MAXICARE HEALTH PLANS INC
Form 10-K
April 11, 2003

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One) x	**ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2002

or

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

Commission file number: 0-12024

Maxicare Health Plans, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**95-3615709**
(State or other jurisdiction of incorporation or organization)	*(IRS Employer Identification No.)*
11231 South La Cienega Boulevard, Los Angeles, California	**90045**
(Address of principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code: (310) 649-7166

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

Title of each class	Name of each exchange

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, $.01 par value

(Title of Class)

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 x 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. x

The aggregate market value of the voting stock held by non-affiliates of the registrant as of April 10, 2003.

Common Stock, $.01 par value $38,965

The number of shares outstanding of each of the issuer s classes of capital stock, as of April 10, 2003.

Common Stock, $.01 par value 9,741,926 shares

DOCUMENTS INCORPORATED BY REFERENCE

Part III is incorporated by reference from the registrant s definitive proxy statement in connection with its 2003 Annual Meeting of Shareholders to be filed within 120 days of the close of the registrant s fiscal year.

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PART I

Item 1. *Business*

General

Since January 1, 2002 we have not been engaged in any active business and we have no reasonable prospects of obtaining or generating any ongoing business. At December 31, 2002 we had a substantial capital deficiency.

As noted above, we have no continuing business activities. We are in the process of exploring possible strategies to realize any possible value remaining in the Company. It is likely, however, that it will be necessary for us to liquidate. We cannot give assurance that any liquidation would provide any value to our shareholders.

We are a Delaware Corporation, organized on January 5, 1981. Our executive offices are located at 11231 South La Cienega Boulevard, Los Angeles, California 90045 and our telephone number is (310) 649-7166.

Disposition of Subsidiaries

Through our wholly-owned subsidiaries, we operated health maintenance organizations (HMOs) in California (through May 25, 2001) and Indiana (through May 3, 2001). Maxicare Life and Health Insurance Company, our licensed insurance company, operated preferred provider organizations (PPOs) in California (through December 31, 2001) and Indiana (through May 3, 2001) in conjunction with the HMO products of Maxicare (our California HMO) and Maxicare Indiana, Inc. (our Indiana HMO). As of January 1, 2002 our operations were substantially terminated.

On May 25, 2001, the California Department of Managed Health Care issued an order appointing a conservator for the California HMO. Also on that date the California HMO filed for Chapter 11 bankruptcy protection. Effective June 5, 2001, the California HMO and the California Department of Managed Health Care reached an agreement allowing the California HMO s bankruptcy filing to remain in effect. Effective August 31, 2001, the California HMO terminated its Medicare product. Effective November 30, 2001 the California HMO completed the assignment of its Medi-Cal contracts to other health care providers, effectively terminating the California HMO s Medi-Cal line of business. Effective December 31, 2001, all commercial membership was transferred to other health plans, leaving the California HMO with no operations. On December 31, 2001 the California HMO surrendered its California HMO license. On February 26, 2003 the California HMO s Liquidating Plan of Reorganization was confirmed in the United States Bankruptcy Court. It is unlikely that we will receive any distribution of assets from the California HMO.

The Indiana HMO is incorporated under the laws of the state of Indiana and is primarily regulated by the Indiana Department of Insurance. On May 4, 2001, the Indiana Department of Insurance placed the Indiana HMO into rehabilitation. The effect of this action was to terminate the ongoing operations of the Indiana HMO as of that date. The Indiana HMO was formally placed into liquidation on July 3, 2001. On that date the Indiana Commissioner of Insurance was appointed as Liquidator. It is unlikely that we will receive any distribution of assets from the Indiana HMO.

Maxicare Life and Health Insurance Company, Inc. is incorporated under the laws of the state of Missouri and is primarily regulated by the Missouri Department of Insurance. On May 24, 2001 the Missouri Department of Insurance placed Maxicare Life and Health Insurance Company, Inc. under administrative supervision. Maxicare Life and Health Insurance Company, Inc. ceased offering all products effective December 31, 2001, effectively ceasing all operations. On January 28, 2002 the Missouri Department of Insurance placed Maxicare Life and Health Insurance Company, Inc. into rehabilitation. . On March 4, 2003 the Board of Directors of Maxicare Life and Health Insurance Company agreed to its liquidation. It is unlikely that we will receive any distribution of assets from Maxicare Life and Health Insurance Company.

