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PROXYMED INC /FT LAUDERDALE/  
Form 10-Q  
May 15, 2003

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended MARCH 31, 2003

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

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

Commission file number: 000-22052

PROXYMED, INC.

(Exact name of registrant as specified in its charter)

FLORIDA

65-0202059

-----  
(State or other jurisdiction of  
incorporation or organization)

-----  
(I.R.S. Employer  
Identification No.)

2555 DAVIE ROAD, SUITE 110, FT. LAUDERDALE, FLORIDA

33317

-----  
(Address of principal executive offices)

-----  
(Zip Code)

(954) 473-1001

-----  
(Registrant's telephone number)

-----  
(Former name, former address and former fiscal year,  
if changed since last report)

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  No

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of

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common stock, as of the latest practicable date:

COMMON STOCK, \$.001 PAR VALUE  
6,782,938 SHARES AS OF MAY 14, 2003

## PART 1 - FINANCIAL INFORMATION

### ITEM 1 - FINANCIAL STATEMENTS

#### PROXYMED, INC. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	March 31, 2003	Dec 31, 2002
	-----	-----
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 10,347,000	\$ 10,347,000
Accounts receivable - trade, net	10,970,000	10,970,000
Notes and other receivables	502,000	502,000
Inventory	2,912,000	2,912,000
Other current assets	1,614,000	1,614,000
	-----	-----
Total current assets	26,345,000	26,345,000
Property and equipment, net	5,827,000	5,827,000
Goodwill, net	32,944,000	32,944,000
Purchased technology, capitalized software and other intangible assets, net	17,800,000	17,800,000
Restricted cash	1,151,000	1,151,000
Other assets	400,000	400,000
	-----	-----
Total assets	\$ 84,467,000	\$ 84,467,000
	=====	=====

#### LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:		
Notes payable and current portion of long-term debt	\$ 1,193,000	\$ 1,193,000
Accounts payable and accrued expenses	16,671,000	16,671,000
Deferred revenue	494,000	494,000
	-----	-----
Total current liabilities	18,358,000	18,358,000
Convertible notes	13,400,000	13,400,000
Other long-term debt	1,938,000	1,938,000
Long-term deferred revenue and other long-term liabilities	2,488,000	2,488,000
	-----	-----
Total liabilities	36,184,000	36,184,000
	-----	-----

Stockholders' equity:

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Series C 7% Convertible preferred stock - \$.01 par value.	--	
Authorized 300,000 shares; issued 253,265 shares;		
outstanding 2,000 shares; liquidation preference \$13,333		
Common stock - \$.001 par value. Authorized 13,333,333 shares;	7,000	
issued and outstanding 6,782,938 shares		
Additional paid-in capital	146,187,000	14
Accumulated deficit	(97,725,000)	(9
Note receivable from stockholder	(186,000)	
	-----	-----
Total stockholders' equity	48,283,000	5
	-----	-----
Total liabilities and stockholders' equity	\$ 84,467,000	\$ 8
	=====	=====

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

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PROXYMED, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

	Three Months Ended March 31,	
	2003	2002
	-----	-----
Revenues:		
Transaction fees, services and license fees	\$ 12,560,000	\$ 6,709,000
Communication devices and other tangible goods	4,870,000	4,794,000
	-----	-----
	17,430,000	11,503,000
	-----	-----
Costs and expenses:		
Cost of transaction fees, services and license fees	4,271,000	2,132,000
Cost of tangible goods	3,222,000	3,247,000
Selling, general and administrative expenses	10,760,000	5,493,000
Depreciation and amortization	1,330,000	569,000
Loss on disposal of assets	125,000	--
	-----	-----
	19,708,000	11,441,000
	-----	-----
Operating income (loss)	(2,278,000)	62,000

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Interest income (expense), net	(174,000)	(13,000)
	-----	-----
Net income (loss)	(2,452,000)	49,000
Deemed dividends	--	612,000
	-----	-----
Net loss applicable to common shareholders	\$ (2,452,000)	\$ (563,000)
	=====	=====
Basic and diluted loss per share	\$ (0.36)	\$ (0.11)
	=====	=====
Basic and diluted weighted average shares outstanding	6,782,938	5,114,596
	=====	=====

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

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PROXYMED, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

	Three Months Ended March	
	2003	20
	-----	-----
Cash flows from operating activities:		
Net income (loss)	\$ (2,452,000)	\$
Adjustments to reconcile net income (loss) to net provided by (used in) operating activities:		
Depreciation and amortization	1,330,000	5
Provision for (recovery of) doubtful accounts	54,000	(
Provision for obsolete inventory	10,000	
Loss on disposal of fixed assets	125,000	
Changes in assets and liabilities, net of effect of acquisitions and dispositions:		
Accounts and other receivables	(984,000)	(
Inventory	(148,000)	(1
Other current assets	(262,000)	(3
Accounts payable and accrued expenses	1,797,000	

