MAXICARE HEALTH PLANS INC
Form 10-Q
May 21, 2001

1

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Act of 1934 for the quarterly period ended March 31, 2001 or

[ ] Transition report pursuant to 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	95-9615709
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1149 South Broadway Street, Los Angeles, California	90015
(Address of principal executive offices)	(Zip Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes [X] No [ ]

Common Stock, $.01 par value - 9,748,438 shares outstanding as of May 21, 2001.

2

PART I: FINANCIAL INFORMATION

Item 1: Financial Statements.

3

MAXICARE HEALTH PLANS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Amounts in thousands except par value)

	March 31, 2001 (Unaudited)
CURRENT ASSETS	
Cash and cash equivalents	$ 69,850
Marketable securities	2,276
Accounts receivable, net	22,632
Prepaid expenses	3,215
TOTAL CURRENT ASSETS	97,973
PROPERTY AND EQUIPMENT	
Leasehold improvements	5,537
Furniture and equipment	20,613
	26,150
Less accumulated depreciation and amortization	21,300

NET PROPERTY AND EQUIPMENT	4,850
LONG-TERM ASSETS	
Restricted investments	6,109
Other long-term assets	3,455
TOTAL LONG-TERM ASSETS	$ 9,564
TOTAL ASSETS	$ 112,387
CURRENT LIABILITIES	
Estimated claims and other health care costs payable	$ 96,011
Accounts payable	2,517
Deferred income	8,743
Accrued salary expense	2,261
Other current liabilities	8,312
TOTAL CURRENT LIABILITIES	117,844
LONG-TERM LIABILITIES	5,974
TOTAL LIABILITIES	123,818
SHAREHOLDERS' EQUITY	
Common stock, $.01 par value - 80,000 shares authorized, 9,748 shares issued and outstanding	98
Additional paid-in capital	283,466
Note receivable from shareholder	(2,887)
Accumulated deficit	(291,918)
Accumulated other comprehensive income (loss)	(190)
TOTAL SHAREHOLDERS' EQUITY	(11,431)
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 112,387

MAXICARE HEALTH PLANS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Amounts in thousands except per share data)
(Unaudited)

	For the three mo ended March 31, 2001	
REVENUES		
Commercial premiums	$ 106,408	$
Medicaid premiums	27,635	
Medicare premiums	21,835	
TOTAL PREMIUMS	155,878	

Investment income	1,180	
Other income	186	
TOTAL REVENUES	157,244	
EXPENSES		
Physician services	61,650	
Hospital services	57,185	
Outpatient services	29,631	
Other health care expense	5,736	
TOTAL HEALTH CARE EXPENSES	154,202	
Marketing, general and administrative expenses	20,822	
Depreciation and amortization	580	
TOTAL EXPENSES	175,604	
INCOME (LOSS) FROM OPERATIONS	(18,360)	
NET INCOME (LOSS)	$ (18,360)	$
NET INCOME (LOSS) PER COMMON SHARE:		
Basic:		
Basic Earnings (Loss) Per Common Share	$ (1.88)	$
Weighted average number of common shares outstanding	9,748	
Diluted:		
Diluted Earnings (Loss) Per Common Share	$ (1.88)	$
Weighted average number of common and common dilutive potential shares outstanding	9,748	

MAXICARE HEALTH PLANS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in thousands)
(Unaudited)

	For the three mon ended March 31	
	2001	20
CASH FLOWS FROM OPERATING ACTIVITIES:		

Net Income (loss)	$(18,360)	$
Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities:		
Depreciation and amortization	580	
Benefit from deferred income taxes		
Management settlement and other charges	(129)	
Changes in assets and liabilities:		
Decrease in accounts receivable	12,796	1
Increase (decrease) in estimated claims and other health care costs payable	(2,987)	8
Increase in deferred income	694	
Changes in other miscellaneous assets and liabilities	(1,289)	
Net cash provided by (used for) operating activities	(8,695)	12
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment and computer software	(2,944)	
Decrease in restricted investments	9	
Proceeds from sales and maturities of marketable securities	1,232	1
Purchases of marketable securities	(299)	(2
Net cash used for investing activities	(2,002)	
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on capital lease obligations	(146)	
Net cash used for financing activities	(146)	
Net increase (decrease) in cash and cash equivalents	(10,843)	11
Cash and cash equivalents at beginning of period	80,693	69
Cash and cash equivalents at end of period	$ 69,850	$ 80
Supplemental disclosures of cash flow information:		
Cash paid during the year for -		
Interest	$ 43	$
Supplemental schedule of non-cash investing activities:		
Capital lease obligations incurred for purchase of property and equipment and intangible assets	$ 91	

MAXICARE HEALTH PLANS, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Amounts in thousands)

