

## THIRD QUARTER REPORT

September 30, 2004

### REPORT TO SHAREHOLDERS

Your Corporation incurred a net loss for the quarter of \$1.0 million. This loss compares to a loss of \$0.7 million in the third quarter of 2003 after adjustment for the favourable settlement of the JTB Canadian Pork claim in the 2003 period. Revenue was \$82.7 million as compared to \$84.2 million in the third quarter of 2003. While we were expecting our financial results to be much better in this period, delays in the completion of our new fabrication facility as well as higher than expected start-up costs combined to hinder our earnings. The quarterly results were also negatively impacted by the lower than expected activity level at Laird Electric.

Our work-in-hand is \$338.4 million, which is similar to the level of \$347.0 million at the end of the second quarter of 2004. An additional \$74.1 million of new work was awarded to Churchill companies during the quarter.

Stuart Olson showed a substantial improvement in earnings during the third quarter. They achieved operational earnings of \$1.6 million as compared to \$0.2 million during the second quarter of this year and a loss of \$1.2 million after adjustment for the JTB recovery in the third quarter of 2003. This improvement over the second quarter was due to increased revenue and substantially improved contract margins. Stuart Olson recently celebrated 65 years in the construction business.

Our insulation companies have experienced an excellent year to date providing operational earnings of \$1.4 million. They completed most of their work on process modules destined for the Fort McMurray oil sands projects early in the third quarter and were able to secure substantial contracts related to the associated field installation of these modules. There was a break in activity prior to this field work commencing in the fourth quarter, which resulted in lower earnings in the third quarter, as compared to the first two quarters of 2004.

Laird Electric continued to be negatively impacted by delays in starts on major oil sands projects. As well, a large portion of their on-going maintenance work for a major client was postponed into 2005, significantly affecting their earnings for both the third quarter and the upcoming fourth quarter. Laird is pursuing several major new projects, which would move into construction in 2005.

Triton has had significant success in securing new contracts on major oil sands projects over the last two quarters.

These are as a direct result of having access to Churchill's new modular fabrication facility. As discussed in previous reports, many of the new oil sands projects are moving towards the use of off-site fabrication of process modules that are then transported to the jobsite and assembled. Triton has secured contracts for both the off-site modular work as well as the field assembly and fit-out. The company now has the largest backlog of work-in-hand in its history with most of this work to be executed during 2005.

Triton incurred an operational loss of \$1.4 million during the quarter. Much of this loss was related to the fabrication plant start-up issues. We believe that these operational issues will lessen in the fourth quarter as they refine and improve their processes.

The Board of Directors of the Corporation, while remaining committed to our strategic and operating plans, has become increasingly concerned about the poorer than expected financial results over the last few quarters. The Directors have joined with senior management to form a special committee to review the operational and control systems of the companies experiencing difficulties, and to implement measures for improvement.

This will be the last report that I will be sending to you as your President and CEO. The last two years have been a challenge and I believe that it is time for me to step aside and allow another to bring our plan to fruition. Hank Reid, who led the Corporation through a successful twelve year period, will be returning as Interim CEO. I will remain with Churchill as a resource to the Board and the CEO. I thank our Board, management, employees, and shareholders for their support over the years. I am convinced that the future holds significant opportunities for our Corporation.



November 10, 2004

Gary R. Bardell, MBA, P.Eng.  
President and Chief Executive Officer

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management's Discussion and Analysis ("MD&A") of the operating performance and financial condition of The Churchill Corporation, prepared as at November 10, 2004, should be read in conjunction with the unaudited Consolidated Financial Statements and related notes, and the Report to Shareholders contained in this 2004 Third Quarter report, as well as the Consolidated Financial Statements and related notes, MD&A and Report to Shareholders contained in the Corporation's 2003 Annual Report and 2004 First and Second Quarter Reports.

Except as discussed below, all other factors referred to and discussed in the MD&A for fiscal 2003 and for the first and second quarters of 2004 remain substantially unchanged.

## ACCOUNTING POLICIES

Churchill continues to use the same accounting policies and methods as described in Note 2 attached to the December 31, 2003 Consolidated Financial Statements, except that the Corporation adopted, effective January 1, 2004, the new CICA Handbook policies related to stock-based compensation and asset impairment. These new policies are described more fully in the MD&A contained in the Corporation's 2004 First Quarter Report. The impact of adopting the fair value based method of accounting for stock-based compensation is disclosed in Note 6. There is no material impact on the current or prior period financial statements resulting from the adoption of the asset impairment policy.

## TERMINOLOGY

Throughout this 2004 Third Quarter Report, and other documents referred to, management uses the following terms which do not have any standardized meaning under Canadian GAAP as set out in the CICA Handbook, and which require definition –

*Contract income margin percentage* is the percentage derived by dividing contract income by contract revenue. Contract income is calculated by deducting all associated direct and indirect costs from contract revenue in the period.

*Work-in-hand* is the unexecuted portion of work that has contractually been awarded to the Corporation. It includes capital construction contracts that have been awarded and are either under construction or expected to commence construction in the normal course, as well as an estimate of the revenue expected to be generated from maintenance contracts during the shorter of (a) the next two years, or (b) the remaining life of the contract.

## CRITICAL ACCOUNTING ESTIMATES

Churchill's financial statements include estimates and assumptions made by management relating to the results of operations, financial conditions, contingencies, commitments, and related disclosures. Actual results may vary from these estimates.

