaling $40,697 to report additional cemetery merchandise and service revenue in the period that such items were delivered or performed. The difference between the $40,697 and the $109,399 described above is that the cemetery contract items within the $109,399 were previously identified by the Company and were recognized as revenue and disclosed as a change in estimate in the period identified. The cemetery contract items within the $40,697 were not previously identified or recognized as revenue by the Company prior to the fourth quarter of 2003. The distribution of the $40.7 million was restated as follows:

	2000	2001	2002	2003	Total
Increased revenues for items for which delivery or performance occurred, but no revenue was recognized	$ 4,874	$ 8,318	$ 8,680	$ 8,662	$ 30,534
Cumulative effect (pretax)	$ 10,163	$	$	$	$ 10,163
Total revenues for items for which delivery or performance occurred, but no revenue was recognized	$ 15,037	$ 8,318	$ 8,680	$ 8,662	$ 40,697

The Company also reviewed its accounting policy for amortizing preneed funeral deferred selling costs and has changed the methodology for amortizing these costs from a straight line basis to a method more in proportion to when the associated revenues are recognized. The Company has included this change in amortization in its restated results.

The effect of the restatement on the Company s previously reported consolidated statement of operations and consolidated balance sheet for the periods described above is as follows:

(Dollars in thousands, except per share data)	Year ended December 31, 2002 As reported	Year ended December 31, 2002 As Restated	Year ended December 31, 2001 As Reported	Year ended December 31, 2001 As Restated	Year ended December 31, 2000 As Reported	Year ended December 31, 2000 As Restated
Selected consolidated statement of operations data:						
Revenues	$ 2,322,249	$ 2,312,439	$ 2,538,148	$ 2,489,005	$ 2,549,755	$ 2,569,538
Costs and expenses	$ (1,959,250)	$ (1,950,430)	$ (2,173,482)	$ (2,166,220)	$ (2,216,388)	$ (2,226,530)
Gross profits	$ 362,999	$ 362,009	$ 364,666	$ 322,785	$ 333,367	$ 343,008
Operating income (loss)	$ 16,827	$ 15,837	$ (189,040)	$ (230,921)	$ (247,165)	$ (237,524)
Loss from continuing operations before income taxes and cumulative effects of accounting changes	$ (118,860)	$ (119,850)	$ (376,736)	$ (418,617)	$ (475,574)	$ (465,933)
Benefit (provision) for income taxes	$ 37,308	$ 37,692	$ (61,570)	$ (45,333)	$ 81,290	$ 77,552
Cumulative effects of accounting changes (net of income taxes)	$ (135,560)	$ (135,560)	$ (7,601)	$ (7,601)	$ (913,599)	$ (870,368)
Net loss	$ (231,880)	$ (232,486)	$ (597,796)	$ (623,440)	$ (1,343,251)	$ (1,294,117)
Basic and diluted earnings per share:						
Loss from continuing operations before cumulative effects of accounting changes	$ (.28)	$ (.28)	$ (1.54)	$ (1.63)	$ (1.45)	$ (1.43)
Net loss	$ (.79)	$ (.79)	$ (2.10)	$ (2.19)	$ (4.93)	$ (4.75)

	As of December 31, 2002 As Reported	As of December 31, 2002 As Restated
Selected consolidated balance sheet data:		
Inventories	$ 135,263	$ 136,666
Total current assets	$ 612,874	$ 614,277
Deferred charges and other assets	$ 719,180	$ 712,030
Total assets	$ 8,253,993	$ 7,798,246
Deferred cemetery contract revenues, net	$ 1,672,661	$ 1,629,540
Deferred income taxes	$ 420,658	$ 435,148
Accumulated deficit	$ (1,046,029)	$ (1,023,145)
Total stockholders equity	$ 1,303,771	$ 1,326,655
Total liabilities and stockholders equity	$ 8,253,993	$ 7,798,246

See note twenty-one to the consolidated financial statements for the effect of the restatement upon quarterly unaudited financial data.

