NOVAMED EYECARE INC
Form 10-Q
November 14, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED: SEPTEMBER 30, 2002

COMMISSION FILE NUMBER: 0-26625

NOVAMED EYECARE, INC.
(Exact name of registrant as specified in its charter)

Delaware	36-4116193
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

980 North Michigan Avenue, Suite 1620, Chicago, Illinois 60611
(Address of principal executive offices)

Registrant's telephone, including area code: (312) 664-4100

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 and Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes | X | No | |

As of November 13, 2002, there were outstanding 23,156,867 shares of the registrant's common stock, par value $.01 per share.

NOVAMED EYECARE, INC.
FORM 10-Q FOR QUARTERLY PERIOD ENDED SEPTEMBER 30, 2002
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Part I

Item 1.

NOVAMED EYECARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except share data)

ASSETS	September 30, 2002
Current assets:	(unaudited)
Cash and cash equivalents	$ 1,965
Accounts receivable, net	7,331
Notes and amounts due from affiliated providers	1,725
Inventory	1,385
Current tax assets, net	4,111
Other current assets	1,238
Current assets of discontinued operations	6,462
Total current assets	24,217
Property and equipment, net	7,022
Intangible assets, net	26,741
Noncurrent deferred tax assets, net	10,774
Other assets, net	1,812
Noncurrent assets of discontinued operations, net	5,876
Total assets	$ 76,442
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 3,870
Accrued expenses	2,702
Restructuring reserves	2,429
Current maturities of long-term debt	122
Current liabilities of discontinued operations	7,898
Total current liabilities	17,021

Long-term debt, net of current maturities	7,871
Minority interest	1,101
Commitments and contingencies	
Stockholders' equity:	
Series E Junior Participating Preferred Stock, $0.01 par value, 1,912,000 shares authorized, none outstanding at September 30, 2002 and December 31, 2001, respectively	--
Common stock, $0.01 par value, 81,761,465 shares authorized, 23,156,867 and 24,835,108 shares issued and outstanding at September 30, 2002 and December 31, 2001, respectively	249
Additional paid-in-capital	77,716
Retained earnings (deficit)	(26,287)
Treasury stock, at cost, 1,748,640 shares at September 30, 2002	(1,229)
Total stockholders' equity	50,449
Total liabilities and stockholders' equity	$ 76,442

The notes to the interim condensed consolidated financial statements are an integral part of these statements.

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NOVAMED EYECARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Amounts in thousands, except per share data; unaudited)

	Three months ended September 30,		Nine months Septembe
	2002	2001	2002
Net revenue:			
Surgical facilities	$ 8,277	$ 8,018	$24,473
Product sales and other	9,027	7,553	26,950
Total net revenue	17,304	15,571	51,423
Operating expenses:			
Salaries, wages and benefits	3,589	3,908	10,406
Cost of sales and medical supplies	9,637	8,058	28,329
Selling, general and administrative	2,283	2,448	6,713
Restructuring and special charges	--	10,912	--
Other charges	--	3,719	--
Depreciation and amortization	626	1,180	1,896
Total operating expenses	16,135	30,225	47,344
Income (loss) from continuing operations	1,169	(14,654)	4,079

Other (income) expense, net	(444)	226	(756)	
Minority interest	222	--	350	
Income (loss) from continuing operations before income taxes	1,391	(14,880)	4,485	
Income tax provision (benefit)	556	(5,998)	1,794	
Net income (loss) from continuing operations before cumulative effect of change in accounting principle	835	(8,882)	2,691	
Net income from discontinued operations	--	384	181	
Net gain (loss) on disposal of discontinued operations	5	(27,213)	(23)	
Cumulative effect of change in accounting principle, net of tax	--	--	(1,803)	
Net income (loss)	$ 840	$(35,711)	$ 1,046	$
Basic earnings per common share:				
Income (loss) from continuing operations before cumulative effect of change in accounting principle	$ 0.04	$ (0.36)	$ 0.11	$
Income (loss) from discontinued operations	--	(1.08)	--	
Cumulative effect of change in accounting principle	--	--	(0.07)	
Net income (loss)	$ 0.04	$ (1.44)	$ 0.04	$
Diluted earnings per common share:				
Income (loss) from continuing operations before cumulative effect of change in accounting principle	$ 0.04	$ (0.36)	$ 0.11	$
Income (loss) from discontinued operations	--	(1.08)	--	
Cumulative effect of change in accounting principle	--	--	(0.07)	
Net income (loss)	$ 0.04	$ (1.44)	$ 0.04	$
Weighted average common shares outstanding	23,129	24,804	24,170	
Dilutive effect of employee stock options	144	--	65	
Diluted weighted average common shares outstanding	23,273	24,804	24,235	

The notes to the interim condensed consolidated financial statements are an integral part of these statements