As discussed in the MD&A contained in the 2004 First Quarter Report, management has identified the Corporation's most critical accounting estimates to be in the areas of contract revenue and contract income recognition, accounts receivable collectability, goodwill impairment, and income tax provisions. No new critical areas have been identified during the three months ended September 30, 2004.

All estimates are updated each reporting period to reflect actual activity as well as incorporate all new relevant information that has come to the attention of management. Given the nature of construction, with numerous contracts in progress at any given point in time, the impact of the critical accounting estimates on the results of operations is significant. Subsequent activities, or information received subsequent to the date of this MD&A, may cause actual results to vary, which will be reflected in the results of subsequent reporting periods.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

### SELECTED ANNUAL INFORMATION

(\$ millions, except where noted)

	Year ended December 31		
	2003	2002	2001
Contract revenue	\$ 319.2	\$ 311.7	\$ 293.5
Net (loss) earnings	(3.7)	1.0	5.3
Net (loss) earnings per common share			
Basic (\$ per share)	(0.31)	0.09	0.50
Fully diluted (\$ per share)	(0.31)	0.09	0.47
Total assets	102.8	99.0	103.9
Total long-term financial liabilities	7.5	0.4	1.5

Churchill acquired Laird Electric on February 7, 2003. For the year ended December 31, 2003 Laird contributed \$25.6 million of contract revenue. For the nine months ended September 30, 2004 Laird contributed \$14.1 million of contract revenue.

Churchill acquired Lakehead Insulation in January, 2002. For the years ended December 31, 2002 and December 31, 2003 Lakehead contributed \$2.4 million and \$13.8 million of contract revenue, respectively. For the nine months ended September 30, 2004 Lakehead contributed \$3.7 million of contract revenue.

Churchill's 41% interest in the Lafrentz Road Services business was sold in early 2003. Churchill's equity earnings and management fees from Lafrentz were \$0.2 million in 2003, \$0.4 million in 2002, and \$0.1 million in 2001.

### QUARTERLY FINANCIAL INFORMATION

(\$ millions, except where noted)

	2004		
	Sept. 30	June 30	Mar. 31
Contract revenue	\$ 82.7	\$ 77.3	\$ 72.8
Contract income	5.4	6.2	4.5
Contract income - %	6.5%	8.0%	6.2%
Net (loss) earnings	(1.0)	(0.2)	(1.2)
Work-in-hand	338.4	347.0	298.4
Working capital	9.9	13.0	15.2
Shareholders' equity	28.6	29.5	29.2
	<b>2003</b>		
	Dec. 31	Sept. 30	June 30
Contract revenue	\$ 95.6	\$ 84.2	\$ 77.2
Contract income	7.0	5.1	6.1
Contract income - %	7.3%	6.1%	7.9%
Net (loss) earnings	(0.5)	1.0	(2.4)
Work-in-hand	313.7	393.4	393.8
Working capital	17.6	18.9	17.8
Shareholders' equity	30.5	30.8	29.7

## MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

### QUARTERLY FINANCIAL INFORMATION (continued)

(\$ millions, except where noted)

	2002			
	Dec. 31	Sept. 30	June 30	Mar. 31
Contract revenue	\$ 84.6	\$ 85.0	\$ 75.0	\$ 67.1
Contract income	4.4	4.3	6.1	5.8
Contract income - %	5.2%	5.1%	8.1%	8.6%
Net (loss) earnings	Nil	(0.2)	0.8	0.4
Work-in-hand	317.3	319.9	326.5	337.7
Working capital	21.2	20.9	21.7	22.6
Shareholders' equity	31.7	31.9	32.1	31.0

Work-in-hand at December 31, 2002 was \$317.3 million. Contract revenue in the following fiscal 2003 year totaled \$319.2 million, indicating that a significant portion of 2003 revenue, and associated potential contract income margin percentages, had been awarded to the Corporation in 2002 or earlier. Any measures taken by management to improve contract income margin percentages may take several quarters before they are fully reflected in the results.

Work-in-hand at September 30, 2004 was \$338.4 million, up from \$313.7 million at December 31, 2003. The Corporation has been successful in replacing the dollar volume of work executed during the first nine months of 2004.

### RESULTS OF OPERATIONS

For the three months ended September 30, 2004, Churchill incurred a net loss of \$1.0 million (2003 – net income of \$1.0 million) on revenues of \$82.7 million (2003 – \$84.2 million), or a net loss per common share of \$0.08 (2003 – net earnings per common share of \$0.09).

For the nine months ended September 30, 2004, Churchill incurred a net loss of \$2.5 million (2003 – net loss of \$3.2 million) on revenues of \$232.8 million (2003 – \$223.6 million), or a net loss per common share of \$0.20 (2003 – net loss per common share of \$0.27).

The September 30, 2004 results include the activities of Laird Electric for the full period, while the September 30, 2003 results include the activities of Laird from February 8, 2003 to September 30, 2003.

The September 30, 2003 quarterly results were impacted by a \$3.0 million recovery of a bad debt allowance that had been established in the second quarter ended June 30, 2003.

Churchill's 41% interest in the Lafrentz Road Services business was sold in the first quarter of 2003. Churchill realized \$1.5 million in proceeds from the sale and recognized a \$0.1 million gain in the quarter ended March 31, 2003.

