TROVER SOLUTIONS INC
Form 10-Q
August 13, 2003

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2003

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER 0-22585

TROVER SOLUTIONS, INC.
(Exact Name of Registrant as Specified in its Charter)

DELAWARE (State or Other Jurisdiction of Incorporation or Organization)	61-1141758 (I.R.S. Employer Identification No.)
1600 WATTERSON TOWER, LOUISVILLE, KENTUCKY (Address of Principal Executive Offices)	40218 (Zip Code)

(REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE)
(502) 454-1340

Indicate by check mark whether the Registrant (1) has filed all reports

required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

As of August 11, 2003, 8,448,584 shares of the Registrant's Common Stock, $0.001 par value, were outstanding.

TROVER SOLUTIONS, INC.

FORM 10-Q
JUNE 30, 2003

INDEX

		PAGE
	PART I: FINANCIAL INFORMATION	
Item 1.	Financial Statements (Unaudited)	1
	Condensed Balance Sheets as of June 30, 2003 and December 31, 2002	1
	Condensed Statements of Income for the three and six months ended June 30, 2003 and 2002	2
	Condensed Statements of Cash Flows for the six months ended June 30, 2003 and 2002	3
	Notes to Condensed Financial Statements	4
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations (Unaudited)	13
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	24
Item 4.	Controls and Procedures	24
	PART II: OTHER INFORMATION	
Item 1.	Legal Proceedings	25
Item 4.	Submission of Matters to a Vote of Security Holders	30
Item 6.	Exhibits and Reports on Form 8-K	31
Signatures		32

THIS FORM 10-Q AND OTHER STATEMENTS ISSUED OR MADE FROM TIME TO TIME BY TROVER SOLUTIONS, INC. OR MEMBERS OF ITS MANAGEMENT TEAM CONTAIN STATEMENTS WHICH MAY CONSTITUTE "FORWARD-LOOKING STATEMENTS" WITHIN THE MEANING OF THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED BY THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995, 15 U.S.C.A. SECTIONS 77Z-2 AND 78U-5 (SUPP. 1996). THOSE STATEMENTS INCLUDE STATEMENTS REGARDING THE INTENT, BELIEF OR CURRENT EXPECTATIONS OF TROVER SOLUTIONS, INC. AND MEMBERS OF ITS MANAGEMENT TEAM, AS WELL AS THE ASSUMPTIONS ON WHICH SUCH STATEMENTS ARE BASED. PROSPECTIVE INVESTORS ARE CAUTIONED THAT ANY SUCH FORWARD-LOOKING STATEMENTS ARE NOT GUARANTEES OF FUTURE PERFORMANCE AND INVOLVE RISKS AND UNCERTAINTIES, AND THAT ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE CONTEMPLATED BY SUCH FORWARD-LOOKING STATEMENTS. IMPORTANT FACTORS CURRENTLY KNOWN TO MANAGEMENT THAT COULD CAUSE ACTUAL RESULTS TO DIFFER MATERIALLY FROM THOSE IN FORWARD-LOOKING STATEMENTS ARE SET FORTH IN THE SAFE HARBOR COMPLIANCE

STATEMENT FOR FORWARD-LOOKING STATEMENTS INCLUDED AS EXHIBIT 99.1 TO THE TROVER SOLUTIONS, INC. ANNUAL REPORT ON FORM 10-K FOR THE FISCAL YEAR ENDED DECEMBER 31, 2002, AND ARE HEREBY INCORPORATED HEREIN BY REFERENCE. TROVER SOLUTIONS, INC. UNDERTAKES NO OBLIGATION TO UPDATE OR REVISE FORWARD-LOOKING STATEMENTS TO REFLECT CHANGED ASSUMPTIONS OR CIRCUMSTANCES, THE OCCURRENCE OF UNANTICIPATED EVENTS OR CHANGES TO FUTURE OPERATING RESULTS OVER TIME.

i

PART I: FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

TROVER SOLUTIONS, INC.

CONDENSED BALANCE SHEETS

(UNAUDITED)
(IN THOUSANDS, EXCEPT PER SHARE INFORMATION)

	JUNE 30, 2003	DECEMBER 31, 2002
ASSETS		
Current assets:		
Cash and cash equivalents	$ 5,675	$ 2,269
Restricted cash	19,084	17,764
Accounts receivable, less allowance for doubtful accounts of $575 at June 30, 2003 and $531 at December 31, 2002	8,134	9,389
Other current assets	2,054	2,319
Total current assets	34,947	31,741
Property and equipment, net	6,282	6,452
Goodwill, net	29,146	29,146
Identifiable intangibles, net	3,558	3,810
Other assets	2,199	2,424
Total assets	$ 76,132	$73,573
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Trade accounts payable	$ 1,157	$ 1,653
Accrued expenses	4,941	4,699
Accrued bonuses	1,802	3,208
Funds due clients	13,734	12,368
Income taxes payable	840	429
Deferred income tax liability	616	616
Total current liabilities	23,090	22,973
Other liabilities	3,239	3,151
Long-term borrowings	4,000	4,000
Total liabilities	30,329	30,124
Commitments and contingencies	--	--

Stockholders' equity:		
Preferred stock, $.001 par value; 2,000 shares authorized; no shares issued or outstanding	--	--
Common stock, $.001 par value; 20,000 shares authorized; 8,440 and 8,588 shares outstanding as of June 30, 2003 and December 31, 2002, respectively	12	12
Capital in excess of par value	23,280	23,154
Other	(957)	(926)
Treasury stock at cost; 3,260 shares at June 30, 2003 and 3,088 shares at December 31, 2002	(14,455)	(13,553)
Accumulated other comprehensive income	(83)	(87)
Unearned compensation	(33)	(39)
Retained earnings	38,039	34,888
Total stockholders' equity	45,803	43,449
Total liabilities and stockholders' equity	$ 76,132	$73,573

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

1

TROVER SOLUTIONS, INC.

CONDENSED STATEMENTS OF INCOME
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2003 AND 2002
(UNAUDITED)
(IN THOUSANDS, EXCEPT PER SHARE INFORMATION)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Claims revenues	$17,004	$17,294	$33,357	$34,762
Cost of revenues	8,388	8,368	16,731	16,849
Gross profit	8,616	8,926	16,626	17,913
Support expenses	4,967	4,994	9,449	9,893
Depreciation and amortization	849	1,229	1,811	2,517
Operating income	2,800	2,703	5,366	5,503
Interest income	40	58	90	125
Interest expense	83	125	204	264
Income before income taxes	2,757	2,636	5,252	5,364
Provision for income taxes	1,103	1,021	2,101	2,058
Net income	$ 1,654	$ 1,615	$ 3,151	$ 3,306
Earnings per common share (basic)	$ 0.20	$ 0.17	$ 0.37	$ 0.35
Earnings per common share (diluted)	$ 0.19	$ 0.17	$ 0.36	$ 0.34

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

TROVER SOLUTIONS, INC.

CONDENSED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2003 AND 2002
(UNAUDITED)
(IN THOUSANDS)

	SIX MONTHS ENDED JUNE 30,	
	2003	2002
Cash flows from operating activities:		
Net income	$ 3,151	$ 3,306
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,198	2,703
Other	10	(35)
Changes in operating assets and liabilities:		
Restricted cash	(1,313)	439
Accounts receivable	1,255	312
Other current assets	203	253
Other assets	4	(175)
Trade accounts payable	(497)	659
Accrued expenses	(1,138)	(195)
Funds due clients	1,366	(383)
Income taxes payable	411	(37)
Other liabilities	88	179
Net cash provided by operating activities	5,738	7,026
Cash flows from investing activities:		
Purchases of property and equipment	(908)	(1,309)
Capitalization of internally developed software	(592)	(981)
Net cash used in investing activities	(1,500)	(2,290)
Cash flows from financing activities:		
Line of credit repayments	--	(2,500)
Line of credit proceeds	--	800
Repurchase of common stock	(902)	(3,573)
Issuance of common stock	100	104
Other	(30)	(32)
Net cash used in financing activities	(832)	(5,201)
Net increase (decrease) in cash and cash equivalents	3,406	(465)
Cash and cash equivalents, beginning of period	2,269	2,547
Cash and cash equivalents, end of period	$ 5,675	$ 2,082

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

TROVER SOLUTIONS, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS
(UNAUDITED)

1. ORGANIZATION AND BASIS OF PRESENTATION

Trover Solutions, Inc. (hereinafter referred to as the "Company"), a Delaware corporation, was incorporated on June 30, 1988. The Company provides subrogation and certain other claims recovery and cost containment services, on an outsourcing basis, to the private healthcare payor industry and the property and casualty insurance industry. Its primary business is medical claims recovery, and its primary product is subrogation recovery, i.e., the Company identifies, investigates and recovers accident-related medical benefits incurred by its healthcare payor and insurance clients on behalf of their insureds, but for which other persons or entities have primary responsibility. The Company's clients' rights to recover the value of these medical benefits, arising by law or contract, are generally known as the right of subrogation and are generally paid from the proceeds of liability or workers' compensation insurance. The Company's other medical claims recovery services include (1) the auditing of the bills of medical providers, particularly hospitals, for accuracy, correctness and compliance with contract terms ("provider bill audit"), (2) the recovery of overpayments attributable to duplicate payments, failures to coordinate benefits and similar errors in payment ("overpayments"), and (3) the auditing of physician evaluation and management claims for consistency with medical records, in accordance with federal guidelines ("MD Audit").

The accompanying financial statements are presented in a condensed format and consequently do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America or those normally made in the Company's annual financial statements. Accordingly, for further information, the reader of this Form 10-Q may wish to refer to the Company's audited financial statements as of and for the year ended December 31, 2002, contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2002, filed with the Securities and Exchange Commission on March 27, 2003.

The financial information has been prepared in accordance with the Company's customary accounting practices and is unaudited. In the opinion of management of the Company, the information presented reflects all adjustments necessary for a fair presentation of interim results. All such adjustments are of a normal and recurring nature.

2. STOCK-BASED COMPENSATION

In December 2002, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 148, "Accounting for Stock-Based Compensation -- Transition and Disclosure -- an Amendment of SFAS 123" which provides alternative methods for a voluntary change to the fair value method of accounting for stock-based compensation and amends the disclosure requirements of SFAS 123. The Company has elected to continue to account for its stock-based compensation plans under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB No. 25), and related interpretations. The following disclosures are provided in accordance with SFAS 148.

The Company has various stock-based compensation plans including stock option plans and an employee stock purchase plan. No stock-based employee compensation cost is reflected in net income as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the

Company had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" to stock-based employee compensation (dollars in thousands, except per share results):

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Net income as reported	$1,654	$1,615	$3,151	$3,306
Less: total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(71)	(168)	(226)	(426)
Proforma net income	$1,583	$1,447	$2,925	$2,880
Earnings per common share:				
As reported (basic)	$ 0.20	$ 0.17	$ 0.37	$ 0.35
As reported (diluted)	0.19	0.17	0.36	0.34
Proforma (basic)	0.19	0.16	0.35	0.30
Proforma (diluted)	0.18	0.15	0.34	0.29

3. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In November 2002, the FASB issued EITF 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables" which addresses revenue recognition accounting by a vendor for arrangements under which it will perform multiple revenue-generating activities. The provisions of this statement are effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. The Company is evaluating the effect that EITF 00-21 may have on its financial statements.

