MANOR CARE INC
Form 10-Q
April 29, 2003

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2003

OR

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

COMMISSION FILE NUMBER: 1-10858

MANOR CARE, INC.
(Exact name of registrant as specified in its charter)

DELAWARE	34-1687107
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
333 N. SUMMIT STREET, TOLEDO, OHIO	43604-2617
(Address of principal executive offices)	(Zip Code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (419) 252-5500

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 Rule12b-2 of the Exchange Act). Yes X No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the close of business on April 24, 2003.

Common stock, $0.01 par value - 90,008,649 shares

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

MANOR CARE, INC.
Consolidated Balance Sheets

	March 31, 2003 (Unaudited)	De
	(In thousands, except p	
Assets		
Current assets:		
Cash and cash equivalents	$ 16,044	$
Receivables, less allowances for doubtful accounts of $59,754 and $60,093, respectively	381,069	
Prepaid expenses and other assets	23,834	
Deferred income taxes	63,736	
Total current assets	484,683	
Property and equipment, net of accumulated depreciation of $733,892 and $704,348, respectively	1,538,005	1
Goodwill	86,591	
Intangible assets, net of amortization of $3,030 and $9,234, respectively	10,169	
Other assets	167,163	
Total assets	$ 2,286,611	$ 2
Liabilities And Shareholders' Equity		
Current liabilities:		
Accounts payable	$ 90,005	$
Employee compensation and benefits	125,811	
Accrued insurance liabilities	94,652	
Income tax payable	6,127	
Other accrued liabilities	48,229	
Long-term debt due within one year	2,649	
Total current liabilities	367,473	
Long-term debt	608,923	
Deferred income taxes	92,188	
Other liabilities	202,645	
Shareholders' equity:		
Preferred stock, $.01 par value, 5 million shares authorized		
Common stock, $.01 par value, 300 million shares authorized, 111.0 million shares issued	1,110	
Capital in excess of par value	346,966	
Retained earnings	1,037,088	1
Accumulated other comprehensive income (loss)	225	
	1,385,389	1
Less treasury stock, at cost (17.6 and 16.0 million shares, respectively)	(370,007)	
Total shareholders' equity	1,015,382	1
Total liabilities and shareholders' equity	$ 2,286,611	$ 2

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See notes to consolidated financial statements.

MANOR CARE, INC.
Consolidated Statements Of Income
(Unaudited)

	Three Months Ended March 31	
	2003	200
	(In thousands, except earnings per	
Revenues	$ 730,520	$ 715,9
Expenses:		
Operating	611,487	590,3
General and administrative	30,709	29,9
Depreciation and amortization	31,674	31,7
	673,870	652,0
Income before other income (expenses) and income taxes	56,650	63,9
Other income (expenses):		
Interest expense	(8,875)	(9,9
Gain (loss) on sale of assets	189	(9
Equity in earnings of affiliated companies	1,541	7
Interest income and other	701	6
Total other expenses, net	(6,444)	(9,5
Income before income taxes	50,206	54,4
Income taxes	19,078	20,6
Income before cumulative effect	31,128	33,7
Cumulative effect of change in accounting for goodwill		(1,3
Net income	$ 31,128	$ 32,4
Earnings per share - basic and diluted:		
Income before cumulative effect	$ .33	$.
Cumulative effect		(.
Net income	$ .33	$.
Weighted average shares:		
Basic	93,659	101,0
Diluted	94,504	102,1

See notes to consolidated financial statements.