#### *Buildings*

Stuart Olson had work-in-hand of \$260.3 million at June 30, 2004. For the three months ended September 30, 2004 they secured a further \$24.9 million of contracts, and executed and took into revenue \$61.8 million. The

company had \$223.4 million of work-in-hand at September 30, 2004, of which \$158.1 million is expected to carry over into 2005 and beyond.

Stuart Olson's revenues for the three months ended September 30, 2004 were \$61.8 million, up substantially from \$46.3 million for the same period last year as projects that had been delayed moved into construction. After adjusting for the \$3.0 million recovery of bad debt that was recorded in the third quarter of 2003, earnings before income taxes improved by \$2.8 million in the third quarter of 2004 as compared to the same period of 2003. Earnings before income taxes for the three months ended September 30, 2004 were \$1.6 million, compared to a loss before income taxes of \$1.2 million after removing the \$3.0 million reversal of bad debt recorded in the period. The improvement was the result of higher revenues and improved contract income margin percentages.

For the nine months ended September 30, 2004, Stuart Olson realized earnings before income taxes of \$1.3 million on contract revenue of \$177.5 million, compared to a loss before income taxes of \$2.7 million on contract revenue of \$134.3 million for the nine months to September 30, 2003.

#### *Industrial General Contracting*

Triton had work-in-hand of \$33.2 million at June 30, 2004. For the three months ended September 30, 2004 they secured a further \$37.2 million of contracts, and executed and took into revenue \$10.5 million. The company had

\$59.9 million of work-in-hand at September 30, 2004, of which \$36.7 million is expected to carry over into 2005 and beyond.

Triton's revenues for the three months ended September 30, 2004 were \$10.5 million, down marginally from \$11.0 million for the three months ended September 30, 2003. Triton's loss before income taxes for the three months ended September 30, 2004 was \$1.4 million, compared to a loss before income taxes of \$0.4 million for the same period last year. Triton incurred cost overruns in the third quarter on a specific field construction project. As well, start-up inefficiencies in the new modular fabrication facility resulted in Triton recognizing a loss in the quarter on the work that was progressing through the facility.

For the nine months ended September 30, 2004, Triton realized a loss before income taxes of \$2.2 million on contract revenue of \$21.1 million, compared to a loss before income taxes of \$2.4 million on contract revenue of \$29.3 million for the nine months to September 30, 2003.

#### ***Industrial Insulation Contracting***

Fuller Austin and Northern Industrial Insulation had a combined work-in-hand of \$10.5 million at June 30, 2004. For the three months ended September 30, 2004 they secured a further \$24.6 million of contracts, and executed and took into revenue \$8.6 million. The company had \$26.5 million of work-in-hand at September 30, 2004, of which \$16.2 million is expected to carry over into 2005.

Revenues for the three months ended September 30, 2004 were \$8.6 million, compared to revenues of \$21.0 million for the three months ended September 30, 2003. Activity levels in the third quarter of 2003 were high, with several major contracts in progress. No similar contracts were in place in the third quarter of 2004. Earnings before taxes were \$0.1 million for the three months ended September 30, 2004, down from \$1.1 million for the same period last year. While contract income margin percentages increased on a year over year basis for the period, lower revenues contributed less dollars of earnings for the three months ended September 30, 2004.

For the nine months ended September 30, 2004, the insulation companies realized earnings before income taxes of \$1.4 million on contract revenue of \$25.3 million, compared to earnings before income taxes of \$1.6 million on contract revenue of \$41.5 million for the nine months to September 30, 2003.

#### ***Industrial Electrical Contracting***

Laird Electric had work-in-hand of \$43.0 million at June 30, 2004. For the three months ended September 30, 2004 their work-in-hand was reduced by \$11.4 million relating to changes in contracts, and they executed and took

into revenue \$3.0 million. The company had \$28.6 million of work-in-hand at September 30, 2004, of which \$22.5 million is expected to carry over into 2005 and beyond.

For the three months ended September 30, 2004, Laird's revenues were \$3.0 million, as compared to \$6.3 million for the same period last year. The decline in Laird's third quarter revenues, on a year over year basis as well as compared to the first and second quarters of 2004, is due primarily to their major customer deferring its maintenance program for the remainder of 2004. Laird estimates that the majority of the deferred maintenance will likely be performed sometime in 2005. As a result of lower revenues, Laird realized a loss before income taxes of \$0.9 million for the three months ended September 30, 2004, compared to earnings before income taxes of \$0.3 million for the same period last year.

For the nine months ended September 30, 2004, Laird incurred a loss before income taxes of \$1.5 million on contract revenue of \$14.1 million, compared to earnings before income taxes of \$1.0 million on contract revenue of \$20.6 million for the nine months ended September 30, 2003.

#### ***Corporate and Other***

For the three months ended September 30, 2004, the Corporate and Other segment incurred \$0.7 million of indirect and administrative expenses and \$0.1 million of interest and other costs, essentially unchanged from the comparable figures for the three months ended September 30, 2003.

For the nine months ended September 30, 2004, the Corporate and Other segment incurred \$2.1 million of indirect and administrative expenses and \$0.3 million of interest and other costs, as compared to \$1.9 million of indirect and administrative expenses and \$0.3 million of interest and other costs for the nine months ended September 30, 2003. The current year's costs include \$0.1 million associated with preparing to meet the new public company certification requirements that were introduced in the first quarter of 2004.

The Corporation incurred legal fees during the quarter ended September 30, 2004 with a law firm for which a Director of the Corporation is also a partner of the firm. The fees were for services rendered in the ordinary course of business. The amount paid in the quarter was thirty four thousand dollars.