In January 2003, the FASB issued FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51". FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective for all new variable interest entities created or acquired after January 31, 2003. For variable interest entities created or acquired prior to February 1, 2003, the provision of FIN 46 must be applied for the first interim or annual period beginning after June 15, 2003. The Company does not have any variable interest entities as defined under FIN 46.

In April 2003, the FASB issued SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" which amends and clarifies the accounting guidance on derivative instruments and hedging activities that fall within the scope of SFAS 133, "Accounting for Derivative Instruments and Hedging Activities". SFAS 149 is effective (1) for contracts entered into or modified after June 30, 2003, with certain exceptions, and (2) for hedging relationships designated after June 30, 2003. The Company will apply the provisions of SFAS 149 to contracts entered into or hedging relationships designated after June 30, 2003.

In May 2003, the FASB issued SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" which establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective for the Company on July 1, 2003. The adoption of SFAS 150 did not have a significant impact on the Company's financial statements.

4. EARNINGS PER COMMON SHARE

Reconciliations of the average number of common shares outstanding used in the calculation of earnings per common share and earnings per common share assuming dilution are as follows (dollars and shares in thousands, except per share results):

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Weighted average number of common shares outstanding	8,438	9,319	8,456	9,533
Add: Dilutive stock options	280	277	260	290
Number of common shares outstanding (diluted)	8,718	9,596	8,716	9,823
Net earnings for earnings per common share (basic and diluted)	$1,654	$1,615	$3,151	$3,306
Earnings per common share:				
Basic	$ 0.20	$ 0.17	$ 0.37	$ 0.35
Diluted	$ 0.19	$ 0.17	$ 0.36	$ 0.34

Basic earnings per common share were computed based on the weighted-average number of shares outstanding during the period. The dilutive effect of stock options was calculated using the treasury stock method. Options to purchase 921,367 and 940,617 shares for the three and six months ended June 30, 2003, respectively, were not included in the computation of diluted earnings per

common share because their effect would be anti-dilutive.

5. INCOME TAXES

For the three and six months ended June 30, 2003, the Company accrued income taxes at a 40.0% effective tax rate. This is a reduction from the Company's pre-2002 historical effective tax rate due to the implementation of state tax planning initiatives beginning July 1, 2002.

The Company accrued income taxes at a 38.7% and 38.4% effective tax rate during the three and six months ended June 30, 2002, respectively, due to non-recurring research and experimental tax credits of $72,500 and $167,500, respectively.

6. RELATED PARTY TRANSACTIONS

The Company has entered into a contract for legal services with a professional service corporation, Sharps & Associates, PSC, an entity owned solely by one of the Company's officers, Douglas R. Sharps. This arrangement exists solely for the benefit of the Company. Its purpose is to minimize the costs of legal services purchased by the Company on behalf of its clients. Mr. Sharps receives no financial or other personal benefit from his ownership of the firm. All payments to Sharps & Associates, PSC are reviewed and approved by the Audit Committee of the Company's Board of Directors. For the three and six months ended June 30, 2003, approximately $827,000 and $1,657,000, respectively, was paid to this law firm for such legal services, including all employees and expenses. For the three and six months ended June 30, 2002, the Company paid this law firm approximately $822,000 and $1,656,000, respectively, for legal services.

On February 12, 1999, the Board of Directors approved a loan in the amount of $350,000 to Patrick B. McGinnis, the Chairman and Chief Executive Officer of the Company, in exchange for a full recourse promissory note in the same amount from Mr. McGinnis. On June 30, 2000, at the direction of the Board of

Directors and in accordance with terms authorized by it, the Company loaned Mr. McGinnis an additional $500,000. Under these terms, the $500,000 loan to Mr. McGinnis was combined with his existing debt to the Company of $350,000 of principal and $36,520 of accrued interest. Mr. McGinnis delivered to the Company his full recourse promissory note in the amount of $886,520, bearing interest at a fixed rate of 6.62% per annum, compounded annually (the "Amended Promissory Note"), and the Company cancelled the old promissory note evidencing the prior debt. The Amended Promissory Note provides for mandatory prepayments from certain of the proceeds received by Mr. McGinnis from his sale of the Company's securities and any related transactions. At June 30, 2003 and December 31, 2002, the promissory note of $886,520 and accrued interest of $70,321 and $39,908, respectively, were outstanding. Mr. McGinnis used the proceeds of these loans to repay debts originally incurred by him to pay income taxes related to the ordinary income deemed to have been received by him on account of common stock granted to him by the former shareholder of the Company in connection with the initial public offering of the Company's stock in May 1997, and to purchase additional stock in the initial public offering.

On June 30, 2000, pursuant to Board authorization and in accordance with the terms of the Amended Promissory Note, the Company and Mr. McGinnis entered into a deferred compensation agreement (the "Agreement"). Under the Agreement,

50% of the amount otherwise payable to Mr. McGinnis under the Company's Management Group Incentive Compensation Plan is to be deferred until the Amended Promissory Note is paid in full, with such deferred compensation then being paid in full to Mr. McGinnis within 30 days thereafter. The Company has full right of set-off against any deferred compensation under the Agreement should Mr. McGinnis default under the Amended Promissory Note. At the election of Mr. McGinnis, the payment of the deferred compensation, upon payment of the Amended Promissory Note, may be extended for a period of not more than ten years. At June 30, 2003, the amount of deferred compensation was $182,012, with accrued interest of $12,958. At December 31, 2002, the amount of deferred compensation was $72,354 with accrued interest of $7,627.

Effective January 1, 2003, the Company entered into an employment agreement with Mr. McGinnis. Upon signing the employment agreement, Mr. McGinnis received a bonus of $200,000. The bonus is subject to full or partial reimbursement by Mr. McGinnis to the Company, based on the date of termination, if Mr. McGinnis terminates his employment with the Company during the initial three-year term of his employment. The bonus payment was recorded in "Other Current Assets" on the accompanying Condensed Balance Sheets and is being amortized over the term of the agreement. The balance at June 30, 2003 and December 31, 2002 was approximately $167,000 and $200,000, respectively.

7. PROPERTY AND EQUIPMENT

The property and equipment consists of the following at June 30, 2003 and December 31, 2002 (in thousands):

	JUNE 30, 2003	DECEMBER 31, 2002
Property and equipment, at cost:		
Furniture and fixtures	$ 3,270	$ 3,260
Office equipment	2,056	2,067
Computer equipment	12,033	11,611
Software	10,321	9,584
Leasehold improvements	1,750	1,429
	29,430	27,951
Accumulated depreciation and amortization	(23,148)	(21,499)
Property and equipment, net	$ 6,282	$ 6,452

8. GOODWILL AND OTHER INTANGIBLE ASSETS

Effective January 1, 2002, the Company adopted FAS 142 under which goodwill is no longer amortized but instead will be assessed for impairment at least annually. The Company performs its annual impairment review during the second quarter of each year. The review performed during the quarter ended June 30, 2003 did not result in an impairment charge for the Company. The Company's reporting units are generally consistent with the operating segments underlying the segments identified in Note 15 "Segment Information". All recorded goodwill

and other intangible assets relate to the Healthcare Recovery Services segment.

The carrying value of goodwill, net was approximately $29.1 million at June 30, 2003 and December 31, 2002. There were no goodwill impairment losses recorded during the three and six months ended June 30, 2003.

All of the Company's intangible assets (other than goodwill, net) are subject to amortization. The details of the Company's intangible assets at June 30, 2003 and December 31, 2002 are as follows (in thousands):

	JUNE 30, 2003			DECEMBER 31, 2002		
	COST	ACCUMULATED AMORTIZATION	NET	COST	ACCUMULATED AMORTIZATION	NE
Client lists	$4,900	$1,436	$3,464	$4,900	$1,272	$3,
Backlog	570	504	66	570	447	
Non-compete agreements	530	502	28	530	471	
Total	$6,000	$2,442	$3,558	$6,000	$2,190	$3,

Client lists are being amortized on a straight-line basis over 15 years. Backlog is being amortized over 5 years on a straight-line basis. Non-compete agreements are being amortized on a straight-line basis over periods ranging from 4 years to 5 years.

Amortization expense related to intangible assets for the three and six months ended June 30, 2003 was approximately $122,000 and $253,000, respectively. Over the six months ended December 31, 2003 and each

of the four succeeding fiscal years, amortization expense related to intangible assets is expected to be as follows (in thousands):

Six months ended December 31, 2003	$243
Year ended December 31,:	
2004	340
2005	327
2006	327
2007	327

9. DERIVATIVES

On November 6, 2001, the Company entered into an interest rate swap contract to pay 3.66% and to receive the one-month LIBOR rate on a $4 million notional amount of the Revolving Credit Facility. The Company uses derivative financial instruments to manage the risk that changes in interest rates will affect the amount of its future interest payments. Under the interest rate swap contract, the Company agrees to pay an amount equal to a specified fixed rate of

interest times a notional principal amount, and to receive in return an amount equal to a variable rate of interest times the same notional principal amount. The notional amounts of the contract are not exchanged. No other cash payments are made unless the contract is terminated prior to maturity, in which case the amount paid or received in settlement is established by agreement at the time of termination, and represents the net present value, at current rates of interest, of the remaining obligations to exchange payments under the terms of the contract. The interest rate swap contract was entered into with a major financial institution in order to minimize counterparty credit risk. The interest rate swap transaction qualifies for hedge accounting treatment and is accounted for in accordance with FAS 133, "Accounting for Derivative Instruments and Hedging Activities", as amended by FAS 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities -- an Amendment of FAS 133". At June 30, 2003, the fair value of the hedge was a liability of $138,532 ($83,119, net of tax, is included in Accumulated Other Comprehensive Income (Loss)). At December 31, 2002, the fair value of the hedge was a liability of $144,804 ($86,882, net of tax, is included in Accumulated Other Comprehensive Income (Loss)).

10. CREDIT FACILITY

On November 1, 2001, the Company entered into a revolving credit facility with National City Bank of Kentucky, Bank One Kentucky, N.A. and Fifth Third Bank (the "Revolving Credit Facility"), and the existing Credit Facility was terminated. The Company's obligations under the Revolving Credit Facility are secured by substantially all of the Company's assets, subject to certain permitted exceptions. The Revolving Credit Facility carries a maximum borrowing capacity of $40 million and will mature October 31, 2004. Principal amounts outstanding under the Revolving Credit Facility bear interest at a variable rate based on the Prime Rate or Eurodollar Rate, as applicable, plus a pre-determined fixed margin. At June 30, 2003 and December 31, 2002, the interest rate was 3.06% and 3.19%, respectively, based on the one-month Eurodollar Rate plus the fixed margin. The Revolving Credit Facility contains customary covenants and events of default including, but not limited to, financial tests for interest coverage, net worth levels and leverage that may limit the Company's ability to pay dividends. It also contains a material adverse change clause. At June 30, 2003 and December 31, 2002, $4 million was outstanding under the Revolving Credit Facility.