	Number of Common Shares	Common Stock	Additional Paid-in Capital	Other	Accumul Defic

Balances at December 31, 2000	9,748	$ 98	$ 283,442	$ (2,842)	$(27
Comprehensive income (loss)					
Net loss					(1
Other comprehensive income, net of tax, related to unrealized gains on marketable securities					
Comprehensive loss					
Warrants issued in connection with professional services contract			24		
Note receivable from shareholder				(45)	
Balances at March 31, 2001	9,748	$ 98	$ 283,466	$ (2,887)	$(29

MAXICARE HEALTH PLANS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Maxicare Health Plans, Inc., a Delaware corporation ("MHP"), is a holding company that owns various subsidiaries, primarily in the field of managed care. MHP owns and operates an HMO in California. Prior to May 4, 2001, MHP operated an HMO in Indiana. The Indiana subsidiary owns and operates Maxicare Life and Health Insurance Company, the indemnity provider underwriting the preferred provider organization ("PPO"), point of service ("POS") and life insurance products offered by both our Indiana (PPO only) and California HMOs. On May 4, 2001, the Commissioner of the Indiana Department of Insurance assumed control of the Indiana subsidiary. See Note 3.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information. In the opinion of management, all adjustments considered necessary for a fair presentation, which consist solely of normal recurring adjustments, have been included. All significant intercompany balances and transactions have been eliminated.

For further information on MHP and subsidiaries (collectively "we" or the "Company") and its accounting policies refer to the consolidated financial statements and accompanying footnotes included in our annual report on Form 10-K for the year ended December 31, 2000.

NOTE 2 - REVERSE STOCK SPLIT

On March 27, 2001, we effected a one-for-five reverse split of our common stock. All share and per share information included in this quarterly report on Form 10-Q have been retroactively adjusted to reflect the reverse stock split.

NOTE 3 - SUBSEQUENT EVENTS

On May 4, 2001, the Commissioner of the the Indiana Department of Insurance petitioned the Marion County Circuit Court to place our Indiana HMO into rehabilitation. This action effectively removes all control of our Indiana subsidiary from us and places control of its operations with the Commissioner of the Indiana Department of Insurance. This action was the result of claims that were substantially in excess of our estimates during the fourth quarter of 2000 and the first quarter of 2001.

Our Indiana subsidiary is the sole owner of Maxicare Life and Health Insurance Company, Inc. ("MLH")As a result of the Indiana order of rehabilitation, our ability to effectively control and operate MLH is subject to considerable uncertainty. At March 31, 2001, MLH was in compliance with the statutory net worth requirements in Missouri, where it is organized, but not in California. As a result, MLH may be prohibited from writing new business in California.

NOTE 4 - LIQUIDITY AND GOING CONCERN ISSUES

The significant operating losses we experienced in 2000 and in the three prior years have continued in the first quarter of 2001. As a result of those continuing losses we had at March 31, 2001, a consolidated working capital deficiency of approximately $19.9 million, and a deficiency in stockholders' equity of approximately $11.4 million. Our losses are continuing into the

second quarter of 2001 and may continue thereafter.

In order to provide us with liquidity, we have engaged an investment banking firm to assist us in the sale of all or part of our California operations. We believe that a sale of part of our California operations can generate sufficient liquidity to enable us to continue in business in California on a reduced scale. However, we cannot assure you that we will be successful in selling any of our operations or that any sale will generate sufficient liquidity. We have also taken steps to reduce our operating losses, including improvements in our claims processing procedures, raising premiums for commercial and PPO coverage and reducing our work force.

Our HMOs and MLH are subject to state regulations that require compliance with certain statutory deposit, dividend distribution and net worth requirements. To the extent these subsidiaries must comply with these regulations, they may not have the financial flexibility to transfer funds to MHP. MHP's proportionate share of the net assets of its subsidiaries that may not be transferred to MHP without the consent of a third party is referred to as "Restricted Net Assets." Restricted Net Assets of these subsidiaries were $11.8 million at March 31, 2001 with deposit restrictions representing $3.0 million of the balance and net worth requirements in excess of deposit requirements representing the remainder. In addition to the $3.3 million in cash, cash equivalents and marketable securities held by MHP, approximately $700,000 held by operating subsidiaries could be considered available for transfer to MHP at March 31, 2001.

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations.

RESULTS OF OPERATIONS

We sustained a net loss of $18.4 million, or $1.88 per share (basic and diluted), for the three months ended March 31, 2001 (the "March 2001 quarter"). For the three months ended March 31, 2000 (the "March 2000 quarter") we had net income of $50,000, or $0.00 per share (basic and diluted).