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Deferred revenue	(38,000)	
Other, net	74,000	
	-----	-----
Net cash provided by (used in) operating activities	(494,000)	1
	-----	-----
Cash flows from investing activities:		
Capital expenditures	(910,000)	(4
Capitalized software	(276,000)	(1
Collection of notes receivable	81,000	
Proceeds from sale of fixed assets	64,000	
Increase in restricted cash	(326,000)	
Payments for acquisition-related costs	(3,860,000)	
	-----	-----
Net cash used in investing activities	(5,227,000)	(5
	-----	-----
Cash flows from financing activities:		
Payment of note payable related to acquisition of business	--	(7,0
Payment of notes payable, capital leases and long-term debt	(310,000)	(
	-----	-----
Net cash used in financing activities	(310,000)	(7,0
	-----	-----
Net decrease in cash and cash equivalents	(6,031,000)	(7,4
Cash and cash equivalents at beginning of period	16,378,000	12,6
	-----	-----
Cash and cash equivalents at end of period	\$ 10,347,000	\$ 5,1
	=====	=====

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

PROXYMED, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- (a) BASIS OF PRESENTATION - The accompanying unaudited consolidated financial statements of ProxyMed, Inc. and subsidiaries ("ProxyMed" or the "Company") and the notes thereto have been prepared in accordance with the instructions of Form 10-Q and Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (the "SEC") and do not include all of the information and disclosures required by accounting principles generally accepted in the United States of America. However, such information reflects all adjustments (consisting of normal recurring adjustments), which are, in the

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opinion of management, necessary for a fair statement of results for the interim periods.

On December 31, 2002, the Company acquired all of the capital stock of MedUnite, Inc. ("MedUnite"), a privately-held company providing healthcare claims processing services founded by seven of the nation's largest health insurers, for \$10,000,000 in cash and \$13,400,000 in 4% convertible debt. The operations of MedUnite are reflected with those of the Company for the three months ended March 31, 2003.

The results of operations for the three months ended March 31, 2003 are not necessarily indicative of the results to be expected for the full year. The unaudited consolidated financial statements included herein should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2002 as filed with the SEC on April 15, 2003.

- (b) REVENUE RECOGNITION - Electronic transaction processing fee revenue is recorded in the period the service is rendered. Certain transaction fee revenue is subject to revenue sharing pursuant to agreements with resellers, vendors or gateway partners and are recorded as gross revenues. Revenue from sales of inventory and manufactured goods is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collectibility is probable. Revenue from certain up-front fees is amortized ratably over the expected life of the customer. Revenue from hardware leases, software rentals and maintenance fees is recognized ratably over the applicable period.
- (c) NET LOSS PER SHARE - Basic net loss per share is computed by dividing net loss applicable to common shareholders by the weighted average shares of common stock outstanding during the period. Diluted loss per share reflects the potential dilution from the exercise or conversion of securities into common stock; however, stock options and warrants totaling 1,753,153 shares and 960,378 shares at March 31, 2003 and 2002, respectively, as well as common shares issuable on conversion of Series C preferred stock (13,333 and 20,000 shares, if converted on March 31, 2003 and 2002, respectively), were excluded from the calculation of diluted loss per share because their effects would have been antidilutive.

### PROXYMED, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED), CONTINUED

In December 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure". SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation", to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee

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compensation and the effect of the method used on reported results. The disclosure provisions of SFAS No. 148 are effective for fiscal years ending after December 15, 2002.

ProxyMed continues to apply Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations in accounting for its stock option plans and has not adopted the recognition provisions of SFAS No. 123, as amended by SFAS No. 148. The Company measures compensation expense related to the grant of stock options and stock-based awards to employees (including independent directors) whereby compensation expense, if any, is generally based on the difference between the exercise price of an option, or the amount paid for an award, and the market price or fair value of the underlying common stock at the date of the award or at the measurement date for variable awards. Stock-based compensation arrangements involving non-employees are accounted for based on the fair value of the option or award pursuant to SFAS No. 123.

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### PROXYMED, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED), CONTINUED

Under SFAS No. 123, compensation cost for the Company's stock-based compensation plans would be determined based on the fair value at the grant dates for awards under those plans. Had the Company adopted SFAS No. 123 in accounting for its stock option plans, the Company's consolidated net loss and net loss per share for the quarters ended March 31, 2003 and March 31, 2002 would have been adjusted to the pro forma amounts indicated as follows:

	Three Months Ended March 31,	
	2003	2002
Net loss applicable to common shareholders, as reported	\$ (2,452,000)	\$ (563,000)
Total stock-based employee pro forma compensation expense determined under fair value based method for all awards	(150,000)	(312,000)
Pro forma net loss applicable to common shareholders	\$ (2,602,000)	\$ (875,000)
Basic and diluted net loss per common share:		
As reported	\$ (0.36)	\$ (0.11)
Pro forma	\$ (0.38)	\$ (0.17)

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- (d) NEW ACCOUNTING PRONOUNCEMENTS - In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". SFAS No. 149 amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities". SFAS No. 149 is effective for contracts entered into or modified after June 30, 2003, except for certain provision that relate to SFAS No. 133 implementation issues that have been effective for fiscal quarters that began prior to June 15, 2003 and for hedging relationships designated after June 30, 2003. Since currently the Company does not have derivative instruments, the Company does not believe that the implementation SFAS No. 149 will have a material effect on the Company's consolidated financial statements and related disclosures.