We also own and operate Health Care Assurance Company, Ltd., a captive insurer that provided certain insurance coverage to us and our subsidiaries. Effective January 31, 2002, Health Care Assurance Company, Ltd ceased providing all such insurance. We also served as administrator of the California Access for Infants and Mothers program (AIM) program through another of our subsidiaries. Administration of the AIM program was transferred to another health care provider effective March 15, 2002.

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Forward Looking Statements

Statements in this Form 10-K annual report may be forward looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, but are not limited to, statements that express our intentions, beliefs, expectations, strategies, predictions or any other statements relating to our future activities or other future events or conditions. These statements are based on current expectations, estimates and projections about our business based, in part, on assumptions made by management. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may, and probably will, differ materially from what is expressed or forecasted in the forward-looking statements due to numerous factors, including those described above and those risks discussed from time to time in the Form 10-K annual report, including the risks described under Risks Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations and in other documents which we file with the Securities and Exchange Commission. In addition, such statements could be affected by risks and uncertainties related to our financial condition, as well as general market conditions and growth rates, and general economic conditions. Any forward-looking statements speak only as of the date on which they are made, and we do not undertake any obligation to update any forward-looking statements to reflect events or circumstances after the date of this Form 10-K.

Risk Factors

Because we have no ongoing operations and no prospects of generating funds, we may not be able to continue in existence.

At December 31, 2002:

- We had a consolidated working capital deficiency of approximately $7.5 million.

- We had a deficiency in shareholders equity of approximately $9.6 million.

- Only $183,000 of our cash and cash equivalents of $2.6 million was immediately available to us; the remainder of our cash and cash equivalents was held at subsidiaries where the transfer of cash to us requires the approval of regulatory authorities, which we may not receive. Subsequent to December 31, 2002, we were able to transfer $100,000 from one of our subsidiaries to MHP.

- We had no means of generating cash or working capital.

- We had substantial contingent liabilities, including a claim by the Commissioner of the Indiana Department of Insurance seeking at least $3.5 million in money damages, a claim under a management information services agreement of up to $12.0 million, an undetermined liability in connection with a building we lease that must be returned to its original condition upon termination of the lease, and an undetermined amount due under a pharmacy services agreement.

As a result, we cannot give any assurance that it will not be necessary for us to seek protection under the Bankruptcy Code or liquidate without paying any consideration to our shareholders.

Because our shares are not listed on a stock exchange, our shares are subject to the penny stock rules, which make it difficult to purchase or sell our shares.

Our common stock is subject to the SEC s penny-stock rules, which impose additional sales practice requirements on broker-dealers who sell our stock to persons other than established customers and institutional accredited investors. These rules may affect the ability of broker-dealers to sell our common stock and may affect the ability of our shareholders to sell any common stock they may own.

Employees

As of March 31, 2003 we had no full-time employees. Certain employees of our California HMO work for us on a part time basis. We reimburse the California HMO for the cost of their time under an established agreement.

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Our Executive Officers

Our executive officers at March 31, 2003 were as follows:

Name	Age	Position
Paul R. Dupee, Jr.	59	Chairman of the Board of Directors, Chief Executive Officer
Alan D. Bloom	57	Senior Vice President, Secretary and General Counsel
Patricia A Fitzpatrick	51	Treasurer
Joseph W. White	44	Chief Financial Officer, Director

Paul R. Dupee, Jr. was appointed Chairman of the Board of Directors in June 1999 and Chief Executive Officer of the Company in August 1999. For more than five years prior hereto, Mr. Dupee has been a private investor. From 1996 through 2000, he served as a Director of the Lynton Group, Inc. serving as Chairman from 1998 to 2000. From 1986 through 1996, Mr. Dupee was Director and Vice Chairman of the Boston Celtics Limited Partnership, which owns the National Basketball Association team, the Boston Celtics. Mr. Dupee has been a director of the Company since May 1998.

Alan D. Bloom has been Senior Vice President, Secretary and General Counsel to the Company since July 1987. Mr. Bloom joined the Company as General Counsel in 1981.

Patricia A. Fitzpatrick has served as Treasurer of the Company since July 1998. Previously, Ms. Fitzpatrick served as Assistant Treasurer of the Company from July 1988 to July 1998.