The Company has changed its method of accounting for insurance funded preneed contracts as it has concluded that its insurance funded preneed funeral contracts are not assets and liabilities as defined by Statement of Financial Accounting Concepts No. 6, *Elements in Financial Statements*. Therefore, the Company has removed from its consolidated balance sheet amounts relating to insurance funded preneed funeral contracts previously recorded in *Preneed funeral receivables and trust investments* and *Deferred preneed funeral revenues*, which at December 31, 2003 and 2002, were $3,505,094 and $2,948,100, respectively. The removal of these amounts did not have an impact on the Company s consolidated stockholders equity, results of operations or cash flows.

NOTE THREE

Summary of Significant Accounting Policies

Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of SCI and all majority-owned subsidiaries. Intercompany balances and transactions have been eliminated in consolidation.

The Company has classified gains and losses associated with early extinguishments of debt as Other income, net in the consolidated statement of operations. Previously, these gains and losses were classified as extraordinary items. Additionally, the Company has classified gains from dispositions within Gains and impairment (losses) on dispositions, net in the consolidated

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statement of operations. Previously, gains from dispositions were presented separately after Operating income in the consolidated statement of operations. The reclassifications have been made for all years presented in accordance with Statement of Financial Accounting Standards (SFAS) No. 145, *Revision of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections* .

The Company has reported general agency (GA) revenues as funeral revenues for all periods presented. Previously, the Company reported these GA revenues as a reduction to selling expense in the consolidated statement of operations. See note five to the consolidated financial statements for further discussion of GA revenues. Additionally, certain other reclassifications have been made to prior years to conform to current period presentation with no effect on the Company s consolidated financial position, results of operations or cash flows.

Use of Estimates in the Preparation of Financial Statements

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that may affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of expenses during the reporting period. As a result, actual results could differ from these estimates.

In 2002, the Company changed its allocation methodology of overhead costs in North America to be based on funeral and cemetery reporting unit revenues. The change in overhead allocation has not impacted the Company s reported results of operations, financial position or cash flows.

During the second quarter of 2002, the Company decided to implement new information technology systems, including a new North America point of sale system and an upgraded general ledger system. As a result of this decision, the Company accelerated amortization of its existing capitalized systems costs beginning in the second quarter of 2002 to reflect the remaining estimated useful lives of these systems. These existing systems were fully amortized by the conclusion of the third quarter of 2003. The Company capitalized application development stage costs associated with new system implementation in accordance with SOP 98-1, *Accounting for the Costs of Computer software Developed or Obtained for Internal* Use (SOP 98-1). The Company began amortizing such costs upon implementation of this new system in the fourth quarter of 2003 at which time the old systems were fully amortized. The Company recognized additional amortization related to this change in estimate of approximately $13,800 and $13,500 in the years ended December 31, 2003 and 2002, respectively. This change in estimate impacted net income by approximately $8,694, or diluted income per share of $.03 in 2003 and impacted net loss by approximately $8,500, or diluted loss per share $.03 in 2002.

Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Inventories and Cemetery Property

Funeral merchandise and cemetery burial property and merchandise are stated at the lower of average cost or market.

Property, Plant and Equipment, net

Property, plant and equipment, net are recorded at cost. Maintenance and repairs are charged to expense whereas renewals and major replacements that extend the assets useful lives are capitalized. Depreciation is provided using the straight line method over the estimated useful lives of the various classes of assets. Property and plant are depreciated over a period ranging from seven to forty years, equipment is depreciated over a period from three to eight years and leasehold improvements are depreciated over the shorter of the lease term or ten years. When property is sold or retired, the cost and related accumulated depreciation are removed from the consolidated balance sheet; resulting gains and losses are included in the consolidated statement of operations.

Goodwill

The excess of purchase price over the fair value of identifiable net assets acquired in business combinations accounted for as purchases is recorded as goodwill. Prior to 2002, goodwill was amortized over its estimated life. Since then, goodwill is no longer amortized but is tested annually for impairment by assessing the fair value of each of the Company s reporting units (which is generally one level below the Company s reportable segments). As of December 31, 2003, the Company s funeral segment reporting units are North America, France, Germany and Singapore. The Company s cemetery segment reporting units are North America and Chile.

