NOVAMED EYECARE INC
Form 10-Q
August 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: JUNE 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 August 12, 2002, there were outstanding 23,128,908 shares of the registrant's common stock, par value $.01 per share.

NOVAMED EYECARE, INC.
FORM 10-Q FOR QUARTERLY PERIOD ENDED JUNE 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)

	June 3
ASSETS	2002
Current assets:	(unau
Cash and cash equivalents	$
Accounts receivable, net	
Notes and amounts due from affiliated providers	
Inventory	
Current tax assets, net	
Other current assets	
Current assets of discontinued operations	
Total current assets	
Property and equipment, net	
Intangible assets, net	
Noncurrent deferred tax assets, net	
Other assets, net	
Noncurrent assets of discontinued operations, net	
Total assets	$
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$
Accrued expenses	
Restructuring reserves	
Current maturities of long-term debt	
Current liabilities of discontinued operations	
Total current liabilities	
Long-term debt, net of current maturities	

Minority interest	
Commitments and contingencies	
Stockholders' equity:	
Series E Junior Participating Preferred Stock, $0.01 par value, 1,912,000 shares authorized, none outstanding at June 30, 2002 and December 31, 2001, respectively	
Common stock, $0.01 par value, 81,761,465 shares authorized, 23,128,908 and 24,835,108 shares issued and outstanding at June 30, 2002 and December 31, 2001, respectively	
Additional paid-in-capital	
Retained earnings (deficit)	(
Treasury stock, at cost, 1,748,640 shares at June 30, 2002	
Total stockholders' equity	
Total liabilities and stockholders' equity	$

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 OPERATIONS
(Amounts in thousands, except per share data; unaudited)

	Three months ended June 30,	
	2002	2001
Net revenue:		
Surgical facilities	$ 8,331	$ 9,467
Product sales and other	9,381	7,976
Total net revenue	17,712	17,443
Operating expenses:		
Salaries, wages and benefits	3,518	4,476
Cost of sales and medical supplies	9,828	8,454
Selling, general and administrative	2,200	2,279
Depreciation and amortization	671	1,156
Total operating expenses	16,217	16,365
Income from continuing operations	1,495	1,078
Other (income) expense, net	(261)	247
Income from continuing operations		

before income taxes	1,756	831
Income tax provision	702	368
Net income from continuing operations before cumulative effect of change in accounting principle	1,054	463
Net income from discontinued operations	259	766
Cumulative effect of change in accounting principle, net of tax	--	--
Net income	$ 1,313	$ 1,229
Basic earnings per common share:		
Income from continuing operations before cumulative effect of change in accounting principle	$ 0.04	$ 0.02
Income from discontinued operations	0.01	0.03
Cumulative effect of change in accounting principle	--	--
Net income	$ 0.05	$ 0.05
Diluted earnings per common share:		
Income from continuing operations before cumulative effect of change in accounting principle	$ 0.04	$ 0.02
Income (loss) from discontinued operations	0.01	0.03
Cumulative effect of change in accounting principle	--	--
Net income	$ 0.05	$ 0.05
Weighted average common shares outstanding	24,563	24,803
Dilutive effect of employee stock options	52	500
Diluted weighted average common shares outstanding	24,615	25,303

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)

	S
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Cash flows from operating activities:	
Net income	$
Adjustments to reconcile net income to net cash provided by continuing operations, net of effects of purchase transactions--	
Net earnings of discontinued operations	
Cumulative effect of change in accounting principle, net	

Gain on sale of minority interest	
Depreciation and amortization	
Minority interest	
Deferred taxes	
Changes in working capital items--	
Accounts receivable	
Inventory	
Other current assets	
Accounts payable and accrued expenses	
Other	
Net cash provided by operating activities	
Cash flows from investing activities:	
Purchases of property and equipment	
Acquisitions of ASCs	
Proceeds from sale of minority interest	
Other	
Net cash used by investing activities	
Cash flows from financing activities:	
Borrowings under revolving line of credit	
Payments under revolving line of credit	(
Other	
Net cash used by financing activities	(
Cash flows from discontinued operations:	
Operating activities	
Proceeds from divestitures	
Investing activities	
Financing activities	
Net cash provided by discontinued operation	
Net decrease in cash and cash equivalents	
Cash and cash equivalents, beginning of period	
Cash and cash equivalents, end of period	$
Noncash investing activity:	
Fair value of stock received in divestiture transactions	$