Joseph W. White has served as Chief Financial Officer of the Company since November 2001. Prior to November 2001 Mr. White served as Controller and Interim Chief Financial Officer since February 2001. Mr. White was named a Director of the Company in March 2002 and has served in various financial positions with the Company since March 1987. Mr. White is a certified public accountant.

Item 2. ***Properties***

We lease space at three locations in California. All of these leases have remaining terms of less than two years. Our executive offices are located at 11231 South La Cienega Boulevard, Los Angeles, California 90045, pursuant to a lease expiring in May 2004. Under the terms of this lease, we pay a monthly rental of approximately $19,500, plus a percentage of operating costs and annual increases. Through March 31, 2003, the California HMO and Maxicare Life and Health Insurance Company were sharing space with us and paying a substantial portion of our lease costs, and may continue to do so.

Item 3. ***Legal Proceedings***

a. Promissory Note

At April 1, 2001, a note held by MHP in the approximate amount of $2.9 million (including accrued interest) became due. The note, issued by Eugene Froelich, a shareholder and former executive officer of MHP, was not paid, and we commenced an action in California state court to collect on the note. On October 18, 2001, the court granted summary adjudication and judgment was entered in our favor. On November 14, 2002, the California Court of Appeals affirmed the judgment**.** On or about March 14, 2003, Mr. Froelich satisfied the judgment in the net stipulated amount of $3.41 million by paying $2.583 million to MHP and by paying over the balance of $.767 million to the Sheriff pursuant to an attachment by Peter J. Ratican, as more fully set forth below. Offset against the judgment of $3.41 million was $.06 million that Mr. Froelich agreed to accept in full settlement of his claim against the Company in connection with his benefits under our Supplemental Executive Retirement Plan.

b. Indiana Department of Insurance

On or about June 25, 2001, the Commissioner of the Indiana Department of Insurance (the Commissioner), as the rehabilitator of Maxicare Indiana, Inc., the Company s Indiana HMO, filed a complaint (the Complaint) in the Marion County Circuit Court of Indiana against the Company and the five directors of the Indiana HMO, one of whom was a director of the Company. The Commissioner amended the Complaint on February 1, 2002. The Complaint, as amended, alleges, in substance, that: (1) the directors of the Indiana HMO breached their fiduciary duty by failing to maintain a plan providing for continuation of care benefits in the event that the Indiana HMO was placed in receivership, and that the Company is also liable for such failure; (2) the Company fraudulently

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concealed the financial condition of the Indiana HMO; (3) the Company manipulated the finances of the Indiana HMO for the Company s own benefit; and (4) the Company received preferential and/or fraudulent transfers of money from the Indiana HMO. The amended Complaint requests money damages but does not specify the amount of damages sought, except that it seeks approximately $3.5 million respecting the alleged preferential and/or fraudulent transfers. All defendants answered the amended Complaint on April 5, 2002. Pre-trial discovery is proceeding but is not yet completed. The Company believes that the claims against it are without merit and intends to vigorously defend the suit.

c. Derivative Action

On or about June 6, 2002, Mr. Froelich commenced a purported derivative action in the Superior Court of the State of California, Los Angeles County, on behalf of the Company against certain of its former and current officers and directors. The complaint, which names the Company as a nominal defendant, alleges, in substance, that the officers and directors breached their fiduciary duty to the Company in that they flagrantly mismanaged company affairs. The action seeks compensatory damages of not less than $10 million, together with an unspecified amount of punitive damages. On November 14, 2002 the Court dismissed the complaint with leave to replead. By order dated February 4, 2003, the action was dismissed without prejudice.

d. Executive Retirement

On or about July 1, 2002, Mr. Froelich commenced an action in the Superior Court of the State of California, County of Los Angeles, against the Company and certain unnamed Company officers/directors. The complaint alleges that defendants denial of a lump sum payment to Mr. Froelich under the Company s Supplemental Executive Retirement Program and the suspension of payments to him under such Program for one year constituted breaches of contract, breaches of fiduciary duty and violations of the Employee Retirement Income Security Act. The action seeks compensatory damages of no less than $1.0 million, punitive damages in an amount to be determined and an award of attorneys fees. On July 23, 2002, defendants served an answer to the complaint, and on July 26, 2002, defendants removed the case from California state court to the United States District Court for the Central District of California. On January 31, 2003, the District Court granted summary judgment in favor of the Company dismissing the action, and Mr. Froelich s time to appeal has now expired. On March 14, 2003 the Company satisfied its liability to Mr. Froelich under the Supplemental Executive Retirement Plan in conjunction with the settlement of a judgment against Mr. Froelich (see Item 3. Legal Proceedings, a. Promissory Note).