The Company s policy is to test for impairment of goodwill in accordance with SFAS 142 *Goodwill and Other Intangible Assets* (SFAS 142) annually as of September 30 each year. For the current year, the Company performed such test on September 30, 2003.

The Company tests for impairment of its goodwill using a two-step approach as prescribed in SFAS 142. The first step of the Company s goodwill impairment test compares the fair value of a reporting unit with its carrying amount, including goodwill. The Company does not record an impairment of goodwill in instances where the fair value of a reporting unit exceeds its carrying amount. The second step of the Company s goodwill impairment test is required only in situations where the carrying amount of the reporting unit exceeds its fair value as determined in the first step. In such instances, the Company compares the implied fair value of goodwill (as defined in SFAS 142) to its carrying amount of goodwill. If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. Fair market value of a reporting unit is determined using a calculation based on multiples of revenue and multiples of EBITDA of both the Company and its competitors. Based on our test at September 30, 2003, the Company concluded that there was no impairment of goodwill in accordance with SFAS 142.

Deferred Selling Costs

The Company defers selling costs that vary with and are primarily related to the acquisition of preneed funeral (trust funded only) and preneed cemetery contracts, and to expense such costs in proportion to the revenue recognized. The deferral, which is calculated based on deferral rates discussed below, and amortization model follows the provisions of SFAS 60, *Accounting and Reporting by Insurance Enterprises* (SFAS 60). The selling costs subject to deferral are the pool of compensation expense and related fringe costs incurred by the Company s sales counselors and sales managers. Other selling costs associated with the sales and marketing of preneed funeral and cemetery contracts (e.g., lead procurement costs, brochures and marketing materials, advertising and general administrative costs) are expensed as incurred.

Deferral rates are determined for the following:

- Preneed funeral contracts
- Preneed cemetery contract items:
  - interment rights (burial property)
  - merchandise
  - services

These deferral rates are based on the ratio of the selling compensation and fringe costs to preneed funeral and cemetery production (in dollars) weighted accordingly in the manner for which the counselor is compensated (with interment rights, or burial property, being the highest and preneed cemetery services being the lowest compensation to the counselor). In developing the deferral rates, the Company reviews various rate scenarios to ensure the finalized rates, when applied to forecasted production dollars, are reasonable compared to forecasted selling compensation. Additionally, the developed deferral rates are reviewed annually for reasonableness compared to current and historical commission rates used by the Company.

As preneed funeral and cemetery contracts are processed, the rates are applied systematically to the production dollars and the resulting amount is deferred. As a result, the funeral and cemetery deferred selling costs are only generated when preneed funeral and cewmetery contract production is recorded. Therefore, these deferred selling costs vary with and relate primarily to the production of the preneed cemetery merchandise, and preneed cemetery services. The deferred preneed funeral and cemetery revenue accounts are recorded similarly.

Periodically, the selling costs deferred are compared to the actual costs incurred to ensure there is not a significant variance between the two.

The deferred selling costs are expensed in proportion to the revenue when recognized (proportionate method). This is determined annually by the ratio of the unamortized deferred selling costs (funeral, cemetery interment rights, cemetery merchandise and cemetery services) to the associated deferred revenue, and systematically applying this ratio against the deferred selling cost accounts as the applicable revenues are recognized.

The Company does not attribute deferred selling costs to each individual contract (or each item in the case of cemetery deferred selling costs) because our systems do not currently have the complete functionality to defer and amortize the costs and the Company has no other cost effective means by which to do so. The Company believes using the proportionate method of amortization and the homogenous nature of the 430,000 preneed funereal contracts and 3.6 million of preneed cemetery contract items (as separated by interment rights, merchandise and services) allows for a systematic match of costs with related revenues.