NOVAMED EYECARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands; unaudited)

	Nine months ended Septemb	
	2002	2
Cash flows from operating activities:		
Net income (loss)	$ 1,046	$(3
Adjustments to reconcile net income (loss) to net cash provided by continuing operations, net of effects of purchase transactions--		
Net (income) loss of discontinued operations	(158)	2

Restructuring and other charges	--	1
Cumulative effect of change in accounting principle, net	1,803	
Gain on sale of minority interests	(537)	
Depreciation and amortization	1,896	
Minority interest	350	
Distribution to minority partners	(45)	
Deferred taxes	1,900	(
Changes in operating assets and liabilities--		
Accounts receivable	292	
Inventory	(152)	
Other current assets	1,305	
Accounts payable and accrued expenses	1,019	(
Other	(47)	
Net cash provided by operating activities	8,672	
Cash flows from investing activities:		
Purchases of property and equipment	(1,051)	(
Acquisitions of ASCs	(6,151)	
Proceeds from sale of minority interest	937	
Other	(222)	
Net cash used by investing activities	(6,487)	(
Cash flows from financing activities:		
Borrowings under revolving line of credit	24,590	3
Payments under revolving line of credit	(37,420)	(3
Other	(379)	
Net cash used by financing activities	(13,209)	(
Cash flows from discontinued operations:		
Operating activities	3,508	
Proceeds from divestitures	8,975	
Investing activities	(433)	(
Financing activities	(28)	
Net cash provided by discontinued operation	12,022	
Net increase in cash and cash equivalents	998	
Cash and cash equivalents, beginning of period	967	
Cash and cash equivalents, end of period	$ 1,965	$
Noncash investing activity:		
Fair value of stock received in divestiture transactions	$ 1,229	$

The notes to the interim condensed consolidated financial statements are an integral part of these statements.

NOVAMED EYECARE, INC. AND SUBSIDIARIES
NOTES TO THE INTERIM
CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2002
(Dollars in thousands, except per share data; unaudited)

1. BASIS OF PRESENTATION

The information contained in the interim consolidated financial statements and notes is condensed from that which would appear in the annual consolidated financial statements. Accordingly, the interim condensed consolidated financial statements included herein should be read in conjunction with the consolidated financial statements as of and for the year ended December 31, 2001, filed by NovaMed Eyecare, Inc. with the Securities and Exchange Commission on Form 10-K. The unaudited interim condensed consolidated financial statements as of September 30, 2002 and for the three and nine months ended September 30, 2002 and 2001, include all normal recurring adjustments which management considers necessary for a fair presentation. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the entire fiscal year.

Prior year amounts have been reclassified to conform to current year presentation as further discussed in Note 3 below.

2. GOODWILL AND OTHER INTANGIBLE ASSETS-- CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE

Effective January 1, 2002 we adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (FAS 142). Under the new rules, we are no longer required to amortize goodwill and other intangible assets with indefinite lives. We are required to periodically evaluate the carrying value of these assets for impairment. Impairment losses for goodwill and indefinite-lived intangible assets that arise due to the initial application of FAS 142 are required to be reported as a change in accounting principle.

We performed an evaluation of all our existing goodwill as of January 1, 2002 and determined that the goodwill associated with one of our ancillary businesses was impaired. This business sells marketing products to the laser vision correction market, which has lately shown a downturn in demand. This downturn has negatively impacted the prospects for this business. We are in the process of developing new products at this business to diversify its revenue base. The business was evaluated using an expected cash flow valuation method that indicated the carrying value of the business had been impaired by approximately $2.9 million. We recorded a net of tax charge of $1.8 million to write-off a portion of acquired goodwill in our first quarter financial statements as a change in accounting principle. All intangible assets are reported in our Corporate segment.

The intangible assets that are continuing to be amortized over 25 years are related to the Management Services Agreements at our remaining optical dispensaries.

	Unamortized Intangible Assets	Amortizable Intangible Assets
Balance as of December 31, 2001	$23,365	$432
Initial impairment upon adoption of FAS 142	(2,911)	--
Acquisition of ASCs	5,869	--
Amortization expense	--	(14)

Balance as of September 30, 2002	$26,323	$418
	=======	====

NOVAMED EYECARE, INC. AND SUBSIDIARIES
NOTES TO THE INTERIM
CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
September 30, 2002
(Dollars in thousands, except per share data; unaudited)

The following tables summarize the results of continuing operations and earnings per share had FAS 142 been adopted at the beginning of 2001:

	Three Months ended September 30, 2001	Nine M end Septem 20
Reported net loss from continuing operations	$(8,882)	$(8
Add back: Goodwill amortization	246	
Less: Related tax effect	(59)	
Adjusted net loss from continuing operations	$(8,695)	$(7