e. Consulting Agreement

On or about February 10, 2003, Peter J. Ratican, a shareholder and former executive officer and director of MHP, commenced an action against the Company in the Superior Court of the State of California, alleging that the Company had breached his consulting agreement with it and claiming damages in excess of $700,000. On March 11, 2003, Mr. Ratican obtained an attachment in the amount of $767,000 against the Company in connection with his claim. There has been no pre-trial discovery to date in the case. The Company intends to defend the action and to assert offsets and counterclaims against Mr. Ratican.

f. Business Services Agreement

On September 1, 2000 the Company entered into an Application and Business Services Agreement (the Trizetto Agreement) with the Trizetto Group, Inc. (TZG). The Trizetto Agreement called for TZG to provide a full range of management information services to us over a period of seven years in exchange for monthly payments. It also called for a termination payment to be made by us under certain circumstances. In March 2001, the Company assigned the Trizetto Agreement to Maxicare, the Company s California HMO. The California Department of Managed Health Care and the Committee of Creditors Holding Unsecured Claims in the California HMO s bankruptcy proceeding have questioned the validity of that assignment. The California HMO has continued to pay TZG for post-petition services at a monthly amount less than that contemplated in the Trizetto Agreement while TZG has provided services at a lower level than that contemplated in the Trizetto Agreement. TZG has asserted various pre- and post-petition claims in the California bankruptcy proceeding in connection with the Trizetto Agreement. On or about March 13, 2003, TZG sued the Company in California state court, alleging breach of the Trizetto Agreement and claiming over $12 million in damages. There have been no further proceedings to date in this case.

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g. Office of Personnel Management

In or about November 1999, in substance, MHP, on its own behalf and also on behalf of various closed and then operating subsidiaries, commenced an action in the United States Court of Federal Claims against the United States, seeking to recover approximately $9 million for the underpayment of amounts due for health care coverage provided to employees of the United States Office of Personnel Management. The parties are engaged in settlement discussions. We cannot give any assurances as to the ultimate collection of amounts associated with this action.

h. Back Office Services Agreement

Effective February 2, 2000, the Company entered into a Services Agreement for Back Office Administration with Nichols TXEN Corporation calling for Nichols TXEN to provided certain claims adjudication services to certain of our subsidiaries in exchange for a predetermined per member per month fee. On September 18, 2002 CSC Healthcare, Inc. (CSC), the successor in interest to Nichols TXEN, filed a complaint in the Circuit Court of Jefferson County, Alabama seeking approximately $880,000 plus interest from the Company under the contract. This action has been stayed and the claim is now being heard in arbitration, which is in a preliminary stage. The Company believes that the claim against it is without merit and intends to vigorously defend the arbitration. The Company has asserted counterclaims against CSC in the arbitration alleging that it was fraudulently induced to enter into the contract and that CSC failed to perform under the contract, thereby causing damages to the Company in an amount not less than $5 million.

i. Other Litigation

We are also involved in other legal actions in the normal course of business. We do not believe that any ultimate liability in excess of amounts accrued which would likely arise from these actions would materially affect our consolidated financial position, results of operations or cash flows, except that the matters described above involving the Indiana Department of Insurance and TZG, as well as certain other matters described in Item 8 of Part II hereof, may have such effect.

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

No matter was submitted to a vote of security holders during the three months ended December 31, 2002.

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PART II

Item 5. ***Market for the Registrant s Common Stock and Related Shareholder Matters***

(a) *Market Information*

Our Common Stock trades on the Over the Counter Bulletin Board under the trading symbol MAXIQ.

The following table sets forth the high and low sale prices per share of our common stock. The quotations are interdealer prices without retail mark-ups, markdowns, or commissions, and may not represent actual transactions.