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

June 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 June 30, 2002 and for the three and six months ended June 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	
Balance as of December 31, 2001	$ 23,365	$
Initial impairment upon adoption of FAS 142	(2,911)	
Acquisition of ASCs	1,296	
Amortization expense	--	
Balance as of June 30, 2002	$ 21,750	$

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NOVAMED EYECARE, INC. AND SUBSIDIARIES
NOTES TO THE INTERIM
CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
June 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 June 30, 2001
Reported net income from continuing operations	$ 463
Add back: Goodwill amortization	247
Less: Related tax effect	(71)
Adjusted net income from continuing operations	$ 639

	Three Months ended June 30, 2001
Basic Earnings Per Share	
Reported net income from continuing operations	$ 0.02
Goodwill amortization	0.01
Adjusted net income from continuing operations	$ 0.03
Diluted Earnings Per Share	
Reported net income from continuing operations	$ 0.02
Goodwill amortization	0.01
Adjusted net income from continuing operations	$ 0.03

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. In the first half of 2002, we sold two ambulatory surgery centers and two optical dispensary businesses and agreed to sell one additional optical dispensary, 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.

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 June 30, 2002, we had completed seven of eighteen planned divestiture transactions.

To date, from the sale of our discontinued operations, we have received proceeds of $9.1 million, consisting of $7.3 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.

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

Net interest expense allocated to discontinued operations was $32,500 and $288,000 for the three months ended June 30, 2002 and 2001 and $125,000 and $597,000 for the six months ended June 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 June 30, 2002	Three months ended June 30, 2001
Net revenue	$ 11,963	$ 19,910
Operating expenses	11,683	18,250
Interest and other expense, net	34	280
Income from operations before income taxes	246	1,380
Income tax provision	98	614
Net income from operations	148	766
Gain (loss) on sale of discontinued operations	263	--
Income tax expense (benefit)	100	--

Net gain (loss) on sale of discontinued operations	163	--
Net income from discontinued operations	$ 311	$ 766

During the three and six months ended June 30, 2002, $52,000 and $310,000, respectively, of the net income was credited to the discontinued operations reserves previously established and reported under APB 30, which resulted in a reported net income of discontinued operations of $259,000 and $153,000 for the respective periods.

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

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

	June 30, 2002	December 31, 2001
Accounts and notes receivable	$ 6,699	$ 14,098
Inventories	374	1,310
Other current assets	586	723
Current assets of discontinued operations	$ 7,659	$ 16,131
Net property and equipment	$ 4,017	$ 5,494
Intangible assets	3,779	8,188
Noncurrent assets of discontinued operations	$ 7,796	$ 13,682
Accounts payable	$ 782	$ 1,174
Accrued expenses	1,263	2,590
Notes payable and capitalized lease obligations	88	78
Discontinued operations reserves	5,714	5,242
Current liabilities of discontinued operations	$ 7,847	$ 9,084

During the first six months of 2002, approximately $1.3 million of cash payments and $550,000 of noncash items were charged against the reserves to exit the PPM business. The reserves increased by approximately $2.3 million for discontinued operating results and net gains on disposals. Included in the balance sheet caption "Discontinued operations reserves" at June 30, 2002 are reserves of $2.7 million for projected operating results and estimated gain or loss on disposal and $3.0 million for costs to exit the PPM business.

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

4. RESTRUCTURING RESERVES

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

	Reserve at December 31, 2001	Charges Utilized	Reserve June 3 2002
Facility closures--			
Asset impairments	$ 905	$ (210)	$
Lease commitments	1,717	(577)	1
Contract termination	1,836	(1,702)	
Reorganization of IT--			
Asset impairments	12	--	
Lease commitments	456	--	
Other	97	(35)	
Total reserve balance	$ 5,023	$ (2,524)	$ 2

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

5. OTHER (INCOME) EXPENSE

	Three months ended June 30,		S
	2002	2001	20
Interest expense	$ 121	$ 280	$
Interest income	(34)	(14)	
Minority interest	90	--	
Losses of equity affiliates	--	3	
Gain on sale of minority interest	(436)	--	
Other, net	(2)	(22)	
Other (income) expense, net	$ (261)	$ 247	$

During the second quarter of 2002 we sold a 20% interest in an ASC to two former affiliated eye care professionals resulting in a pre-tax gain of $436,000.