11. CONTINGENCIES

The Company is engaged in the business of identifying and recovering subrogation and related claims of its clients, many of which arise in the context of personal injury lawsuits. As such, the Company operates in a litigation-intensive environment. The Company has been, from time to time, and in the future expects to be,

named as a party in litigation incidental to its business operations. To date, the Company has not been involved in any litigation which resulted in a material adverse effect upon the Company, but there can be no assurance that pending litigation or future litigation will not have a material adverse effect on the Company's business, results of operations or financial condition.

12. STOCK REPURCHASE PLAN

The Company's Board of Directors authorized the repurchase of up to $20

million of the Company's Common Stock in the open market at prices per share deemed favorable by the Company. Shares may be repurchased using cash from operations and borrowed funds and may continue until such time as the Company has repurchased $20 million of the Company's Common Stock or until it otherwise terminates the stock repurchase plan. The Company did not repurchase any common stock during the three months ended June 30, 2003. The Company repurchased 172,622 shares of common stock during the six months ended June 30, 2003 at a cost of $0.9 million, or an average price of $5.23 per share. From inception of the program through June 30, 2003, the Company repurchased 3,269,630 shares at a cost of $14.5 million, or an average cost of $4.43 per share. Except for 9,397 shares previously repurchased but reissued in connection with an employee restricted stock award, all of the reacquired shares of Common Stock through June 30, 2003 are reflected as treasury stock on the accompanying Condensed Balance Sheets (Unaudited).

13. OTHER COMPREHENSIVE INCOME (LOSS)

Other comprehensive income (loss) for the three and six months ended June 30, 2003 and 2002 consists of the following (in thousands):

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Net income	$1,654	$1,615	$3,151	$3,306
Other comprehensive income (loss):				
Deferred gain (loss) on cash flow hedge, net	4	(56)	4	(43)
Comprehensive income	$1,658	$1,559	$3,155	$3,263

Accumulated other comprehensive (loss) income consists of the following:

	CASH FLOW HEDGE
Balance, December 31, 2002	$(87)
First quarter 2003 change	--
Balance, March 31, 2003	(87)
Second quarter 2003 change	4
Balance, June 30, 2003	$(83)

14. CONCENTRATION OF CLIENTS AND CREDIT RISK

The Company has two clients that individually comprise more than 10% of the Company's revenue. The Company's largest source of revenue is UnitedHealth Group ("UHG"). For the three and six month periods ended June 30, 2003, UHG generated 23% and 26% of the Company's revenues, respectively. Wellpoint Health Network Inc. accounted for 16% and 15% of the Company's total revenues for the three and six months ended June 30, 2003, respectively, as well as 41% and 32% of the

Company's accounts receivable

balance at June 30, 2003 and December 31, 2002, respectively. Health Net, Inc. accounted for 8% and 15% of the Company's accounts receivable balance at June 30, 2003 and December 31, 2002, respectively.

During 2002, UHG management informed the Company of its intention to terminate subrogation services with respect to all but 1.8 million lives of the 9.7 million lives then subject to the Company's services under a contract with UHG. UHG's termination of these services resulted from its decision to bring subrogation recovery services back inside UHG, where they will be performed by its Ingenix strategic business unit. The Company expects to continue recovering on the backlog as to which UHG terminated the Company's services, a process that the Company expects will be completed in 5 to 6 years. The Company's contract with UHG expired in accordance with its terms on February 1, 2003, except with respect to 1.8 million lives as to which the Company continues to provide healthcare subrogation recovery services.

15. SEGMENT INFORMATION

The accounting policies of the Company's reportable segments are the same as those accounting policies described in the summary of significant accounting policies in the Company's Annual Report on Form 10-K for the year ended December 31, 2002. The Company has three reportable segments based on qualitative guidelines. The Company's three segments are: (1) Healthcare Recovery Services, which encompasses its four healthcare recovery products: healthcare subrogation, provider bill audit, overpayments and MD Audit; (2) Property and Casualty Recovery Services, which is subrogation recovery services for property and casualty insurers, sold under the name TransPaC Solutions; and (3) Software, which is subrogation recovery software in a browser-based application service provider (ASP) form. The segment profit measure is income before income taxes.

Segment results for the three and six months ended June 30, 2003 and 2002 are as follows (in thousands):

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Claims revenues:				
Healthcare Recovery Services	$16,713	$17,178	$32,820	$34,579
Property and Casualty Recovery Services	276	116	505	183
Software	405	165	718	280
Elimination of intercompany revenue	(390)	(165)	(686)	(280)
Total claims revenues	$17,004	$17,294	$33,357	$34,762
Operating income (loss):				
Healthcare Recovery Services	$ 7,257	$ 7,144	$14,010	$14,316
Property and Casualty Recovery Services	(188)	(284)	(420)	(577)
Software	(147)	(209)	(380)	(370)
Unallocated Corporate support expenses	(4,122)	(3,948)	(7,844)	(7,866)

Total operating income	$ 2,800	$ 2,703	$ 5,366	$ 5,503

TROVER SOLUTIONS, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS -- (CONTINUED)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Depreciation and amortization:				
Healthcare Recovery Services	$ 682	$ 1,059	$ 1,469	$ 2,177
Property and Casualty Recovery Services	22	27	45	54
Software	11	11	24	25
Unallocated Corporate depreciation and amortization expense	134	132	273	261
Total depreciation and amortization	$ 849	$ 1,229	$ 1,811	$ 2,517
Income (loss) before income taxes:				
Healthcare Recovery Services	$ 7,260	$ 7,156	$14,027	$14,337
Property and Casualty Recovery Services	(196)	(295)	(438)	(595)
Software	(172)	(243)	(435)	(432)
Unallocated Corporate expenses and other charges	(4,135)	(3,982)	(7,902)	(7,946)
Total income before income taxes	$ 2,757	$ 2,636	$ 5,252	$ 5,364

Unallocated Corporate amounts include corporate expenses and other miscellaneous charges. Because this category includes a variety of miscellaneous items not attributable to one particular segment, it is subject to fluctuation on a quarterly and annual basis. The Company does not allocate assets.

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

The Company believes it is a leading independent provider of outsourcing of subrogation and certain other medical claims recovery and cost containment services to the private healthcare payor industry in the United States, based on the Company's experience and assessment of its market. The Company's primary business is medical claims recovery and its primary product is subrogation recovery, which generally entails the identification, investigation and recovery of accident-related medical benefits incurred by its clients on behalf of their insureds, but for which other persons or entities have primary responsibility. The Company's clients' rights to recover the value of these medical benefits, arising by law or contract, are known generally as the right of subrogation and are generally paid from the proceeds of liability or workers' compensation

insurance. The Company's other medical claims recovery services include (1) the auditing of the bills of medical providers, particularly hospitals, for accuracy, correctness and compliance with contract terms ("provider bill audit"), (2) the recovery of overpayments attributable to duplicate payments, failures to coordinate benefits and similar errors in payment ("overpayments"), and (3) the auditing of physician evaluation and management claims for consistency with medical records, in accordance with federal guidelines ("MD Audit"). The Company offers its healthcare recovery services on a nationwide basis to health maintenance organizations ("HMOs"), indemnity health insurers, self-funded employee health plans, companies that provide claims administration services to self-funded plans (referred to as "third-party administrators"), Blue Cross and Blue Shield organizations and provider organized health plans. Current clients include Humana Inc., Kaiser Permanente, Wellpoint Health Network Inc., and The Principal Financial Group. The Company had 35.2 million and 42.4 million lives under contract from its clientele at June 30, 2003 and 2002, respectively.

The Company has three segments: (1) Healthcare Recovery Services, which encompasses its four healthcare recovery products: healthcare subrogation, provider bill audit, overpayments and MD Audit; (2) Property and Casualty Recovery Services, which is subrogation recovery services for property and casualty insurers, sold under the name TransPaC Solutions; and (3) Software, which is subrogation recovery software in a browser-based application service provider (ASP) form.

HEALTHCARE RECOVERY SERVICES

OVERVIEW OF OPERATIONS

For a typical new healthcare subrogation or other medical claims recovery client, it takes up to six months from the contract signing (when the lives are "sold") to complete the construction of electronic data interfaces necessary for the Company to begin providing service. At this point, the client is considered "installed." During the installation period, the Company must also hire and train quality staff necessary to provide contractual services. After installation, the Company receives files and data from the client from which it creates an inventory of backlog.

"Backlog" is the total dollar amount of potentially recoverable claims that the Company is pursuing or auditing on behalf of its clients at a given point in time. These claims are gross figures, prior to estimates of claim settlements and rejections. Backlog increases when the Company opens new files of potentially recoverable claims and decreases when files are recovered and closed or, after further investigation, determined to be nonrecoverable. Backlog for a client will range from newly identified potential recoveries to potential recoveries that are in the late stages of the recovery process. Historically, recoveries (the amount actually recovered for the Company's clients prior to the Company's fee) have been produced from backlog in a generally predictable cycle. Any group of potential recoveries, sufficiently large in number to display statistically significant characteristics and that originates from a defined time period, tends to produce recovery results that are comparable to other groups having similar characteristics.

For the most part, the Company is paid contingency fees from the amount of claims recoveries it makes from backlog or recoveries it identifies through other cost containment and related recovery services on behalf of its clients. The Company's revenues are a function of recoveries and effective fee rates. Effective fee rates vary depending on the mix between services provided and client fee schedules. The fee schedules for each

client are separately negotiated and reflect the Company's standard fee rates, the services to be provided and the anticipated volume of services. The Company grants volume discounts and, for its recovery services, negotiates a lower fee when it assumes backlog from a client because the client will have already completed some of the recovery work. Because the Company records expenses as costs are incurred and records revenues only when a file is settled, there is a lag between the recording of expenses and related revenue recognition.

The Company's expenses are determined primarily by the number of employees directly engaged in recovery activities ("cost of revenues") and by the number of employees engaged in a variety of support activities ("support expenses"). Recovery personnel must be hired and trained in advance of the realization of recoveries and revenues. Historically, support expenses have not grown in direct proportion to revenues.

RESULTS OF OPERATIONS

The following tables present certain key operating indicators for the Healthcare Recovery Services segment for the periods indicated (lives and dollars in millions):

HEALTHCARE RECOVERY SERVICES -- KEY OPERATING INDICATORS

LIVES SOLD AND INSTALLED*

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Cumulative lives sold, beginning of period	34.3	46.4	41.6	49.1
Lives from existing client loss, net(1)	(0.2)	(4.3)	(7.6)	(8.2)
Lives added from new contracts with existing clients	1.0	0.1	1.1	0.8
Lives added from contracts with new clients	0.1	0.2	0.1	0.7
Cumulative lives sold, end of period	35.2	42.4	35.2	42.4
Lives sold eliminations/cross-sold lives(2)	14.4	5.7	14.4	5.7
Lives installed, end of period	32.2	41.7	32.2	41.7
Lives installed eliminations/cross-installed lives(3)	5.7	4.0	5.7	4.0

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* All references to "lives" in the table, whether reported as from existing client loss, added from new contracts with existing clients or with new clients, lives sold, lives sold eliminations/cross-sold, lives installed, or lives installed eliminations/cross-installed lives, are derived by the Company from information provided to it by clients, which may contain estimates.

(1) Represents the net of losses from contract terminations and organic declines in the clients' installed base measured in the number of persons covered by

clients, and gains from organic growth in the clients' installed base measured in the number of persons covered by clients.