On March 27, 2001 we effected a one-for-five reverse split of our common stock. All share and per share information in this Annual Report on Form 10-K retroactively reflect the reverse split as if it had been in effect from the beginning of the periods covered.

Common Stock

	Sale Price	
	High	Low
2002		
First Quarter	$ .02	$ .01
Second Quarter	$ .01	$ .01
Third Quarter	$ .01	$ .01
Fourth Quarter	$ .01	$ .01
2001		
First Quarter	$5.00	$2.03
Second Quarter	$2.19	$ .01
Third Quarter	$ .05	$ .01
Fourth Quarter	$ .03	$ .01

Our common stock is subject to the SEC s penny-stock rules, which impose additional sales practice requirements on broker-dealers who sell our stock to persons other than established customers and institutional accredited investors. These rules may affect the ability of broker-dealers to sell our common stock and may affect the ability of our shareholders to sell any common stock they may own.

(b) *Holders*

There were 896 holders of record of our Common Stock as of December 31, 2002.

(c) *Dividends*

We have not paid any cash dividends on our Common Stock and have no intention of doing so in the near future.

(d) *Sales of Unregistered Equity Security*

During 2002 we had no sales of unregistered equity securities.

(e) *Securities Authorized for Issuance Under Equity Compensation Plans*

No securities were authorized for issuance during 2002 pursuant to equity compensation plans.

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Item 6. ***Selected Financial Data***

	For the Years Ended December 31,				
	2002	**2001**	**2000**	**1999**	**1998**
	(Amounts in thousands except per share and membership data)				
Continuing operations(1):					
Revenues					
Premiums	$	$ 1,819	$ 2,343	$ 1,928	$ 1,798
Investment income(2)	569	239	529	288	888
Inter-company service agreement income			11,599	13,035	11,848
Other income	268	971	398	4,103	1,734
Total revenues	837	3,029	14,869	19,354	16,268
Expenses					
Health care expenses (credits)	(312)	582	2,615	866	521
Salary, general and administrative expenses	1,062	4,998	23,147	13,339	16,822
Depreciation and amortization	120	704	962	916	548
Impairment of leased assets	1,036				
Charges for litigation and management settlements(3)	209		1,510	5,500	250
Total expenses	2,115	6,284	28,234	20,621	18,141
Loss from continuing operations before income taxes	(1,278)	(3,255)	(13,365)	(1,267)	(1,873)
Income tax provision			(18,229)		
Net loss from continuing operations	(1,278)	(3,255)	(31,594)	(1,267)	(1,873)
Discontinued operations:					
Loss from discontinued operations (4)		(28,095)	(33,352)	(10,997)	(25,660)
Write-off of excess of rehabilitated and bankrupt subsidiaries liabilities over assets (5)		16,423			
Loss from discontinued operations	0	(11,672)	(33,352)	(10,997)	(25,660)
Net Loss	$(1,278)	$(14,927)	$(64,946)	$(12,264)	$(27,533)
Net loss per common share:					
Basic:(6)					
Basic loss per common share from continuing operations	$ (.13)	$ (.33)	$ (6.46)	$ (.35)	$ (.52)
Basic loss per common share from discontinued operations	$	$ (1.20)	$ (6.81)	$ (3.07)	$ (7.16)
Weighted average number of common shares outstanding	9,742	9,742	4,894	3,585	3,586

Diluted:(6)					
Diluted loss per common share from continuing operations	$ (.13)	$ (.33)	$ (6.46)	$ (.35)	$ (.52)
Diluted loss per common share from discontinued operations	$	$ (1.20)	$ (6.81)	$ (3.07)	$ (7.16)
Weighted average number of common and common dilutive potential shares outstanding	9,742	9,742	4,894	3,585	3,586

	At December 31,				
	2002	**2001**	**2000**	**1999**	**1998**
Balance Sheet Data:					
Assets of continuing operations	$ 2,643	$ 5,136	$ 13,198	$ 29,151	$ 32,181
Indebtedness of continuing operations(7)	$12,250	$12,942	$ 17,099	$ 19,931	$ 10,557
Net assets of discontinued operations(1)	$	$	$ 11,042	$ 33,936	$ 31,332
Shareholders equity (deficit)	$ (9,607)	$ (7,806)	$ 7,141	$ 43,156	$ 52,956
Membership Data:					
Number of members	0	0	416,000	466,600	512,000

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NOTES TO SELECTED FINANCIAL DATA

The selected financial data should be read in conjunction with Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations and Item 8. Financial Statements and Supplementary Data.