Through May 4, 2001, we operated HMOs in California and Indiana. On May 4, 2001, the Commissioner of the Indiana Department of Insurance petitioned the Marion County Circuit Court to place our Indiana subsidiary into rehabilitation. This action effectively removes all control of our Indiana subsidiary from us and places control with the Commissioner of the Indiana Department of Insurance. Accordingly, since May 4, 2001, our operations did not include the Indiana operations, and our California HMO currently represents almost all of our operations. At March 31, 2000 and 2001 and December 31, 2000 membership of the California and Indiana HMOs was as follows. Membership numbers include lives underwritten by Maxicare Life and Health Insurance Company ("MLH") which amounted to less than 3% of total membership at any of the dates listed. MLH is a wholly-owned subsidiary of our Indiana HMO and effectively ceased to be under our control on May 4, 2001.

As of March 31, 2001	COMMERCIAL	MEDICAID	MEDICARE	TOTAL
California................	158,800	88,200	12,150	259,150
Indiana..................	83,100	14,100	0	97,200
Total Membership	241,900	102,300	12,150	356,350

As of December 31, 2000	COMMERCIAL	MEDICAID	MEDICARE	TOTAL
California.................	155,000	84,900	11,600	251,500
Indiana....................	102,400	59,300	2,800	164,500
Total Membership	257,400	144,200	14,400	416,000

As of March 31, 2000	COMMERCIAL	MEDICAID	MEDICARE	TOTAL
California.................	150,600	100,150	11,850	262,600
Indiana....................	107,500	60,700	6,100	174,300
Total Membership	258,100	160,850	17,950	436,900

March 31, 2000 data excludes membership of Maxicare Louisiana, Inc. which was sold effective August 1, 2000.

Commercial premium revenues for the first quarter of 2001 decreased by $1.8 million, or 1.6%, as compared to 2000. This decrease was a result of:

- the sale of our Louisiana HMO on August 1, 2000, which contributed commercial premium revenues of $5.5 million to first quarter 2000 results; and
- a 22.4% decrease in Indiana enrollment, offset by rate increases in both Indiana and California. Commercial premium revenues on a per member per month basis increased by 11.8% for the first quarter of 2001 when compared to the first quarter of 2000.

MLH has written all of our life and PPO insurance in California. Since MLH, as a subsidiary of our Indiana subsidiary, is effectively under the control of the Commissioner of the Indiana Department of Insurance, our ability to offer life and PPO insurance may be impaired. Although life and PPO coverage did not represent more than 3% of our revenue for the March 2001 quarter, the inability to offer this coverage may make it more difficult to sell HMO coverage. Furthermore, our financial condition, including the Indiana rehabilitation proceeding and the stipulation with the California Department of Managed Health Care, which is discussed under "Liquidity and Capital Resources," may also impair our ability to offer insurance in California.

Medicare premium revenues decreased by $7.4 million in the first quarter of 2001 reflecting the termination of our Louisiana business and our Indiana Medicare business, which contributed Medicare revenue of approximately $1.1 million and $8.3 million, respectively, to the March 2000 quarter.

Medicaid premium revenues declined by $18.4 million due to a substantial decline in Indiana Medicaid enrollment statewide and a decline in California Medicaid membership in the Sacramento area. Medicaid premium revenues on a per member per month basis decreased by 1.8% for the March 2001 quarter when compared to the March 2000 quarter.

Investment income was essentially constant for the first quarter of 2001 as compared to the first quarter of 2000.

Health care expenses for the March 2001 quarter were $154.2 million as compared to $167.8 million for the March 2000 quarter due to lower enrollment. Health care costs computed on per member per month basis increased by 18.6% in the March 2001 quarter as compared to the March 2000 quarter. The increase in health care costs on a per member per month basis results from claims which were substantially in excess of anticipated amounts. These increased costs resulted in the losses sustained by our Indiana subsidiary which in turn resulted in the rehabilitation proceeding and the assumption of control of our Indiana subsidiary by the Commissioner of the Indiana Department of Insurance.

Marketing, general and administrative expenses for the March 2001 quarter increased $4.1 million to $20.8 million as compared to $16.7 million for the March 2000 quarter. Salary expenses contributed $1.0 million of the increase, while consulting fees associated with various new internal initiatives contributed another $2.1 million of the increase. Marketing, general and administrative expenses represented 13.4% and 9.1% of premium revenues for the first quarter of 2001 and 2000, respectively.

LIQUIDITY AND CAPITAL RESOURCES

At March 31, 2001, we had a consolidated working capital deficiency of approximately $19.9 million, and we had a deficiency in stockholders' equity of approximately $11.4 million. The significant operating losses we experienced in 2000 and in the three prior years have continued in the first quarter of 2001, are continuing in the second quarter of 2001, and may continue thereafter. We cannot assure you that we will be able to operate profitably in the future.