	Three Months ended September 30, 2001	Nine M end Septem 20
Basic Earnings Per Share		
Reported net loss from continuing operations	$ (0.36)	$ (
Goodwill amortization	0.01	
Adjusted net loss from continuing operations	$ (0.35)	$ (
Diluted Earnings Per Share		
Reported net loss from continuing operations	$(0.36)	$ (
Goodwill amortization	0.01	
Adjusted net loss from continuing operations	$(0.35)	$ (

3. DISCONTINUED OPERATIONS

As required, effective January 1, 2002 we adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-lived Assets" ("FAS 144") under which we will report as discontinued operations certain entities that have been disposed of or are classified as held for sale. Under FAS 144 projected operating results and the estimated gain or loss on sale is no longer accrued for when the decision to sell is made. Rather, the earnings or losses of discontinued operations continue to be reported, and any gain or loss is recognized at the time of sale. We have sold two ambulatory surgery centers and three optical dispensary businesses during 2002, all of which are reported as discontinued operations under the provisions of FAS 144. Prior period financial statements have been restated to reflect these entities as discontinued.

(Dollars in thousands, except per share data; unaudited)

During 2001, we implemented a Plan of Discontinued Operations and Restructuring (the "Plan"). This involves the divestiture of the management services segment or physician practice management ("PPM") business. The results of these discontinued operations are accounted for under Accounting Principles Board Opinion No. 30 "Reporting the Results of Operations -- Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" ("APB 30"). Under APB 30, the projected operating results and the estimated gain or loss on disposal was accrued for at the date the plan was adopted. We reported a charge of $27.2 million, net of tax in our third quarter 2001 financial statements. As of September 30, 2002, we had completed nine planned divestiture transactions.

As of September 30, 2002, from the sale of our discontinued operations, we have received proceeds of $11.7 million, consisting of $9.5 million in cash and $2.2 million in promissory notes with multi-year terms. We also received as consideration 1.7 million shares of our common stock.

Net interest expense allocated to discontinued operations was $0 and $212,000 for the three months ended September 30, 2002 and 2001, respectively, and $125,000 and $809,000 for the nine months ended September 30, 2002 and 2001, respectively. Interest was allocated to discontinued operations accounted for under APB 30, based on the proportion of net assets of discontinued operations to consolidated net assets plus consolidated debt as prescribed by EITF 87-24 -- Allocation of Interest to Discontinued Operations.

The operating results of all discontinued operations are summarized below.

	Three months ended September 30,		Nine months ende September 30,	
	2002	2001	2002	200
Net revenue	$ 9,974	$ 19,129	$37,762	$ 59,2
Operating expenses	10,029	18,252	36,891	55,0
Interest and other expense, net	(1)	202	106	7
Income (loss) from operations before income taxes	(54)	675	765	3,4
Income tax provision (benefit)	(22)	291	306	1,4
Net income (loss) from operations	(32)	384	459	1,9
(Income) loss charged (credited) to reserves	32	--	(278)	

Net income (loss) per statement of operations	$ --	$ 384	$ 181	$ 1,9
Gain (loss) on disposal of discontinued operations	$ 10	$(43,922)	$ (37)	$(43,9
Income tax expense (benefit)	(5)	(16,709)	(14)	(16,7
Net gain (loss) on disposal of discontinued operations	$ 5	$(27,213)	$ (23)	$(27,2

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NOVAMED EYECARE, INC. AND SUBSIDIARIES
NOTES TO THE INTERIM
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September 30, 2002
(Dollars in thousands, except per share data; unaudited)

The balance sheet components of discontinued operations are summarized as follows:

	September 30, 2002	December 31, 2001
Accounts and notes receivable	$ 5,713	$ 14,192
Inventories	382	1,310
Other current assets	367	723
Current assets of discontinued operations	$ 6,462	$ 16,225
Net property and equipment	$ 3,412	$ 5,494
Long-term note receivable	184	184
Intangible assets	2,280	8,188
Noncurrent assets of discontinued operations	$ 5,876	$ 13,866
Accounts payable	$ 696	$ 1,174
Accrued expenses	1,573	2,590
Notes payable and capitalized lease obligations	58	78
Discontinued operations reserves	5,571	5,242
Current liabilities of discontinued operations	$ 7,898	$ 9,084

During the first nine months of 2002, approximately $1.4 million of cash payments and $200,000 of noncash items were charged against the reserves to exit the PPM business. The reserves increased by approximately $2.0 million for discontinued operating results and net gains on disposals. Included in the balance sheet caption "Discontinued operations reserves" at September 30, 2002 are reserves of $2.8 million for projected operating results and estimated gain or loss on disposal and $2.8 million for costs to exit the PPM business.