(2) "Lives sold eliminations/cross-sold lives" specifies the number of lives subject to client contracts under which the Company provides or will provide more than one healthcare recovery service to a client population. By contrast, the number of lives reported in "Cumulative lives sold, end of period" does not include the overlap (i.e., "double counting") that occurs when multiple healthcare recovery services are provided to the same client population.

(3) "Lives installed eliminations/cross-installed lives" specifies the number of lives as to which the Company provides more than one healthcare recovery service to a client population. By contrast, the number of lives reported in "Lives installed, end of period" does not include the overlap (i.e., "double counting") that occurs when multiple healthcare recovery services are provided to the same client population.

14

OTHER KEY OPERATING INDICATORS

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Backlog(1)	$1,570.6(2)	$1,532.6(2)	$1,570.6(2)	$1,532.6(2)
Claims recoveries	$ 60.5	$ 61.4	$ 118.3	$ 125.4
Throughput(3)	3.8%	4.2%	7.6%	8.5%
Effective fee rate	27.6%	28.0%	27.7%	27.7%
Claims revenues	$ 16.7	$ 17.2	$ 32.8	$ 34.6

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(1) Backlog is the total dollar amount of potentially recoverable claims that the Company is pursuing or auditing on behalf of its clients at a given point in time.

(2) At June 30, 2003 and 2002, approximately $329.9 million and $401.9 million, respectively, of the backlog derived from terminated clients and clients that, by that date, had given notice of termination. See "Concentration of Clients".

(3) Throughput equals claims recoveries for the period divided by the average of backlog at the beginning and end of the period.

THREE AND SIX MONTHS ENDED JUNE 30, 2003 COMPARED TO THREE AND SIX MONTHS ENDED JUNE 30, 2002

Claims Revenues. Total Healthcare Recovery Services revenues for the quarter ended June 30, 2003 decreased 2.7%, to $16.7 million from $17.2 million for the same quarter of 2002, and for the six month period ended June 30, 2003, decreased 5.1%, to $32.8 million from $34.6 million in the comparable period of 2002. Healthcare claims recoveries for the quarter ended June 30, 2003 were $60.5 million, a decrease of $0.9 million, or 1.5%, compared to $61.4 million for the same quarter of 2002. For the six month period ended June 30, 2003,

healthcare claims recoveries decreased 5.7%, to $118.3 million from $125.4 million in the comparable period of 2002. The lower recoveries resulted from two causes. The first cause is lower throughput (i.e., yield) from the healthcare subrogation backlog attributable to a shift in its composition, increasingly composed of files from terminated clients. The portion of that backlog derived from terminated clients exhibits a lower throughput rate than does the portion of the backlog derived from active clients, whose files are replenished on an on-going basis. Second, the Healthcare Recovery Services segment had fewer installed lives during the three and six months ended June 30, 2003 because of attrition from client terminations, including the UnitedHealth Group termination (see "Concentration of Clients"), and organic losses of client lives.

The Healthcare Recovery Services effective fee rate for the quarter ended June 30, 2003 decreased to 27.6% from 28.0% for the same quarter of 2002, and remained at 27.7% for the six month period ended June 30, 2003, the same as the comparable period in 2002. The slight decrease in fee rate for the quarter ended June 30, 2003 was primarily attributable to a decrease in the effective fee rate for the provider bill audit division, due to a special audit project performed in the quarter ended June 30, 2002, which had a higher fee rate.

Backlog for the Healthcare Recovery Services segment increased to $1,570.6 million at June 30, 2003 from $1,532.6 million at June 30, 2002, an increase of 2.5%. The provider bill audit services backlog increased approximately $87.8 million while the healthcare subrogation backlog decreased approximately $52.3 million.

The Healthcare Recovery Services segment had a throughput rate of approximately 3.8% and 4.2% of average backlog during the second quarter of 2003 and 2002, respectively. The decrease in throughput from the quarter ended June 30, 2002 is primarily the effect of a shift in the backlog mix, with a greater percentage of backlog and recoveries coming from provider bill audit, which typically exhibits a lower throughput rate than does healthcare subrogation. Throughput for the six month period ended June 30, 2003 also decreased to 7.6% from 8.5% for the comparable period in 2002, for the same reason described above. Lives installed decreased 9.5 million from 41.7 million at June 30, 2002 to 32.2 million at June 30, 2003 primarily because of the lives lost relating to terminations by UnitedHealth Group. See "Concentration of Clients".

Cost of Revenues. Cost of revenues for the Healthcare Recovery Services segment decreased 2.5% for the quarter ended June 30, 2003 to $7.8 million, from $8.0 million for the same quarter in 2002, and was $15.5 million for the six months ended June 30, 2003, a decrease of 3.7% from $16.1 million for the same period in 2002. As a percentage of claims revenues, cost of revenues increased to 46.5% for the quarter ended June 30, 2003 compared to 46.4% for the same quarter in 2002. For the six months ended June 30, 2003, cost of revenues as a percentage of claims revenues increased to 47.3% from 46.6% in 2002, due primarily to a greater percentage of the revenue and recoveries coming from the provider bill audit division. The provider bill audit product has a lower gross margin than does the healthcare subrogation product.

Support Expenses. Support expenses for the Healthcare Recovery Services segment were $1.0 million for the quarters ended June 30, 2003 and 2002, and were $1.8 million for the six months ended June 30, 2003 compared to $2.0 million for the comparable period in 2002. Support expenses increased as a percentage of claims revenues from 5.9% for the second quarter of 2002 to 6.0% for the same quarter in 2003. For the six months ended June 30, 2003, support expenses as a percentage of claims revenues were 5.5%, a decrease from 5.7% for the comparable period in 2002. The decrease in support expenses resulted primarily from a decrease in incentive compensation in the six months ended June

30, 2003 as compared to the six months ended June 30, 2002.

PROPERTY AND CASUALTY RECOVERY SERVICES

OVERVIEW OF OPERATIONS

The Company operates in the subrogation outsourcing market that serves property and casualty ("P&C") insurers. The Company offers its services to the P&C market under the brand name "TransPaC Solutions".

The Company believes that the market for P&C subrogation outsourcing in the United States is substantial and that the potential savings from subrogation recoveries will vary depending upon the P&C line of business. The Company believes that total potential subrogation recoveries in the automobile insurance market exceed $6 billion per year. Based on its research and early experience, the Company believes that there is an opportunity to increase total subrogation recoveries across a wide spectrum of automobile insurers. The Company's marketing strategy is to offer its services to automobile insurers and multi-lines carriers that lack the resources to maximize subrogation recoveries.

The Company believes that it has an opportunity to leverage its healthcare subrogation expertise and resources to provide service to the P&C markets. The primary difference between the two markets is in the acquisition of claims data for investigation of subrogation potential. The P&C industry does not have standard data definitions regarding claims as does the health insurance industry. Nevertheless, the Company used its healthcare subrogation expertise to build data interfaces with several of its P&C customers, and it has created proprietary business processes to acquire paper-based and/or imaged claims data from its customers' claims adjusting offices and archives.

The Company has assessed the competitive environment for P&C subrogation outsourcing and believes that the competition is fragmented and characterized by claims adjusting companies that operate on a local or regional basis and by law firms that specialize in a low volume of legally complex subrogation claims. The Company has identified three competitors that attempt to serve a national market. Two of these competitors are owned and controlled by P&C insurers, and the Company believes that this fact may deter potential buyers of these competitors' services if those potential buyers also compete against the competitors' parent organizations.

The Company currently provides subrogation outsourcing services to 18 P&C insurers, of which 3 are full outsource clients with the remainder being clients for either referral services, in which the Company supplements the capacity of an internal recovery unit, or closed claims reviews, in which the Company recovers subrogation claims missed or ignored by an internal recovery unit. The Company has established a full-time direct sales force of four individuals experienced in P&C sales and marketing. The Company's target

market for its P&C subrogation services is P&C insurers that are personal lines automobile carriers or that are multi-lines carriers which focus on automobile coverage, as well as entities that self-insure P&C liabilities and third party administrators of P&C claims.

RESULTS OF OPERATIONS

The following tables present certain key operating indicators for the Property and Casualty Recovery Services segment for the periods indicated (dollars in millions):

PROPERTY AND CASUALTY RECOVERY SERVICES -- KEY OPERATING INDICATORS

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Contracts in Force, beginning of period	30	21	27	14
Outsourcing(1)	--	1	1	1
Referrals/Closed Claims(2)	1	5	4	12
Terminations	(2)	--	(3)	--
Contracts in Force, end of period	29	27	29	27

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(1) Outsourcing refers to the full replacement of a client's internal subrogation recovery function by TransPaC Solutions, typically with a view to an ongoing relationship of indefinite period.

(2) Referrals and Closed Claims refer to project-related work assumed by TransPaC Solutions, typically with files transmitted by clients from time to time.

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Backlog(1)	$16.3	$9.5	$16.3	$9.5
Claims recoveries	$ 1.3	$0.4	$ 2.4	$0.7
Throughput(2)	7.8%	5.4%	15.2%	11.1%
Effective fee rate	21.6%	26.1%	21.0%	25.2%
Claims revenues	$ 0.3	$0.1	$ 0.5	$0.2

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(1) Backlog is the total dollar amount of potentially recoverable claims that the Company is pursuing on behalf of its clients at a given point in time.

(2) Throughput equals claims recoveries for the period divided by the average of backlog at the beginning and end of the period.

THREE AND SIX MONTHS ENDED JUNE 30, 2003 COMPARED TO THREE AND SIX MONTHS ENDED JUNE 30, 2002

Claims Revenues. Total Property and Casualty Recovery Services revenues for the quarter ended June 30, 2003 increased approximately $160,000, or 138%, from the same quarter in 2002 and increased 176% to $505,000 for the six month period ended June 30, 2003 from $183,000 in the comparable period of 2002. Property and Casualty Recovery Services claims recoveries for the quarter ended June 30, 2003 were $1.3 million, an increase of $0.9 million over the same

quarter in 2002. For the six months ended June 30, 2003, claims recoveries increased 243% to $2.4 million from $0.7 million during the comparable period in 2002.

The Property and Casualty Recovery Services effective fee rate for the quarter ended June 30, 2003 decreased to 21.6% from 26.1% for the same quarter of 2002 and decreased to 21.0% for the six months ended June 30, 2003 as compared to 25.2% for the same period in 2002. The decrease in fee rate was primarily

attributable to the change in mix of referral and closed claim contracts, which typically bear higher fees, and full outsourcing contracts, which typically bear lower fees, that occurred over the past eighteen months.

Backlog. Backlog for the Property and Casualty Recovery Services segment increased to $16.3 million at June 30, 2003 from $9.5 million at June 30, 2002 due to a significant outsourcing contract which was entered into in late June 2002.

The Property and Casualty Recovery Services segment had a throughput rate of approximately 7.8% and 5.4% of average backlog during the second quarter of 2003 and 2002, respectively. Throughput for the six month period ended June 30, 2003 also increased to 15.2% from 11.1% for the comparable period of 2002. The increases were due to recoveries growing more quickly than the average backlog over the three and six month periods ended June 30, 2003.