At September 30, 2004 the Corporation had an interest bearing demand loan outstanding to the President and Chief Executive Officer to assist with housing arrangements in Edmonton in order to allow him to maintain offices in both Edmonton and Calgary. In addition, in relation to this

housing arrangement, market-rate rent payments were made by the Corporation in the amount of six thousand dollars during the quarter. Churchill has the option, renewable annually, to continue the monthly rent payments through September 30, 2006.

## CASH FLOW, FINANCING, CAPITAL REQUIREMENTS, LIQUIDITY

Churchill's working capital position at September 30, 2004 was \$9.9 million, down \$3.1 million from June 30, 2004, and down \$7.7 million from December 31, 2003. The \$3.1 million reduction of working capital during the third quarter of 2004 was the result of spending \$2.5 million on capital expenditures and repaying \$0.6 million in debt.

Capital expenditures for the three months ended September 30, 2004 were \$2.5 million, bringing total capital expenditures to \$7.1 million for the nine month period ended September 30, 2004. The Corporation's new modular fabrication facility is now ramping up production in structural steel and pipe spooling. The painting and fireproofing building was still under construction. Approximately \$3.6 million was spent on this facility in the first and second quarters of 2004, while \$2.1 million was spent in the third quarter. It is expected that an additional \$1.5 million of costs will be recorded in the remainder of 2004 relating to this new facility. The remaining \$0.4 million of capital expenditures in the three month period ended September 30, 2004 were primarily to replace portions of the vehicle fleet and upgrade certain computer hardware.

### Contractual Obligations (\$ millions)

	Payments due in		
	Total	Current year	1-3 years
Acquisition loan	\$ 5.6	\$1.6	\$4.0
Finance contracts and capital lease obligations	1.0	0.3	0.7
	6.6	1.9	4.7
Purchase obligations	1.5	1.5	-
	<u>\$ 8.1</u>	<u>\$3.4</u>	<u>\$4.7</u>

The acquisition loan, finance contracts, and capital lease obligations are more fully described in Note 3 of the Notes to the Consolidated Financial Statements that are included in the September 30, 2004 Third Quarter report.

The purchase obligations represent enforceable commitments made by the Corporation pertaining to the new modular fabrication facility, and will be paid in 2004 and 2005.

The Corporation paid \$0.6 million of long-term debt during the three months ended September 30, 2004 (\$0.5 million

for the three months ended September 30, 2003), and \$1.4 million for the nine months ending September 30, 2004 (\$1.3 million for the nine months ended September 30, 2003) in accordance with the established repayment schedules.

In addition, the Corporation had available at September 30, 2004 an operating line of credit of up to \$6.0 million (December 31, 2003 – \$10.5 million) which was not being utilized. The amount available under this facility is subject to limits based on certain financial ratios. The Corporation's previously unused equipment purchase line of credit was cancelled effective September 30, 2004.

Subsequent to September 30th, Churchill has raised \$5.3 million of long-term debt, replenishing working capital with the proceeds. On October 8, 2004 Churchill placed a \$1.3 million, 5 year mortgage on one of its properties. The mortgage bears interest at 6.45%, is secured by the mortgage and a site specific General Securities Agreement, and is repayable in blended monthly payments of ten thousand dollars, commencing December 1, 2004. On October 22, 2004, the Corporation entered into a \$4.0 million, 5 year term loan with its existing lender, secured by the existing General Securities Agreements, as well as a mortgage on the new modular fabrication facility. Interest on this loan is currently at prime plus 1.25%, but can be converted to a fixed interest rate at any time up to May 31, 2005. Principal repayments of \$0.2 million are required quarterly with the first payment due in November, 2004.

The effect of the new term loan, and mortgage was to increase cash by \$5.3 million, increase the current portion of long-term debt by \$0.8 million, and increase long-term debt by \$4.5 million thereby increasing working capital by \$4.5 million.

The acquisition loan, new \$4.0 million 5 year term loan, and the line of credit are subject to certain debt covenants calculated on a quarterly basis including but not limited to tests of tangible net worth, leverage and interest coverage. At September 30, 2004, the Corporation was not in compliance with certain of its debt covenants. The lender has provided waivers and revised covenants such that the Corporation is in compliance with the covenants in question, effective as at September 30, 2004 and through to September 30, 2005. Should future non-compliance of its financial covenants occur, the lender would be in a position to demand repayment of any balances outstanding under these facilities. The Corporation monitors the financial covenants on a continuous basis.

The Corporation continues to be a partner in two joint ventures. In each instance the Corporation has provided a joint and several guarantee, increasing the maximum potential payment to the full value of the work remaining

under the contract. The Corporation also provided a joint and several guarantee as part of the transaction in the first quarter of 2003 in which Churchill's interest in the Lafrentz Road Services business was sold to a third party. There is no maximum potential payment under the guarantee. The Corporation placed a portion of its proceeds from Lafrentz into an escrow account until February, 2008 as a reserve against potential claims under the guarantee. At September 30, 2004, \$0.2 million was in escrow.

As part of the purchase of Lakehead Insulation by Fuller Austin in January, 2002, there is potential future consideration of up to \$0.3 million payable to the vendors based on Lakehead's earnings for the three year period ending December 31, 2004. No contingent consideration has been earned to September 30, 2004 under this arrangement.