4. RESTRUCTURING RESERVES

The following represents activity in the restructuring reserves from year-end through September 30, 2002:

	Reserve at December 31, 2001	Charges Utilized	Reserv Septemb 200
Facility closures--			
Asset impairments	$ 905	$ (215)	$ 6
Lease commitments	1,717	(615)	1,1
Contract termination	1,836	(1,702)	1
Reorganization of IT--			
Asset impairments	12	--	
Lease commitments	456	(26)	4
Other	97	(36)	
Total reserve balance	$ 5,023	$ (2,594)	$ 2,4

During the first nine months of 2002, we terminated a contract to purchase an ASC and negotiated the sublease of one closed LVC center.

NOVAMED EYECARE, INC. AND SUBSIDIARIES
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5. OTHER (INCOME) EXPENSE

	Three months ended September 30, 2002	Three months ended September 30, 2001	Ni 20
Interest expense	$ 108	$ 218	$
Interest income	(7)	(5)	
Legal settlement	(443)	--	
Losses of equity affiliates	--	17	
Gain on sale of minority interest	(101)	--	
Other, net	(1)	(4)	

(Dollars in thousands, except per share data; unaudited)

Other (income) expense, net	$ (444)	$ 226	$

During the second quarter of 2002 we sold a 20% interest in an ASC to two former affiliated eye care professionals and during the third quarter of 2002 we sold a 5% interest in that ASC to another former affiliated eye care professional, reducing our interest in that ASC to 75%. During the third quarter of 2002, we received proceeds from the settlement of an antitrust class action lawsuit against a joint venture of two laser manufacturers.

6. REVOLVING CREDIT FACILITY

At September 30, 2002, we had $7.9 million outstanding under our revolving credit facility that expires on June 30, 2003. The maximum commitment available under our facility is $30 million. Under the credit facility, interest on borrowings is payable at an annual rate equal to the lender's published base rate plus the applicable borrowing margin ranging from 0% to 1.0% or LIBOR plus a range from 1.5% to 3.0%, varying upon our ability to meet financial covenants. The weighted average annual interest rate on credit line borrowings was 5.1% and 4.9% for the three and nine months ended September 30, 2002, respectively, and 3.7% at September 30, 2002. The credit agreement contains covenants that include limitations on indebtedness, liens, capital expenditures, acquisitions and affiliations and ratios that define borrowing availability and restrictions on the payment of dividends. We are required to use 100% of the cash proceeds from our divestiture transactions to pay down outstanding debt. In addition, the terms of our credit facility allow us to sell minority interests in our existing ASCs to the extent such a sale, when combined with other minority interest sales during the preceding twelve month period, does not reduce our EBITDA by more than $3 million. As of September 30, 2002, we were in compliance with all our credit agreement covenants.

7. OPERATING SEGMENTS

The table below presents information about operating data and segment assets as of and for the three and nine months ended September 30, 2002 and 2001:

	Surgical Facilities	Product Sales and Other	Corporate
Three months ended September 30, 2002			
Net revenue	$ 8,277	$ 9,027	$ --
Earnings (loss) before tax	2,346	342	(1,297)

Depreciation and amortization	455	74	97
Interest income	2	--	5
Interest expense	2	--	106
Identifiable assets	9,508	5,772	61,162
Three months ended September 30, 2001			
Net revenue	$ 8,018	$ 7,553	$ --
Earnings (loss) before tax	2,127	469	(17,476)
Depreciation and amortization	515	81	584
Interest income	--	--	5
Interest expense	1	2	215
Identifiable assets	11,303	6,362	83,205
Nine months ended September 30, 2002			
Net revenue	$ 24,473	$ 26,950	$ --
Earnings (loss) before tax	7,636	1,259	(4,410)
Depreciation and amortization	1,372	213	311
Interest income	3	1	64
Interest expense	5	--	359
Identifiable assets	9,508	5,772	61,162
Nine months ended September 30, 2001			
Net revenue	$ 26,788	$ 22,857	$ --
Earnings (loss) before tax	8,494	1,835	(23,673)
Depreciation and amortization	1,450	205	1,760
Interest income	--	3	41
Interest expense	2	2	798
Identifiable assets	11,303	6,362	83,205

Item 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF CONTINUING OPERATIONS

The discussion below contains forward-looking statements (as such term is defined in Section 21E of the Securities Exchange Act of 1934) that are based on the beliefs of our management, as well as assumptions made by, and information currently available to, our management. Our results, performance and achievements in 2002 and beyond could differ materially from those expressed in, or implied by, any such forward looking statements. See "Cautionary note regarding forward-looking statements" on page 16.

Management's discussion and analysis of financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the U.S. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures. On an ongoing basis, we evaluate our estimates and judgments based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

General

We provide a comprehensive range of eye care services, focused primarily around our surgical facilities, including our ownership and operation of 16 ambulatory surgery centers ("ASCs"), and our operation of 11 laser vision correction ("LVC") centers and fixed-site laser services agreements. Eye care professionals perform cataract, laser vision correction and other eye-related surgical procedures in the surgical facilities we own and/or operate.

