

CONTINUCARE CORP  
Form 10-Q  
May 07, 2009

**Table of Contents**

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

**Part I** **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2009  
OR**

**Part II** **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number 001-12115  
CONTINUCARE CORPORATION**

(Exact Name of Registrant as Specified in Its Charter)

**Florida**

(State or Other Jurisdiction of  
Incorporation or Organization)

**59-2716023**

(IRS Employer Identification No.)

**7200 Corporate Center Drive  
Suite 600**

**Miami, Florida**

(Address of Principal Executive Offices)

**33126**

(Zip Code)

**(305) 500-2000**

(Registrant's Telephone Number, Including Area Code)  
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class  
**COMMON STOCK**  
\$.0001 PAR VALUE

Name of Each Exchange On Which Registered  
**NYSE AMEX LLC**

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, and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐ Smaller reporting company ☐  
(Do not check if a smaller reporting company)

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

At April 30, 2009, the Registrant had 59,383,549 shares of \$0.0001 par value common stock outstanding.

---

**CONTINUOCARE CORPORATION  
INDEX**

**PART I FINANCIAL INFORMATION**

<b><u>ITEM 1.</u></b>	<b><u>FINANCIAL STATEMENTS (Unaudited)</u></b>	
	<u>Condensed Consolidated Balance Sheets March 31, 2009 and June 30, 2008</u>	3
	<u>Condensed Consolidated Statements of Income Three-Months Ended March 31, 2009 and 2008</u>	4
	<u>Condensed Consolidated Statements of Income Nine-Months Ended March 31, 2009 and 2008</u>	5
	<u>Condensed Consolidated Statements of Cash Flows Nine-Months Ended March 31, 2009 and 2008</u>	6
	<u>Notes to Condensed Consolidated Financial Statements March 31, 2009</u>	7
<b><u>ITEM 2.</u></b>	<b><u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u></b>	12
<b><u>ITEM 3.</u></b>	<b><u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u></b>	21
<b><u>ITEM 4.</u></b>	<b><u>CONTROLS AND PROCEDURES</u></b>	22

**PART II OTHER INFORMATION**

<b><u>ITEM 1.</u></b>	<b><u>LEGAL PROCEEDINGS</u></b>	22
<b><u>ITEM 1A.</u></b>	<b><u>RISK FACTORS</u></b>	23
<b><u>ITEM 2.</u></b>	<b><u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u></b>	23
<b><u>ITEM 3.</u></b>	<b><u>DEFAULTS UPON SENIOR SECURITIES</u></b>	23
<b><u>ITEM 4.</u></b>	<b><u>SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS</u></b>	23
<b><u>ITEM 5.</u></b>	<b><u>OTHER INFORMATION</u></b>	24
<b><u>ITEM 6.</u></b>	<b><u>EXHIBITS</u></b>	24

SIGNATURES

25

EX-31.1

EX-31.2

EX-32.1

EX-32.2

**Table of Contents****PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

**CONTINUCARE CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(Unaudited)**

	<b>March 31, 2009</b>	<b>June 30, 2008</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 10,327,402	\$ 9,905,740
Due from HMOs, net of a liability for incurred but not reported medical claims of approximately \$22,532,000 and \$23,900,000 at March 31, 2009 and June 30, 2008, respectively	14,172,292	15,325,783
Prepaid expenses and other current assets	857,177	708,841
Deferred income tax assets	411,182	413,932
Total current assets	25,768,053	26,354,296
Certificates of deposit, restricted	1,294,035	1,274,147
Property and equipment, net	9,863,395	8,363,427
Goodwill	73,204,582	73,204,582
Intangible assets, net of accumulated amortization of approximately \$3,097,000 and \$2,168,000 at March 31, 2009 and June 30, 2008, respectively	5,563,332	6,492,333
Deferred income tax assets	2,689,484	2,574,472
Other assets, net	101,882	227,047
Total assets	\$ 118,484,763	\$ 118,490,304
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 900,722	\$ 402,718
Accrued expenses and other current liabilities	3,410,354	4,458,119
Income taxes payable	1,010,076	1,198,722
Total current liabilities	5,321,152	6,059,559
Deferred income tax liabilities	6,206,611	6,256,205
Other liabilities	937,013	948,263
Total liabilities	12,464,776	13,264,027
Commitments and contingencies		
Shareholders' equity:		
Common stock, \$0.0001 par value: 100,000,000 shares authorized; 59,383,549 shares issued and outstanding at March 31, 2009 and 64,796,303 shares issued and outstanding at June 30, 2008	5,938	6,480
Additional paid-in capital	104,826,660	114,514,853
Accumulated earnings (deficit)	1,187,389	(9,295,056)

Total shareholders' equity	106,019,987	105,226,277
Total liabilities and shareholders' equity	\$ 118,484,763	\$ 118,490,304

**THE ACCOMPANYING NOTES ARE AN INTEGRAL PART  
OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

3

---

**Table of Contents**

**CONTINUCARE CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)**

	<b>Three Months Ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
Revenue	\$ 75,395,799	\$ 65,936,165
Operating expenses:		
Medical services:		
Medical claims	53,217,866	45,132,244
Other direct costs	7,232,634	6,902,514
Total medical services	60,450,500	52,034,758
Administrative payroll and employee benefits	3,539,646	3,489,077
General and administrative	4,364,000	4,341,247
Total operating expenses	68,354,146	59,865,082
Income from operations	7,041,653	6,071,083
Other income (expense):		
Interest income	27,843	147,799
Interest expense	(9,087)	(5,079)
Income before income tax provision	7,060,409	6,213,803
Income tax provision	2,733,906	2,538,302
Net income	\$ 4,326,503	\$ 3,675,501
Net income per common share:		
Basic	\$ .07	\$ .05
Diluted	\$ .07	\$ .05
Weighted average common shares outstanding:		
Basic	59,904,532	68,352,586
Diluted	60,848,054	69,473,743

**THE ACCOMPANYING NOTES ARE AN INTEGRAL PART  
OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**



**Table of Contents**

**CONTINUCARE CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)**

	<b>Nine Months Ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
Revenue	\$ 206,000,328	\$ 188,344,274
Operating expenses:		
Medical services:		
Medical claims	145,683,860	133,856,761
Other direct costs	21,534,562	20,436,307
Total medical services	167,218,422	154,293,068
Administrative payroll and employee benefits	9,393,652	8,912,191
General and administrative	12,410,761	12,272,352
Total operating expenses	189,022,835	175,477,611
Income from operations	16,977,493	12,866,663
Other income (expense):		
Interest income	151,634	508,302
Interest expense	(17,184)	(17,033)
Income before income tax provision	17,111,943	13,357,932
Income tax provision	6,629,498	5,249,249
Net income	\$ 10,482,445	\$ 8,108,683
Net income per common share:		
Basic	\$ .17	\$ .12
Diluted	\$ .17	\$ .11
Weighted average common shares outstanding:		
Basic	62,059,381	69,402,996
Diluted	63,119,454	70,559,450

**THE ACCOMPANYING NOTES ARE AN INTEGRAL PART  
OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**Table of Contents**

**CONTINUCARE CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**

	<b>Nine Months Ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 10,482,445	\$ 8,108,683
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,660,956	1,904,069
Loss on disposal of fixed assets	64,586	
Provision for bad debts		181,081
Compensation expense related to issuance of stock options	908,954	1,036,002
Deferred income tax expense	(161,856)	(134,130)
Changes in operating assets and liabilities:		
Due from HMOs, net	1,153,491	840,297
Prepaid expenses and other current assets	(148,336)	335,293
Other assets, net	93,555	(87,263)
Accounts payable	498,004	(848,148)
Accrued expenses and other current liabilities	(1,079,590)	(682,033)
Income taxes payable	(188,646)	1,383,378
Net cash provided by operating activities	13,283,563	12,037,229
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sales of certificates of deposit		15,000
Purchase of certificates of deposit	(19,888)	(101,677)
Purchase of property and equipment	(2,161,231)	(777,415)
Net cash used in investing activities	(2,181,119)	(864,092)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Repayment on long-term debt		(6,083)
Principal repayments under capital lease obligations	(83,092)	(85,351)
Proceeds from exercise of stock options	10,625	64,375
Payment of fees related to issuance of stock		(45,000)
Repurchase and retirement of common stock	(10,608,315)	(5,639,003)
Net cash used in financing activities	(10,680,782)	(5,711,062)
Net increase in cash and cash equivalents	421,662	5,462,075
Cash and cash equivalents at beginning of period	9,905,740	7,262,247
Cash and cash equivalents at end of period	\$ 10,327,402	\$ 12,724,322

SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND  
FINANCING ACTIVITIES:

Purchase of property and equipment with proceeds of capital lease obligations	\$ 103,667	\$ 38,922
---	------------	-----------

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

Cash paid for taxes	\$ 6,980,000	\$ 4,000,000
---------------------	--------------	--------------

Cash paid for interest	\$ 12,184	\$ 17,033
------------------------	-----------	-----------

**THE ACCOMPANYING NOTES ARE AN INTEGRAL PART  
OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**Table of Contents**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
MARCH 31, 2009  
(UNAUDITED)**

**NOTE 1 UNAUDITED INTERIM INFORMATION**

The accompanying unaudited condensed consolidated financial statements of Continucare Corporation ( Continucare or the Company ) have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine-month periods ended March 31, 2009 are not necessarily indicative of the results that may be reported for the remainder of the fiscal year ending June 30, 2009 or future periods. Except as otherwise indicated by the context, the terms the Company or Continucare mean Continucare Corporation and its consolidated subsidiaries. All references to a fiscal year refer to the Company's fiscal year which ends June 30. As used herein, Fiscal 2009 refers to the fiscal year ending June 30, 2009, Fiscal 2008 refers to the fiscal year ended June 30, 2008, and Fiscal 2007 refers to the fiscal year ended June 30, 2007.

The balance sheet at June 30, 2008 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for Fiscal 2008. These interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes to consolidated financial statements included in that report.

Certain reclassifications have been made to the prior year amounts to conform to the current year presentation.

**NOTE 2 GENERAL**

The Company is a provider of primary care physician services on an outpatient basis in Florida. The Company provides medical services to patients through employee physicians, advanced registered nurse practitioners and physician's assistants. Additionally, the Company provides practice management services to independent physician affiliates ( IPAs ). Substantially all of the Company's revenue is derived from managed care agreements with three health maintenance organizations, Humana Medical Plans, Inc. ( Humana ), Vista Healthplan of South Florida, Inc. and its affiliated companies including Summit Health Plan, Inc. ( Vista ) and Wellcare Health Plans, Inc. and its affiliated companies ( Wellcare ) (collectively, the HMOs ). The Company was incorporated in 1996 as the successor to a Florida corporation formed earlier in 1996.

**NOTE 3 ACQUISITION**

Effective October 1, 2006, the Company completed its acquisition (the Acquisition ) of Miami Dade Health Centers, Inc. and its affiliated companies (collectively, the MDHC Companies ). In connection with the completion of the Acquisition and in consideration for the assets acquired pursuant to the Acquisition, the Company paid the MDHC Companies approximately \$6.7 million in cash, issued to the MDHC Companies 19.7 million shares of the Company's common stock and assumed or repaid certain indebtedness and liabilities of the MDHC Companies.

The purchase price, including acquisition costs, of approximately \$66.2 million has been allocated to the estimated fair value of acquired tangible assets of \$13.9 million, identifiable intangible assets of \$8.7 million and assumed liabilities of \$15.3 million as of October 1, 2006, resulting in goodwill totaling \$58.9 million. This purchase price allocation includes certain adjustments recorded during the three-month period ended September 30, 2007 that resulted in a decrease in goodwill of approximately \$0.5 million. These adjustments primarily related to Medicare risk adjustment payments relating to the operations of the MDHC Companies for periods prior to completion of our acquisition. The identifiable intangible assets of \$8.7 million consist of estimated fair values of \$1.6 million assigned to the trade name, \$6.2 million to customer relationships and \$0.9 million to a noncompete agreement.

**Table of Contents**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
MARCH 31, 2009  
(UNAUDITED)**

The trade name was determined to have an estimated useful life of six years and the customer relationships and noncompete agreements were each determined to have an estimated useful life of eight and five years, respectively. The fair values of the customer relationships and other identifiable intangible assets are amortized over their estimated lives using the straight-line method. The customer relationships are non-contractual. The fair value of the identifiable intangible assets was determined, with the assistance of an outside valuation firm, based on standard valuation techniques. The Acquisition consideration of \$66.2 million includes the estimated fair value of Continucare's common stock issued to the MDHC Companies of \$58.5 million, cash paid to the principal owners of \$5.7 million at the closing of the Acquisition, cash paid to the principal owners of \$1.0 million in October 2007, and acquisition costs of approximately \$1.0 million.

**NOTE 4 RECENT ACCOUNTING PRONOUNCEMENTS**

In December 2007, the FASB issued SFAS No. 141 (revised 2007), Business Combinations (SFAS No. 141R). SFAS No. 141R expands the definition of a business combination and requires the fair value of the purchase price of an acquisition, including the issuance of equity securities, to be determined on the acquisition date. SFAS No. 141R also requires that all assets, liabilities, contingent consideration, and contingencies of an acquired business be recorded at fair value at the acquisition date. In addition, SFAS No. 141R requires that acquisition costs generally be expensed as incurred, restructuring costs generally be expensed in periods subsequent to the acquisition date and changes in accounting for deferred income tax asset valuation allowances and acquired income tax uncertainties after the measurement period impact income tax expense. SFAS No. 141R is effective for the Company's fiscal years beginning on or after December 15, 2008, with early adoption prohibited. The effect of SFAS No. 141R on the Company's financial statements will be dependent on the nature and terms of any business combination consummated by the Company on or after July 1, 2009.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51 (SFAS No. 160). SFAS No. 160 requires minority interests to be recharacterized as noncontrolling interests and reported as a component of equity. In addition, SFAS No. 160 requires that purchases or sales of equity interests that do not result in a change in control be accounted for as equity transactions and, upon a loss of control, requires the interests sold, as well as any interests retained, to be recorded at fair value with any gain or loss recognized in earnings. SFAS No. 160 is effective for fiscal years beginning on or after December 15, 2008, with early adoption prohibited. No material impact on the Company's financial statements is expected from the adoption of this standard.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivatives and Hedging Activities, which enhances the requirements under SFAS No. 133, Accounting for Derivatives and Hedging Activities. SFAS No. 161 requires enhanced disclosures about an entity's derivatives and hedging activities and how they affect an entity's financial position, financial performance, and cash flows. This Statement will be effective for fiscal years and interim periods beginning after November 15, 2008. No material impact on the Company's financial statements is expected from the adoption of this standard.

**NOTE 5 SHARE-BASED PAYMENT**

The Company accounts for share-based compensation expense under SFAS No. 123(R), Share-Based Payment, which is a revision of SFAS No. 123 (SFAS 123(R)), using the modified prospective transition method.

The Company calculates the fair value for employee stock options using a Black-Scholes option pricing model at the time the stock options are granted and that amount is amortized over the vesting period of the stock options, which is generally up to four years. The fair value for employee stock options granted during the three-month periods ended March 31, 2009 and 2008 was calculated based on the following assumptions: risk-free interest rate ranging from 0.66% to 2.28% and 1.61% to 2.71%, respectively; dividend yield of 0%; volatility factor of the expected market price of the Company's common stock of 60.7% and 59.6%, respectively; and weighted-average expected life of the options ranging from 2 to 6 years, depending on the vesting provisions of each option. The fair value for employee stock options granted during the nine-month periods ended March 31, 2009 and 2008 was calculated based on the following

assumptions: risk-free interest rate ranging from 0.66% to 3.09% and 1.61% to

8

---

**Table of Contents**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**MARCH 31, 2009**  
**(UNAUDITED)**

4.22%, respectively; dividend yield of 0%; volatility factor of the expected market price of the Company's common stock of 58.6% and 59.5%, respectively; and weighted-average expected life of the options ranging from 2 to 6 years, depending on the vesting provisions of each option. The expected life of the options is based on the historical exercise behavior of the Company's employees. The expected volatility factor is based on the historical volatility of the market price of the Company's common stock as adjusted for certain events that management deemed to be non-recurring and non-indicative of future events.