The Company applies the requirements of SFAS No. 60 *Accounting and Reporting by Insurance Enterprises* (SFAS 60) to test for impairment of our deferred selling costs as prescribed by the AICPA Industry Guide, *Life and Health Insurance Entities*. Accordingly, when circumstances indicate that actual experience for a portfolio of contracts, regardless of the year of origin may result in losses, the Company assesses whether the expected gross contract revenues for each portfolio of preneed funeral contracts or preneed cemetery contracts less all related expected contract costs is sufficient to cover the current unamortized deferred selling costs associated with each portfolio. For purposes of applying this policy, a portfolio of preneed funeral contracts or preneed cemetery contracts is comprised of all such contracts executed within a given market (i.e., an area of operation). If deferred selling costs for a portfolio of contracts exceeds the related gross contract revenue less expected contract costs, the excess is charged to expense. The Company believes this is the most appropriate way to evaluate impairment because it is consistent with the manner in which it acquires services and measures the profitability of its preneed funeral and preneed cemetery contracts. The sales organization is organized by market, and the selling costs incurred and deferred specifically relate to the preneed funeral and cemetery deferred revenues recorded in the operating market.

An allowance is provided against the deferred selling costs associated with contract cancellations, with a corresponding charge to the consolidated statement of operations. The allowance for cancellations is determined from the Company s historical experience and is based on the amount of unrecoverable deferred selling costs in relation to the associated deferred revenue.

The following table depicts the activity in the allowance for deferred selling costs for the years ended December 31, 2003 and 2002.

(Dollars in thousands)	Beginning Balance	Change in Allowance	Change for Divestitures	Ending Balance
2003				
Allowance for funeral deferred selling costs	$ (8,911)	$ 83	$ 86	$ (8,742)
Allowance for cemetery deferred selling costs	(14,020)	(1,135)	111	(15,044)
2002				
Allowance for funeral deferred selling costs	$ (8,950)	$ 4	$ 35	$ (8,911)
Allowance for cemetery deferred selling costs	(14,299)	279		(14,020)

The change in the allowance account relates to 1) the periodic adjustment based on the Company s historical cancellations and 2) reductions associated with the effects of divestitures.

Impairment or Disposal of Long-Lived Assets

Except as noted for Goodwill and deferred selling costs, the Company reviews its long-lived assets for impairment when changes in circumstances indicate that the carrying amount of the asset may not be recoverable in accordance with Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144). SFAS 144 requires that long-lived assets to be held and used be reported at the lower of carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to the Company are recorded at the lower of carrying amount or fair value less estimated cost to sell.

In January 2002, the Company ceased depreciation of certain operating assets held for sale (which primarily included France and Chile). The Company later determined transactions to sell or joint venture these assets would be delayed. As a result, the Company resumed normal depreciation of those assets held in France and Chile in the third quarter of 2002. In January 2003, the Company once again classified the France operating assets held for sale and ceased depreciation. In March 2004, the Company sold 100% of its funeral operations in France and then purchased a 25% equity interest in the acquiring company.

Stock Options

The Company accounts for employee stock-based compensation expense under the intrinsic value method. Under the intrinsic value method, no compensation expense is recognized on stock options if the grant price equals the market value on the date of grant. All of the Company stock option grants have been at market value on the dates of each grant.

If the Company had elected to recognize compensation expense for its stock option plans, based on the fair value of awards at their grant dates, net income (loss) and earnings (loss) per share would have changed for the years ended December 31 to the following pro forma amounts:

	2003	2002 (Restated) note 2	2001 (Restated) note 2
Net income (loss)	$ 85,082	$ (232,486)	$ (623,440)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax expense	(6,720)	(13,537)	(17,680)
Pro forma net income (loss)	$ 78,362	$ (246,023)	$ (641,120)
Basic and diluted net earnings (loss) per share	$ .28	$ (.79)	$ (2.19)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax expense	(.02)	(.04)	(0.06)
Pro forma basic and diluted net earnings (loss) per share	$		