Cost of Revenues. Cost of revenues for the Property and Casualty Recovery Services segment increased 33% for the quarter ended June 30, 2003 to $0.4 million, from $0.3 million for the same quarter in 2002, and was $0.7 million for the six months ended June 30, 2003, an increase of 40% from $0.5 million for the same period in 2002. The increase in cost of revenues results from production expenses that are incurred prior to the recognition of revenue, which reflects the nature of the subrogation business. As a percentage of claims revenues, cost of revenues decreased to 129% for the quarter ended June 30, 2003 compared to 218% for the same quarter in 2002. For the six months ended June 30, 2003, the cost of revenues as a percentage of revenue decreased to 138% from 263% in 2002. The decrease in cost of revenues as a percentage of claims revenues resulted from the increase in revenue described above.

Support Expenses. Support expenses for the Property and Casualty Recovery Services segment were $0.1 million for the quarters ended June 30, 2003 and 2002, and were $0.2 million for the six months ended June 30, 2003 and 2002. Support expenses decreased as a percentage of claims revenues from 103% for the second quarter of 2002 to 31% for the same quarter in 2003. For the six months ended June 30, 2003, support expenses as a percentage of claims revenues were 36%, a decrease from 123% in the comparable period of 2002. The decrease in support expenses as a percentage of claims revenues resulted from the increase in revenue described above.

SOFTWARE

OVERVIEW OF OPERATIONS

The Company has developed a web-enabled subrogation software application. The Company sells this product as an application service provider ("ASP"), under the trade name "Troveris", to participants in both the health insurance and benefits market and the P&C market which historically have not outsourced subrogation recoveries. The Company currently estimates that 40% to 50% of the private health insurance and health benefits markets do not outsource

subrogation recoveries. Public sector markets, such as Medicaid and Medicare, have virtually no outsourcing of subrogation recoveries. These programs typically rely on their claims administration contractors to provide subrogation services as part of a bundled service contract. The Company believes that, like the health insurance market, certain participants in the P&C insurance market are less likely to outsource subrogation services. The Company believes mutual insurers have organizational and cultural biases against outsourcing and larger P&C insurers have sufficient resources to develop relatively sophisticated internal departments. In June 2002, the Company made its first sale of the Troveris software to an outside client (United Medical Resources). Additionally, the Company has received indications of interest from other potential purchasers.

The Troveris marketing strategy combines the opportunity for an internal subrogation department to gain operating efficiency through the functionality of state-of-the-art desktop software and to leverage its ability to produce recoveries through the purchase of unbundled components of the Company's traditional subrogation outsourcing services. The Troveris software application allows the Company to administer these customized relationships using the same proprietary processes as it uses for those customers who purchase turnkey subrogation outsourcing services. An additional benefit of the Troveris software application is that the

Company believes that it will substantially reduce future expenses for maintaining software applications that it uses to provide turnkey outsourcing services.

In addition to being offered for sale as an on-line subrogation recovery system in an ASP-model, Troveris also constitutes the systems platform for the Company's recovery operations. All of those operations are currently conducted on Troveris except healthcare subrogation. The Company began to migrate its internal healthcare subrogation operations to a version of Troveris during the fourth quarter of 2001, at which time it anticipated reducing its technology expense, net of the expense of maintaining the Troveris application, by at least $600,000 per year. At present, substantially all of that expense reduction has been captured and is included in the Company's guidance for 2003 financial results. The Company currently expects to complete the migration to Troveris in the third quarter of 2003, and shortly thereafter to abandon its legacy subrogation system. Given the complexities of software development and change management, the Company may lengthen this schedule in order to assure that there is no disruption in operations. If the Company does lengthen the transition schedule, the Company believes that such a change will have no adverse financial consequence for the Company or its clients. The Troveris application also enables the Company to expand its ability to manage its knowledge workers via telecommuting arrangements. While the Company believes it can achieve the foregoing transition and corresponding reduction of expenses in the outlined timeframe, future facts and circumstances could change these estimates. See "Safe Harbor Compliance Statement for Forward-Looking Statements" included as Exhibit 99.1 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2002.

The Company has identified one competitor offering subrogation software in an ASP model for the healthcare payor industry, and one large competitor in the P&C insurance industry. The P&C competitor is partially owned and controlled by a major P&C insurer, and the Company believes that this relationship will reduce the ability of the competitor to sell its services to other P&C insurers.

RESULTS OF OPERATIONS

THREE AND SIX MONTHS ENDED JUNE 30, 2003 COMPARED TO THREE AND SIX MONTHS ENDED JUNE 30, 2002

Revenue. Revenue for the Software segment increased $240,000, or 145%, for the quarter ended June 30, 2003. For the six months ended June 30, 2003, revenue increased to $718,000 from $280,000 for the comparable period in 2002. All but $15,000 and $32,000 of the revenue for the three and six months ended June 30, 2003, respectively, was derived from internal clients (i.e., the Healthcare Recovery Services and Property and Casualty Services segments). For the three and six months ended June 30, 2002, all revenue was derived from internal clients.

Cost of Revenues. Cost of revenues for the Software segment for the three months ended June 30, 2003 was approximately $255,000, an increase of $107,000, or 72%, over the comparable period in 2002. This includes approximately $208,000 and $107,000 for the three months ended June 30, 2003 and 2002, respectively, of depreciation and amortization of software in service. Approximately $47,000 and $41,000 of the cost of revenues for the three months ended June 30, 2003 and 2002, respectively, relate to the support and maintenance of the software. For the six months ended June 30, 2003, cost of revenues was $495,000, an increase of 88% from $263,000 for the six months ended June 30, 2002. Depreciation and amortization of software in service comprised $388,000 and $187,000 of the cost of revenues for the six months ended June 30, 2003 and 2002, respectively. Approximately $107,000 and $76,000 of the cost of revenues for the six months ended June 30, 2003 and 2002, respectively, relate to the support and maintenance of the software.

Support Expenses. For the three months ended June 30, 2003 and 2002, the Software segment incurred approximately $528,000 and $507,000, respectively, in expenditures in connection with the creation of new products for the insurance industry. Approximately $242,000 and $292,000 of support expenditures were capitalized in the quarters ended June 30, 2003 and 2002, respectively, resulting in net reported support expenses of approximately $286,000 and $215,000, respectively. For the six months ended June 30, 2003 and 2002, approximately $1.0 million and $908,000, respectively, in expenditures were incurred in connection with the creation of new products for the insurance industry. Approximately $445,000 and $546,000 of support

expenditures were capitalized during the six months ended June 30, 2003 and 2002, respectively, resulting in net reported support expenses of $579,000 and $362,000, respectively.

ENTIRE COMPANY

EMPLOYEES

	JUNE 30, 2003	DECEMBER 31, 2002	JUNE 30, 2002
Direct operations	500	522	532
Support	142	144	154
Total employees	642	666	686

STATEMENTS OF INCOME AS A PERCENTAGE OF REVENUES

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2003	2002	2003	2002
Claims revenues..................................	100.0%	100.0%	100.0%	100.0%
Cost of revenues.................................	49.3	48.4	50.2	48.5
Support expenses.................................	29.2	28.9	28.3	28.5
Depreciation and amortization....................	5.0	7.1	5.4	7.2
Operating income.................................	16.5	15.6	16.1	15.8
Interest expense, net............................	(0.3)	(0.4)	(0.3)	(0.4)
Income before income taxes.......................	16.2	15.2	15.7	15.4
Net income.......................................	9.7	9.3	9.4	9.5

Depreciation and Amortization. Depreciation and amortization expense decreased 30.9% to $849,000 for the quarter ended June 30, 2003 from $1.2 million for the same quarter in 2002, and decreased 28.0% to $1.8 million for the six months ended June 30, 2003 from $2.5 million for the comparable period in 2002. The decreases were due to a significant amount of fixed assets acquired in 1997 becoming fully depreciated during the twelve months ended June 30, 2003.

Interest Income. Interest income decreased 31.0%, or $18,000, for the quarter ended June 30, 2003 as compared to the same quarter in 2002. For the six months ended June 30, 2003, interest income decreased $35,000, or 28.0%, from $125,000 to $90,000. The decreases were due primarily to lower interest rates.

Interest Expense. Interest expense totaled approximately $83,000 for the quarter ended June 30, 2003, a decrease of 33.6%, or $42,000 from the quarter ended June 30, 2002. For the six months ended June 30, 2003, interest expense decreased 22.7% to $204,000 from $264,000 in the comparable period in 2002. The decreases in interest expense for the three and six months ended June 30, 2003, as compared with the same periods in 2002, were primarily due to a decrease in borrowed funds during the 2003 periods.

Tax. For the three and six months ended June 30, 2003, the Company accrued income taxes at a 40.0% effective tax rate. This is a reduction from the Company's pre-2002 historical effective tax rate due to the implementation of state tax planning initiatives beginning July 1, 2002.

The Company accrued income taxes at a 38.7% and 38.4% effective tax rate during the three and six months ended June 30, 2002, respectively, due to non-recurring research and experimental tax credits of $72,500 and $167,500, respectively.

Net Income. Net income for the quarter ended June 30, 2003 increased $39,000, or 2.4%, to $1.7 million, or $0.19 per diluted common share, from $1.6 million, or $0.17 per diluted common share, for the comparable quarter in 2002. For the six months ended June 30, 2003, net income decreased 4.7% to

$3.2 million, or $0.36 per diluted common share, from $3.3 million, or $0.34 per diluted common share, for the comparable period in 2002.

LIQUIDITY AND CAPITAL RESOURCES

The Company's statements of cash flows for the six months ended June 30, 2003 and 2002 are summarized below:

	SIX MONTHS ENDED JUNE 30,	
	2003	2002
	(IN THOUSANDS)	
Net cash provided by operating activities..................	$ 5,738	$ 7,026
Net cash used in investing activities......................	(1,500)	(2,290)
Net cash used in financing activities......................	(832)	(5,201)
Net increase (decrease) in cash and cash equivalents........	$ 3,406	$ (465)

The Company had working capital of $11.9 million at June 30, 2003, including cash and cash equivalents of $5.7 million, compared with working capital of $8.8 million at December 31, 2002. The primary reason for the increase in working capital was the accumulation of cash generated from operating activities.

Net cash provided by operating activities was $5.7 million, a decrease of $1.3 million for the six months ended June 30, 2003, compared to the same six months in 2002. The decrease is primarily attributable to a decrease in accounts payable from June 30, 2002 to June 30, 2003, due to timing of payments. A decrease in accrued expenses primarily as a result of payment of more incentive compensation during the first six months of 2003 compared to 2002, was off-set by a decrease in accounts receivable, caused by improved collections. In addition, net income plus depreciation and amortization is approximately $0.7 million less for the six months ended June 30, 2003 compared to the same period in 2002.

Net cash used in investing activities includes purchases of property and equipment principally related to the development of and conversion to the Troveris software. During the six month periods ended June 30, 2003 and 2002, the Company capitalized approximately $0.6 million and $1.0 million of internally-developed software, respectively.

Net cash used in financing activities for the six months ended June 30, 2003 and 2002, reflects $0.9 million and $3.6 million in treasury stock purchases, respectively. During the six months ended June 30, 2002, the Company paid down a net of $1.7 million on its long-term borrowings.