Shareholder's equity was \$28.6 million at September 30, 2004, as compared to \$29.5 million at June 30, 2004 and \$30.5 million at December 31, 2003. There were no purchases under the Normal Course Issuer Bid during the third quarter of 2004. Contributed surplus increased twenty six thousand dollars during the three months ended September 30, 2004 as a result of applying the new accounting principle related to stock-based compensation. Retained earnings declined during the third quarter, from \$19.9 million at June 30, 2004 to \$18.9 million at September 30, 2004, reflecting the \$1.0 million net loss for the quarter.

As at September 30, 2004, the Corporation had outstanding 12,223,352 common shares and 679,334 options convertible into common shares (December 31, 2003 – 11,863,652 common shares and 1,046,334 options), which is unchanged from June 30, 2004.

During the period October 1, 2004 to November 10, 2004, no options were issued or exercised, and no common shares were issued by the Corporation or purchased by the Corporation under the Normal Course Issuer Bid.

## **RISKS AND RISK MANAGEMENT**

Churchill's management team assesses risk on an ongoing basis, while management and the Board of Directors

periodically conduct a complete risk management assessment. The identified risks, such as oil and gas commodity pricing, oil and gas industry activity levels, severe weather changes, labour shortages, labour cost pressures, pre-construction third party activities, design-build project issues, bonding availability, project execution, and acquisition integration are considered with each major decision.

During the third quarter, Laird's financial results suffered as customers deferred work to future periods, while Triton incurred losses as a result of start-up in the fabrication facility and project execution in the field. Triton's management is revising field reporting processes in order to gain timelier job status information, which in turn should result in more timely corrective action. Triton is also enhancing the existing cost monitoring processes established for the fabrication facility.

The Board of Directors of the Corporation has become increasingly concerned about the poorer than expected financial results over the last few quarters. The Directors have joined senior management to form a special committee to review the operational and control systems of the companies experiencing difficulties, and to implement measures for improvement. The Board remains committed to the Corporation's strategic and operating plans.

## **2004 OUTLOOK**

During the three months ended September 30, 2004, Churchill secured a further \$74.1 million of contracts, and executed and took into revenue \$82.7 million net of \$1.2 million of inter-segment revenue. At September 30, 2004 the Corporation had \$338.4 million of work-in-hand, of which \$233.5 million is expected to carry forward into 2005 and beyond.

Churchill has experienced several operational issues over the nine months to September 30, 2004 that have resulted in disappointing contributions from Triton and Laird Electric. Management continues to focus its efforts on rectifying those situations in order to return Churchill to profitability.

## CONSOLIDATED BALANCE SHEETS

(\$ thousands)	September 30 2004 (Unaudited)	December 31 2003 (Audited)	September 30 2003 (Unaudited)
<b>ASSETS</b>			
Current assets			
Cash (Note 2)	\$ 14,002	\$ 14,622	\$ 7,748
Accounts receivable	74,454	67,513	77,432
Inventories and prepaid expenses	2,320	1,410	2,042
Properties for sale	103	103	103
Future income tax assets	1,765	-	-
Current portion of agreements receivable	-	138	103
	<b>92,644</b>	<b>83,786</b>	<b>87,428</b>
Agreements receivable	-	-	33
Future income tax assets	452	376	327
Property and equipment	14,618	9,568	9,095
Intangible assets	289	784	1,003
Goodwill	8,315	8,315	8,263
	<b>\$ 116,318</b>	<b>\$ 102,829</b>	<b>\$ 106,149</b>
<b>LIABILITIES</b>			
Current liabilities			
Accounts payable	\$ 56,346	\$ 50,949	\$ 50,656
Contract advances and unearned income	22,772	11,454	12,551
Income taxes payable	1,731	1,105	3,454
Future income tax liabilities	-	858	-
Current portion of long-term debt (Note 3)	1,878	1,864	1,819
	<b>82,727</b>	<b>66,230</b>	<b>68,480</b>
Long-term debt (Note 3)	4,686	5,635	6,126
Future income tax liabilities	350	483	734
	<b>87,763</b>	<b>72,348</b>	<b>75,340</b>
<b>SHAREHOLDERS' EQUITY</b>			
Share capital (Note 4)	4,265	3,794	3,624
Contributed surplus (Note 6)	5,380	5,128	5,128
Retained earnings	18,910	21,559	22,057
	<b>28,555</b>	<b>30,481</b>	<b>30,809</b>
	<b>\$ 116,318</b>	<b>\$ 102,829</b>	<b>\$ 106,149</b>

*The accompanying notes are an integral part of these consolidated financial statements.*

## CONSOLIDATED STATEMENTS OF EARNINGS

(\$ thousands, except per share amounts)	Three months ended September 30 (Unaudited)		Nine months ended September 30 (Unaudited)	
	2004	2003	2004	2003
Contract revenue	\$ 82,673	\$ 84,229	\$ 232,841	\$ 223,608
Contract costs	77,284	79,047	216,759	209,470
Contract income	5,389	5,182	16,082	14,138
Interest income	117	95	337	397
Sundry income	11	307	222	418
Indirect and administrative expenses	(5,859)	(5,600)	(17,362)	(17,026)
Bad debt recovery (expense)	(31)	3,000	21	(3)
Depreciation and amortization	(957)	(822)	(2,466)	(2,343)
Interest expense	(132)	(225)	(373)	(488)
Earnings (loss) before income taxes	(1,462)	1,937	(3,539)	(4,907)
Income tax (expense) recovery	480	(867)	1,081	1,732
Net earnings (loss)	\$ (982)	\$ 1,070	\$ (2,458)	\$ (3,175)
Net earnings (loss) per common share (Note 5)				
Basic	\$ (0.08)	\$ 0.09	\$ (0.20)	\$ (0.27)
Fully diluted	\$ (0.08)	\$ 0.09	\$ (0.20)	\$ (0.27)