Our California HMO entered into a stipulation with the California Department of Managed Health Care providing the Department with a limited degree of oversight over our California HMO's financial operations. The stipulation, in part, requires us to obtain the approval of the Department before certain payments can be made. We believe that the requirements imposed upon us by the stipulation are unlikely to have a material adverse impact on our operations.

In order to operate in California, our California HMO was required to maintain a tangible net equity of approximately $8.0 million at March 31, 2001. Our California subsidiary reports its tangible net equity to the Department of Managed Health Care on a monthly basis. At the time we filed our March 2001 report, based on the information available to us at the time, we believed that we were in compliance with the California tangible net equity requirements. Unless we are able to provide the California HMO with additional capital, we will not be in compliance with the net tangible equity requirements. As a result, we may be precluded from operating in California and the Department could take control of our California subsidiary's operations.

In order to provide us with liquidity, we have engaged an investment banking firm to assist us in the sale of all or part of our California operations. We believe that a sale of part of our California operations can generate sufficient liquidity to enable us to continue in business in California on a reduced scale. However, we cannot assure you that we will be successful in selling any of our operations or that any sale will generate sufficient proceeds.

We have also taken steps to reduce our operating losses, including improvements in our claims processing procedures, raising premiums for commercial and PPO coverage and reducing our work force.

In the event that we are not successful in raising the necessary cash and significantly improving our operating results, our California HMO may be subject to greater regulatory intervention, including a possible seizure of the California HMO.

At March 31, 2001, MLH was in compliance with the statutory new worth requirements in Missouri, where it is organized, but not in California. As a result, MLH may be prohibited from writing new business in California.

Our HMOs and MLH are subject to state regulations that require compliance with certain statutory deposit, dividend distribution and net worth requirements. To the extent these subsidiaries must comply with these regulations, they may not have the financial flexibility to transfer funds to us. Our proportionate share of the net assets of its subsidiaries that may not be transferred to us without the consent of a third party is referred to as "restricted net assets." Restricted net assets of these subsidiaries were $11.8 million at March 31, 2001 with deposit restrictions representing $3.0 million of the balance and net worth requirements in excess of deposit requirements representing the remainder. In addition to the $3.3 million in cash, cash equivalents and marketable securities held by us, approximately $700,000 in funds held by operating subsidiaries could be considered available for transfer to us at March 31, 2001.

FORWARD LOOKING INFORMATION

This Quarterly Report on Form 10-Q contains and incorporates by reference forward looking statements within the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. Reference is made in particular to the discussions set forth under "Risk Factors" in our Report on Form 10-K for the year ended December 31, 2000 and under "Management's Discussion and Analysis of Financial Condition and Results of Operations" in both our Form 10-K and this Form 10-Q. Such statements are based on certain assumptions and current expectations that involve a number of risks and uncertainties, many of which are beyond our control. These statements are forward looking and actual results could differ materially from those projected in the forward looking statements, which statements involve risks and uncertainties. In addition, past financial performance is not necessarily a reliable indicator of future performance and investors should not use historical performance to anticipate results or future period trends. Shareholders are also directed to disclosures in this and other documents filed by us with the SEC.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

As of March 31, 2001, we had approximately $78.2 million in cash and cash equivalents, marketable securities and restricted investments. Marketable securities of $2.3 million are classified as available-for-sale investments and restricted investments of $6.1 million are classified as held-to-maturity investments. Marketable securities include $1.6 million of warrants for the purchase of common stock of the TriZetto Group, Inc. ("TZG"). We have partnered with TZG to upgrade our management information systems. The value of these warrants is subject to considerable fluctuation based on the price of TZG's common shares. Our remaining investments are primarily in fixed income, investment grade securities. Our investment policies emphasize return of principal and liquidity and are focused on fixed returns that limit volatility and risk of principal. Because of our investment policies, the primary market risk associated with our portfolio is interest rate risk. As of March 31, 2001, the Company did not have any outstanding bank borrowings or debt obligations.

PART II: OTHER INFORMATION

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

On March 14, 2001, the stockholders approved an amendment to our certificate of incorporation that effected a one-for-five reverse split. Action was taken by the written consent of the holders of 31,076,085 (pre-reverse split) shares of our common stock, which constituted 63.8% of our then outstanding shares of common stock.

Item 6: Exhibits and Reports on Form 8-K.

(a) Exhibits

None

(b) Reports on Form 8-K

None

SIGNATURES

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

MAXICARE HEALTH PLANS, INC.

(Registrant)

May 21, 2001	/s/ Paul R. Dupee, Jr.
Date	Paul R. Dupee, Jr., Chief Executive Officer
May 21, 2001	/s/ Joseph W. White
Date	Joseph W. White Controller and Interim Chief Financial Officer