MANOR CARE, INC.
Consolidated Statements Of Cash Flows
(Unaudited)

	Three Months 2003
	(In t
OPERATING ACTIVITIES	
Net income	$ 31,128
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization	31,674
Asset impairment and other non-cash charges	
Provision for bad debts	10,025
Deferred income taxes	19,708
Net (gain) loss on sale of assets	(189)
Equity in earnings of affiliated companies	(1,541)
Changes in assets and liabilities, excluding sold facilities and acquisitions:	
Receivables	(5,134)
Prepaid expenses and other assets	(1,951)
Liabilities	(2,979)
Total adjustments	49,613
Net cash provided by operating activities	80,741
INVESTING ACTIVITIES	
Investment in property and equipment	(23,245)
Investment in systems development	(1,177)
Acquisitions	(10,868)
Adjustment of acquisition of assets from development joint venture	
Proceeds from sale of assets	1,975
Net cash used in investing activities	(33,315)
FINANCING ACTIVITIES	
Net repayments under bank credit agreements	(23,400)
Principal payments of long-term debt	(5,563)
Proceeds from exercise of stock options	100
Purchase of common stock for treasury	(33,073)
Net cash used in financing activities	(61,936)
Net decrease in cash and cash equivalents	(14,510)
Cash and cash equivalents at beginning of period	30,554

Cash and cash equivalents at end of period	$ 16,044

See notes to consolidated financial statements.

MANOR CARE, INC.
Notes To Consolidated Financial Statements
(Unaudited)

NOTE 1 - ACCOUNTING POLICIES

BASIS OF PRESENTATION
The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management of Manor Care, Inc. (the Company), the interim data includes all adjustments necessary for a fair statement of the results of the interim periods and all such adjustments are of a normal recurring nature. Operating results for the three months ended March 31, 2003 are not necessarily indicative of the results that may be expected for the year ending December 31, 2003.

The balance sheet at December 31, 2002 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in Manor Care, Inc.'s annual report on Form 10-K for the year ended December 31, 2002.

At March 31, 2003, the Company operated 296 skilled nursing facilities, 70 assisted living facilities, 92 outpatient therapy clinics and 88 home health and hospice offices.

COMPREHENSIVE INCOME
Comprehensive income represents the sum of net income plus other comprehensive income. Comprehensive income totaled $31.4 million and $32.6 million for the first quarter of 2003 and 2002, respectively. The other comprehensive income primarily represents the unrealized gain on investments.

INSURANCE LIABILITIES
At March 31, 2003 and December 31, 2002, the workers' compensation liability consisted of short-term reserves of $26.4 million and $26.3 million, respectively, which were included in accrued insurance liabilities, and long-term reserves of $37.5 million and $32.5 million, respectively, which were included in other long-term liabilities. The expense for workers' compensation was $12.3 million and $11.1 million for the first quarters of 2003 and 2002, respectively. Although management believes that the Company's liability reserves are adequate, there can be no assurance that these reserves will not require material adjustment in future periods. See Note 3 for discussion of the Company's general and professional liability.

STOCK-BASED COMPENSATION
Stock options are granted for a fixed number of shares to employees with an exercise price equal to the fair market value of the shares at the date of grant. The Company accounts for the stock option grants in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related Interpretations. Accordingly, the Company recognizes no compensation expense for the stock options.

The following table illustrates the effect on net income and earnings per share as if the Company had applied the fair value recognition provisions of Financial Accounting Standards Board (FASB) Statement No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation for options granted since 1995.

	Three months ended March 2003 (In thousands, except earning
Net income -- as reported	$31,128
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(1,801)
Net income -- pro forma	$29,327
Earnings per share -- as reported:	
Basic and diluted	$ .33
Earnings per share -- pro forma:	
Basic	$ .31
Diluted	$ .31

NEW ACCOUNTING STANDARD
In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities, an interpretation of Accounting Research Bulletin No. 51" (the Interpretation). The Interpretation requires the consolidation of variable interest entities in which an enterprise absorbs a majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both, as a result of ownership, contractual or other financial interests in the entity. Currently, entities are generally consolidated by an enterprise that has a controlling financial interest through ownership of a majority voting interest in the entity. The Interpretation provides that an enterprise with a variable interest in specified assets of a variable interest entity (VIE) is to treat a portion of the entity as a separate VIE if the specified assets are essentially the only source of payment for specified liabilities.