On November 1, 2001, the Company entered into a revolving credit facility with National City Bank of Kentucky, Bank One Kentucky, N.A. and Fifth Third Bank (the "Revolving Credit Facility"). The Company's obligations under the Revolving Credit Facility are secured by substantially all of the Company's assets, subject to certain permitted exceptions. The Revolving Credit Facility carries a maximum borrowing capacity of $40 million and will mature October 31, 2004. Principal amounts outstanding under the Revolving Credit Facility bear interest at a variable rate based on the Prime Rate or Eurodollar Rate, as applicable, plus a pre-determined fixed margin. At June 30, 2003 and December 31, 2002, the interest rate was 3.06% and 3.19%, respectively, based on the one-month Eurodollar Rate plus the fixed margin. The Revolving Credit Facility contains customary covenants and events of default including, but not limited to, financial tests for interest coverage, net worth levels and leverage that

may limit the Company's ability to pay dividends. It also contains a material adverse change clause. At June 30, 2003 and December 31, 2002, $4 million was outstanding under the Revolving Credit Facility. (See Item 1. "Financial Statements (Unaudited) -- Note 9 -- Derivatives and Note 10 -- Credit Facility".)

At June 30, 2003 and December 31, 2002, the Company reported on its balance sheets, as a current asset, restricted cash of $19.1 million and $17.8 million, respectively. Restricted cash at June 30, 2003 and December 31, 2002 represented claims recoveries by the Company for its clients. At June 30, 2003 and December 31, 2002, the Company reported on its balance sheets, as a current liability, funds due clients of

$13.7 million and $12.4 million, respectively, representing claims recoveries to be distributed to clients, net of the fee earned on such recoveries.

In light of its acquisition strategy, the Company continues to assess, from time to time, its opportunities for capital formation. The Company believes that its available cash resources, together with the borrowings available under the Revolving Credit Facility, will be sufficient to meet its current operating requirements and acquisition and internal development activities. See "Evaluation of Strategic Alternatives".

EXTERNAL FACTORS

The business of recovering subrogation and other claims for healthcare payors is subject to a wide variety of external factors. Prominent among these are factors that would materially change the healthcare payment, fault-based liability or workers' compensation systems. Examples of these factors include, but are not limited to, 1) the non-availability of recovery from such sources as property and casualty and workers' compensation coverages, 2) law changes that limit the use of or access to claims and medical records, or 3) the ability of healthcare payors to recover related claims and audit medical records. Because the Company's profitability depends in large measure upon obtaining and using claims data and medical records, the non-availability or decrease in their availability could have a material adverse effect on the Company.

Moreover, because the Company's revenues are derived from the recovery of the costs of medical treatment, material changes in such costs will tend to affect the Company's backlog or its rate of backlog growth, as well as its revenue or its rate of revenue growth. The healthcare industry, and particularly the business of healthcare payors, is subject to various external factors that may have the effect of significantly altering the costs of healthcare and the environment for the sale or delivery of medical claims recovery and cost containment services. The Company is unable to predict which of these factors, if any, could have a potentially material impact on healthcare payors and through them, the healthcare recovery and cost containment industry.

CONCENTRATION OF CLIENTS

The Company provides services to healthcare plans that as of June 30, 2003 covered approximately 35.2 million lives. The Company's clients are national and regional healthcare payors, large third-party administrators or self-insured corporations. The Company has two clients that individually comprise more than 10% of the Company's revenue. The Company's largest source of revenue is UnitedHealth Group ("UHG"). For the six month periods ended June 30, 2003 and 2002, UnitedHealth Group generated 26% and 27% of the Company's revenues, respectively. Wellpoint Health Network Inc. accounted for 15% and 13% of the Company's total revenues for the six months ended June 30, 2003 and 2002,

respectively, as well as 41% and 32% of the Company's accounts receivable balance at June 30, 2003 and December 31, 2002, respectively. Health Net, Inc. accounted for 8% and 15% of the Company's accounts receivable balance at June 30, 2003 and December 31, 2002, respectively.

The Company's revenues are earned under written contracts with its clients that generally provide for contingency fees from recoveries under a variety of pricing regimes. The pricing arrangements offered by the Company to its clients include a fixed fee percentage, a fee percentage that declines as the number of lives covered by the client and subject to the Company's service increases and a fee percentage that varies with the Company's recovery performance.

The Company performs its services on a reasonable efforts basis and does not obligate itself to deliver any specific result. Contracts with its customers are generally terminable on 60 to 180 days' notice by either party, although in a few cases the contracts extend over a period of years. The Company's contracts generally provide that in the event of termination, the Company is entitled to complete the recovery process on the existing backlog or to receive a cash payment designed to approximate the gross margin that would otherwise have been earned from the recovery on the backlog of the terminating client. On June 30, 2003, the Company had Healthcare Recovery Services backlog of $1,570.6 million.

During 2002, UHG management informed the Company of its intention to terminate subrogation services with respect to all but 1.8 million lives of the 9.7 million lives then subject to the Company's services under a contract with UHG. UHG's termination of these services resulted from its decision to bring subrogation recovery services back inside UHG, where they will be performed by its Ingenix strategic business unit. The Company expects to continue recovering on the backlog as to which UHG terminated the Company's services, a process that the Company expects will be completed in 5 to 6 years. The Company's contract with UHG expired in accordance with its terms on February 1, 2003, except with respect to 1.8 million lives as to which the Company continues to provide healthcare subrogation recovery services.

CRITICAL ACCOUNTING POLICIES

The Company has identified critical accounting policies that, as a result of the judgments, uncertainties, uniqueness and complexities of the underlying accounting standards and operations involved, could result in material changes to its financial condition or results of operations under different conditions or using different assumptions. The Company believes its most significant accounting policies are related to the following areas, among others: revenue recognition, accounts receivable and collectibility, capitalization of software costs, valuation of long-lived and intangible assets, accrued expenses and common stock options. Details regarding the Company's use of these policies and the related estimates are described more fully in the Company's Annual Report on Form 10-K for the year ended December 31, 2002, filed with the Securities and Exchange Commission on March 27, 2003. During the six months ended June 30, 2003, there have been no material changes to the Company's critical accounting policies that impacted the Company's financial condition or results of operations.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In November 2002, the FASB issued EITF 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables" which addresses revenue recognition accounting by a vendor for arrangements under which it will perform multiple revenue-generating activities. The provisions of this statement are effective for revenue arrangements entered into in fiscal periods beginning after June 15,

2003. The Company is evaluating the effect that EITF 00-21 may have on its financial statements.

In January 2003, the FASB issued FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51". FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective for all new variable interest entities created or acquired after January 31, 2003. For variable interest entities created or acquired prior to February 1, 2003, the provision of FIN 46 must be applied for the first interim or annual period beginning after June 15, 2003. The Company does not have any variable interest entities as defined under FIN 46.

In April 2003, the FASB issued SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" which amends and clarifies the accounting guidance on derivative instruments and hedging activities that fall within the scope of SFAS 133, "Accounting for Derivative Instruments and Hedging Activities". SFAS 149 is effective (1) for contracts entered into or modified after June 30, 2003, with certain exceptions, and (2) for hedging relationships designated after June 30, 2003. The Company will apply the provisions of SFAS 149 to contracts entered into or hedging relationships designated after June 30, 2003.

In May 2003, the FASB issued SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" which establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective for the Company on July 1, 2003. The adoption of SFAS 150 did not have a significant impact on the Company's financial statements.

EVALUATION OF STRATEGIC ALTERNATIVES

As previously announced in a press release issued August 1, 2003, the Company's Board of Directors has formed a Special Committee to evaluate strategic alternatives available to the Company, including a leveraged recapitalization, a sale of all or any portion of the Company to a third party, or the formation of an employee stock ownership plan which would acquire the Company. The Special Committee has engaged Houlihan Lokey Howard and Zukin as its financial advisor.

STOCK REPURCHASE PLAN

The Company's Board of Directors authorized the repurchase of up to $20 million of the Company's Common Stock in the open market, including $10 million authorized on May 10, 2002, at prices per share deemed favorable by the Company. Shares may be repurchased using cash from operations and borrowed funds and may continue until such time as the Company has repurchased $20 million of the Company's Common Stock or until it otherwise determines to terminate the stock repurchase plan. During the quarter ended June 30, 2003, the Company did not repurchase any shares of common stock. The Company repurchased 172,622 shares of common stock during the six months ended June 30, 2003 at a cost of $0.9 million, or an average price of $5.23 per share. From inception of the program through June 30, 2003, the Company repurchased 3,269,630 shares at a cost of $14.5 million, or an average cost of $4.43 per share. Except for 9,397 shares

previously repurchased but reissued in connection with an employee restricted stock award, all of the reacquired shares of Common Stock through June 30, 2003 are reflected as treasury stock on the accompanying Condensed Balance Sheets (Unaudited).

During the term of the Special Committee, the Company does not anticipate repurchasing shares of its common stock.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

An element of market risk exists for the Company from changes in interest rates related to its Revolving Credit Facility, which matures October 31, 2004. The impact on earnings and value of any debt on the Company's balance sheets are subject to change as a result of movements in market rates and prices as the Revolving Credit Facility is subject to variable interest rates. However, the Company does not expect changes in interest rates to have a material effect on its financial position, results of operations or cash flows in 2003. As of June 30, 2003, the Company had $4 million outstanding under its Revolving Credit Facility. Through the interest rate swap contract the Company has entered into, the Company has fixed the interest rate on the entire $4 million of the Revolving Credit Facility at 5.41% or 5.66% (contingent on the status of a financial ratio). See Item 1. "Financial Statements (Unaudited) -- Note 9 -- Derivatives" and "-- Note 10 -- Credit Facility" and Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources".

ITEM 4. CONTROLS AND PROCEDURES

As required by Securities and Exchange Commission rules, the Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this quarterly report. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the design and operation of the Company's disclosure controls and procedures are effective. The Company's management, including the Chief Executive Officer and Chief Financial Officer, also conducted an evaluation of the Company's internal control over financial reporting to determine whether any changes occurred during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Based on that evaluation, there has been no such change during the quarter covered by this report.

PART II: OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is engaged in the business of identifying and recovering subrogation and related claims of its clients, many of which arise in the context of personal injury lawsuits. As such, the Company operates in a litigation-intensive environment. Consequently, since its founding in 1988 the Company has been involved with many litigation matters related to its subrogation business, sometimes as a defendant and sometimes through a defendant client. The plaintiffs' attorneys attempting to defeat the clients' subrogation liens often threaten litigation against the Company and its clients as a negotiating tactic. Most of the lawsuits that have been filed against the Company or its clients concern the entitlement to recover a specific, individual

subrogation claim or the amount of the subrogation claim. Typically, these actions do not ask for punitive damages, are not pled as class actions, and do not have wide implications with respect to the Company's ongoing business practices.

To date, however, the Company has encountered eight noteworthy instances in addition to the pending lawsuits described under "-- Current Litigation", in which lawsuits were filed against it or its clients that sought punitive damages, were pled as class actions, or otherwise made claims or requested relief that could have materially affected the Company's business practices. The risk profile for this sort of business practices litigation includes not only the usual considerations of the potential amount, effect, and likelihood of loss, but also specifically the potential for punitive damages and class certification, the possible effects of an adverse verdict on the Company's business practices, and the likelihood of specific plaintiffs' attorneys bringing similar actions in other jurisdictions.