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

6. REVOLVING CREDIT FACILITY

At June 30, 2002, we had $6.9 million outstanding under our revolving credit facility that expires on June 30, 2003. 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 5.0% and 4.8% for three and six months ended June 30, 2002, respectively, and 3.6% at June 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.

The sale of optical dispensary assets and one of our ambulatory surgery centers in the 2002 second quarter required the approval of our lenders under our credit facility. In addition to seeking their consent to this transaction, we also approached our lenders about other modifications to our credit facility, including an expansion of our ability to sell minority interests in our existing ambulatory surgery centers, as well as providing us with the ability to sell other optical dispensary assets as part of our divestiture transactions as we deem appropriate. After considering these requests, our lenders consented to this transaction and agreed to the other requested modifications. Previously, the terms of our credit facility limited our ability to sell minority interests in our existing ASCs to the extent any such sales reduced our overall EBITDA in any 12-month period by more than $1 million. Our lenders agreed to increase this limit from $1 million to $3 million.

In consideration for the lenders consenting to the sale of our ambulatory surgery center and approving these modifications to our credit facility, we agreed to reduce the maximum commitment available under our facility to $35 million effective as of June 13, 2002, with an additional reduction to $30 million as of October 1, 2002. Before giving effect to this amendment, the maximum commitment available under our credit facility had been $40 million, with additional quarterly reductions of $2.5 million on each of July 1, 2002 and October 1, 2002, resulting in a maximum commitment of $35 million as of October 1, 2002. As of June 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 six months ended June 30, 2002 and 2001:

	Surgical Facilities	Product Sales and Other	Corporate

Three months ended June 30, 2002			
Net revenue	$ 8,331	$ 9,381	$ --
Earnings (loss) before tax	2,808	425	(1,477)
Depreciation and amortization	454	70	147
Interest income	1	--	33
Interest expense	2	--	119
Identifiable assets	9,710	5,893	58,048
Three months ended June 30, 2001			
Net revenue	$ 9,467	$ 7,976	$ --
Earnings (loss) before tax	3,066	656	(2,891)
Depreciation and amortization	495	65	596
Interest income	--	1	13
Interest expense	1	--	279
Identifiable assets	14,180	6,509	100,937
Six months ended June 30, 2002			
Net revenue	$ 16,196	$ 17,922	$ --
Earnings (loss) before tax	5,301	916	(3,123)
Depreciation and amortization	918	139	213
Interest income	2	--	59
Interest expense	3	--	253
Identifiable assets	9,710	5,893	58,048
Six months ended June 30, 2001			
Net revenue	$ 18,771	$ 15,304	$ --
Earnings (loss) before tax	6,367	1,366	(6,202)
Depreciation and amortization	935	125	1,175
Interest income	--	2	36
Interest expense	1	--	587
Identifiable assets	14,180	6,509	100,937

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.

Outlook

We provide a comprehensive range of eye care services, focused primarily around our surgical facilities, including our ownership and operation of 15 ambulatory surgery centers ("ASCs"), and our operation of 13 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 six months ended June 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 June 30, 2002 Compared to the Three Months Ended June 30, 2001

Net Revenue. Net revenue increased 1.7% from $17.4 million to $17.7 million. Surgical facilities net revenue decreased 11.7% from $9.4 million to $8.3 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 30.7% of the decrease in surgical facilities revenue. During the second quarter of 2002, total surgical procedures performed in our surgical facilities decreased 18.7% to 9,354. Cataract procedures increased 5.0%, LVC procedures decreased 47.9% and other procedures decreased 12.0%, compared to 2001. Management believes that the demand for elective LVC surgery continues to be negatively impacted by the general economic conditions. The increase in cataract procedures came from our Thibodaux, Louisiana and Colorado Springs, Colorado ASCs, which we acquired in November 2001 and May 2002, respectively.

Product sales and other net revenue increased 17.5% from $8.0 million to $9.4 million, primarily as a result of a 26.5% net revenue increase at our optical products purchasing organization coupled with a 3.0% increase in net revenue at our optical laboratories. These increases were offset by a 35.7% decrease in net revenue at our optical dispensaries and a 33.3% decrease in net revenue at our marketing products business. Approximately 48% 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. As a condition to each applicable divestiture transaction, we are attempting 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 64% 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 22.2% from $4.5 million to $3.5 million. As a percentage of net revenue, salaries, wages and benefits expense decreased from 25.7% to 19.9%. Of the decrease in salaries, wages and benefits expense, approximately 65% 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 first quarter of 2002.