A subsidiary of the Company leases the Company's corporate headquarters from an unconsolidated VIE under an operating lease, which expires in January 2009. A third party has invested capital at risk exceeding 3 percent of the assets of the VIE with the remainder being financed through a debt obligation. Under this, and certain other criteria, the proper accounting was not to consolidate the VIE in the Company's financial statements prior to adopting the Interpretation. Rather, the Company accounts for the arrangement as an operating lease. Accordingly, neither the leased corporate headquarters nor the related debt is reported in the Company's accompanying balance sheets.

The Company expects to begin consolidating the VIE effective July 1, 2003, because the Company believes it is the VIE's primary beneficiary under the Interpretation's requirements. The corporate headquarters' lease obligation includes the annual operating lease payments that reflect interest only payments on the lessor's $22.8 million of underlying debt, as well as a residual guarantee of that amount at maturity. On July 1, 2003, the Company expects to include the residual value guarantee of $22.8 million as an increase to property and equipment and debt. The Company expects no effect on the results of operations other than the classification of operating lease payments as interest expense.

NOTE 2 - REVENUES

Revenues for certain health care services are as follows:

	Three months ended March	
	2003	2
	(In thousands)	
Skilled nursing and assisted living services	$629,969	$6
Home health and hospice services	72,888	
Rehabilitation services (excludes intercompany revenues)	20,924	
Hospital care		
Other services	6,739	
	$730,520	$7

NOTE 3 - CONTINGENCIES

One or more subsidiaries or affiliates of Manor Care of America, Inc. (MCA) have been identified as potentially responsible parties (PRPs) in a variety of actions (the Actions) relating to waste disposal sites which allegedly are subject to remedial action under the Comprehensive Environmental Response Compensation Liability Act, as amended, 42 U.S.C. Sections 9601 et seq. (CERCLA) and similar state laws. CERCLA imposes retroactive, strict joint and several liability on PRPs for the costs of hazardous waste clean-up. The Actions arise out of the alleged activities of Cenco, Incorporated and its subsidiary and affiliated companies (Cenco). Cenco was acquired in 1981 by a wholly owned subsidiary of MCA. The Actions allege that Cenco transported and/or generated hazardous substances that came to be located at the sites in question. Environmental proceedings such as the Actions may involve owners and/or operators of the hazardous waste site, multiple waste generators and multiple waste transportation disposal companies. Such proceedings involve efforts by governmental entities and/or private parties to allocate or recover site investigation and clean-up costs, which costs may be substantial. The potential liability exposure for currently pending environmental claims and litigation, without regard to insurance coverage, cannot be quantified with precision because of the inherent uncertainties of litigation in the Actions and the fact that the ultimate cost of the remedial actions for some of the waste disposal sites where MCA is alleged to be a potentially responsible party has not yet been quantified. Based upon its current assessment of the likely outcome of the Actions, the Company believes that its future environmental liabilities will be about $4.5 million. The Company has received insurance proceeds that will offset amounts due as a result of these exposures, depending upon the ultimate liabilities.

The Company is party to various other legal matters arising in the ordinary course of business including patient care-related claims and litigation. At March 31, 2003 and December 31, 2002, the general and professional liability consisted of short-term reserves of $52.2 million and $50.3 million, respectively, which were included in accrued insurance liabilities, and long-term reserves of $117.5 million, which were included in other long-term liabilities. The expense for general and professional liability claims, premiums and administrative fees was $20.8 million and $17.6 million for the first quarter of 2003 and 2002, respectively, which was included in operating expenses. Although management believes that the Company's liability reserves are adequate, there can be no assurance that such provision and liability will not require material adjustment in future periods.