For the three-month periods ended March 31, 2009 and 2008, the Company recognized share-based compensation expense of \$0.3 million and \$0.4 million, respectively. For the nine-month periods ended March 31, 2009 and 2008, the Company recognized share-based compensation expense of \$0.9 million and \$1.0 million, respectively. For the three and nine-month periods ended March 31, 2009 and 2008, the Company had no excess tax benefits resulting from the exercise of stock options.

**NOTE 6 DEBT**

The Company has in place a credit facility that provides for a revolving loan to the Company of \$5.0 million (the Credit Facility) with a maturity date of December 31, 2009. The Credit Facility has a variable interest rate at a per annum rate equal to the sum of 2.5% and the 30-day Dealer Commercial Paper Rate (0.55% at March 31, 2009). The Credit Facility includes covenants requiring the Company and its subsidiaries, on a consolidated basis, to maintain a tangible net worth of \$12 million and a debt coverage ratio of 1.25 to 1. Substantially all assets of the Company serve as collateral for the Credit Facility.

In connection with the Acquisition, the Company entered into two term loan facilities funded out of lines of credit (the Term Loans) with maximum loan amounts of \$4.8 million and \$1.0 million, respectively. Each of the Term Loans requires mandatory monthly payments that reduce the lines of credit under the Term Loans. Subject to the terms and conditions of the Term Loans, any prepayments made to the Term Loans may be re-borrowed on a revolving basis so long as the line of credit applicable to such Term Loan, as reduced by the mandatory monthly payment, is not exceeded. As of March 31, 2009, the total maximum amount available for borrowing under the two Term Loans was approximately \$4.6 million. The Term Loans mature on October 31, 2011 and October 31, 2010, respectively. Each of the Term Loans (i) has variable interest rates at a per annum rate equal to the sum of 2.4% and the One-Month LIBOR (0.50% at March 31, 2009), (ii) requires the Company and its subsidiaries, on a consolidated basis, to maintain a tangible net worth of \$12 million and a debt coverage ratio of 1.25 to 1 and (iii) are secured by substantially all of the assets of the Company and its subsidiaries.

At March 31, 2009, there was no outstanding principal balance on the Credit Facility or the Term Loans.

**NOTE 7 EARNINGS PER SHARE**

A reconciliation of the denominator of the basic and diluted earnings per share computation is as follows:

	<b>Three Months Ended March 31,</b>		<b>Nine Months Ended March 31,</b>	
	<b>2009</b>	<b>2008</b>	<b>2009</b>	<b>2008</b>
Basic weighted average number of shares outstanding	59,904,532	68,352,586	62,059,381	69,402,996
Dilutive effect of stock options	943,522	1,121,157	1,060,073	1,156,454
Dilutive weighted average number of shares outstanding	60,848,054	69,473,743	63,119,454	70,559,450

Not included in calculation of diluted earnings per share as impact is

antidilutive:

Stock options outstanding	4,133,250	2,982,000	4,133,250	2,982,000
---------------------------	-----------	-----------	-----------	-----------

9



**Table of Contents**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
MARCH 31, 2009  
(UNAUDITED)**

**NOTE 8 INCOME TAXES**

The Company accounts for income taxes under FASB Statement No. 109, Accounting for Income Taxes ( SFAS 109 ). Deferred income tax assets and liabilities are determined based upon differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

The Company recorded an income tax provision of \$2.3 million and \$2.5 million for the three-month periods ended March 31, 2009 and 2008, respectively, and \$6.2 million and \$5.2 million for the nine-month periods ended March 31, 2009 and 2008, respectively.

Effective July 1, 2007, the Company adopted the provisions of Interpretation 48 ( FIN 48 ), Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109. The implementation of FIN 48 had no impact on our liability for unrecognized tax benefits which was approximately \$0.8 million at March 31, 2009 and July 1, 2007 and is included in other liabilities on the condensed consolidated balance sheet. The total amount of unrecognized tax benefits that if recognized would affect the effective tax rate is \$0.9 million, which includes accrued interest and penalties of approximately \$52,000 and \$47,000, respectively, at March 31, 2009 and June 30, 2008. The Company recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expense. The Company does not currently anticipate that the total amount of unrecognized tax benefits will significantly increase or decrease by the end of Fiscal 2009. The Company is no longer subject to tax examinations by tax authorities for fiscal years ended on or prior to June 30, 2005.

**NOTE 9 RELATED PARTY TRANSACTIONS**

As a result of the Acquisition, the Company became a party to two lease agreements for office space owned by Dr. Luis Cruz and Jose M. Garcia, principal owners of the MDHC Companies. Dr. Cruz is a director of the Company and Mr. Garcia was an officer of the Company through January 15, 2009. The Company terminated one of the lease agreements effective September 30, 2007. Expenses related to these leases were approximately \$0.1 million for each of the three-month periods ended March 31, 2009 and 2008, and \$0.3 million for each of the nine-month periods ended March 31, 2009 and 2008.

Effective November 1, 2007, the Company entered into agreements with Centers of Medical Excellence, Inc., an entity owned by Dr. Cruz pursuant to which this entity will act as one of the Company's independent physician affiliates in connection with the provision of primary care health services to a limited number of Medicare Advantage members enrolled in plans sponsored by CarePlus Health Plans, Inc. The arrangement is on substantially similar terms to those between the Company and its other independent physician affiliates under at risk arrangements where the Company provides medical utilization services and pays a primary care capitation fee to the provider. Under this arrangement, CarePlus pays the Company a global per member capitation fee and the Company in turn pays a monthly primary care capitation fee to Centers of Medical Excellence based on the number of CarePlus Medicare Advantage members who have selected Centers of Medical Excellence as their primary care provider. Centers of Medical Excellence is also eligible to receive a bonus from the Company if they operate in cumulative surplus. For the nine-month period ended March 31, 2009, the Company sustained an operating loss of \$0.4 million under this arrangement.

On September 19, 2008, the Company purchased an aggregate of 400,000 shares of its common stock from certain family trusts of Dr. Cruz. Dr. Cruz does not have a beneficial ownership in the shares of common stock held by these family trusts. Continucare paid \$2.14 per share for the shares for an aggregate purchase price of \$856,000. The per share purchase price paid by Continucare represented a 10% discount from the closing price of Continucare's common stock on September 19, 2008.

On September 19, 2008, the Company purchased an aggregate of 600,000 shares of its common stock from Mr. Garcia. Continucare paid \$2.14 per share for the shares for an aggregate purchase price of \$1,284,000. The per share purchase price paid by Continucare represented a 10% discount from the closing price of Continucare's common stock on September 19, 2008.



**Table of Contents**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
MARCH 31, 2009  
(UNAUDITED)**

On October 23, 2008, the Company entered into a joint venture with Dr. Jacob Nudel, a director of the Company that will seek to establish special purpose medical provider networks. As of March 31, 2009, the Company had made contributions of approximately \$0.2 million to fund operations of the joint venture.

On January 15, 2009, the Company purchased an aggregate of 1,100,000 shares of its common stock from Mr. Garcia. Continucare paid \$1.71 per share for the shares for an aggregate purchase price of \$1,881,000. The per share purchase price paid by Continucare was the closing price of Continucare's common stock on January 15, 2009.