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PROXYMED, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED), CONTINUED

(2) INVENTORY

Inventory consists of the following at March 31, 2003:

Materials, supplies and component parts	\$2,014,000
Work in process	211,000
Finished goods	687,000
	-----
	\$2,912,000
	=====

(3) GOODWILL AND OTHER INTANGIBLE ASSETS

- (a) GOODWILL - The changes in the carrying amounts of goodwill for the three months ended March 31, 2003 by operating segment are as follows:

	Electronic healthcare transaction processing -----	Laboratory communication solutions -----	Tot -----
Balance as of December 31, 2002	\$30,695,000	\$2,102,000	\$32,797,000
Purchase price adjustments	147,000	--	147,000
	-----	-----	-----
Balance as of March 31, 2003	\$30,842,000	\$2,102,000	\$32,944,000
	=====	=====	=====



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- (b) OTHER INTANGIBLE ASSETS - The carrying amounts of other intangible assets as of March 31, 2003 and December 31, 2002, by category, are as follows:

	March 31, 2003			Dece
	Carrying Amount	Accumulated Amortization	Net	Carrying Amount
Capitalized software	\$ 759,000	\$ (82,000)	\$ 677,000	\$ 527,000
Purchased technology	9,172,000	(1,705,000)	7,467,000	9,127,000
Customer relationships	10,251,000	(595,000)	9,656,000	10,251,000
	-----	-----	-----	-----
	\$ 20,182,000	\$ (2,382,000)	\$17,800,000	\$ 19,905,000
	=====	=====	=====	=====

Amortization expense of other intangible assets was \$697,000 and \$149,000 for the three months ended March 31, 2003 and 2002, respectively.

As of March 31, 2003, estimated future amortization expense of other intangible assets is as follows: \$2,615,000 for the remaining quarters of 2003, \$2,693,000 in 2004, \$2,572,000 in 2005, \$2,425,000 in 2006, \$2,274,000 in 2007, and \$1,790,000 in 2008.

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PROXYMED, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED), CONTINUED

(4) DEBT OBLIGATIONS

In February 2003, the Company financed \$422,000 and \$306,000 for certain liability insurance policies over 7 months at 4.76% and 24 months at 5.25%, respectively. The note for \$422,000 is unsecured while the note for \$306,000 is collateralized by a letter of credit in the amount of \$325,000 (supported with restricted cash) at March 31, 2003.

In March 2003, the Company restructured \$3,368,000 in accounts payable and accrued expenses acquired from MedUnite and outstanding at December 31, 2002 to one vendor by paying \$750,000 in cash and financing the balance of \$2,618,000 with an unsecured note payable over 36 months at 8% commencing March 2003.

In April 2003, the Company financed a net total of \$1,990,000 (\$2,797,000 in accounts payable and accrued expenses offset by \$807,000 in accounts receivable) existing at December 31, 2002 from MedUnite to a former

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owner of MedUnite by issuing an unsecured note payable over 24 months at 6%.

### (5) EQUITY TRANSACTIONS

- (a) SERIES C PREFERRED CONVERSION OFFER - On December 13, 2001, the Company offered to convert its then outstanding Series C Preferred into shares of common stock at a reduced conversion price (the "Conversion Offer"). For a period of sixty days ending February 11, 2002, the holders of the Series C Preferred shares were able convert such shares at a reduced conversion price of \$13.05 per share instead of the original conversion price of \$15.00. At the conclusion of the Conversion Offer on February 11, 2002, holders of 98.5% of the outstanding Series C Preferred had converted their shares into a total of 1,538,636 common shares. A deemed dividend charge of \$612,000 was recorded in the first quarter of 2002 for conversions consummated after the 2001 year end.
- (b) STOCK OPTIONS - During the three months ended March 31, 2003, the Company granted a total of 50,000 stock options at exercise prices between \$7.50 and \$10.01 per share to employees. Such options are for a ten-year term and vest equally over the following three years.

In April 2003, the six outside directors of ProxyMed were each granted 10,000 stock options at an exercise price of \$7.28 per share. Such options are for a ten-year term and vest equally over the following three years.

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### PROXYMED, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED), CONTINUED

### (6) SEGMENT INFORMATION

ProxyMed operates in two reportable segments that are separately managed: Electronic healthcare transaction processing and Laboratory communication solutions. Electronic healthcare transaction processing includes transaction and value-added services principally between physicians and insurance companies (Payer Services) and physicians and pharmacies (Prescription Services); and Laboratory communication solutions includes the sale, lease and service of communication devices principally to laboratories and the contract manufacturing of printed circuit boards (Laboratory Services). Intersegment sales are not material, and there were no foreign sales for any periods presented.