NOTE 4 - EARNINGS PER SHARE
The calculation of earnings per share (EPS) is as follows:

	Three months ended March 31,	
	2003	200
	(In thousands, except earnings p	
Numerator:		
Income before cumulative effect	$31,128	$33
Denominator:		
Denominator for basic EPS - weighted-average shares	93,659	101
Effect of dilutive securities:		
Stock options	551	
Non-vested restricted stock	294	
Denominator for diluted EPS - adjusted for weighted-average shares and assumed conversions	94,504	102
EPS - Income before cumulative effect:		
Basic and diluted	$ .33	$

Options to purchase shares of the Company's common stock that were not included in the computation of diluted EPS because the options' exercise prices were greater than the average market price of the common shares were: 5.3 million shares with an average exercise price of $24 for the first quarter of 2003 and 2.2 million shares with an average exercise price of $31 for the first quarter of 2002.

NOTE 5 - SEGMENT INFORMATION

The Company provides a range of health care services. The Company has one reportable operating segment, long-term care, which includes the operation of skilled nursing and assisted living facilities. The "Other" category includes the non-reportable segments and corporate items. The revenues in the "Other" category include services for rehabilitation, home health and hospice, and hospital care. The Company's hospital was sold on April 30, 2002. Asset information, including capital expenditures, is not reported by segment by the Company. Operating performance represents revenues less operating expenses and does not include general and administrative expense, depreciation and amortization, other income and expense items, income taxes and cumulative effect.

	Long-Term Care	Other
	(In thousands)	
Three months ended March 31, 2003		
Revenues from external customers	$ 629,969	$ 100,551
Intercompany revenues		14,486
Depreciation and amortization	29,522	2,152
Operating margin	104,435	14,598
Three months ended March 31, 2002		
Revenues from external customers	608,297	107,690
Intercompany revenues		13,537
Depreciation and amortization	28,680	3,089
Operating margin	115,592	10,065

NOTE 6 - SUBSEQUENT EVENT RELATED TO DEBT, REFINANCING AND SHARE REPURCHASE

In April 2003, the Company refinanced its five-year, $500 million revolving credit facility that was scheduled to mature September 24, 2003. As a result of the refinancing, the Company classified the $235.9 million outstanding under the five-year credit agreement at March 31, 2003 as long-term debt. The financing package includes a new three-year $200 million revolving credit facility, $200 million of 6.25% Senior Notes due in 2013 and $100 million of 2.125% Convertible Senior Notes due in 2023.

Manor Care, Inc.'s three-year $200 million revolving credit facility was established with a group of banks. As of April 24, 2003, there were no loans outstanding under this agreement and after consideration of usage for letters of credit, there was $164.2 million available for future borrowing. Loans under the three-year credit facility are guaranteed by substantially all of the Company's subsidiaries. This credit agreement contains various covenants, restrictions and events of default. Among other things, these provisions require the Company to maintain certain financial ratios and impose certain limits on its ability to incur indebtedness, create liens, pay dividends, repurchase stock, dispose of assets and make acquisitions.

Loans under the three-year credit facility bear interest at variable rates that reflect, at the election of the Company, the agent bank's base lending rate or an increment over Eurodollar indices of 1.025 percent to 1.325 percent, depending on the quarterly performance of a key ratio. The three-year credit facility also provides for a fee on the total amount of the facility, ranging from .225 percent to .425 percent, depending on the performance of the same key ratio. In addition to direct borrowings, the three-year credit facility may be used to support the issuance of up to $100 million of letters of credit.