On March 12, 2009, the Company purchased an aggregate of 350,000 shares of its common stock from certain family trusts of Dr. Cruz. Dr. Cruz does not have a beneficial ownership in the shares of common stock held by these family trusts. Continucare paid \$1.69 per share for the shares for an aggregate purchase price of \$591,500. The per share purchase price paid by Continucare represented a 5% discount from the closing price of Continucare's common stock on March 12, 2009.

**NOTE 10 CONTINGENCIES**

The Company is involved in legal proceedings incidental to its business that arise from time to time in the ordinary course of business including, but not limited to, claims related to the alleged malpractice of employed and contracted medical professionals, workers' compensation claims and other employee-related matters, and minor disputes with equipment lessors and other vendors. The Company has recorded an accrual for claims related to legal proceedings, which includes amounts for insurance deductibles and projected exposure, based on management's estimate of the ultimate outcome of such claims. The Company does not believe that the ultimate resolution of these matters will have a material adverse effect on the Company's business, results of operations, financial condition, or cash flows.

However, the results of these matters cannot be predicted with certainty, and an unfavorable resolution of one or more of these matters could have a material adverse effect on the Company's business, results of operations, financial condition, cash flow, and prospects.

**Table of Contents**

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Unless otherwise indicated or the context otherwise requires, all references in this Quarterly Report on Form 10-Q to we, us, our, Continucare or the Company refers to Continucare Corporation and its consolidated subsidiaries. references to the MDHC Companies refer to Miami Dade Health Centers, Inc. and its affiliated companies.

The following discussion and analysis should be read in conjunction with the unaudited condensed consolidated financial statements and notes thereto appearing elsewhere in this Quarterly Report on Form 10-Q.

**General**

We are a provider of primary care physician services. Through our network of 18 medical centers, we provide primary care medical services on an outpatient basis. We also provide practice management services to independent physician affiliates ( IPAs ) at 22 medical offices. All of our medical centers and IPAs are located in Miami-Dade, Broward and Hillsborough Counties, Florida. Substantially all of our revenues are derived from managed care agreements with three health maintenance organizations ( HMOs ), Humana Medical Plans, Inc. ( Humana ), Vista Healthplan of South Florida, Inc. and its affiliated companies including Summit Health Plan, Inc. ( Vista ) and Wellcare Health Plans, Inc. and its affiliated companies ( Wellcare ). Our managed care agreements with these HMOs are primarily risk agreements under which we receive for our services a monthly capitated fee with respect to the patients assigned to us. The capitated fee is a percentage of the premium that the HMOs receive with respect to those patients. In return, we assume full financial responsibility for the provision of all necessary medical care to our patients even for services we do not provide directly. For the nine-month period ended March 31, 2009, approximately 90% and 7% of our revenue was generated by providing services to Medicare-eligible and Medicaid-eligible members, respectively, under such risk arrangements. As of March 31, 2009, we provided services to or for approximately 25,600 patients on a risk basis and approximately 8,200 patients on a limited or non-risk basis. Additionally, we also provided services to over 2,500 patients as of March 31, 2009 on a non-risk fee-for-service basis.

**Medicare and Medicaid Considerations**

Substantially all of our revenue is generated by providing services to Medicare-eligible members and Medicaid-eligible members. The federal government and state governments, including Florida, from time to time explore ways to reduce medical care costs through Medicare and Medicaid reform, specifically, and through health care reform generally. Any changes that would limit, reduce or delay receipt of Medicare or Medicaid funding or mandate increased benefit levels or any developments that would disqualify us from receiving Medicare or Medicaid funding could have a material adverse effect on our business, results of operations, prospects, financial results, financial condition and cash flows. Due to the diverse range of medical care related proposals put forth and the uncertainty of any proposal's adoption, we cannot predict what impact any Medicare reform proposal ultimately adopted may have on our business, financial position or results of operations.

The Centers for Medicare and Medicaid Services ( CMS ) recently announced that it will reduce Medicare Advantage premiums effective January 2010. Based on information received from our HMO affiliates and CMS, we believe that the capitation payments we receive under our percentage of premium arrangements with our HMO affiliates for our Medicare Advantage patients will decrease by approximately 5% effective January 1, 2010 without taking into account any adjustments resulting from changes in Medicare risk adjustment scores. We anticipate that our HMO affiliates will address this premium reduction by reducing plan benefits. In an effort to further mitigate the effects of this premium reduction, we will seek to improve medical claims expense management and pursue other cost reduction strategies. There is, however, no assurance that our Medicare capitation payments will decrease by this amount or that the HMO benefit reductions or our cost reduction strategies will mitigate the Medicare Advantage premium reduction. Failure to mitigate the effects of the Medicare Advantage premium reduction may have a material adverse effect on our results of operations, financial position and cash flows.

**Table of Contents**

On January 1, 2006, the Medicare Prescription Drug Plan created by the Medicare Modernization Act became effective. As a result, our HMO affiliates have established or expanded prescription drug benefit plans for their Medicare Advantage members. Under the terms of our risk arrangements, we are financially responsible for a substantial portion of the cost of the prescription drugs our patients receive, and, in exchange, our HMO affiliates have agreed to provide us with an additional per member capitated fee related to prescription drug coverage. However, there can be no assurance that the additional fee that we receive will be sufficient to reimburse us for the additional costs that we may incur under the Medicare Prescription Drug Plan.

In addition, the premiums our HMO affiliates receive from CMS for their Medicare Prescription Drug Plans is subject to periodic adjustment, positive or negative, based upon the application of risk corridors that compare their plans' revenues targeted in their bids to actual prescription drug costs. Variances exceeding certain thresholds may result in CMS making additional payments to the HMOs or require the HMOs to refund to CMS a portion of the payments they received. Our contracted HMO affiliates estimate and periodically adjust premium revenues related to the risk corridor payment adjustment, and a portion of the HMO's estimated premium revenue adjustment is allocated to us. As a result, the revenues recognized under our risk arrangements with our HMO affiliates are net of the portion of the estimated risk corridor adjustment allocated to us. The portion of any such risk corridor adjustment that the HMOs allocate to us may not directly correlate to the historical utilization patterns of our patients or the costs that we may incur in future periods. Our HMO affiliates allocated to us adjustments related to their risk corridor payments which had the effect of reducing our operating income by approximately \$0.5 million and \$1.1 million, respectively, during the three-month periods ended March 31, 2009 and 2008, and \$1.5 million and \$2.8 million, respectively, during the nine-month periods ended March 31, 2009 and 2008.

The Medicare Prescription Drug Plan has also been subject to significant public criticism and controversy, and members of Congress have discussed possible changes to the program as well as ways to reduce the program's cost to the federal government. We cannot predict what impact, if any, these developments may have on the Medicare Prescription Drug Plan or on our future financial results.

**Critical Accounting Policies and Estimates**

Our significant accounting policies are described in Note 2 to the consolidated financial statements included in our Annual Report on Form 10-K for Fiscal 2008. Included within these policies are certain policies which contain critical accounting estimates and, therefore, have been deemed to be critical accounting policies. Critical accounting estimates are those which require management to make assumptions about matters that were uncertain at the time the estimate was made and for which the use of different estimates, which reasonably could have been used, or changes in the accounting estimates that are reasonably likely to occur from period to period, could have a material impact on the presentation of our financial condition, changes in financial condition or results of operations.

We base our estimates and assumptions on historical experience, knowledge of current events and anticipated future events, and we continuously evaluate and update our estimates and assumptions. However, our estimates and assumptions may ultimately prove to be incorrect or incomplete and our actual results may differ materially. We believe the following critical accounting policies involve the most significant judgments and estimates used in the preparation of our consolidated financial statements.

***Revenue Recognition***

Under our risk contracts with HMOs, we receive a percentage of premium or other capitated fee for each patient that chooses one of our physicians as their primary care physician. Revenue under these agreements is generally recorded in the period we assume responsibility to provide services at the rates then in effect as determined by the respective contract. As part of the Medicare Advantage program, CMS periodically recomputes the premiums to be paid to the HMOs based on updated health status of participants and updated demographic factors. We record any adjustments to this revenue at the time that the information necessary to make the determination of the adjustment is received from the HMO.