	Three Months Ended March 31,	
	2003	2002
Net revenues:		
Electronic healthcare transaction processing	\$ 11,291,000	\$ 5,278,000
Laboratory communication solutions	6,139,000	6,225,000
	\$ 17,430,000	\$ 11,503,000

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	=====	=====
Operating income (loss):		
Electronic healthcare transaction processing	\$ (1,941,000)	\$ 152,000
Laboratory communication solutions	587,000	593,000
Corporate and consolidating	(924,000)	(683,000)
	-----	-----
	\$ (2,278,000)	\$ 62,000
	=====	=====
	March 31,	
	-----	-----
	2003	2002
	-----	-----
Total assets:		
Electronic healthcare transaction processing	\$ 60,400,000	\$ 14,211,000
Laboratory communication solutions	12,424,000	8,648,000
Corporate and consolidating	11,643,000	6,161,000
	-----	-----
	\$ 84,467,000	\$ 29,020,000
	=====	=====

(7) INCOME TAXES

As of March 31, 2003, the Company had a net deferred tax asset of approximately \$66.0 million, which was fully offset by a valuation allowance. Realization of the net deferred tax asset is dependent upon the Company generating sufficient taxable income prior to the expiration of the federal net operating loss carryforwards. The Company will adjust this valuation reserve, if during future periods, management believes the Company will generate sufficient taxable income to realize the net deferred tax asset.

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PROXYMED, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED), CONTINUED

(8) LEASES

In April 2003, the Company terminated MedUnite's facility lease in San Diego, California effective July 1, 2003 in consideration for a \$750,000 letter of credit held by the landlord (supported with restricted cash), furniture at the facility with a value of approximately \$153,000, and other costs of \$69,000. As a replacement for this facility, the Company subleased office space in the same geographic area at a monthly rent of \$6,000 per month through September 2004.

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### RESULTS OF OPERATIONS

#### GENERAL

ProxyMed is an electronic healthcare transaction processing services company providing connectivity services and related value-added products to physician offices, payers, medical laboratories, pharmacies, and other healthcare providers. Our electronic transaction processing services support a broad range of both financial and clinical transactions. To facilitate these services, we operate ProxyNet, our secure, proprietary national electronic information network, which provides physicians and other healthcare providers with direct connectivity to one of the industry's largest group of payers, the largest group of clinical laboratories, and the largest group of chain and independent pharmacies. Our products and services are currently provided from our main operating facilities located in Fort Lauderdale, Florida; New Albany, Indiana; Santa Ana, California; Norcross, Georgia; and Sioux Falls, South Dakota. We also operate our clinical network and portions of our financial and real-time production computer networks from a secure co-location site in Atlanta, Georgia.

We remain committed to our strategy, which is focused on leveraging our leading position as an independent back-end connectivity provider to small physician offices. Through strategic relationships and partnerships with front-end solutions providers, our goal is to drive more healthcare transactions through PROXYNET while remaining neutral in the battle for the physician's desktop. Additionally, since we have an existing customer base of physicians and other healthcare providers, we expect that there will be opportunities to increase revenues by cross-selling our existing products and services to these current customers, as well as revenue opportunities from the development of new services from our development efforts, including Internet-based transaction services, and from opportunities afforded by HIPAA as it relates to privacy, security and education. We remain committed to developing additional capabilities and value-added products and services, and to expanding our back-end connectivity network.

On December 31, 2002, we acquired all of the outstanding stock of MedUnite, Inc. ("MedUnite") for \$10,000,000 in cash and aggregate of \$13,400,000 principal amount of 4% convertible promissory notes. In addition, we incurred \$8,321,000 in transaction and exit related costs. Interest on the convertible notes is payable in cash on a quarterly basis. The convertible promissory notes are payable in full on December 31, 2008 and are convertible into an aggregate of 731,322 shares of our common stock if the founders of MedUnite achieve certain revenue-based triggers over the next three and one-half year period. The shares of our common stock issuable upon conversion of the convertible notes will be registered by us promptly after a stockholder achieves a conversion trigger event. If and when these notes become convertible, we will record a beneficial conversion charge in our operations to the extent that the fair market value of the common stock is in excess of the conversion price. The operations of MedUnite are reflected with those of the Company for the three months ended March 31, 2003.

### RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2003 COMPARED TO THREE MONTHS ENDED MARCH 31, 2002.

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NET REVENUES. Consolidated net revenues for the three months ended March 31, 2003 increased by \$5,927,000, or 52%, to \$17,430,000 from consolidated net revenues of \$11,503,000 for the three months ended March 31, 2002. Net revenues classified by our reportable segments are as follows:

	Three Months Ended March 31,	
	2003	2002
Electronic healthcare transaction processing	\$11,291,000	\$ 5,278,000
Laboratory communication solutions	6,139,000	6,225,000
	-----	-----
	\$17,430,000	\$11,503,000
	=====	=====

Net revenues in our Electronic healthcare transaction processing segment increased by 114% over the 2002 period. This increase is primarily due to the acquisition of MedUnite which contributed \$4,628,000, or 41%, of the segment revenues. Excluding MedUnite, revenue growth from our existing transaction business increased by 26% between periods.

Total healthcare transactions processed during the three months ended March 31, 2003 were 56,479,000 (including 21,862,000 transactions from MedUnite) equating to an annualized run rate of over 225 million transactions processed. Excluding MedUnite, transaction growth between the periods was 31%. A summary of the number of transactions we processed for the periods presented is as follows:

	Three Months Ended March 31,	
	2003	2002
Core transactions	49,601,000	20,220,000
Encounters	6,878,000	6,198,000
	-----	-----
Total transactions	56,479,000	26,418,000
	=====	=====

"Core" transactions represent all transactions except for encounters. "Encounters" are an administrative reporting transaction for payers but do not generate revenue for the provider who must submit them. Accordingly, rather than submitting on a routine basis, most providers choose to periodically "catch up" on their submissions, creating monthly and quarterly swings in both the number of encounters we process and what percentage of our transaction mix they represent. Since encounters are at a significantly lower price point than claims, these swings make it difficult to easily analyze our quarter-over-quarter growth in our core business. In addition, we do not expect our encounter volume to grow on an annual basis, as payers are not expanding the capitated service model that is the foundation of encounters. Therefore, we believe that breaking out encounters shows more clearly our growth in core

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transactions, which are the growth engine for our Electronic healthcare transaction services segment.

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For the 2003 period, approximately 65% of our revenues came from our Electronic healthcare transaction processing segment compared to 46% from this segment for the 2002 period. For the remainder of 2003 and beyond, it is anticipated that our greatest growth will come from this segment.

Laboratory communication solutions segment net revenues decreased by 1% from the 2002 period. While our revenues in this segment started the year slowly as we had expected, most of our revenues in this segment comes from the sale of fixed assets to our lab and contract manufacturing customers. We believe that overall spending for fixed assets is down across the economy and will continue to be soft going into the summer. In addition, we expected to start the year slowly due to the effect of the 2002 merger and acquisition activity among our top lab customers. Typically, our business with labs decreases for a period of time after the acquisition, and then rebounds. We anticipate that a strengthening economy, a resumption of normal ordering from the merged labs and increased penetration into the hospital outreach market will help to improve revenue for our Laboratory communications solutions segment over the balance of the year.

**COST OF SALES.** Consolidated cost of sales decreased as a percentage of net revenues to 43% for the three months ended March 31, 2003 from 47% for the three months ended March 31, 2002. Cost of sales classified by our reportable segments is as follows:

	Three Months Ended March 31,	
	2003	2002
Electronic healthcare transaction processing	\$4,266,000	\$2,132,000
Laboratory communication solutions	3,227,000	3,247,000
	\$7,493,000	\$5,379,000

Cost of sales in our Electronic healthcare transaction processing segment consists of transaction fees, services and license fees, third-party electronic transaction processing costs, certain telecommunication and co-location center costs, revenue sharing arrangements with our business partners, third-party database licenses, and certain travel expenses. Cost of sales as a percentage of revenues decreased to 38% in the 2003 period compared to 40% in the same period last year primarily due to a change in the mix of transaction types from higher cost patient statements to lower costs claims.

Cost of sales in the Laboratory communication solutions segment includes hardware, third-party software, and consumable materials. Cost of sales

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as a percentage of revenues remained constant in the 2003 period compared to the same period last year.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES. Consolidated SG&A increased for the three months ended March 31, 2003 by \$5,267,000, or 96%, to \$10,760,000 from consolidated SG&A of \$5,493,000 for the three months ended March 31, 2002. Consolidated SG&A expenses as a percentage of consolidated revenues increased to 62% for the 2003 period compared to 48% in the same period last year. SG&A expenses classified by our reportable segments are as follows:

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	Three Months Ended March 31,	
	2003	2002
	-----	-----
Electronic healthcare transaction processing	\$ 7,787,000	\$2,630,000
Laboratory communication solutions	2,093,000	2,230,000
Corporate	880,000	633,000
	-----	-----
	\$10,760,000	\$5,493,000
	=====	=====

Electronic healthcare transaction processing segment SG&A expenses for the three months March 31, 2003 increased 196% over the same period last year primarily due to the incremental expenses incurred in the operations of MedUnite. Excluding MedUnite, SG&A expenses in this segment increased by 23% due to costs related to our HIPAA compliance efforts, implementation staffing and sales/marketing programs implemented since the first quarter of last year.