The Company issued $200 million principal amount of 6.25% Senior Notes due in 2013, priced at 99.686 percent to yield 6.29 percent. Interest is payable each May 1 and November 1, beginning November 1, 2003. The Company also issued $100 million principal amount of 2.125% Convertible Senior Notes due in 2023, priced at 100 percent. Interest is payable each April 15 and October 15, beginning October 15, 2003. The Company may not redeem the Convertible Senior Notes before April 15, 2010. Starting with the six-month period beginning April 15, 2010, the Company may be obligated to pay contingent interest to the holders of the Convertible Senior Notes under certain circumstances. The initial conversion price is $31.12 per share of common stock, equivalent to 32.1337 shares of the Company's common stock per $1,000 principal amount of notes. The conversion price is subject to adjustment in certain events. The holders of the Convertible Senior Notes may convert their notes into shares of the Company's common stock prior to the stated maturity at their option only under the following circumstances: (1) if the average of the last reported sales price of the Company's common stock for the 20 trading days immediately prior to the conversion date is greater than or equal to 120% of the conversion price per share of common stock on such conversion date; (2) if the notes have been called for redemption; (3) upon the occurrence of specified corporate transactions; and (4) if the credit ratings assigned to the notes decline to certain levels. The holders of the Convertible Senior Notes may require the Company to purchase all or a portion of their notes at any of five specified dates during the life of the notes, with the first such date being April 15, 2005. Except for the initial repurchase date, the Company may elect to satisfy the repurchase in whole or in part with common stock rather than cash.

The initial net proceeds of approximately $293.2 million from the closing of the three-year credit facility, Senior Notes and Convertible Senior Notes were used to repay borrowings outstanding under the Company's five-year revolving credit facility and to purchase $25.0 million of the Company's common stock concurrent with the refinancing transactions. The Company is in the process of registering the Senior Notes and Convertible Senior Notes with the Securities and Exchange Commission. The Senior Notes and Convertible Senior Notes are guaranteed by substantially all of the Company's subsidiaries.

In April 2003, the Company's board of directors authorized management to spend an additional $100 million to purchase common stock through December 31, 2004. The Company purchased 1,775,400 shares in the first quarter of 2003 for $33.1 million and an additional 3,449,047 shares through April 24, 2003 for $68.9 million, including the $25 million repurchased concurrently with the Convertible Senior Notes offering. At April 24, 2003, the Company had remaining unused repurchase authority of $135.9 million.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

CRITICAL ACCOUNTING POLICIES

General and Professional Liability. Our general and professional reserves include amounts for patient care-related claims and incurred but not reported claims. The amount of our reserves is determined based on an estimation process that uses information obtained from both company-specific and industry data. The estimation process requires us to continuously monitor and evaluate the life cycle of the claims. Using data obtained from this monitoring and our assumptions about emerging trends, we along with our independent actuary develop information about the size of ultimate claims. The most significant assumptions used in the estimation process include determining the trend in costs, the expected cost of claims incurred but not reported and the expected costs to settle unpaid claims. Our assumptions take into consideration our internal efforts to contain our costs by reviewing our risk management programs, our operational and clinical initiatives, and other industry changes affecting the long-term care market. In comparing the first quarter of 2003 with the first quarter of 2002, the number of new claims is flat and our average settlement costs per claim have decreased slightly. Although we believe our reserves are adequate, we can give you no assurance that this liability will not require material adjustment in future periods.

RESULTS OF OPERATIONS -
QUARTER ENDED MARCH 31, 2003 COMPARED TO QUARTER ENDED MARCH 31, 2002

Revenues. Our revenues increased $14.5 million, or 2 percent, from the first quarter of 2002 to 2003. Excluding the results of our hospital that we sold in April 2002, our revenues increased $30.5 million, or 4 percent. Revenues from our long-term care segment (skilled nursing and assisted living facilities) increased $21.7 million, or 4 percent, due to increases in rates/patient mix--$18.0 million and occupancy--$5.7 million that were partially offset by a decrease in capacity--$2.0 million. Our revenues from the home health and hospice business increased $6.2 million, or 9 percent, primarily because of an increase in hospice services.