Each of these cases has been completely resolved, by decision of a court or settlement by the parties, but prior to resolution the Company did not regard all of these cases as being material in and of themselves. In management's opinion, these eight cases share a common profile with each other and with the lawsuits described below under the caption "-- Current Litigation".

Five of the eight lawsuits named the Company as a defendant and were pled as class actions. Two of these five cases, one in federal court and the other in state court, alleged that the Company violated state and federal laws on fair debt collection practices. In the state court action, the court granted the Company's motion for summary judgment on all claims in the complaint, which the court of appeals affirmed. In the federal court action, the Company settled the matter, prior to the court's ruling on the Company's motion for summary judgment, for a nominal amount.

Three of those five lawsuits pled as class actions and naming the Company as a defendant were filed in federal court and charged the Company with a variety of violations of laws and sought punitive damages. The complaints alleged, among other things, that the Company committed negligence, fraud and breach of its duties under ERISA by attempting to recover and actually recovering, by subrogation, the reasonable value of medical benefits which were provided by the Company's clients under capitation or discounted-fee-for-service arrangements. One of these lawsuits was dismissed in a ruling on the merits. Another was settled, after the court denied class certification, for a nominal amount paid by the Company's client, a co-defendant in the case. The third case, DeGarmo et al. v. Healthcare Recoveries, Inc., was concluded in mid-July 2001 for a settlement payment of $3 million and nonmonetary terms that management regards as immaterial to the Company's ongoing business.

The remaining three lawsuits did not name the Company as a defendant. These three lawsuits did, however, involve the Company's clients and implicate important Company business practices. The complaints in these cases alleged, among other things, violation of state law with respect to the payment of plaintiffs' attorneys' fees and unfair trade practices, violation of the federal Health Maintenance Organization Act of 1973, misrepresentation of the rightful amounts of subrogation claims, and impermissible enforcement of recovery rights. Two of these cases resulted in judgments in favor of the Company's clients after litigation of the merits before trial and appellate courts. The other case was settled for an immaterial amount.

Management believes that the lawsuits described above will not, as a general matter, have precedential value for either the cases described below

under the caption "-- Current Litigation" or for any future litigation matters (all these cases being referred to as the "Pending and Potential Cases"). Indeed, the courts hearing the Pending and Potential Cases may not even become aware of the outcomes in the eight lawsuits described above. Management expects that each of the Pending and Potential Cases will be decided on its own merits under the relevant state and federal laws, which will vary from case to case and jurisdiction to jurisdiction. The descriptions of the outcomes in the eight cases dealing with business practices are included here in order to describe the contexts for this kind of litigation and the Company's relative successes in handling past business practices litigation, but are not necessarily predictive of the outcomes of any of the Pending and Potential Cases.

Moreover, there can be no assurance that the Company will not be subject to further class action litigation similar to that described below under the caption "-- Current Litigation", that existing and/or future class action litigation against the Company and its clients will not consume significant management time and/or attention or that the cost of defending and resolving such litigation will not be material.

CURRENT LITIGATION

CAJAS ET AL. V. PRUDENTIAL HEALTH CARE PLAN AND HEALTHCARE RECOVERIES

On October 28, 1999, a class action plaintiff's Original Petition ("Petition") was filed against the Company and one of the Company's clients in the District Court for the 150th Judicial District, Bexar County, Texas, Joseph R. Cajas, on behalf of himself and all others similarly situated v. Prudential Health Care Plan, Inc. and Healthcare Recoveries, Inc. The plaintiff asserts that the Company's subrogation recovery efforts on behalf of its client Prudential Health Care Plan, Inc. ("Prudential") violated a number of common law duties, as well as the Texas Insurance Code and the Texas Business and Commerce Code. The Petition alleges that the Company, as the subrogation agent for Prudential, made fraudulent misrepresentations in the course of unlawfully pursuing subrogation and reimbursement claims that the plaintiff asserts are unenforceable because (1) prepaid medical service plans may not exercise rights of subrogation and reimbursement; (2) the subrogation and reimbursement claims asserted by the Company are not supported by contract documents that provide enforceable recovery rights and/or do not adequately describe the recovery rights; and (3) the sums recovered pursuant to such claims unlawfully exceed the amount Prudential paid for medical goods and services. The Company was served with the Petition in November 1999, and has answered, denying all allegations. The court has not yet addressed the question of whether to certify the putative class. After the defendants filed a motion for summary judgment in January 2002, the plaintiff moved the court to delay consideration of the motion until the plaintiff could complete additional discovery. The plaintiff's motion to delay consideration was granted. On October 25, 2002, the plaintiff filed an amended petition naming one additional plaintiff as a purported class representative. The amended petition does not add any new claims. The defendants filed a motion for summary judgment on January 24, 2003 and the plaintiffs filed a cross motion for summary judgment. On February 25, 2003, a state court judge denied the defendants' motion for summary judgment that the defendants were entitled to enforce the terms of Prudential's policies. The same judge granted the plaintiffs' motion for summary judgment to the extent that Prudential could not recover more than its costs. The Company believes that the Court will provide a written opinion clarifying the impact of the ruling. The Court has not yet considered whether to certify a plaintiff class in the lawsuit.

MARTIN ET AL. V. COMPANION HEALTH CARE AND HEALTHCARE RECOVERIES

In December 1999, a purported class action complaint ("Complaint") was filed against the Company and one of the Company's clients in the Court of Common Pleas of Richland County, South Carolina, Estalita Martin et al. vs.

Companion Health Care Corp., and Healthcare Recoveries, Inc. In January 2000, the defendant Companion Healthcare Corp. ("CHC") filed an Answer and Counterclaim and the plaintiff Martin filed a First Amended Complaint ("Amended Complaint"). The Amended Complaint asserts that the Company's subrogation recovery efforts on behalf of its client, CHC, violated a number of common law duties, as well as the South Carolina Unfair Trade Practices Act. The Amended Complaint alleges that the Company, as the subrogation agent for CHC, made fraudulent misrepresentations in the course of unlawfully

pursuing subrogation and reimbursement claims that the plaintiffs assert are unenforceable because (1) prepaid medical service plans may not exercise rights of subrogation and reimbursement; (2) the subrogation and reimbursement claims asserted by the Company are not supported by contract documents that provide enforceable recovery rights and/or do not adequately describe the recovery rights; and (3) the sums recovered pursuant to such claims unlawfully exceed the amount CHC was entitled to collect for such medical goods and services. The Amended Complaint further alleges that the Company and CHC unlawfully pursued subrogation and reimbursement claims by (1) failing to pay pro rata costs and attorney's fees to attorneys who represented purported class members with respect to tort claims underlying the subrogation and reimbursement claims; and (2) failing to include in subrogation and reimbursement claims all applicable discounts that CHC received for such medical goods and services. The plaintiffs, on behalf of the purported class, demand compensatory damages, punitive damages, and treble damages, disgorgement of unjust profits, costs, prejudgment interest and attorneys' fees. The Company was served with the original Complaint in late December 1999 and answered denying all allegations. The Company filed a motion to dismiss in August 2000 and in June 2001 the court granted the Company's motion to dismiss. The plaintiffs filed a notice of appeal in July 2001. All parties have filed briefs, but the appellate court has not yet ruled on the plaintiffs' appeal of the dismissal, nor has oral argument been scheduled.

HAMILTON V. HEALTHCARE RECOVERIES

On March 12, 2001, a Complaint ("Complaint") was filed against the Company in the United States District Court for the Eastern District of Louisiana, in a putative class action brought by Kyle M. Hamilton. In that action, Hamilton v. Healthcare Recoveries, Inc., No. 01-650, the plaintiff asserts that the Company's subrogation recovery efforts on behalf of its clients violate certain Louisiana state laws, the federal Fair Debt Collection Practices Act and the Louisiana Unfair Trade Practices Act. The Complaint alleges that the Company intentionally and negligently interfered with the plaintiff's and the putative class members' rights to settle certain personal injury claims. The Complaint further alleges that the Company unlawfully pursued subrogation and reimbursement claims that the plaintiff asserts are unenforceable because the clauses in the Company's clients' coverage documents that create such recovery rights are rendered null and void by Louisiana statutes that generally prohibit coordination of benefits with individually underwritten insurance coverages. The plaintiff purports to represent a class consisting of all persons covered under group health policies that were issued or delivered in the State of Louisiana and who received any communication from the Company attempting to enforce any clauses that allegedly were rendered null and void by Louisiana law. The plaintiff seeks on behalf of the purported class compensatory and statutory damages, interest, costs, attorneys' fees and such additional damages and relief as may be allowed by any applicable law. In July 2001, the court granted a motion for summary judgment filed by the Company as concerned the plaintiff's Fair Debt Collection Practices Act ("FDCPA") claim, dismissing those claims with prejudice. The court denied the Company's motion for summary judgment, without prejudice to the right of the Company to reassert its motion, with respect to the plaintiff's state law claims. The court ordered that the parties submit

memoranda addressing whether the court still had subject matter jurisdiction, given dismissal of the federal claim. In August 2001, the court ruled that it lacked subject matter jurisdiction, thus dismissing the remaining claims, without prejudice. The plaintiff filed an appeal to the United States Fifth Circuit Court of Appeals. In November 2002, the Court of Appeals rendered its opinion reversing the dismissal of the FDCPA claims. The court also affirmed the trial court's determination that diversity jurisdiction did not exist in the case. The court remanded the case to the federal district court for further proceedings. On April 29, 2003, the Company filed a Petition for Writ of Certiorari asking the U.S. Supreme Court to accept an appeal of the Court of Appeals ruling. The Supreme Court denied the Petition on June 9, 2003.

After the case was remanded to the trial court, the Company filed a second Motion for Summary Judgment. On May 13, 2003, the Court entered an Order granting the Company's Motion for Summary Judgment, dismissing with prejudice the Plaintiff's claims under the FDCPA and dismissing without prejudice the Plaintiff's remaining state law claims. On May 27, 2003, the plaintiff filed a Notice of Appeal to the United States Fifth Circuit Court of Appeals. The Company intends to file its Appellee brief in August 2003. The Company disputes the plaintiff's allegations regarding the applicability of the FDCPA and intends to vigorously defend its position in this case.

27

In addition to filing the appeal in federal court, the Hamilton plaintiff in October 2001 filed a new complaint in the Civil District Court for the Parish of Orleans, Louisiana, in a putative class action styled Hamilton v. Healthcare Recoveries, Inc., 2001-15989. This state court action asserts claims substantially similar to those in the federal court action. In November 2001, the Company filed preliminary exceptions to this new complaint. There were no further proceedings in the case until March 2003 when the Company filed a motion to stay any further proceedings in that case due to the related case pending in federal court. On April 25, 2003, the state court entered an order granting the Company's motion to stay the lawsuit.