The discussion set forth below analyzes certain factors and trends related to the financial results of continuing operations for each of the three and nine months ended September 30, 2002 and 2001. This discussion should be read in conjunction with the condensed consolidated financial statements and notes to the condensed consolidated financial statements above.

Results of Operations

Three Months Ended September 30, 2002 Compared to the Three Months Ended September 30, 2001

Net Revenue. Net revenue increased 10.9% from $15.6 million to $17.3 million. Surgical facilities net revenue increased 3.8% from $8.0 million to $8.3 million due to the acquisition of new ASCs. During the third quarter of 2002, total surgical procedures performed in our surgical facilities decreased 5.1% to 9,428. Cataract procedures increased 12.0%, LVC procedures decreased 44.0% and other procedures increased 9.8%, compared to 2001. The increase in cataract and other procedures came from our Thibodaux, Louisiana, Colorado Springs, Colorado and Tyler, Texas ASCs, which we acquired in November 2001, May 2002 and September 2002, respectively. Management believes that the demand for elective LVC surgery continues to be negatively impacted by the general economic conditions.

Product sales and other net revenue increased 18.4% from $7.6 million to $9.0 million, primarily as a result of a 28.7% net revenue increase at our optical products purchasing organization. This increase was offset by a 24.1% decrease in net revenue at our optical dispensaries, a 34.9% decrease in net revenue at our marketing products business and a 3.5% decrease in net revenue at our optical laboratories. Approximately 54% of the increase in net revenue at our optical products purchasing organization is from sales to optical businesses that we divested that were previously eliminated as intercompany sales. In connection with each applicable divestiture transaction, we seek to negotiate multi-year supply agreements where we will continue to be the primary supplier of optical products to our former affiliated eye care professionals. Approximately 46% of the decrease in net revenue from our optical dispensaries was due to the closing of optical dispensaries in 2001. Our marketing products business has sold products primarily to the laser vision correction market. Management believes the downturn in this market was the cause of the decline in net revenue at this business.

Salaries, Wages and Benefits. Salaries, wages and benefits expense decreased 7.7% from $3.9 million to $3.6 million. As a percentage of net revenue, salaries, wages and benefits expense decreased from 25.1% to 20.7%. The decrease in salaries, wages and benefits expense is the result of certain corporate salaries being charged to the discontinued operations reserves in accordance with the Plan; staff reductions at some surgical facilities in response to the reduction in LVC procedures; and the closure of several LVC centers and optical dispensaries in the fourth quarter of 2001 and the first quarter of 2002.

Cost of Sales and Medical Supplies. Cost of sales and medical supplies expense increased 18.5% from $8.1 million to $9.6 million. As a percentage of net revenue, cost of sales and medical supplies expense increased from 51.8% to 55.7%. The absolute increase in cost of sales and medical supplies expense is primarily a result of higher sales volumes at our optical products purchasing organization. The increase in cost of sales and medical supplies as a percentage of net revenue is due to our product sales and other segment net revenue increasing to 52.2% of total net revenue in the third quarter of 2002, up from 48.5% in 2001. This segment has a much higher cost of sales and medical supplies expense relative to net revenue than our surgical facilities segment.

Selling, General and Administrative. Selling, general and administrative ("SG&A") expense decreased 4.2% from $2.4 million to $2.3 million. As a percentage of net revenue, SG&A expense decreased from 15.7% to 13.2%. The absolute decrease in SG&A expense is primarily the result of closing several LVC centers and optical dispensaries in the fourth quarter of 2001 and the first quarter of 2002 coupled with cost reductions at our corporate office. The effect of these reductions was somewhat offset by expenses at newly acquired ASCs.

Depreciation and Amortization. Depreciation and amortization expense decreased 47.8% from $1.2 million to $626,000. The cessation of goodwill amortization as of January 1, 2002 contributed $246,000 of this decrease as compared to the same quarter of 2001. The remainder of the decrease is due to the write-off of assets at the end of our 2001 third quarter related to our restructuring plan.

Other Income / Expense. We recognized $444,000 of other income in the third quarter of 2002 versus other expense of $226,000 in the third quarter of 2001. The current year income includes a $101,000 gain on the sale of a 5% interest in one of our ASCs and $443,000 of income from proceeds received from a class action lawsuit settlement. Excluding these items, other expense of $100,000 was down from the prior year level. The decrease in other expense was primarily related to a decrease in interest expense as a result of lower average interest rates during the third quarter of 2002 (5.1%) as compared to the third quarter of 2001 (6.0%) as well as lower average borrowings of $7.7 million during the third quarter of 2002 as compared to $25.0 million during the third quarter of 2001.