(1) The placement of our Indiana HMO into rehabilitation on May 4, 2001 and the bankruptcy filing of our California HMO on May 25, 2001 have effectively ended our involvement in the managed care industry. As a result, we have treated our HMO subsidiaries as discontinued operations in the preparation of these financial statements. (See Item 8. Financial Statements and Supplementary Data Notes 2 and 10 to our Consolidated Financial Statements .)

(2) In 2002 we recorded investment income of $521,000 in connection with the March, 2003 collection of a note that had been issued by a former executive officer of the Company. (See Item 8. Financial Statements and Supplementary Data Note 5 to our Consolidated Financial Statements .)

(3) In 2002 we recognized a gain of $671,000 in connection with the settlement of a former executive s benefits under our Supplemental Executive Retirement Plan. Additionally in 2002 we recorded $880,000 in legal reserves in connection with a contract we had previously entered into for the benefit of our subsidiaries. In 2000 we recorded charges of $785,000 for employee severance costs and $725,000 in litigation reserves for costs associated with the defense and settlement of various legal actions. A $5.5 million charge for management settlement costs was recorded in 1999. A $250,000 charge for litigation costs was recorded in 1998. (See Item 8. Financial Statements and Supplementary Data Note 9 to our Consolidated Financial Statements .)

(4) The loss from discontinued operations in 2000 includes charges of $4.9 million, for losses associated with certain of our capitated provider arrangements. The loss from discontinued operations for 1999 includes a $3.0 million charge for loss contracts related to the Carolinas commercial line of business. The loss from discontinued operations for 1998 includes a $10 million charge for loss contracts and divestiture costs and a $6.25 million charge for litigation, provider insolvency/impairment, and an increase to the loss contracts and divestiture costs reserve. (See Item 8. Financial Statements and Supplementary Data Note 10 to our Consolidated Financial Statements .)

(5) The results of discontinued operations for the year ended December 31, 2001 include a gain of $16.4 million realized by MHP in the second quarter of 2001 upon the placement of the Indiana HMO into rehabilitation, the subsequent disposition of Maxicare Life and Health Insurance Company, and the placement of the California HMO into Chapter 11 bankruptcy. This gain represents the extent to which consolidated losses of those entities through May 3, 2001 (the Indiana HMO and Maxicare Life and Health Insurance Company, Inc.) and May 24, 2001 (the California HMO) exceeded MHP s investment in those subsidiaries. (See Item 8. Financial Statements and Supplementary Data Note 2 to our Consolidated Financial Statements .)

(6) All share and per share amounts have been retroactively restated to reflect the one for five reverse stock split completed on March 27, 2001.

(7) Includes long-term liabilities of $2.1 million, $3.8 million, $5.1 million, $1.2 million and $.1 million, in 2002, 2001, 2000, 1999, and 1998, respectively.

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

Current Status

We have no active business and no reasonable prospects of obtaining or generating any active business

On December 31, 2001, we effectively ceased all operations. On that date, our California HMO and PPO terminated all membership. Our remaining operations at December 31, 2001 consisted of Health Care Assurance Company, Ltd., a captive insurer that provided certain insurance coverage to us and our subsidiaries, and our administration of the California Access for Infants and Mothers (AIM) program through another of our subsidiaries. The activities of Health Care Assurance Company, Ltd., essentially ended with the termination of our HMO and PPO business. Our involvement with the AIM program ended on March 15, 2002.

We are exploring possible strategies to realize any possible value remaining in the Company. Any such strategy may include the ultimate liquidation of Health Care Assurance Company, Ltd.; however, because of our financial condition and the claims of our creditors, we may seek protection under the Bankruptcy Code.

Liquidity/ Working Capital Deficiency

As noted above, we have terminated all operations. At December 31, 2002, we had a consolidated working capital deficiency of approximately $7.5 million, and a deficiency in shareholders equity of approximately $9.6 million. Furthermore, of our total cash and cash equivalents of $2.6 million at December 31, 2002, all but $183,000 was held at subsidiaries where the transfer of cash to MHP requires the approval of regulatory authorities. Subsequent to December 31, 2002, we were able to transfer $100,000 from one of our subsidiaries to MHP. We may not be able to transfer any more funds from our subsidiaries to MHP. MHP has certain contractual undertakings for which it may be liable and there are various alleged claims that may be asserted against it, including, among others, undertakings to and/or purported claims against it by vendors and former employees of its subsidiaries who have provided goods or services to those subsidiaries.