ROGALLA V. CHRISTIE CLINIC, PERSONALCARE HEALTH MANAGEMENT AND HEALTHCARE RECOVERIES

On December 14, 2001, Valerie Rogalla, the plaintiff in a putative class action against a health care provider, amended her complaint to add Healthcare Recoveries, Inc. as a defendant in Valerie Rogalla v. Christie Clinic, P.C., PersonalCare Health Management, Inc. and Healthcare Recoveries, Inc., No. 01-L-203, Circuit Court of the Sixth Judicial Circuit, Champaign County, Illinois. In her complaint, the plaintiff makes allegations on behalf of herself and all others similarly situated. The complaint asserts that the Company, as subrogation agent for PersonalCare Health Management, made fraudulent misrepresentations in the course of unlawfully pursuing subrogation and reimbursement claims. The complaint seeks recovery from the Company for compensatory damages, punitive damages and costs. The Company disputes the plaintiff's allegations and intends to vigorously defend its position in this case. Each defendant filed a motion to dismiss the action. In October 2002, the Court granted each of the defendants' motions and dismissed the plaintiff's action entirely. The plaintiff subsequently filed her notice of appeal and, the Appellate Court heard oral argument of the appeal on April 23, 2003. On June 20, 2003, the Appellate Court entered an order affirming the trial court's ruling. On July 3, 2003, the plaintiff filed a motion seeking leave to appeal the case to the Illinois Supreme Court. The Company intends to vigorously oppose the motion.

CHAN V. TROVER SOLUTIONS

On November 19, 2002, a Complaint ("Complaint") was filed against the

Company in the Superior Court of the State of California for the County of Los Angeles in a putative class action brought by Roger Chan. In that action, Roger Chan v. Healthcare Recoveries, Inc. and Trover Solutions, Inc. and Does 1 through 100, inclusive, No. CV 03-0465 FMC, the plaintiff asserts that the Company's subrogation recovery efforts violate California's unfair trade practices statute by pursuing recovery from ERISA members' personal injury recoveries when case law allegedly held that ERISA plans could not enforce their recovery rights. The Company timely removed the action to federal court and filed a motion to dismiss. The plaintiff filed a motion to remand the case back to the state court. On March 3, 2003, the Court entered an order denying the plaintiff's motion to remand and denying the defendant's motion to dismiss. In June 2003, the plaintiff and the Company agreed to settle all claims in the case in exchange for payment of $7,000 from the Company to the plaintiff. The settlement is subject to court approval.

BRUUN ET AL. V. PRUDENTIAL HEALTH CARE PLAN, PRUDENTIAL INSURANCE COMPANY OF AMERICA, AETNA, INC. AND TROVER SOLUTIONS

On October 30, 2002, the Cajas and Franks plaintiff's counsel filed a class action lawsuit in the United States District Court for the District of New Jersey on behalf of two Texas residents against the Company, one of the Company's clients, Prudential Insurance Company, a subsidiary of the client, PruCare HMO, and a company which had acquired the business of the client company, Aetna. The complaint was served on the Company on February 27, 2003.

In the complaint, plaintiffs Kimberly Bruun and Ashley Emanis, on behalf of themselves and similarly situated persons, asserted claims on behalf of a nationwide class of persons who were members of PruCare HMO health plans governed by ERISA from whom the Company, under its contract with the client, recovered reimbursement. The complaint alleged that reimbursement recoveries made by PruCare HMO and the Company violate the terms of the standard PruCare HMO plan documents, and that reimbursement recoveries violate the Conformity with Law provision in the standard plan documents because subrogation and reimbursement are prohibited under the federal HMO Act. The complaint further alleged that the defendants'

28

subrogation and reimbursement recoveries resulted in a double recovery to PruCare HMO because PruCare HMO did not account for subrogation and reimbursement recoveries as offsets to expenses when setting premium rates. The complaint further alleged that the defendants improperly recovered in subrogation or reimbursement for services provided by capitated providers, or that in the alternative, the defendants improperly recovered more for capitated services than was paid for the services, or alternatively, that the defendants improperly collected amounts that exceeded the reasonable cash value of capitated services. The plaintiffs allege that PruCare HMO, Prudential, Aetna and the Company are fiduciaries and that they each have breached their fiduciary duty to the plaintiffs. Alternatively, the plaintiffs allege that if Aetna, Prudential and the Company are not fiduciaries, that they knowingly participated in PruCare HMO's breach of fiduciary duty.

The plaintiffs, on behalf of the class, demand enforcement of the plan documents under certain sections of ERISA. The plaintiffs also demand restitution and disgorgement of sums recovered by defendants and the establishment of a constructive trust. The plaintiffs also demand an accounting of PruCare HMO's and Aetna's rate documents, the subrogation and reimbursement claims for capitated services, and/or the actual costs paid by PruCare HMO and Aetna for the capitated services.

On April 16, 2003, the defendants filed motions seeking to dismiss the lawsuit or to change the venue of the lawsuit to a federal court in Texas. The

court has not ruled on the motions.

GODAIR V. AMERICAN HOME ASSURANCE COMPANY, TROVER SOLUTIONS, AND HMO PARTNERS

On March 14, 2003, Lawrence Godair, the plaintiff in a putative class action against a motor vehicle insurer, amended his complaint to add the Company, and a client of the company, HMO Partners, as defendants in Lawrence Godair v. American Home Assurance Company, Trover Solutions, Inc. and HMO Partners, Inc., No. 4:02 CV 00407 SMR, United States District Court for the Eastern District of Arkansas, Western Division. In the amended complaint (the "Amended Complaint"), the plaintiff makes allegations on behalf of himself and a purported class of others similarly situated. The complaint asserts that the Company, as subrogation agent for HMO Partners, unlawfully demanded payment of a subrogation claim against proceeds of a medical payments insurance policy issued to the plaintiff by American Home. The Amended Complaint also alleges that the Company was unjustly enriched because the plaintiff was not fully compensated ("made whole") for his injuries in violation of the Arkansas no-fault motor vehicle insurance statute and because the payment constituted a double recovery to the Company and to HMO Partners, in violation of the Arkansas Health Maintenance Organizations Act. The Amended Complaint further alleges that in recovering the subrogation claim the Company acted negligently, that it interfered with the plaintiff's contractual relationship with the motor vehicle insurer and that the Company may be directly or vicariously liable for the acts of other defendants. The Amended Complaint demands relief on behalf of a purported class of persons who purchased medical payments coverage as required by the Arkansas no-fault motor vehicle insurance statute and who were entitled to but did not receive benefits under such policies due to the payment of those benefits to third parties, including the Company and HMO Partners. The Amended Complaint demands compensatory and punitive damages, 12% statutory penalties, costs, expenses, interest and attorney's fees.

The Company was served with the Amended Complaint on March 18, 2003 and filed an Answer denying the plaintiff's claims on May 5, 2003. The Company intends to vigorously defend itself against these allegations.

The Cajas, Martin or Bruun lawsuits, or any one of them, if successful, could prevent the Company from recovering the "reasonable value" of medical treatment under discounted fee for service ("DFS"), capitation and other payment arrangements. The Cajas, Martin, Hamilton, Rogalla, Chan and Bruun lawsuits, or any one or more of them, if successful, could require the Company to refund, on behalf of its clients, recoveries in a material number of cases. In addition, an adverse outcome in any of the above referenced lawsuits could impair materially the Company's ability to assert subrogation or reimbursement claims on behalf of its clients in the future. Based on the current disposition of these lawsuits, the Company regards such an adverse outcome to be a remote possibility.

29

In terms of the Company's business practices and the allegations underlying the Cajas, Martin and Bruun cases, at the end of 1993 the Company had ceased the practice of recovering the "reasonable value" of medical treatment provided by medical providers under DFS arrangements with the Company's clients. From that date, the Company's policy has been not to recover the "reasonable value" of medical treatment in DFS arrangements. However, the Company historically and currently recovers the "reasonable value" of medical treatment provided under capitation arrangements and other payment arrangements with medical providers on behalf of those clients that compensate medical providers under these payment mechanisms, to the extent that these benefits are related to treatment of the injuries as to which clients have recovery rights. The Company believes that its clients' contracts, including the contracts that provide for recovery under DFS, capitation and other payment arrangements are enforceable under the laws

potentially applicable in these cases. As a result, and taking into account the underlying facts in each of these cases, the Company believes it has meritorious grounds to defend these lawsuits, it intends to defend the cases vigorously, and it believes that the defense and ultimate resolution of the lawsuits should not have a material adverse effect upon the business, results of operations or financial condition of the Company. Nevertheless, if any of these lawsuits or one or more other lawsuits seeking relief under similar theories were to be successful, it is likely that such resolution would have a material adverse effect on the Company's business, results of operations and financial condition.

Management of the Company has observed that, in parallel with widely-reported legislative concerns with the healthcare payment system, there also has occurred an increase in litigation, actual and threatened, including class actions brought by nationally prominent attorneys, directed at healthcare payors and related parties. As a result of the foregoing, there can be no assurance that the Company will not be subject to further class action litigation, that existing and/or future class action litigation against the Company and its clients will not consume significant management time and/or attention or that the cost of defending and resolving such litigation will not be material.

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

The Company held its Annual Meeting of Stockholders on May 9, 2003. Of the 8,451,229 shares of Common Stock outstanding as of the record date, March 18, 2003, and entitled to vote at this meeting, 7,583,590 were represented at the meeting in person or by proxy. The following matters were voted upon:

(a) The following members were elected to the Board of Directors to hold office for a three year term:

NOMINEE	SHARES VOTED FOR	SHARES VOTED AGAINST	SHARES ABSTAINED	TERM
Patrick B. McGinnis........................	7,479,205	0	104,385	2006
Jill L. Force..............................	7,514,553	0	69,037	2006

The Company's other directors continuing after the Annual Meeting are as follows:

William C. Ballard
John H. Newman
Lauren N. Patch
Chris B. Van Arsdel

(b) The ratification of the appointment of PricewaterhouseCoopers LLP as independent public accountants of the Company to serve for 2003. The result of the vote was 7,484,681 shares in favor, 60,036 opposed and 38,873 abstained. Accordingly, the appointment of PricewaterhouseCoopers LLP was ratified.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

The following list of Exhibits includes both exhibits submitted with this

Form 10-Q as filed with the Commission and those incorporated by reference to other filings:

3.1	--	Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2002).
3.2	--	Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit 3.2 of Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2000).
4.1	--	Specimen Common Stock Certificate (incorporated by reference to Exhibit 4.1 of Registrant's Amendment No. 1 to Registration Statement on Form S-1, File No. 333-23287).
4.2	--	Rights Agreement, dated February 12, 1999, between the Registrant and National City Bank of Kentucky, as Rights Agent, which includes as Exhibit A the Form of Certificate of Designations of the Preferred Stock, as Exhibit B the Form of Right Certificate and as Exhibit C the Summary of Rights to Purchase Preferred Stock (incorporated by reference to Exhibit 4.1 of Registrant's Form 8-A, filed February 16, 1999, File No. 0-22585).
31.1	--	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	--	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	--	Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.1	--	Trover Solutions, Inc. Private Securities Litigation Reform Act of 1995 Safe Harbor Compliance Statement for Forward-Looking Statements (incorporated by reference to Exhibit 99.1 of Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2002).

(b) Reports on Form 8-K

ITEM REPORTED	DATE FURNISHED
Items 9 and 12 -- Text of Earnings Release and Slide Show Presentation...	May 1, 2003

SIGNATURES

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

TROVER SOLUTIONS, INC.

Date: August 13, 2003

/s/ PATRICK B. MCGINNIS

Patrick B. McGinnis
Chairman, President and Chief Executive Officer

Date: August 13, 2003

/s/ DOUGLAS R. SHARPS

Douglas R. Sharps
Executive Vice President and Chief Financial Offi
Principal Financial and Accounting Officer