Provision for Income Taxes. The effective tax rate was 40.0% for the third quarter of 2002 as compared to an effective rate of 40.3% in the third quarter of 2001. A rate of 38.0% was used to determine the tax benefit from restructuring and other charges recorded during the third quarter of 2001 which reduced our overall effective rate that had exceeded 43% prior to our adoption of the Plan. The adoption of FAS 142 at the beginning of 2002 reduced our effective tax rate to 40.0% from the 2001 rates because under the new accounting pronouncement we no longer amortize most of our intangible assets which substantially reduces the amount of permanent differences in our tax calculation.

Nine Months Ended September 30, 2002 Compared to the Nine Months Ended September 30, 2001

Net Revenue. Net revenue increased 3.6% from $49.6 million to $51.4 million. The contribution from our operating segments shifted from 54.0% surgical facilities and 46.0% product sales in 2001 to 47.6% surgical facilities and 52.4% product sales in 2002. Surgical facilities net revenue decreased 8.6% from $26.8 million to $24.5 million primarily due to the decrease in surgical procedures performed as well as the change in surgical procedure mix. LVC centers closed during 2001 and the first quarter of 2002 accounted for 55.7% of the decrease in surgical facilities revenue. During the first nine months of 2002, total surgical procedures performed in our surgical facilities decreased 14.6% to 28,440. Cataract procedures increased 7.1%, LVC procedures decreased 44.5% and other procedures decreased 2.0%, compared to 2001. The increase in cataract procedures came from our Thibodaux, Louisiana, Colorado Springs, Colorado and Tyler, Texas ASCs, which we acquired in November 2001, May 2002 and September 2002, respectively. Management believes that the demand for elective LVC surgery continues to be negatively impacted by the general economic conditions.

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Product sales and other net revenue increased 17.9% from $22.9 million to $27.0 million, primarily as a result of a 27.4% net revenue increase at our optical products purchasing organization coupled with an 2.5% increase in net revenue at our optical laboratories. These increases were offset by a 34.3% decrease in net revenue at our optical dispensaries and a 30.6% decrease in net revenue at our marketing products business. Approximately 40% of the increase in net revenue at our optical products purchasing organization and optical laboratories is from sales to optical businesses that we divested that were previously eliminated as intercompany sales. Approximately 62% of the decrease in net revenue from our optical dispensaries was due to the closing of optical dispensaries in 2001. Our marketing products business has sold products primarily to the laser vision correction market. Management believes the downturn in this market was the cause of the decline in net revenue in this business and led us to take a $1.8 million net charge to write off a portion of the carrying value of goodwill created when we acquired the company in 2000. This charge is reported as a change in accounting principle.

Salaries, Wages and Benefits. Salaries, wages and benefits expense decreased 18.8% from $12.8 million to $10.4 million. As a percentage of net revenue, salaries, wages and benefits expense decreased from 25.7% to 20.2%. Of the decrease in salaries, wages and benefits expense approximately 74% is due to the fact that certain corporate salaries were charged to the discontinued operations reserves in accordance with the Plan. The remaining decrease in salaries, wages and benefits expense is a result of staff reductions at some surgical facilities in response to the reduction in LVC procedures as well as corporate staff reductions and the closure of several LVC centers and optical dispensaries in the fourth quarter of 2001 and the first quarter of 2002.

Cost of Sales and Medical Supplies. Cost of sales and medical supplies expense increased 16.9% from $24.2 million to $28.3 million. As a percentage of net revenue, cost of sales and medical supplies expense increased from 48.8% to 55.1%. The absolute increase in cost of sales and medical supplies expense is primarily a result of higher sales volumes at our optical products purchasing organization. The increase in cost of sales and medical supplies as a percentage of net revenue is due to our product sales and other segment net revenue increasing to 52.4% of total net revenue in the first nine months of 2002, up from 46.0% in 2001. This segment has a much higher cost of sales and medical supplies expense relative to net revenue than our surgical facilities segment.

Selling, General and Administrative. Selling, general and administrative expense decreased 5.6% from $7.1 million to $6.7 million. As a percentage of net revenue, SG&A expense decreased from 14.3% to 13.1%. The absolute decrease in SG&A expense is the result of closing several LVC centers and optical dispensaries in the fourth quarter of 2001 and the first quarter of 2002. Excluding those closures, SG&A expense increased 0.9% compared to the prior year due to expenses at newly acquired ASCs.

Depreciation and Amortization. Depreciation and amortization expense decreased 44.1% from $3.4 million to $1.9 million. The cessation of goodwill amortization as of January 1, 2002 contributed $740,000 of this decrease as compared to the first nine months of 2001. The remainder of the decrease is due to the write-off of assets at the end of our 2001 third quarter related to our restructuring plan.