Cost of Sales and Medical Supplies. Cost of sales and medical supplies expense increased 15.3% from $8.5 million to $9.8 million. As a percentage of net revenue, cost of sales and medical supplies expense increased from 48.5% to 55.5%. 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 53.0% of total net revenue in the second quarter of 2002, up from 45.7% 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 4.3% from $2.3 million to $2.2 million. As a percentage of net revenue, SG&A expense decreased from 13.1% to 12.4%. 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 first quarter of 2002. Excluding those closures, SG&A expense increased 1.4% compared to the prior year quarter due to expenses at newly acquired ASCs.

Depreciation and Amortization. Depreciation and amortization expense decreased 42.0% from $1.2 million to $671,000. The cessation of goodwill amortization as of January 1, 2002 contributed $247,000 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 $261,000 of other income in the second quarter of 2002 versus other expense of $247,000 in the second quarter of 2001. The current year income includes a $436,000 gain on the sale of a 20% interest in one of our ASCs. Excluding this gain, other expense of $175,000 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 second quarter of 2002 (5.0%) as compared to the 2001 quarter (6.8%) as well as lower average borrowings of $11.3 million during the second quarter of 2002 as compared to $27.4 million during the second quarter of 2001.

Provision for Income Taxes. The adoption of FAS 142 reduced our effective tax rate to 40.0% from 44.3% in the second quarter of 2002. 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.

Six Months Ended June 30, 2002 Compared to the Six Months Ended June 30, 2001

Net Revenue. Net revenue was $34.1 million for both the six months ended June 30, 2002 and 2001. The contribution from our operating segments shifted from 55.1% surgical facilities and 44.9% product sales in 2001 to 47.5% surgical facilities and 52.5% product sales in 2002. Surgical facilities net revenue decreased 13.8% from $18.8 million to $16.2 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 first quarter of 2002 accounted for 44.4% of the decrease in surgical facilities revenue. During the first half of 2002, total surgical procedures performed in our surgical facilities decreased 18.6% to 19,012. Cataract procedures increased 4.5%, LVC procedures decreased 44.7% and other procedures decreased 7.5%, compared to 2001. Management believes that the demand for elective LVC surgery continues to be negatively impacted by the general economic conditions. The increase in cataract procedures came from our Thibodaux, Louisiana and Colorado Springs, Colorado ASCs, which we acquired in November 2001 and May 2002, respectively.

Product sales and other net revenue increased 17.0% from $15.3 million to $17.9 million, primarily as a result of a 26.8% net revenue increase at our optical products purchasing organization coupled with an 5.6% increase in net revenue at our optical laboratories. These increases were offset by a 38.6% decrease in net revenue at our optical dispensaries and a 28.8% decrease in net revenue at our marketing products business. Approximately 32% of the increase in net revenue at our optical products purchasing organization and optical laboratories is from sales to optical businesses that were divested from the company that were previously eliminated as intercompany sales. Approximately 65% 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 22.7% from $8.8 million to $6.8 million. As a percentage of net revenue, salaries, wages and benefits expense decreased from 26.0% to 20.0%. Of the decrease in salaries, wages and benefits expense approximately 64% 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 first quarter 2002.

Cost of Sales and Medical Supplies. Cost of sales and medical supplies expense increased 15.4% from $16.2 million to $18.7 million. As a percentage of net revenue, cost of sales and medical supplies expense increased from 47.4% to 54.8%. 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 52.5% of total net revenue in the first half of 2002, up from 44.9% 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 4.3% from $4.6 million to $4.4 million. As a percentage of net revenue, SG&A expense decreased from 13.6% to 13.0%. 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 first quarter 2002. Excluding those closures, SG&A expense increased 1.8% compared to the prior year due to expenses at newly acquired ASCs.

Depreciation and Amortization. Depreciation and amortization expense decreased 40.9% from $2.2 million to $1.3 million. The cessation of goodwill amortization as of January 1, 2002 contributed $495,000 of this decrease as compared to the first six 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 $184,000 of other income for the first six months of 2002 versus other expense of $660,000 in 2001. The current year income includes a $436,000 gain on the sale of a 20% interest in one of our ASCs. Excluding this gain, other expense of $252,000 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 (4.8%) as compared to the 2001 period (7.4%) as well as lower average borrowings of $15.1 million during the first half of 2002 as compared to $27.9 million during the same period of 2001.