**Table of Contents**

Under our risk agreements, we assume responsibility for the cost of all medical services provided to the patient, even those we do not provide directly, in exchange for a percentage of premium or other capitated fee. To the extent that patients require more frequent or expensive care, our revenue under a contract may be insufficient to cover the costs of care provided. When it is probable that expected future health care costs and maintenance costs under a contract or group of existing contracts will exceed anticipated capitated revenue on those contracts, we recognize losses on our prepaid health care services with HMOs. No contracts were considered loss contracts at March 31, 2009 because we have the right to terminate unprofitable physicians and close unprofitable centers under our managed care contracts.

Under our limited risk and non-risk contracts with HMOs, we receive a capitation fee based on the number of patients for which we are providing services on a monthly basis. The capitation fee is recorded as revenue in the period in which services are provided as determined by the respective contract.

Payments under both our risk contracts and our non-risk contracts (for both the Medicare Advantage program as well as Medicaid) are also subject to reconciliation based upon historical patient enrollment data. We record any adjustments to this revenue at the time that the information necessary to make the determination of the adjustment is received from the HMO or the applicable governmental body.

*Medical Claims Expense Recognition*

The cost of health care services provided or contracted for is accrued in the period in which the services are provided. This cost includes our estimate of the related liability for medical claims incurred in the period but not yet reported, or IBNR. IBNR represents a material portion of our medical claims liability which is presented in the balance sheet net of amounts due from HMOs. Changes in this estimate can materially affect, either favorably or unfavorably, our results of operations and overall financial position.

We develop our estimate of IBNR primarily based on historical claims incurred per member per month. We adjust our estimate if we have unusually high or low utilization or if benefit changes provided under the HMO plans are expected to significantly increase or reduce our claims exposure. We also adjust our estimate for differences between the estimated claims expense recorded in prior months to actual claims expense as claims are paid by the HMO and reported to us. We use an actuarial analysis as an additional tool to further corroborate our estimate of IBNR.

Based on our analysis, as of March 31, 2009, we recorded a liability of approximately \$22.5 million for IBNR. The liability for IBNR decreased by \$1.4 million or 5.7% to \$22.5 million as of March 31, 2009 from \$23.9 million as of June 30, 2008 primarily due to the timing of claims paid by our HMO affiliates and a decrease in patients under risk arrangements. The liability for IBNR as of March 31, 2008 of \$23.4 million was relatively unchanged from the liability for IBNR of \$23.6 million recorded as of June 30, 2007.

*Consideration of Impairment Related to Goodwill and Other Intangible Assets*

Our balance sheet includes intangible assets, including goodwill and other separately identifiable intangible assets, of approximately \$78.8 million, which represented approximately 66% of our total assets at March 31, 2009. The most significant component of the intangible assets consists of the intangible assets recorded in connection with the acquisition (the Acquisition) of Miami Dade Health Centers, Inc. and its affiliated companies (collectively, the

MDHC Companies). The purchase price, including acquisition costs, of approximately \$66.2 million was allocated to the estimated fair value of acquired tangible assets of \$13.9 million, identifiable intangible assets of \$8.7 million and assumed liabilities of \$15.3 million, resulting in goodwill totaling \$58.9 million.

Under Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, goodwill and intangible assets with indefinite useful lives are no longer amortized, but are reviewed for impairment on an annual basis or more frequently if certain indicators of impairment arise. Intangible assets with definite useful lives are amortized over their respective useful lives to their estimated residual values and also reviewed for impairment annually or more frequently if certain indicators of impairment arise. Indicators of an impairment include, among other things, a significant adverse change in legal factors or the business climate, the loss of a key

**Table of Contents**

HMO contract, an adverse action by a regulator, unanticipated competition, and the loss of key personnel or allocation of goodwill to a portion of business that is to be sold.

Because we operate in a single segment of business, we have determined that we have a single reporting unit and we perform our impairment test for goodwill on an enterprise level. In performing the impairment test, we compare the total current market value of all of our outstanding common stock, to the current carrying value of our total net assets, including goodwill and intangible assets. Depending on the market value of our common stock at the time that an impairment test is required, we may also perform other valuation techniques to measure market value before reaching a conclusion that impairment exists. Depending on the outcome of our analyses, there is a risk that a portion of our intangible assets would be considered impaired and must be written-off during that period. We completed our annual impairment test as of May 1, 2008 and determined that no impairment existed. In addition, no indicators of impairment were noted and accordingly, no impairment charges were required for the three and nine-month periods ended March 31, 2009. Should we later determine that an indicator of impairment exists, we would be required to perform an additional impairment test.

*Realization of Deferred Income Tax Assets*

We account for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes ( SFAS 109 ) which requires that deferred income tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. SFAS No. 109 also requires that deferred income tax assets be reduced by a valuation allowance if it is more likely than not that some portion or all of the deferred income tax asset will not be realized.

As part of the process of preparing our consolidated financial statements, we estimate our income taxes based on our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. We also recognize as deferred income tax assets the future tax benefits from net operating loss carryforwards. We evaluate the realizability of these deferred income tax assets by assessing their valuation allowances and by adjusting the amount of such allowances, if necessary. Among the factors used to assess the likelihood of realization are our projections of future taxable income streams, the expected timing of the reversals of existing temporary differences, and the impact of tax planning strategies that could be implemented to avoid the potential loss of future tax benefits. However, changes in tax codes, statutory tax rates or future taxable income levels could materially impact our valuation of tax accruals and assets and could cause our provision for income taxes to vary significantly from period to period. At March 31, 2009, we had deferred income tax liabilities in excess of deferred income tax assets of approximately \$3.1 million.

*Stock-Based Payment*

We use the modified prospective transition method under SFAS 123(R). SFAS 123(R) requires us to recognize compensation costs in our financial statements related to our share-based payment transactions with employees and directors. SFAS 123(R) requires us to calculate this cost based on the grant date fair value of the equity instrument. As a result of adopting SFAS No. 123(R), we recognized share-based compensation expense of \$0.3 million and \$0.4 million, respectively, for the three-month periods ended March 31, 2009 and 2008 and \$0.9 million and \$1.0 million, respectively, for the nine-month periods ended March 31, 2009 and 2008. For the three and nine-month periods ended March 31, 2009 and 2008, the Company had no excess tax benefits resulting from the exercise of stock options.

Consistent with our practices prior to adopting SFAS 123(R), we have elected to calculate the fair value of our employee stock options using the Black-Scholes option pricing model. Using this model we calculated the fair value for employee stock options granted during the three-month periods ended March 31, 2009 and 2008 based on the following assumptions: risk-free interest rate ranging from 0.66% to 2.28% and 1.61% to 2.71%, respectively; dividend yield of 0%; weighted-average volatility factor of the expected market price of our common stock of 60.7% and 59.6%, respectively, and weighted-average expected life of the options ranging from 2 to 6 years, depending on the vesting provisions of each option. The fair value for employee stock options granted during the nine-month periods ended March 31, 2009 and 2008 based on the following assumptions: risk-free interest rate ranging from 0.66% to 3.09% and 1.61% to 4.22%, respectively; dividend yield of 0%; weighted-average volatility factor of the expected market price of our common stock of 58.6% and 59.5%, respectively, and weighted-average





**Table of Contents**

expected life of the options ranging from 2 to 6 years, depending on the vesting provisions of each option. The expected life of the options is based on the historical exercise behavior of our employees. The expected volatility factor is based on the historical volatility of the market price of our common stock as adjusted for certain events that management deemed to be non-recurring and non-indicative of future events.

SFAS 123(R) does not require the use of any particular option valuation model. Because our stock options have characteristics significantly different from traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, it is possible that existing models may not necessarily provide a reliable measure of the fair value of our employee stock options. We selected the Black-Scholes model based on our prior experience with it, its wide use by issuers comparable to us, and our review of alternate option valuation models.