Other Income / Expense. We recognized $756,000 of other income for the first nine months of 2002 versus other expense of $881,000 in 2001. The current year income includes an aggregate gain of $537,000 from the sales of a 20% interest and 5% interest in one of our ASCs and $443,000 of income from proceeds received from a class action lawsuit settlement. Excluding these items, other expense of $224,000 was down from the prior year level. The decrease in other expense was primarily related to a decrease in interest expense as a result of lower average interest rates during the 2002 period (4.9%) as compared to the 2001 period (6.9%) as well as lower average borrowings of $12.6 million during the first nine months of 2002 as compared to $27.0 million during the same period of 2001.

Provision for Income Taxes. The effective tax rate was 40.0% for the first nine months of 2002 as compared to an effective rate of 39.5% for the first nine months of 2001. A rate of 38.0% was used to determine the tax benefit from restructuring and other charges recorded during the third quarter of 2001 which reduced our overall effective rate that had exceeded 43% prior to our adoption of the Plan. The adoption of FAS 142 at the beginning of 2002 reduced our effective tax rate to 40.0% from the 2001 rates because under the new accounting pronouncement we no longer amortize most of our intangible assets which substantially reduces the amount of permanent differences in our tax calculation.

Liquidity and Capital Resources

Net cash provided by continuing operating activities was $8.7 million and $2.1 for the nine months ended September 30, 2002 and 2001, respectively. The period ended September 30, 2002 included a $1.5 million refund of 2001 estimated federal tax payments and $443,000 of proceeds from a class action lawsuit. We used $6.5 million of cash for investing activities during the first nine months of 2002, which included the purchase of a majority interest in ambulatory surgery centers in Colorado Springs, Colorado and Tyler, Texas. During the first nine months of 2002, our net borrowings under our revolving credit line decreased $12.8 million from the December 31, 2001 level, using cash generated by operations and proceeds from divestiture transactions. At September 30, 2002, we had working capital of $10.5 million (excluding restructuring reserves and discontinued operations).

During the first nine months of 2002, we completed eight divestiture transactions. We received total proceeds of $10.5 million, consisting of $8.8 million in cash and $1.8 million in promissory notes with multi-year terms. We also received as consideration 1.7 million shares of our common stock. In addition, we sold a 25% interest in one of our ASCs to three former affiliated eye care professionals during the second and third quarters of 2002. The cash proceeds from these transactions were used to reduce debt as required under our revolving credit facility.

At September 30, 2002, we had $7.9 million outstanding under our revolving credit facility that expires on June 30, 2003. The maximum commitment available under our facility is $30 million. Under the credit facility, interest on borrowings is payable at an annual rate equal to the lender's published base rate plus the applicable borrowing margin ranging from 0% to 1.0% or LIBOR plus a range from 1.5% to 3.0%, varying upon our ability to meet financial covenants. The weighted average annual interest rate on credit line borrowings was 5.1% and 4.9% for three and nine months ended September 30, 2002, respectively, and 3.7% at September 30, 2002. The variance between the weighted average interest rate for the three and nine months and the 3.7% at September 30, 2002 is primarily due to declining interest rates and the inclusion of commitment fees on our unused line of credit in the three and nine month numbers. The credit agreement contains covenants that include limitations on indebtedness, liens, capital expenditures, acquisitions and affiliations and ratios that define borrowing availability and restrictions on the payment of dividends. We are required to use 100% of the cash proceeds from our divestiture transactions to pay down outstanding debt. In addition, the terms of our credit facility allow us to sell minority interests in our existing ASCs to the extent such a sale, when combined with other minority interest sales during the preceding twelve month period, does not reduce our EBITDA by more than $3 million. As of September 30, 2002, we were in compliance with all our credit agreement covenants. We believe that our cash flow from operations and cash proceeds from divestiture transactions will allow us to continue to pay down our outstanding debt. We plan to use the funds available under our credit facility to finance acquisitions. Before June 30, 2003, when our existing credit facility terminates, we intend to negotiate either an extension of our existing credit facility or a new credit facility.

We believe that our cash flow from operations and funds available under our existing revolving credit facility will be sufficient to fund our operations for at least 12 months. Our future capital requirements and the adequacy of our available funds will depend on many factors, including the timing of our acquisition activities, capital requirements associated with our surgical facilities, expansion and the future cost of surgical equipment, and cost of completing our discontinued operations plan.

One of our former affiliated eye care professionals has the option, exercisable beginning January 1, 2004 through January 1, 2006, to acquire up to a 30% interest in one of our ASCs. In July 2002, we sold a 5% interest in one of our ASCs to a former affiliated eye care professional, and simultaneously entered into an agreement with such professional whereby he has an option, beginning July 1, 2003 through July 1, 2005 to acquire an additional 5% interest in the ASC. One of our partners in an ASC in which we own a majority interest has the right to sell us up to a 10% interest in the ASC in November 2004 and up to an additional 10% interest in November 2006.