While we expected to incur significant SG&A costs related to the MedUnite operations in the first quarter of 2003, we also expected to reduce them at a higher rate than we achieved during the early part of the quarter. In addition, we incurred some unbudgeted expenses of about \$100,000 for additional transaction-related accounting and legal fees. Despite these challenges, we exited the quarter on an expense run rate in line with our initial expectations. With continued expense reduction efforts anticipated in the second quarter, we expect to achieve positive cash flow in our MedUnite operations before the fourth quarter of 2003.

Laboratory communication solutions segment SG&A expenses for the three month ended March 31, 2003 decreased by 6% over the same period last year primarily due to cost cutting measures implemented in the fourth quarter of last year. As a result, segment SG&A expenses as a percentage of segment net revenues decreased to 34% for the 2003 period compared to 36% for the same period last year.

Corporate SG&A expenses increased 39% for the three months ended 2003 compared to the same period last year primarily due to increased insurance premiums, professional fees and personnel costs.

DEPRECIATION AND AMORTIZATION. Consolidated depreciation and

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amortization increased by \$761,000 to \$1,330,000 for the three months ended 2003 from \$569,000 for the same period last year. This increase was primarily due to \$465,000 for the amortization of intangible assets acquired in the MedUnite acquisition. Depreciation and amortization classified by our reportable segments is as follows:

	Three Months Ended March 31,	
	2003	2002
Electronic healthcare transaction processing	\$1,056,000	\$364,000
Laboratory communication solutions	230,000	155,000
Corporate	44,000	50,000
	\$1,330,000	\$569,000

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LOSS ON DISPOSAL OF ASSETS. As a result of the consolidation of the ProxyMed and MedUnite offices in Atlanta during the quarter ended March 31, 2003, we recorded \$125,000 in losses primarily related to the disposition of certain assets owned and leased that were acquired in our acquisition of MDP Corporation in 2001. The consolidation of our Atlanta offices is expected to save us over \$300,000 on an annual basis going forward in rents and other occupancy costs.

OPERATING INCOME (LOSS). As a result of the foregoing, consolidated operating loss for the three months ended March 31, 2003 was \$2,278,000 compared to operating income of \$62,000 for the same period last year. Operating income (loss) classified by our reportable segments is as follows:

	Three Months Ended March 31,	
	2003	2002
Electronic healthcare transaction processing	\$(1,941,000)	\$ 152,000
Laboratory communication solutions	587,000	593,000
Corporate	(924,000)	(683,000)
	\$(2,278,000)	\$ 62,000



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INTEREST, NET. Consolidated net interest expense for the three months ended March 31, 2003 was \$174,000 compared to \$13,000 for the same period last year. This increase in expense is primarily due to interest related to our convertible debt issued to the former owners of MedUnite and the financing of certain liabilities of MedUnite during the 2003 period.

NET INCOME (LOSS). As a result of the foregoing, consolidated net loss for the three months ended March 31, 2003 was \$2,452,000 compared to net income of \$49,000 for the same period last year.

DEEMED DIVIDENDS. We incurred deemed dividends of \$612,000 during the three months ended March 31, 2002 as a result of non-cash accounting charges for the conversion of 31,650 preferred shares into 242,510 shares of common stock by our Series C preferred shareholders in 2002 pursuant to our offer to convert their shares commencing in December 2001.

NET LOSS APPLICABLE TO COMMON SHAREHOLDERS. As a result of the foregoing, we reported net loss applicable to common shareholders of \$2,452,000 for the three months ended March 31, 2003 compared to \$563,000 for the for the three months ended March 31, 2002.

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### LIQUIDITY AND CAPITAL RESOURCES

In the three months ended March 31, 2003, cash used by operating activities totaled \$494,000. During this period, we paid \$3,860,000 in acquisition related costs for MedUnite; paid \$1,186,000 for fixed assets and capitalized software; paid \$310,000 against our notes payable and certain long term debt; and transferred \$325,000 as support for a letter of credit used to collateralize the financing of a certain liability insurance policy. These activities were principally financed through available cash resources. After these activities, we had cash and cash equivalents totaling \$10,347,000 as of March 31, 2003. These available funds will be used for operations, strategic acquisitions, the further development of our products and services, and other general corporate purposes. We continue to evaluate other acquisition opportunities and strategic alternatives that may add synergies to our product offerings and business strategy.

At the current time, we do not have any material commitments for capital expenditures except for approximately \$333,000 that is committed evenly over the next two years related to the licensing of software for use in our internal systems. In February 2003, we paid the second \$167,000 towards this commitment.

Excluding MedUnite, we expect to incur \$600,000 for various development projects originally scheduled to be undertaken by us in 2003. Additionally, we expect to incur additional development and related hardware/software costs of up to approximately \$2.0 million in the future related to the completion of enhancements for the real-time network platform acquired from MedUnite.