The effect of applying the fair value method of accounting for stock options on reported net income for any period may not be representative of the effects for future periods because our outstanding options typically vest over a period of several years and additional awards may be made in future periods.

**RESULTS OF OPERATIONS****COMPARISON OF THE THREE-MONTH PERIOD ENDED MARCH 31, 2009 TO THE THREE-MONTH PERIOD ENDED MARCH 31, 2008***Revenue*

Revenue increased by \$9.5 million, or 14.3%, to \$75.4 million for the three-month period ended March 31, 2009 from \$65.9 million for the three-month period ended March 31, 2008 due primarily to increases in our Medicare revenue.

The most significant component of our revenue is the revenue we generate from Medicare patients under risk arrangements which increased by \$10.2 million, or 17.4%, during the three-month period ended March 31, 2009. During the three-month period ended March 31, 2009, revenue generated by our Medicare risk arrangements increased approximately 19.9% on a per patient per month basis and Medicare patient months decreased by approximately 2.1% over the comparable period of Fiscal 2008. The increase in the per member per month Medicare revenue was primarily due to a rate increase in the Medicare premiums and an increase in premiums resulting from the Medicare risk adjustment program. The increase in Medicare revenue was partially offset by a \$1.0 million decrease in revenue generated by our Medicaid patients due primarily to a decrease in Medicaid patient months.

Under the Medicare risk adjustment program, the health status and demographic factors of Medicare Advantage participants are taken into account in determining premiums paid for each participant. CMS periodically recomputes the premiums to be paid to the HMOs based on the updated health status and demographic factors of the Medicare Advantage participants. In addition, the premiums paid to the HMOs for their Medicare Prescription Drug Plan are subject to periodic adjustment based upon CMS's risk corridor adjustment methodology. The net effect of the premium adjustments included in revenue for the three-month period ended March 31, 2008 was a favorable retroactive Medicare adjustment of approximately \$0.4 million. There were no retroactive premium adjustments included in revenue for the three-month period ended March 31, 2009. Future Medicare risk adjustments may result in reductions of revenue depending on the future health status and demographic factors of our patients as well as the application of CMS's risk corridor methodology to the HMOs Medicare Prescription Drug Programs.

Revenue generated by our managed care entities under contracts with Humana, Vista and Wellcare accounted for approximately 72%, 19% and 7%, respectively, of our total revenue for the three-month period ended March 31, 2009. Revenue generated by our managed care entities under contracts with Humana, Vista and Wellcare accounted for approximately 73%, 17% and 9%, respectively, of our total revenue for the three-month period ended March 31, 2008.

**Table of Contents***Operating Expenses*

Medical services expenses are comprised of medical claims expense and other direct costs related to the provision of medical services to our patients. Because our risk contracts with HMOs provide that we are financially responsible for the cost of substantially all medical services provided to our patients under those contracts, our medical claims expense includes the costs of prescription drugs our patients receive as well as medical services provided to patients under our risk contracts by providers other than us. Other direct costs consist primarily of salaries, taxes and benefits of our health professionals providing primary care services including a portion of our stock-based compensation expense, medical malpractice insurance costs, capitation payments to our IPA physicians and fees paid to independent contractors providing medical services to our patients.

Medical services expenses for the three-month period ended March 31, 2009 increased by \$8.5 million, or 16.2%, to \$60.5 million from \$52.0 million for the three-month period ended March 31, 2008. Medical claims expense, which is the largest component of medical services expense, increased by \$8.1 million, or 17.9%, to \$53.2 million for the three-month period ended March 31, 2009 from \$45.1 million for the three-month period ended March 31, 2008 primarily due to an increase in Medicare claims expense of \$7.9 million, or 19.4%. The increase in Medicare claims expense resulted from a 21.9% increase on a per patient per month basis in medical claims expenses related to our Medicare patients and a decrease of 2.1% in Medicare patient months. The increase in Medicare per patient per month medical claims expense is primarily attributable to enhanced benefits offered by our HMO affiliates, inflationary trends in the health care industry and higher than usual favorable adjustments relating to prior period medical claims expenses during the three-month period ended March 31, 2008.

As a percentage of revenue, medical services expenses increased to 80.2% of revenue for the three-month period ended March 31, 2009 as compared to 78.9% for the three-month period ended March 31, 2008. Our claims loss ratio (medical claims expense as a percentage of revenue) increased to 70.6% for the three-month ended March 31, 2009 from 68.4% for the three-month period ended March 31, 2008. These increases were primarily due to an increase in Medicare revenue at a lower rate than the increase in Medicare claims expense on a per patient per month basis. HMOs are under continuous competitive pressure to offer enhanced and possibly more expensive, benefits to their Medicare Advantage members. The premiums CMS pays to HMOs for Medicare Advantage members are generally not increased as a result of those benefit enhancements. This could increase our claims loss ratio in future periods, which could reduce our profitability and cash flows.

Other direct costs increased by \$0.3 million, or 4.8%, to \$7.2 million for the three-month period ended March 31, 2009 from \$6.9 million for the three-month period ended March 31, 2008. As a percentage of revenue, other direct costs decreased to 9.6% for the three-month period ended March 31, 2009 from 10.5% for the three-month period ended March 31, 2008. The increase in the amount of other direct costs was primarily due to an increase in payroll expense and related benefits for physicians and medical support personnel at our medical centers and patient transportation related expenses.

Administrative payroll and employee benefits expense remained relatively unchanged at \$3.5 million for the three-month periods ended March 31, 2009 and 2008. As a percentage of revenue, administrative payroll and employee benefits expense decreased to 4.7% for the three-month period ended March 31, 2009 from 5.3% for the three-month period ended March 31, 2008.

General and administrative expenses remained relatively unchanged at \$4.4 million and \$4.3 million for the three-month periods ended March 31, 2009 and 2008, respectively. As a percentage of revenue, general and administrative expenses decreased to 5.8% for the three-month period ended March 31, 2009 from 6.6% for the three-month period ended March 31, 2008.

*Income from Operations*

Income from operations for the three-month period ended March 31, 2009 increased by \$0.9 million, or 16.0%, to \$7.0 million from \$6.1 million for the three-month period ended March 31, 2008.

## **Table of Contents**

### *Taxes*

An income tax provision of \$2.7 million and \$2.5 million was recorded for the three-month periods ended March 31, 2009 and 2008, respectively. The effective income tax rates were 38.7% and 40.8% for the three-month periods ended March 31, 2009 and 2008, respectively.

### *Net Income*

Net income for the three-month period ended March 31, 2009 increased by \$0.6 million, or 17.7%, to \$4.3 million from \$3.7 million for the three-month period ended March 31, 2008.

## **COMPARISON OF THE NINE-MONTH PERIOD ENDED MARCH 31, 2009 TO THE NINE-MONTH PERIOD ENDED MARCH 31, 2008**

### *Revenue*

Revenue increased by \$17.7 million, or 9.4%, to \$206.0 million for the nine-month period ended March 31, 2009 from \$188.3 million for the nine-month period ended March 31, 2008 due primarily to increases in our Medicare revenue.

The most significant component of our revenue is the revenue we generate from Medicare patients under risk arrangements which increased by \$19.0 million, or 11.4%, during the nine-month period ended March 31, 2009. During the nine-month period ended March 31, 2009, revenue generated by our Medicare risk arrangements increased approximately 12.3% on a per patient per month basis and Medicare patient months decreased by approximately 0.8% over the comparable period of Fiscal 2008. The increase in the per patient per month Medicare revenue was primarily due to a rate increase in the Medicare premiums and an increase in premiums resulting from the Medicare risk adjustment program. Included in revenue for the nine-month periods ended March 31, 2009 and 2008 were favorable retroactive Medicare adjustments of \$0.6 million and unfavorable retroactive Medicare adjustments of \$1.1 million, respectively, related to Medicare premiums and risk corridor adjustments. Future Medicare risk adjustments may result in reductions of revenue depending on the future health status and demographic factors of our patients as well as the application of CMS's risk corridor methodology to the HMOs Medicare Prescription Drug Programs. The increase in Medicare revenue was partially offset by a \$2.1 million decrease in revenue generated by our Medicaid patients due primarily to a decrease in Medicaid patient months.