Our rate increases for the long-term care segment related to Medicaid and private pay. Our average Medicaid rate increased 6 percent from $121 per day in the first quarter of 2002 to $128 per day in the first quarter of 2003. Private and other rates for our skilled nursing facilities increased 5 percent from $180 per day in the first quarter of 2002 to $189 per day in the first quarter of 2003. The increase in overall rates was also a result of a shift in the mix of our patients to a higher percentage of Medicare patients, even though the Medicare rate decreased because certain of the increases in Medicare reimbursement for skilled nursing facilities provided for under the Medicare, Medicaid and SCHIP Balanced Budget Refinement Act of 1999, or BBRA 99, and the Medicare, Medicaid, and SCHIP Benefits Improvement and Protection Act of 2000, or BIPA 2000, expired on September 30, 2002, the so-called Medicare

Cliff. Our average Medicare rate was $333 per day in the first quarter of 2002 compared with $310 in the first quarter of 2003.

Our occupancy levels were 87 percent for the first quarter of 2002 compared with 88 percent for the first quarter of 2003. Excluding start-up facilities, our occupancy levels were 88 percent for the first quarters of 2002 and 2003. Our occupancy levels for skilled nursing facilities were 88 percent for the first quarter of 2002 compared with 89 percent for the first quarter of 2003. The quality mix of revenues from Medicare, private pay and insured patients that related to skilled nursing and assisted living facilities and rehabilitation operations remained constant at 68 percent for the first quarters of 2002 and 2003.

Our bed capacity declined between the first quarter of 2002 and 2003 primarily because we closed or sold three skilled nursing facilities with 498 beds, which was partially offset by opening three assisted living facilities with 188 beds.

Operating Expenses. Our operating expenses in the first quarter of 2003 increased $21.2 million, or 4 percent, compared with the first quarter of 2002. Excluding the results of our hospital that was sold on April 30, 2002, operating expenses increased $35.3 million, or 6 percent. Operating expenses from our long-term care segment increased $32.8 million, or 7 percent. Our operating expenses from our home health and hospice business increased $5.1 million, or 9 percent, because of an increase in services.

We attribute the largest portion ($20.3 million) of the long-term care operating expense increase between the first quarter of 2002 and 2003 to wages, temporary staffing and payroll overhead. Our other operating expense increases for this segment included ancillary costs, excluding internal labor, of $2.2 million and general and professional liability expense of $3.6 million. Ancillary costs, which include various types of therapies, medical supplies and prescription drugs, increased as a result of our more medically complex patients. Our general and professional liability expense increased primarily because of our increase in the monthly claims accrual from $5.0 million in the first quarter of 2002 to $6.0 million in the first quarter of 2003.

Depreciation and Amortization. Our depreciation increased $0.6 million from the first quarter of 2002 to 2003. The increase in depreciation related to our capital expenditures in the past year and 11 facilities that were held for sale in 2002, which was partially offset by a decline in depreciation of $1.0 million from the sale of our hospital and writedown of asset values due to impairment in 2002. Amortization decreased $0.7 million primarily due to a decrease in software amortization.

Interest Expense. Interest expense decreased $1.1 million related to a decline in debt levels. With the refinancing of our five-year credit facility in April 2003, we expect our interest expense to increase by approximately $1.0 million per month. See Note 6 to the consolidated financial statements for discussion of our debt refinancing.

Gain (Loss) on Sale of Assets. Our loss on sale of assets in 2002 related to sales of land that we decided not to develop.

Equity in Earnings of Affiliated Companies. Our equity earnings increased in the first quarter of 2003 compared with 2002 primarily because of our ownership interests in two hospitals acquired on April 30, 2002.

Cumulative Effect of Change in Accounting Principle. In July 2001, the Financial Accounting Standards Board issued Statement No. 142, "Goodwill and Other Intangible Assets," that we adopted January 1, 2002. Under this Statement, goodwill and indefinite-lived intangible assets are no longer amortized but are reviewed annually for impairment, or more frequently if impairment indicators arise. We completed our initial impairment test in the second quarter of 2002 and determined that $1.3 million of our goodwill related to our vision business was impaired. The impairment loss, with no tax effect, was recorded retroactive to January 1, 2002 as a cumulative effect of a change in accounting principle.