Provision for Income Taxes. The adoption of FAS 142 reduced our effective tax rate to 40.0% from 43.5% in the first half of 2001. 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 $5.6 million and $708,000 for the six months ended June 30, 2002 and 2001, respectively. The period ended June 30, 2002 included a $1.5 million refund of 2001 estimated federal tax payments. We used $1.4 million of cash for investing activities during the first six months of 2002, which included the purchase of a majority interest in an ambulatory surgery center in Colorado Springs, CO.

During the first six months of 2002, our net borrowings under our revolving credit line decreased $13.8 million from the December 31, 2001 level, using cash generated by operations and proceeds from divestiture transactions. At June 30, 2002, we had working capital of $ 9.0 million (excluding restructuring reserves and discontinued operations).

During the first half of 2002, we completed six divestiture transactions. We received total proceeds of $7.9 million, consisting of $6.5 million in cash and $1.4 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 20% interest in one of our ASCs to two former affiliated eye care professionals during the second quarter of 2002. The cash proceeds from these transactions were used to reduce debt as required under our revolving credit facility.

At June 30, 2002, we had $6.9 million outstanding under our revolving credit facility that expires on June 30, 2003. 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 5.0% and 4.8% for three and six months ended June 30, 2002, respectively, and 3.6% at June 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. Although 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 also plan to use the funds available under our credit facility to finance acquisitions. Therefore, 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.

The sale of optical dispensary assets and one of our ambulatory surgery centers in the 2002 second quarter required the approval of our lenders under our credit facility. In addition to seeking their consent to this transaction, we also approached our lenders about other modifications to our credit facility, including an expansion of our ability to sell minority interests in our existing ambulatory surgery centers, as well as providing us with the ability to sell other optical dispensary assets as part of our divestiture transactions as we deem appropriate. After considering these requests, our lenders consented to this transaction and agreed to the other requested modifications. Previously, the terms of our credit facility limited our ability to sell minority interests in our existing ASCs to the extent any such sales reduced our overall EBITDA in any 12-month period by more than $1 million. Our lenders agreed to increase this limit from $1 million to $3 million.

In consideration for the lenders consenting to the sale of our ambulatory surgery center and approving these modifications to our credit facility, we agreed to reduce the maximum commitment available under our facility to $35 million effective as of June 13, 2002, with an additional reduction to $30 million as of October 1, 2002. Before giving effect to this amendment, the maximum commitment available under our credit facility had been $40 million, with additional quarterly reductions of $2.5 million on each of July 1, 2002 and October 1, 2002, resulting in a maximum commitment of $35 million as of October 1, 2002. As of June 30, 2002, we were in compliance with all our credit agreement covenants.

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. We also expect the cash proceeds from divestitures to supplement our cash flow.

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.

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 grow or manage our growth; our ability to acquire, develop or manage a sufficient number of profitable surgical facilities; reduced prices and reimbursement rates for surgical procedures; the continued acceptance of laser vision correction and other refractive surgical procedures; demand for elective surgical procedures generally and in response to a protracted economic downturn; our ability to successfully implement our discontinued operations plan on acceptable terms consistent with our credit facility; 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.

PART II. OTHER INFORMATION

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

We held our 2002 Annual Meeting of Stockholders on May 23, 2002 at which the stockholders voted to re-elect three Class III directors for a term of three years expiring at our 2005 Annual Meeting of Stockholders. Results of the voting were as follows:

Directors	For	Authority Withheld	Abstentions
R. Judd Jessup	15,624,552	191,788	--
Scott H. Kirk, M.D.	15,624,552	191,788	
Steven V. Napolitano	15,624,552	191,788	--

C.A. Lance Piccolo and Stephen J. Winjum continued their terms of office as directors of the Company after the 2002 Annual Meeting of Stockholders. The election of directors was the only item submitted to and voted upon by the stockholders.

Item 6. Exhibits and Reports on Form 8-K

A. Exhibits

Exhibit 10.30	Consent and Second Amendment to Second Amended and Restated Credit Agreement
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 did not file any reports on Form 8-K during the second quarter of

2002.

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	August 14, 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	August 14, 2002
Robert L. Hiatt Vice President Finance (on behalf of Registrant and as principal accounting officer)	Date