During the nine-month period ended March 31, 2008, we received payments and recorded amounts due from our HMO affiliates of approximately \$0.5 million related primarily to Medicare risk adjustments relating to the operations of the MDHC Companies for periods prior to completion of the Acquisition. While these transactions ordinarily are reflected in our results of operations, since they related to periods prior to our acquisition of the MDHC Companies, they were instead recorded as purchase accounting adjustments which decreased the amount of goodwill we recorded for the Acquisition.

Revenue generated by our managed care entities under contracts with Humana, Vista and Wellcare accounted for approximately 72%, 18% and 8%, respectively, of our total revenue for the nine-month period ended March 31, 2009. Revenue generated by our managed care entities under contracts with Humana, Vista and Wellcare accounted for approximately 72%, 19% and 8%, respectively, of our total revenue for the nine-month period ended March 31, 2008.

### *Operating Expenses*

Medical services expenses for the nine-month period ended March 31, 2009 increased by \$12.9 million, or 8.4%, to \$167.2 million from \$154.3 million for the nine-month period ended March 31, 2008. Medical claims expense, which is the largest component of medical services expense, increased by \$11.8 million, or 8.8%, to \$145.7 million for the nine-month period ended March 31, 2009 from \$133.9 million for the nine-month period ended March 31, 2008 primarily due to an increase in Medicare claims expense of \$12.6 million, or 10.5%. The

**Table of Contents**

increase in Medicare claims expense resulted from an 11.4% increase in medical claims expense on a per patient per month basis and a 0.8% decrease in Medicare patient months. The increase in Medicare per patient per month medical claims expense is primarily attributable to enhanced benefits offered by our HMO affiliates and inflationary trends in the health care industry. The increase in Medicare claims expense was partially offset by a decrease in Medicaid claims expense of \$0.4 million due primarily to a decrease in Medicaid patient months.

As a percentage of revenue, medical services expenses decreased to 81.2% of revenue for the nine-month period ended March 31, 2009 as compared to 81.9% for the nine-month period ended March 31, 2008. Our claims loss ratio (medical claims expense as a percentage of revenue) decreased to 70.7% for the nine-month ended March 31, 2009 from 71.1% for the nine-month period ended March 31, 2008. These decreases were primarily due to an increase in Medicare revenue at a greater rate than the increase in Medicare claims expense on a per patient per month basis.

Other direct costs increased by \$1.1 million, or 5.4%, to \$21.5 million for the nine-month period ended March 31, 2009 from \$20.4 million for the nine-month period ended March 31, 2008. As a percentage of revenue, other direct costs decreased to 10.5% for the nine-month period ended March 31, 2009 from 10.9% for the nine-month period ended March 31, 2008. The increase in the amount of other direct costs was primarily due to an increase in payroll expense and related benefits for physicians and medical support personnel at our medical centers.

Administrative payroll and employee benefits expense increased by \$0.5 million, or 5.4%, to \$9.4 million for the nine-month period ended March 31, 2009 from \$8.9 million for the nine-month period ended March 31, 2008. As a percentage of revenue, administrative payroll and employee benefits expense decreased to 4.6% for the nine-month period ended March 31, 2009 from 4.7% for the nine-month period ended March 31, 2008. The increase in administrative payroll and employee benefits expense was primarily due to increases in salaries.

General and administrative expenses remained relatively unchanged at \$12.4 million and \$12.3 million for the nine-month periods ended March 31, 2009 and 2008, respectively. As a percentage of revenue, general and administrative expenses decreased to 6.0% for the nine-month period ended March 31, 2009 from 6.5% for the nine-month period ended March 31, 2008.

***Income from Operations***

Income from operations for the nine-month period ended March 31, 2009 increased by \$4.1 million, or 31.9%, to \$17.0 million from \$12.9 million for the nine-month period ended March 31, 2008.

***Taxes***

An income tax provision of \$6.6 million and \$5.2 million was recorded for the nine-month periods ended March 31, 2009 and 2008, respectively. The effective income tax rates were 38.7% and 39.3% for the nine-month periods ended March 31, 2009 and 2008, respectively.

***Net Income***

Net income for the nine-month period ended March 31, 2009 increased by \$2.4 million, or 29.3%, to \$10.5 million from \$8.1 million for the nine-month period ended March 31, 2008.

**LIQUIDITY AND CAPITAL RESOURCES**

At March 31, 2009, working capital was \$20.4 million, an increase of \$0.1 million from \$20.3 million at June 30, 2008. Cash and cash equivalents increased by \$0.4 million to \$10.3 million at March 31, 2009 compared to \$9.9 million at June 30, 2008. The increases in cash and cash equivalents was primarily due to cash provided by operating activities of \$13.3 million, partially offset by cash used to repurchase our common stock of \$10.6 million and cash used for the purchase of property and equipment of \$2.2 million.

## **Table of Contents**

Net cash of \$13.3 million was provided by operating activities for the nine-month period ended March 31, 2009 compared to \$12.0 million for the nine-month period ended March 31, 2008. The \$1.3 million increase in cash provided by operating activities was primarily due to an increase in net income of \$2.4 million, partially offset by a net decrease in income taxes payable of \$1.6 million.

Net cash of \$2.2 million was used for investing activities for the nine-month period ended March 31, 2009 compared to \$0.9 million for the nine-month period ended March 31, 2008. The \$1.3 million increase in net cash used for investing activities primarily related to an increase in cash used for leasehold improvements.

Net cash of approximately \$10.7 million was used for financing activities for the nine-month period ended March 31, 2009 compared to \$5.7 million for the nine-month period ended March 31, 2008. The \$5.0 million increase in cash used for financing activities for the nine-month period ended March 31, 2009 was primarily due to a \$5.0 million net increase in cash used for the repurchase of common stock.

Pursuant to the terms under our managed care agreements with certain of our HMO affiliates, we posted irrevocable standby letters of credit amounting to \$1.2 million to secure our payment obligations to those HMOs. We are required to maintain these letters of credit throughout the term of the managed care agreements.

In March 2009, our Board of Directors increased our previously announced program to authorize the repurchase of an additional 2,500,000 shares of our common stock bringing the total number of shares of common stock authorized for repurchase under the program to 15,000,000 shares. Any such repurchases will be made from time to time at the discretion of our management in the open market or in privately negotiated transactions subject to market conditions and other factors. We anticipate that any such repurchases of shares will be funded through cash from operations. During the three and nine-month periods ended March 31, 2009, we repurchased 1,562,232 shares and 5,419,004 shares of our common stock, respectively, for approximately \$2.7 million and \$10.6 million, respectively. During the period from April 1, 2009 through April 30, 2009, we did not repurchase any shares. As of April 30, 2009, we had repurchased 11,907,004 shares of our common stock for approximately \$25.0 million.

We believe that we will be able to fund our capital commitments and our anticipated operating cash requirements for the foreseeable future and satisfy any remaining obligations from our working capital, anticipated cash flows from operations, our Credit Facility, and our Term Loans. At March 31, 2009, approximately \$9.6 million was available for future borrowing under the Term Loans and the Credit Facility.