*The accompanying notes are an integral part of these consolidated financial statements.*

## CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

(\$ thousands)	Three months ended September 30 (Unaudited)		Nine months ended September 30 (Unaudited)	
	2004	2003	2004	2003
Retained earnings, beginning of period	\$ 19,892	\$ 20,987	\$ 21,559	\$ 25,253
Stock-based compensation (Note 6)	-	-	(176)	-
Retained earnings, beginning of period, restated	19,892	20,987	21,383	25,253
Net earnings (loss)	(982)	1,070	(2,458)	(3,175)
Share redemption in excess of stated capital	-	-	(15)	(21)
Retained earnings, end of period	\$ 18,910	\$ 22,057	\$ 18,910	\$ 22,057

*The accompanying notes are an integral part of these consolidated financial statements.*

## CONSOLIDATED STATEMENTS OF NET CASH FLOW

(\$ thousands)	Three months ended September 30 (Unaudited)		Nine months ended September 30 (Unaudited)	
	2004	2003	2004	2003
<b>OPERATING ACTIVITIES</b>				
Net earnings (loss)	\$ (982)	\$ 1,070	\$ (2,458)	\$ (3,175)
Non-cash items				
Net equity earnings of affiliate	-	-	-	(80)
Depreciation and amortization	957	822	2,466	2,343
Gain on disposal of property and equipment	(1)	-	(57)	-
Future income taxes	(1,974)	-	(2,832)	(5,732)
Stock-based compensation (Note 6)	26	-	76	-
	<b>(1,974)</b>	1,892	<b>(2,805)</b>	(6,644)
Net change in accounts receivable, inventories and prepaid expenses	<b>(13,180)</b>	(11,891)	<b>(7,851)</b>	(746)
Net change in accounts payable, contract advances and unearned income	<b>8,370</b>	477	<b>16,715</b>	311
Net change in income taxes payable/recoverable	<b>2,684</b>	4,006	<b>626</b>	5,972
	<b>(4,100)</b>	(5,516)	<b>6,685</b>	(1,107)
<b>INVESTING ACTIVITIES</b>				
Proceeds from agreement receivable	-	(2)	<b>138</b>	126
Proceeds on disposal of property and equipment	<b>16</b>	19	<b>128</b>	83
Distributions from equity investee	-	-	-	1,496
Acquisition of subsidiary	-	-	-	(13,165)
Acquisition of property and equipment	<b>(2,539)</b>	(356)	<b>(7,092)</b>	(1,125)
	<b>(2,523)</b>	(339)	<b>(6,826)</b>	(12,585)
<b>FINANCING ACTIVITIES</b>				
Issuance of long-term debt	<b>272</b>	45	<b>494</b>	8,574
Repayment of long-term debt	<b>(588)</b>	(544)	<b>(1,429)</b>	(1,307)
Issuance of common shares	-	-	<b>474</b>	104
Redemption of common shares	-	-	<b>(18)</b>	(24)
	<b>(316)</b>	(499)	<b>(479)</b>	7,347
Decrease in cash	<b>(6,939)</b>	(6,354)	<b>(620)</b>	(6,345)
Net cash, beginning of period	<b>20,941</b>	14,102	<b>14,622</b>	14,093
Net cash, end of period	<b>\$ 14,002</b>	\$ 7,748	<b>\$ 14,002</b>	\$ 7,748

*The accompanying notes are an integral part of these consolidated financial statements.*

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### 1. *Basis of Presentation*

These interim unaudited consolidated financial statements should be read in conjunction with the audited financial statements for the fiscal year ended December 31, 2003 and notes thereto. These financial statements are prepared in accordance with generally accepted accounting principles for interim financial information in Canada; however, they do not conform in all respects to the disclosure requirements of generally accepted accounting principles for annual financial statements. The same accounting policies and methods were followed as were followed in the preparation of the audited annual financial statements for the financial year ended December 31, 2003, except for the application of the following new CICA Handbook Sections:

**Stock-based compensation** – Effective January 1, 2004, the Corporation adopted the fair value based method of accounting for stock options which were granted to employees on or after January 1, 2002, in accordance with the new recommendations of CICA Handbook Section 3870 *Stock-Based Compensation and Other Stock-based Payments*. The change was adopted retroactively without restatement. Under this method, the estimated fair value of the stock options granted is recognized over the applicable vesting period as a charge to stock compensation expense and a credit to contributed surplus. When these options are exercised, the proceeds received and the related amounts of contributed surplus are credited to share capital. For options granted prior to January 1, 2002, the Corporation continues to follow the applicable generally accepted accounting principle under which no expense is recognized; when these options are exercised, the proceeds are a credit to share capital. The impact on the financial statements arising from adoption of the fair value method is disclosed in Note 6.