At April 1, 2001, a note held by MHP in the approximate amount of $2.9 million (including accrued interest) became due. The note, issued by a shareholder and former executive officer of MHP, was not paid, and we commenced an action in California state court to collect on the note. On October 18, 2001, the court granted summary adjudication in our favor. On November 14, 2002 the California Court of Appeal affirmed the summary adjudication. On March 14, 2003, the former executive satisfied the judgment in the net stipulated amount of $3.41 million by paying $2.583 million to MHP and by paying over the balance of $.767 million to the Sheriff pursuant to an attachment by another former executive. Offset against the judgment of $3.41 million was $.06 million that the former executive agreed to accept in full settlement of his claim against the Company in connection with his benefits under our Supplemental Executive Retirement Plan. The note is presented as a reduction in shareholders equity in the consolidated balance sheets at December 31, 2002 and 2001.

In or about November 1999, in substance, MHP, on its own behalf and also on behalf of various closed and then operating subsidiaries, commenced an action in the United States Court of Federal Claims against the United States, seeking to recover approximately $9 million for the underpayment of amounts due for health care coverage provided to employees of the United States Office of Personnel Management. This action remains pending.

MHP has defaulted in making the monthly payments due a former executive under his consulting agreement since October of 2001. The total amount due the former executive for the period of October 2001 through December 2002 is approximately $645,000. Under that agreement, the former executive may elect to receive the present value of the remaining consulting fees due to him through June 30, 2003, which is estimated at no more than $950,000. On March 11, 2003, the former executive obtained an attachment in the amount of approximately $767,000 against the Company in connection with his claim.

We are involved in various legal actions brought against us in the normal course of business, some of which seek damages in amounts that exceed those accrued in our consolidated balance sheets. The ultimate liability for these legal actions cannot be determined and could materially affect our consolidated financial position, results of operations or cash flows, if resolved unfavorably. See Item 8 Note 3 Commitments and Contingencies .

Disposition of Subsidiaries

On May 25, 2001, the California Department of Managed Health Care issued an order appointing a conservator for the California HMO. Also on that date the California HMO filed for Chapter 11 bankruptcy protection. Effective June 5, 2001, the California HMO and the California Department of Managed Health Care reached an agreement allowing the California HMO s bankruptcy filing to remain in effect. Effective August 31, 2001, the California HMO terminated its Medicare product. Effective November 30, 2001 the California HMO completed the assignment of its Medi-Cal contracts to other health care providers, effectively terminating the California HMO s Medi-Cal line of business. Effective December 31, 2001, all commercial membership was transferred to other health plans, leaving the California HMO with no operations. On December 31, 2001 the California HMO surrendered its California HMO license. On February 26, 2003 the California HMO s Liquidating Plan of Reorganization was confirmed in the United States Bankruptcy Court. It is unlikely that we will receive any distribution of assets from the California HMO.

On May 24, 2001 the Missouri Department of Insurance placed our subsidiary, Maxicare Life and Health Insurance Company, Inc., under administrative supervision. Maxicare Life and Health Insurance Company, Inc. ceased offering all products effective December 31, 2001, effectively ceasing all operations. On January 28, 2002 the Missouri Department of Insurance placed Maxicare Life and Health Insurance Company, Inc. into rehabilitation. On March 4, 2003 the Board of Directors of Maxicare Life and Health Insurance Company agreed to its liquidation. It is unlikely that we will receive any distribution of assets from Maxicare Life and Health Insurance Company.

On May 4, 2001, the Indiana Department of Insurance placed the Indiana HMO into rehabilitation. The effect of this action was to terminate the ongoing operations of the Indiana HMO as of that date. The Indiana HMO was formally placed into liquidation on July 3, 2001. On that date the Indiana Commissioner of Insurance was appointed as Liquidator. It is unlikely that we will receive any distribution of assets from the Indiana HMO.