## **FORWARD-LOOKING STATEMENTS**

Our business, financial condition, results of operations, cash flows and prospects, and the prevailing market price and performance of our common stock, may be adversely affected by a number of factors, including the matters discussed below. Certain statements and information set forth in this Quarterly Report on Form 10-Q, as well as other written or oral statements made from time to time by us or by our authorized executive officers on our behalf, constitute forward-looking statements within the meaning of the Federal Private Securities Litigation Reform Act of 1995. We intend for our forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and we set forth this statement and these risk factors in order to comply with such safe harbor provisions. You should note that our forward-looking statements speak only as of the date of this report or when made and we undertake no duty or obligation to update or revise our forward-looking statements, whether as a result of new information, future events or otherwise. Although we believe that the expectations, plans, intentions and projections reflected in our forward-looking statements are reasonable, such statements are subject to risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. The risks, uncertainties and other factors that our shareholders and prospective investors should consider include, but are not limited to, the following:

Our operations are dependent on three health maintenance organizations;

Under our most important contracts we are responsible for the cost of medical services to our patients in return for a capitated fee;

**Table of Contents**

If we are unable to manage medical benefits expense effectively, our profitability will likely be reduced;

Medicare premiums have generally risen more slowly than the cost of providing health care services;

A failure to estimate incurred but not reported benefits expense accurately will affect our profitability;

We compete with many health care providers for patients and HMO affiliations;

We may not be able to successfully recruit or retain existing relationships with qualified physicians and medical professionals;

Our business exposes us to the risk of medical malpractice lawsuits;

Our revenues will be affected by the Medicare Risk Adjustment program;

We presently operate only in Florida;

Failure to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act could have a material adverse effect on our business and stock price;

A significant portion of our voting power is concentrated;

We are dependent on our executive officers and other key employees;

We depend on the management information systems of our affiliated HMOs;

We depend on our information processing systems;

Volatility of our stock price could adversely affect you;

The Internal Revenue Service may disagree with the parties' description of the federal income tax consequences;

Goodwill and other intangible assets represent a substantial portion of our total assets;

Competition for acquisition targets and acquisition financing and other factors may impede our ability to acquire other businesses and may inhibit our growth;

Our acquisitions could result in integration difficulties, unexpected expenses, diversion of management's attention and other negative consequences;

We are subject to government regulation;

The health care industry is subject to continued scrutiny;

Our insurance coverage may not be adequate, and rising insurance premiums could negatively affect our profitability;

Deficit spending and economic downturns could negatively impact our results of operations;

Many factors that increase health care costs are largely beyond our ability to control; and

Health care reform initiatives, particularly changes to the Medicare system, could adversely affect our operations.

We assume no responsibility to update our forward-looking statements as a result of new information, future events or otherwise. Additional information concerning these and other risks and uncertainties is contained in our filings with the Securities and Exchange Commission, including the section entitled "Risk Factors" in our Annual Report on Form 10-K for Fiscal 2008 and in Item 1A of Part II of this Quarterly Report Form 10-Q.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

At March 31, 2009, we held certificates of deposit and cash equivalent investments in high grade, short-term securities, which are not typically subject to material market risk. At March 31, 2009, we had capital lease obligations outstanding at fixed rates. For loans with fixed interest rates, a hypothetical 10% change in interest rates would have no material impact on our future earnings and cash flows related to these instruments and would have an immaterial impact on the fair value of these instruments. Our Term Loans and Credit Facility have variable interest rates and are interest rate sensitive, however, we had no amount outstanding under these facilities at March 31, 2009. We have no material risk associated with foreign currency exchange rates or commodity prices.

**Table of Contents**

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) or Rule 15d-15(e)) as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of March 31, 2009, our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Our Chief Executive Officer's and Chief Financial Officer's conclusions regarding the effectiveness of our disclosure controls and procedures should be considered in light of the following limitations on the effectiveness of our disclosure controls and procedures, some of which pertain to most, if not all, business enterprises, and some of which arise as a result of the nature of our business. Our management, including our Chief Executive Officer and our Chief Financial Officer, does not expect that our disclosure controls and procedures will prevent all errors or improper conduct. A control system, no matter how well conceived and operated, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of improper conduct, if any, will be detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the controls. Further, the design of any control system is based, in part, upon assumptions about the likelihood of future events, and there can be no assurance that any control system design will succeed in achieving its stated goals under all potential future conditions. Additionally, over time, controls may become inadequate because of changes in conditions or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. In addition, we depend on our HMO affiliates for certain financial and other information that we receive concerning the revenue and expenses that we earn and incur. Because our HMO affiliates generate that information for us, we have less control over the manner in which that information is generated.

**Changes in Internal Control over Financial Reporting**

In connection with its evaluation of the effectiveness of our internal control over financial reporting, our management did not identify any changes in our internal control over financial reporting that occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Section 302 Certifications**

Provided with this report are certifications of our Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and the SEC's implementing regulations. This Item 4 contains the information concerning the evaluations referred to in those certifications, and you should read this information in conjunction with those certifications for a more complete understanding of the topics presented.

**PART II OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

See Note 10 of our Condensed Consolidated Financial Statements.



**Table of Contents****ITEM 1A. RISK FACTORS**

There have been no material changes to the risk factors previously disclosed in our Annual Report on Form 10-K for Fiscal 2008 and in other reports filed from time to time with the SEC since the date we filed our Annual Report on Form 10-K. Readers are urged to carefully review our risk factors since they may cause our results to differ from the forward-looking statements made in this report or otherwise made by or on our behalf. Those risk factors are not the only ones we face. Additional risks not presently known to us or other factors not perceived by us to present significant risks to our business at this time also may impair our business operation.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

In March 2009, we increased our previously announced stock repurchase program to authorize the repurchase of an additional 2,500,000 shares of common stock bringing the total number of shares of common stock authorized for repurchase under the program to 15,000,000 shares. Any such repurchases will be made from time to time at the discretion of our management in the open market or in privately negotiated transactions subject to market conditions and other factors. We anticipate that any such repurchases of shares will be funded through cash from operations. The stock repurchase program was originally approved by the Board of Directors in February 2005. There is no expiration date specified for this program. The following table provides information with respect to our stock repurchases during the second quarter of Fiscal 2009:

<b>Period</b>	<b>Total Number of Shares Purchased</b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plan</b>	<b>Maximum Number of Shares that May Yet Be Purchased Under the Plan</b>
January 1 to January 31, 2009	1,137,300	\$ 1.71	1,137,300	3,517,928
February 1 to February 28, 2009	27,600	\$ 1.95	27,600	3,490,328
March 1 to March 31, 2009	397,332	\$ 1.70	397,332	3,092,996
Totals	1,562,232	\$ 1.71	1,562,232	

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

At our Annual Meeting of Shareholders held on March 12, 2009, our shareholders voted to re-elect each of the Director nominees and to ratify the appointment of Ernst & Young LLP as our independent registered public accounting firm.

The number of votes cast for or withheld, with respect to each of the nominees, were as follows:

<b>Nominee</b>	<b>For</b>	<b>Withheld</b>
Richard C. Pfenniger, Jr.	54,688,350	548,752
Luis Cruz, M.D.	49,724,333	5,512,769
Robert J. Cresci	54,931,778	305,324
Neil Flanzraich	54,891,524	345,578
Phillip Frost, M.D.	50,060,544	5,176,558
Jack Nudel, M.D.	55,090,938	146,164
Jacqueline Simkin	55,089,938	147,164
A. Marvin Strait	55,087,213	149,889



**Table of Contents**

There were no other nominees for director.

The number of votes cast for, against or abstain with respect to the ratification of the appointment of Ernst & Young LLP were as follows:

For	Against	Abstain
55,099,565	16,722	120,815

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

Exhibits

31.1 Section 302 Certification of the Chief Executive Officer.

31.2 Section 302 Certification of the Chief Financial Officer.

32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**Table of Contents**

**SIGNATURES**

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

**CONTINUCARE CORPORATION**

Dated: May 7, 2009

By: /s/ Richard C. Pfenniger, Jr.  
Richard C. Pfenniger, Jr.  
Chairman of the Board, Chief Executive  
Officer  
and President

By: /s/ Fernando L. Fernandez  
Fernando L. Fernandez  
Senior Vice President Finance, Chief  
Financial Officer, Treasurer and  
Secretary