During the 2002 year, we consistently improved our operating results as a result of both internal and external growth, successful cross-selling of our transaction services, and our ability to monitor expenses. With our additional equity financing at the end of the first quarter of 2002, we were able to consummate four acquisitions during the year, culminating with our acquisition of MedUnite at the end of the year. Unfortunately, MedUnite had incurred

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significant losses since its inception and was utilizing cash significantly in excess of amounts it was generating primarily due to technical and research and development activities related to their various processing platforms. As a result, at the time we acquired MedUnite, there were substantial liabilities and obligations as well as future commitments (both recorded and unrecorded at December 31, 2002) associated with the business in addition to the transaction and exit costs associated with the acquisition.

In an effort to immediately curtail and reduce the expenditure levels, MedUnite's senior management team was terminated along with approximately 20% of the general workforce in an effort to control these costs as many duplicative positions were eliminated. While we did not achieve the expected reductions in MedUnite's costs early in the first quarter, we did exit the quarter on an expense run rate in line with our expectations. Furthermore, in February 2003, we moved our prior Atlanta facility into MedUnite's Norcross facility and in April 2003 terminated our San Diego facility lease effective July 1, 2003 in return for a \$750,000 letter of credit held by the current landlord and furniture at that facility.

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Additionally, other contractual obligations have been or are in the process of being cancelled or renegotiated with the respective vendors. We have attempted to enter into financing agreements with certain major vendors as a means to settling liabilities that existed at December 31, 2002, and to date have financed \$3,368,000 of liabilities to one vendor; \$1,990,000 in net liabilities to a former owner of MedUnite; and \$382,000 for a required insurance policy as part of the acquisition. Between these financing agreements, existing capital leases, and the convertible notes issued in the acquisition, we will incur significant interest expense charges in 2003. With continued efforts during second quarter of 2003, we now anticipate that we will be able to drive positive cash flow in this business before the fourth quarter of 2003.

We believe that we have sufficient cash and cash equivalents on hand to fund our future operational capital requirements and expenditures, and a sufficient level of capital in order to fund specific research and development projects or to pursue smaller additional strategic acquisitions. However, if we need additional capital funding in the future to further our strategic plans, there can be no assurance that any additional funding will be available to us, or if available, that it will be available on acceptable terms. If we are successful in obtaining additional financing, the terms of the financing may have the effect of significantly diluting or adversely affecting the holdings or the rights of the holders of our common stock. We believe that if we are not successful in obtaining additional financing for further product development or strategic acquisitions, such inability may adversely impact our ability to successfully execute our business plan and may put us at a competitive disadvantage.

### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of our financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the

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results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions but we believe that any variation in results would not have a material effect on our financial condition. On an ongoing basis, we evaluate our estimates.

We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements. For a detailed discussion on the application of these and other accounting policies, see Note 1 in the Notes to Consolidated Financial Statements beginning on Page F-7 in our Form 10-K for the year ended December 31, 2002.

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REVENUE RECOGNITION - Electronic transaction processing fee revenue is recorded in the period the service is rendered. Certain transaction fee revenue may be subject to revenue sharing per agreements with resellers, vendors or gateway partners and are recorded as gross revenues. Revenue from sales of inventory and manufactured goods is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collectibility is probable. Revenue from certain up-front fees is amortized ratably over the expected life of the customer or contract. Revenue from hardware leases, network access and maintenance fees is recognized ratably over the applicable period.

GOODWILL - We adopted the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets" effective January 1, 2002. Under SFAS No. 142, goodwill is reviewed at least annually for impairment. This adoption resulted in the reduction of approximately \$808,000 of amortization relating to its existing goodwill each quarter, which would have otherwise been recorded through the first quarter of 2004. SFAS No. 142 requires that goodwill be tested for impairment at the reporting unit level at adoption and at least annually thereafter, utilizing a "fair value" methodology versus an undiscounted cash flow method required under previous accounting rules. In accordance with its adoption of FAS No. 142, we completed its initial impairment test of goodwill during the first quarter of 2002 and our annual test at December 31, 2002 utilizing various valuation techniques including a market value analysis. No impairment charges were recorded as a result of these tests.

CAPITALIZED SOFTWARE DEVELOPMENT AND RESEARCH AND DEVELOPMENT - Costs incurred internally and fees paid to outside contractors and consultants during the application development stage of our internally used software products are capitalized. Costs of upgrades and major enhancements that result in additional functionality are also capitalized. Costs incurred for maintenance and minor upgrades are expensed as incurred. All other costs are expensed as incurred as research and development expenses (which are included in selling, general and administrative expenses). Application development stage costs generally include software configuration, coding, installation to hardware and testing. Once the project is completed, capitalized costs are amortized over their remaining estimated economic life. Our judgment is used in determining whether costs meet the criteria for immediate expense or capitalization. We periodically review projected cash flows and other criteria in assessing the impairment of any internal-use capitalized software and take impairment charges as needed.