As a result of these events, results for the year ended December 31, 2001 include the Indiana HMO only through May 3, 2001. The financial results of Maxicare Life and Health Insurance Company are also included in the 2001 results only through May 3, 2001, due to the contribution of the capital stock of Maxicare Life and Health Insurance Company to the Indiana HMO effective December 31, 2000. The results of the California HMO are included in our results only through May 24, 2001.

Discontinued Operations

The placement of the Indiana HMO into rehabilitation and the bankruptcy filing of the California HMO have effectively ended our involvement in the managed care industry. As a result, we have treated our HMO subsidiaries and Maxicare Life and Health Insurance Company, Inc. as discontinued operations in the preparation of our financial statements. Although our remaining operations (parent, Health Care Assurance Company, Ltd., and the AIM program through March 15, 2002) are insignificant in size, financially dependent upon our California and Indiana HMOs, and may also be terminated, they represent services not intrinsically linked to the managed care industry and have been treated as continuing operations.

Results of Operations

Year Ended December 31, 2002 Compared to Year Ended December 31, 2001

We reported a net loss of $1.3 million ($.13 per share basic and diluted) for the year ended December 31, 2002. We reported a net loss of $14.9 million ($1.53 per share basic and diluted) for the year ended December 31, 2001. Net income for the year ended December 31, 2002 included investment income of $521,000 recorded in connection with the previously mentioned collection of a note that had been issued by a former executive officer of the Company. In 2002 we also recognized a gain of $671,000 in connection with the settlement of a former executive s benefits under our Supplemental Executive Retirement Plan and $880,000 in legal reserves in connection with a contract we had previously entered into for the benefit of our subsidiaries. Losses from continuing operations for the year ended December 31, 2001 were $3.3 million; losses from discontinued operations for the year ended December 31, 2001 were $11.7 million, which included a gain of $16.4 million realized by MHP upon the placement of our Indiana HMO (to which MHP had contributed the capital stock of Maxicare Life and Health Insurance Company effective December 31, 2000) into rehabilitation and the bankruptcy of our California HMO. This gain represents the extent to which liabilities of those subsidiaries exceeded their assets at May 3, 2001 (the Indiana HMO and Maxicare Life and Health Insurance Company) or May 25, 2001 (the California HMO).

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Year Ended December 31, 2001 Compared to Year Ended December 31, 2000

We reported a net loss of $3.3 million, or $.33 per share (basic and diluted), from continuing operations for the year ended December 31, 2001. We sustained a loss of $31.6 million, or $6.46 per share (basic and diluted), from continuing operations for the year ended December 31, 2000. Year 2000 results from continuing operations included an $18.2 million non-cash charge associated with the write off of deferred tax assets.

Revenues from continuing operations decreased by $11.8 million in 2001 when compared to 2000 due to the assumption of MHP s inter-entity service agreements by the California HMO effective January 1, 2001. Through December 31, 2000, our HMOs and Maxicare Life and Health Insurance Company, Inc. paid monthly fees to MHP pursuant to administrative services agreements for various management, financial, legal, computer and telecommunications services. As a result of a corporate reorganization and simplification implemented on December 31, 2000, certain employees performing functions in support of the administrative service agreements were transferred from MHP to the California HMO. For the period January 1, 2001 to April 30, 2001 the Indiana HMO and Maxicare Life and Health Insurance Company, Inc. paid monthly fees to the California HMO for the services previously provided to them by MHP. Prior to the reclassification of our HMO activities as discontinued operations, the service agreement income and related expense were eliminated in consolidation. Salary, general and administrative expenses of continuing operations declined from $23.1 million in 2000 to $5.0 million in 2001, principally due to decreased salary costs as a result of the transfer of employees from MHP to the California HMO ($5.1 million); reserves taken against certain prepaid items and accounts receivable in 2000 ($4.0 million); and higher consulting costs in 2000 associated with various infrastructure enhancements ($5.9 million).

Results of discontinued operations for the year ended December 31, 2001 include a gain of $16.4 million realized by MHP upon the placement of our Indiana HMO (to which MHP had contributed the capital stock of Maxicare Life and Health Insurance Company effective December 31, 2000), into rehabilitation and the bankruptcy of our California HMO. This gain represents the extent to which liabilities of those subsidiaries exceeded their assets at the date of rehabilitation or bankruptcy. Loss fr