**Asset Impairment** – Effective January 1, 2004, the Corporation adopted the new recommendations of CICA Handbook Section 3063 *Impairment of Long-Lived Assets*. Section 3063 requires that the impairment of long-lived assets held for use be established through a two-step process, with the first step determining when an impairment is recognized, and the second step measuring the amount of the impairment. An impairment loss is recognized when the carrying amount of a long-lived asset exceeds the sum of the undiscounted cash flows expected to result from its use and eventual disposition and is measured as the amount by which the long-lived asset's carrying amount exceeds its fair value. There is no material impact on the financial statements resulting from the adoption of Section 3063 either in the current or prior periods presented.

### 2. *Cash*

(\$ thousands)

Cash includes \$7,393 (December 31, 2003 – \$4,370; September 30, 2003 – \$2,216), which is restricted, under the British Columbia Lien Act, to the payment of direct costs related to specific construction projects.

### 3. *Long-Term Debt*

(\$ thousands)

	September 30, 2004	December 31, 2003	September 30, 2003
Acquisition loan	\$ 5,600	\$ 6,800	\$ 7,200
Finance contracts	957	683	726
Capital leases	7	16	19
	6,564	7,499	7,945
Less current portion	(1,878)	(1,864)	(1,819)
	\$ 4,686	\$ 5,635	\$ 6,126

In conjunction with the acquisition of Laird Electric Inc. in February, 2003, the Corporation entered into \$8,000 of floating-rate term debt, bearing interest at prime plus 1.25%, payable in quarterly installments of \$400 plus interest, and due February, 2008, secured by General Security Agreements. At September 30, 2004, the balance outstanding was \$5,600.

Finance contracts bear effective interest rates ranging from 2.9% to 8.4%, are payable in various monthly installments, mature at various dates up to 2009, and are secured by vehicles with a net book value of \$957.

### 3. *Long-Term Debt (continued)*

Capital leases which mature in 2005 and bear interest at 5.3%, are secured by equipment with a net book value of \$7.

Interest expense on long-term debt for the three months ended September 30, 2004, was \$118 (three months ended September 30, 2003 – \$126). For the nine months ended September 30, 2004, interest expense was \$322 (nine months ended September 30, 2003 – \$388).

In addition, the Corporation had available at September 30, 2004 an operating line of credit of up to \$6,000 (December 31, 2003 – \$10,500) which was not being utilized. The total amount available under this facility is subject to limits based on certain financial ratios. The Corporation's previously unused equipment line of credit was cancelled effective September 30, 2004.

Subsequent to September 30, 2004, the Corporation secured new term financing through two financial institutions –

- The Corporation entered into a \$4,000, 5 year term loan with its existing lender, secured by the existing General Security Agreements as well as a mortgage on the new modular fabrication facility. Interest on this loan is currently at prime plus 1.25%, but can be converted to a fixed interest rate at any time up to May 31, 2005. Principal repayments of \$200 are required quarterly with the first payment due in November, 2004.
- Churchill placed a \$1,300, 5 year mortgage on one of its properties. The mortgage bears interest at 6.45%, is secured by the mortgage and a site specific General Securities Agreement, and is repayable in blended monthly payments of \$10 commencing December 1, 2004.

The effect of the new term loan, and mortgage was to increase cash by \$5,300, increase the current portion of long-term debt by \$832, and increase long-term debt by \$4,468 thereby increasing working capital by \$4,468.

The acquisition loan, new \$4,000 5 year term loan, and the line of credit are subject to certain debt covenants calculated on a quarterly basis including but not limited to tests of tangible net worth, leverage and interest coverage. At September 30, 2004, the Corporation was not in compliance with certain of its debt covenants. The lender has subsequently provided waivers and revised covenants such that the Corporation is in compliance with the covenants in question, effective as at September 30, 2004 and through to September 30, 2005. Should further non-compliance of its financial covenants occur, the lender would be in a position to demand repayment of any balances outstanding under these facilities. The Corporation monitors the financial covenants on a continuous basis.

Estimated principal payments in the next five years, including the \$5,300 of subsequent financing are:

	to December 31,	2004	\$	697
		2005		2,741
		2006		2,709
		2007		2,657
		2008		1,327
		2009		653

### 4. *Share Capital*

(\$ thousands, except per share amounts)

	Nine months ended September 30 (unaudited)			
	2004		2003	
	Shares	Share Capital	Shares	Share Capital
Balance, December 31	11,863,652	\$ 3,794	10,864,040	\$ 1,300
Share options exercised for cash	367,000	474	72,000	104
Shares issued on acquisition	-	-	826,412	2,223
Shares repurchased under Normal Course Issuer Bid	(7,300)	(3)	(11,100)	(3)
<b>Balance, September 30</b>	<b>12,223,352</b>	<b>\$ 4,265</b>	<b>11,751,352</b>	<b>\$ 3,624</b>

#### 4. *Share Capital (continued)*

During 2004, 7,300 common shares (2003 – 11,100) were repurchased for cancellation pursuant to an ongoing Normal Course Issuer Bid at a cost of \$18 (2003 – \$24). Of this amount, \$3 (2003 – \$3) reduced share capital, with \$15 (2003 – \$21) being charged to retained earnings.

As at September 30, 2004 the Corporation had outstanding 679,334 options convertible into common shares (December 31, 2003 – 1,046,334).