EQUITY TRANSACTIONS - Over the past two years, we have engaged in various

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equity transactions. These transactions were first aimed at providing capital to continue to operate and grow our business and then became a critical step aimed at simplifying our capital structure. These transactions are complex and require the application of various accounting rules and standards that have resulted in significant cash and non-cash charges reflected primarily as deemed dividend charges included our net loss applicable to common shareholders.

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**BAD DEBT ESTIMATES** - We rely on estimates to determine the bad debt expense and the adequacy of the reserve for doubtful accounts receivable. These estimates are based on our historical experience and the industry in which we operate. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

### NEW ACCOUNTING PRONOUNCEMENTS

In April 2003, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." SFAS No. 149 amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities". SFAS No. 149 is effective for contracts entered into or modified after June 30, 2003, except for certain provision that relate to SFAS No. 133 implementation issues that have been effective for fiscal quarters that began prior to June 15, 2003 and for hedging relationships designated after June 30, 2003. Since currently we currently not have derivative instruments, we do not believe that the implementation SFAS No. 149 will have a material effect our consolidated financial statements and related disclosures.

### CAUTIONARY STATEMENT PURSUANT TO SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This document contains forward-looking statements that reflect our current assumptions and expectations regarding future events. While these statements reflect our current judgment, they are subject to risks and uncertainties. Actual results may differ significantly from projected results due to a number of factors, including, but not limited to, the soundness of our business strategies relative to the perceived market opportunities; our ability to identify suitable acquisition candidates; our successful integration of MedUnite and any other future acquisitions; our ability to successfully develop, market, sell, cross-sell, install and upgrade our clinical and financial transaction services and applications to new and current physicians, payers, medical laboratories and pharmacies; our ability to compete effectively on price and support services; our assessment of the healthcare industry's need, desire and ability to become technology efficient; and our ability and that of our business associates to comply with various government rules regarding healthcare information and patient privacy. These and other risk factors are more fully discussed the risk factors starting on page 15 in our Form 10-K for the year ended December 31, 2002, which we strongly urge you to read. We expressly disclaim any intent or obligation to update any forward-looking statements. When used in this document, the words "believes", "estimated", "expects", "anticipates", "may" and similar expressions are intended to identify

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forward-looking statements.

### AVAILABLE INFORMATION

Our Internet address is [www.proxymed.com](http://www.proxymed.com). We make available free of charge on or through our Internet website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after such material was electronically filed with, or furnished to, the SEC.

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

We own no derivative financial instruments or derivative commodity instruments. We derive no revenues from international operations and do not believe that we are exposed to material risks related to foreign currency exchange rates.

### ITEM 4. CONTROLS AND PROCEDURES

Within ninety (90) days prior to the filing of this report, the Company evaluated the effectiveness and operation of the Company's disclosure controls and procedures (as defined in Exchange act Rule 13a-14(c)), under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer. Based upon such evaluation, the Chief Executive Officer and Chief Financial Officer concluded that there was no reasonably apparent deficiency in the Company's disclosure controls and procedures such that the controls and procedures should not be expected to operate effectively. The Company is not aware of any significant changes in the Company's internal controls or in other factors that could significantly affect those controls subsequent to the date of the most recent evaluation of such controls by the Company.

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## PART II - OTHER INFORMATION

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

#### (a) Exhibits:

- 99.1 - Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 99.2 - Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

#### (b) Reports on Form 8-K:

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- January 9, 2003 - Report on acquisition of all of the capital stock of MedUnite, Inc. on December 31, 2002.
- February 25, 2003 - Report on fourth quarter and year ended December 31, 2002 teleconference call held on February 20, 2003, including transcript thereon and press release dated February 20, 2003, pursuant to Regulation FD.
- March 17, 2003 - Amendment to Report on Form 8-K filed on January 9, 2003 to provide the financial information required in connection with the acquisition of MedUnite, Inc. on December 31, 2002.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

PROXYMED, INC.

Date: MAY 15, 2003  
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By: /s/ MICHAEL K. HOOVER  
-----  
Michael K. Hoover  
Chief Executive Officer

Date: MAY 15, 2003  
-----

By: /s/ JUDSON E. SCHMID  
-----  
Judson E. Schmid  
Chief Financial Officer

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CERTIFICATIONS

I, Michael K. Hoover, Chief Executive Officer of ProxyMed, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of ProxyMed, Inc;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in

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this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b. evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing of this quarterly report (the "Evaluation Date"); and
  - c. presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to the significant deficiencies and material weaknesses.

Date: MAY 15, 2003

/s/ MICHAEL K. HOOVER

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Michael K. Hoover  
Chief Executive Officer

I, Judson E. Schmid, Chief Financial Officer of ProxyMed, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of ProxyMed, Inc;
2. Based on my knowledge, this quarterly report does not contain any

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untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b. evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing of this quarterly report (the "Evaluation Date"); and
  - c. presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - d. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - e. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to the significant deficiencies and material weaknesses.

Date: MAY 15, 2003

/s/ JUDSON E. SCHMID

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Judson E. Schmid  
Chief Financial Officer