FINANCIAL CONDITION - MARCH 31, 2003 AND DECEMBER 31, 2002

Property and equipment increased $3.7 million primarily because of $23.2 million in new construction and renovations to existing facilities and a $10.1 million cash payment to exercise a purchase option on a leased facility. These increases were partially offset by depreciation of $29.5 million and disposal of assets of $1.9 million.

Accrued insurance liabilities decreased $14.7 million primarily due to an $18.6 million payment of an environmental liability in January 2003. We also received insurance proceeds of $9.5 million in January 2003 to offset half of this payment.

Long-term debt due within one year decreased $264.8 million primarily due to the reclassification of our credit agreement debt of $235.9 million from short-term debt to long-term debt at March 31, 2003 because we refinanced our debt in April 2003, as further discussed in Note 6 to the consolidated financial statements.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flows. During the first quarter of 2003, we satisfied our cash requirements from cash generated from operating activities. Cash flows from operating activities were $80.7 million for the first quarter of 2003. Our operating cash flows decreased $15.5 million from the first quarter of 2002 primarily because of our environmental liability payment of $18.6 million in the first quarter of 2003. We used the cash principally for capital expenditures, acquisitions, to repay debt and to purchase our common stock.

Investing Activities. Our expenditures for property and equipment of $23.2 million in the first quarter of 2003 included $3.0 million to construct new facilities and expand existing facilities. In the first quarter of 2003, we exercised a purchase option for $10.1 million on a facility that was previously leased.

Debt Agreement. At March 31, 2003, outstanding borrowings totaled $235.9 million under our five-year, $500 million revolving credit agreement that was scheduled to mature September 24, 2003 but was refinanced in April 2003. The financing package includes a new three-year $200 million revolving credit facility, $200 million of 6.25% Senior Notes due in 2013 and $100 million of 2.125% Convertible Senior Notes due in 2023. The initial net proceeds of approximately $293.2 million from the closing of these transactions were used to repay borrowings outstanding under the Company's five-year revolving credit facility and to purchase $25.0 million of the Company's common stock concurrent with the refinancing transactions. As of April 24, 2003, there were no loans outstanding under the new three-year revolving credit facility and after consideration of usage for letters of credit, there was $164.2 million available for future borrowing.

Stock Purchase. During 2001 and 2002, our board of directors authorized us to spend up to $300 million to purchase our common stock with $200 million of the authorization expiring on December 31, 2003 and the remaining $100 million on December 31, 2004. In April 2003, our board authorized an additional $100 million through December 31, 2004. With these authorizations, we purchased 1,775,400 shares in the first quarter of 2003 for $33.1 million and an additional 3,449,047 shares through April 24, 2003 for $68.9 million, which includes the $25.0 million repurchased concurrently with the Convertible Senior Notes offering. We have $135.9 million remaining authority to repurchase our shares as of April 24. We may use the shares for internal stock option and 401(k) match programs and for other uses, such as possible future acquisitions.

We believe that a certain amount of debt has an appropriate place in our overall capital structure and it is not our strategy to eliminate all debt financing. Because of our significant annual cash flow, we believe that we will be able to refinance the major pieces of our debt as they mature. Based on our ability to refinance significant portions of our debt as it matures, we believe that our cash flow from operations will be sufficient to cover operating needs, future capital

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expenditure requirements and scheduled debt payments of miscellaneous small borrowing arrangements and capitalized leases. It is likely that we will pursue growth from acquisitions, partnerships and other ventures that we would fund from excess cash from operations, credit available under a refinanced bank credit agreement and other financing arrangements that are normally available in the marketplace.

CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS

This report may include forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events. We identify forward-looking statements in this report by using words or phrases such as "anticipate," "believe," "estimate," "expect," "intend," "may be," "objective," "plan," "predict," "project," and "will be" and similar words or phrases, or the negative thereof.