#### 5. *Net Loss Per Common Share*

(\$ thousands, except per share amounts)

	Nine months ended September 30 (unaudited)	
	2004	2003
Net loss	\$ (2,458)	\$ (3,175)
Weighted average number of common shares outstanding	12,056,363	11,627,916
Incremental number of shares under treasury stock method	134,327	389,476
	12,190,690	12,017,392
Net loss per common share:		
Basic	\$ (0.20)	\$ (0.27)
Fully diluted	\$ (0.20)	\$ (0.27)

For the periods ended September 30, 2004 and September 30, 2003, the effect of outstanding share options on earnings per share were anti-dilutive as the Corporation is in a loss position.

#### 6. *Stock-Based Compensation*

(\$ thousands)

Effective January 1, 2004, the Corporation adopted the fair value method of accounting for employee stock options granted on or after January 1, 2002, retroactively without restatement as allowed under the transitional provision of CICA Handbook Section 3870. As a result, the opening balance of retained earnings has been decreased by \$176 and opening contributed surplus has been increased by a corresponding amount.

Stock compensation expense of \$76 was recognized for the nine months ended September 30, 2004 (2003 – \$0), representing the amortization of the estimated fair value of all options granted since January 1, 2002.

#### 7. *Segmented Information*

(\$ thousands)

The Corporation operates as a construction and maintenance services provider, primarily in western Canada. The Corporation is managed using five operating segments: Buildings, Industrial General Contracting, Industrial Insulation Contracting, Industrial Electrical Contracting, and Corporate and Other.

*Buildings* is active in the construction of commercial, institutional, light-industrial buildings and multi-unit residential buildings.

*Industrial General Contracting* includes heavy-industrial general contracting, fabrication, site work and ongoing maintenance.

*Industrial Insulation Contracting* includes all insulation, siding, fireproofing, asbestos abatement and plant maintenance services including, in certain instances, services provided to our industrial general contracting and industrial electrical contracting companies.

*Industrial Electrical Contracting* includes industrial electrical, instrumentation and power-line construction and maintenance services including, in certain instances, services provided to our industrial general contracting companies.

*Corporate and Other* includes ownership of the fabrication facility, which is available for use on a rental basis by any of the Corporation's segments, as well as all corporate costs not allocated directly to another business segment.

## 7. Segmented Information (continued)

The segmented information provided is after the elimination of inter-segment management fees and loan balances and any related interest charges.

Three Months Ended September 30, 2004	Contract Revenue	Earnings (Loss) Before Tax	Depreciation & Amortization	Goodwill	Total Assets	Capital Expenditures
Buildings	\$ 61,791	\$ 1,551	\$ 171	\$ -	\$ 74,205	\$ 65
Industrial General Contracting	10,460	(1,392)	218	-	8,390	285
Industrial Insulation Contracting	8,612	116	116	-	7,887	10
Industrial Electrical Contracting	2,971	(900)	340	8,315	11,082	16
Corporate and Other	-	(888)	112	-	15,465	2,163
Inter-segment Adjustments	(1,161)	51	-	-	-	-
	\$ 82,673	\$ (1,462)	\$ 957	\$ 8,315	\$ 117,029	\$ 2,539

Three Months Ended September 30, 2003	Contract Revenue	Earnings (Loss) Before Tax	Depreciation & Amortization	Goodwill	Total Assets	Capital Expenditures
Buildings	\$ 46,298	\$ 1,785	\$ 139	\$ -	\$ 55,192	\$ 67
Industrial General Contracting	10,962	(397)	221	-	10,374	176
Industrial Insulation Contracting	21,034	1,050	116	-	13,814	92
Industrial Electrical Contracting	6,318	343	297	8,263	12,376	22
Corporate and Other	-	(681)	49	-	14,393	-
Inter-segment Adjustments	(383)	(163)	-	-	-	(1)
	\$ 84,229	\$ 1,937	\$ 822	\$ 8,263	\$ 106,149	\$ 356

Three Months Ended September 30, 2004	Contract Revenue	Earnings (Loss) Before Tax	Depreciation & Amortization	Goodwill	Total Assets	Capital Expenditures
Buildings	\$ 177,480	\$ 1,282	\$ 508	\$ -	\$ 74,205	\$ 326
Industrial General Contracting	21,094	(2,236)	645	-	8,390	691
Industrial Insulation Contracting	25,329	1,431	345	-	7,887	162
Industrial Electrical Contracting	14,054	(1,498)	776	8,315	11,082	302
Corporate and Other	-	(2,418)	192	-	15,465	5,611
Inter-segment Adjustments	(5,116)	(100)	-	-	-	-
	\$ 232,841	\$ (3,539)	\$ 2,466	\$ 8,315	\$ 117,029	\$ 7,092

Three Months Ended September 30, 2003	Contract Revenue	Earnings (Loss) Before Tax	Depreciation & Amortization	Goodwill	Total Assets	Capital Expenditures
Buildings	\$ 134,273	\$ (2,705)	\$ 445	\$ -	\$ 55,192	\$ 286
Industrial General Contracting	29,253	(2,445)	657	-	10,374	365
Industrial Insulation Contracting	41,454	1,616	353	-	13,814	222
Industrial Electrical Contracting	20,620	1,020	737	8,263	12,376	217
Corporate and Other	-	(2,218)	151	-	14,393	36
Inter-segment Adjustments	(1,992)	(175)	-	-	-	(1)
	\$ 223,608	\$ (4,907)	\$ 2,343	\$ 8,263	\$ 106,149	\$ 1,125

## 8. Comparative Figures

Certain of the comparative figures have been adjusted to be consistent with the current year's presentation.

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Inquiries regarding change of address, registered shareholdings,  
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