Subsequent Event

On October 18, 2002, we consummated a divestiture transaction with the physician-shareholders of Hunkeler Eye Centers, P.C. ("HEC"), a professional entity that had been a party to a long-term services agreement with us since March 1997. Consistent with our plan to discontinue our management services business, this transaction involved the termination of our long-term services agreement with HEC, as well as the sale of management services assets to the physician-shareholders of HEC.

In addition to selling management services assets, we entered into agreements to sell minority equity interests in our three ASCs located in the Kansas City metropolitan area. We sold a 20% equity interest in one of these ASCs to two HEC physicians, and entered into an agreement to sell to these two physicians a 20% equity interest in a second ASC (subject to state licensure approvals). We also sold a 49% equity interest in the third ASC to two other HEC physicians. We also restructured our laser vision correction business in the Kansas City market by entering into fixed-site laser services agreements with four HEC physicians pursuant to which we will provide them with excimer lasers and other surgical equipment on an exclusive basis. In addition, the two physicians who own a 49% minority interest in one of these ASCs have an option to purchase our remaining 51% interest on April 15, 2005 at a purchase price of $1.7 million. While these ASC transactions will increase the minority interest deduction to our income, they are consistent with our previously announced plans to jointly own some or all of our existing ASCs with physicians in the local market.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS. This Form 10-Q contains certain forward-looking statements that reflect our current expectations about our future results of operations, performance and achievements. When used in the Form 10-Q, the words "anticipates," "believes," "estimates," "plans," "intends," and similar expressions, as they relate to us or our management, are intended to identify such forward-looking statements. These forward-looking statements reflect our current beliefs and are based on information currently available to us. Accordingly, these statements are subject to certain risks and uncertainties which could cause our actual results, performance or achievements in 2002 and beyond to differ materially from those expressed in, or implied by, such statements. These risks and uncertainties include: our ability to acquire, develop or manage a sufficient number of profitable surgical facilities; reduced prices and reimbursement rates for surgical procedures; our ability to successfully implement our discontinued operations plan on acceptable terms consistent with our credit facility; the resulting changes in our physician relationships following our divestiture transactions; the increase in minority interest deduction resulting from the sale of minority interests in our existing ASCs, and, absent other factors such as an increase in surgical procedures, the resulting reduction in our income; demand for elective surgical procedures generally and in response to a protracted economic downturn; the continued acceptance of laser vision correction and other refractive surgical procedures, particularly in locations where we are operating under a fixed-site laser services agreement; and the application of existing or proposed government regulations. See "Management's Discussion and Analysis of Financial Conditions and Results of Operations - Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2001 for further discussion. We undertake no obligation to update or revise any such forward-looking statements that may be made to reflect events or circumstances after the date of this Form 10-Q or to reflect the occurrence of unanticipated events.

Item 4. Disclosure Controls and Procedures

Under the supervision and with the participation of the Company's Chairman and Chief Executive Officer, and Executive Vice President and Chief Financial Officer (its principal executive officer and principal financial officer), management has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures within 90 days of the filing date of this quarterly report. Based on that evaluation, the Chairman and Chief Executive Officer, and Executive Vice President and Chief Financial Officer have concluded that these controls and procedures are effective with respect to timely communicating to them all material information required to be disclosed in this report. There were no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation.

PART II. OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

A. Exhibits

Exhibit 21	Subsidiaries of Registrant
Exhibit 99	Certification of CEO and CFO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

B. Reports on Form 8-K

We filed a report on Form 8-K dated June 15, 2002, to report, pursuant to Item 2, a disposition of assets.

We filed a report on Form 8-K dated July 25, 2002, to report, pursuant to Item 4, a change in certifying accountants.

SIGNATURE

Pursuant to the requirement 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.

NOVAMED EYECARE, INC.

/s/ Scott T. Macomber	November 13, 2002
Scott T. Macomber Executive Vice President and Chief Financial Officer (on behalf of Registrant and as principal financial officer)	Date
/s/ Robert L. Hiatt	November 13, 2002
Robert L. Hiatt Vice President Finance (on behalf of Registrant and as principal accounting officer)	Date

Certification
(pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended)

I, Stephen J. Winjum, certify that:

1. I have reviewed this quarterly report on Form 10-Q of NovaMed Eyecare, 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 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 date 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 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 significant deficiencies and material weaknesses.

Date: November 13, 2002

/s/ Stephen J. Winjum

Stephen J. Winjum
Chief Executive Officer

Certification
(pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended)

I, Scott T. Macomber, certify that:

1. I have reviewed this quarterly report on Form 10-Q of NovaMed Eyecare, 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 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 date 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 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 significant deficiencies and material weaknesses.

Date: November 13, 2002

/s/ Scott T. Macomber

Scott T. Macomber
Chief Financial Officer