These forward-looking statements are subject to numerous assumptions, risks and uncertainties. Factors which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by us in those statements include, among others: changes in the health care industry because of political and economic influences; changes in Medicare, Medicaid and certain private payors' reimbursement levels; existing government regulations, including applicable health care, tax and health and safety regulations, and changes in, or the failure to comply with, governmental regulations or the interpretations thereof; legislative proposals for health care reform; competition and general economic and business conditions; the ability to attract and retain qualified personnel; changes in current trends in the cost and volume of patient-care related claims and workers' compensation claims and in insurance costs related to such claims; and other litigation.

Although we believe the expectations reflected in our forward-looking statements are based upon reasonable assumptions, we can give no assurance that we will attain these expectations or that any deviations will not be material. Except as otherwise required by the federal securities laws, we disclaim any obligations or undertaking to publicly release any updates or revisions to any forward-looking statement contained in this report to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

See the discussion of our market risk in our Form 10-K for the year ended December 31, 2002. The fair value of our 7 1/2% and 8% Senior Notes at March 31, 2003 has not changed significantly since year end.

Item 4. Controls and Procedures

Within 90 days of filing this quarterly report, an evaluation was performed under the supervision and with the participation of our management, including the chief executive officer, or CEO, and chief financial officer, or CFO, of the effectiveness of the design and operation of our disclosure procedures. Based on that evaluation, our management, including the CEO and CFO, concluded that our disclosure controls and procedures were effective as of March 31, 2003 and the evaluation date. There have been no significant changes in our internal controls or in other factors that could significantly affect internal controls subsequent to the date of our evaluation.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

See Note 3 - Contingencies in the notes to the consolidated financial statements for a discussion of litigation related to environmental matters and patient-care related claims.

Item 2. Changes in Securities.
None

Item 3. Defaults Upon Senior Securities.
None

Item 4. Submission of Matters to a Vote of Security Holders.
None

Item 5. Other Information.
None

Item 6. Exhibits and Reports on Form 8-K.
(a) Exhibits

S-K Item
601 No.

4.1	$200,000,000 Credit Agreement dated as of April 21, 2003 among Manor Care, Inc., as the Borrower, Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer, and The Other Lenders Party Hereto
99.1	Chief Executive Officer Certification Pursuant To 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 Of The Sarbanes-Oxley Act Of 2002
99.2	Chief Financial Officer Certification Pursuant To 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 Of The Sarbanes-Oxley Act Of 2002

(b) Reports on Form 8-K
None in the first quarter of 2003.

On April 10, 2003, Manor Care, Inc. filed a Form 8-K and under Item 9 included the April 9, 2003 press release announcing the Company's intention to refinance its existing credit facility and to issue $200 million of Senior Notes and $90 million of Senior Convertible Notes. The risk factors that were included in the preliminary Offering Memorandum in connection with the Senior Convertible Notes were included in the Form 8-K.

On April 25, 2003, Manor Care, Inc. filed a Form 8-K and under Item 9 (the information was provided under Item 12 - Results of Operations and Financial Condition) furnished the April 25, 2003 press release reporting the Company's financial results for the first quarter of 2003.

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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.

Manor Care, Inc.
(Registrant)

Date April 28, 2003

By /s/ Geoffrey G. Meyers

Geoffrey G. Meyers, Executive Vice President and Chief Financial Officer

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CERTIFICATIONS

I, Paul A. Ormond, certify that:

(1) I have reviewed this quarterly report on Form 10-Q of Manor Care, Inc.;

(2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact

necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

(3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

(4) The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a. Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b. Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c. Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

(5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a. All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

(6) The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: April 28, 2003

/s/ Paul A. Ormond
Chairman, President and Chief Executive Officer

I, Geoffrey G. Meyers, certify that:

(1) I have reviewed this quarterly report on Form 10-Q of Manor Care, Inc.;

(2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

(3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

(4) The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a. Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b. Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c. Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

(5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a. All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

(6) The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: April 28, 2003

/s/ Geoffrey G. Meyers
Executive Vice President and Chief Financial Officer

EXHIBIT INDEX

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