

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

CORAM HEALTHCARE CORP  
Form 10-Q  
November 19, 2001

=====

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

-----

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2001

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 1-11343

-----

CORAM HEALTHCARE CORPORATION

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

33-0615337  
(I.R.S. Employer  
Identification No.)

1675 Broadway  
Suite 900  
Denver, CO  
(Address of principal executive offices)

80202  
(Zip Code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (303) 292-4973

-----

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

The number of shares outstanding of the Registrant's Common Stock, \$.001 par value, as of November 16, 2001 was 49,638,452.

=====

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

PART I

FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CORAM HEALTHCARE CORPORATION  
 (DEBTOR-IN-POSSESSION)  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	SEPTEMBER 30, 2001	DECEMBER 31, 2000
	-----	-----
	(UNAUDITED)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents .....	\$ 18,230	\$
Cash limited as to use .....	320	
Accounts receivable, net of allowances of \$14,863 and \$17,912 ....	77,387	
Inventories .....	12,092	
Deferred income taxes, net .....	365	
Other current assets .....	5,892	
	-----	
Total current assets .....	127,185	
Property and equipment, net .....	14,930	
Deferred income taxes, net .....	1,612	
Other deferred costs and intangible assets, net of accumulated amortization of \$18,809 and \$16,963 .....	6,905	
Goodwill, net of accumulated amortization of \$95,044 and \$87,770 .....	186,582	
Other assets .....	6,043	
	-----	
Total assets .....	\$ 343,257	\$
	=====	=====
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities not subject to compromise:		
Accounts payable .....	\$ 24,149	\$
Accrued compensation and related liabilities .....	14,366	
Current maturities of long-term debt .....	8	
Insurance and accreditation notes payable .....	876	
Income taxes payable .....	537	
Deferred income taxes .....	956	
Accrued merger and restructuring costs .....	814	
Accrued reorganization costs for administrative professionals ....	7,836	
Other accrued liabilities, including interest payable .....	7,704	
	-----	
Total current liabilities not subject to compromise .....	57,246	
Total current liabilities subject to compromise (See Note 2) ....	167,610	
	-----	
Total current liabilities .....	224,856	
Long-term liabilities not subject to compromise:		
Long-term debt, less current maturities .....	170	
Minority interests in consolidated joint ventures and preferred stock issued by a subsidiary .....	6,079	

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Other liabilities .....	19,108	
Deferred income taxes .....	1,021	
Net liabilities of discontinued operations .....	26,506	
	-----	
Total liabilities .....	277,740	
Commitments and contingencies .....	--	
Stockholders' equity:		
Preferred stock, par value \$.001, authorized 10,000 shares, none issued .....	--	
Common stock, par value \$.001, 150,000 shares Authorized, 49,638 shares issued and outstanding .....	50	
Additional paid-in capital .....	427,360	
Accumulated deficit .....	(361,893)	
	-----	
Total stockholders' equity .....	65,517	
	-----	
Total liabilities and stockholders' equity .....	\$ 343,257	\$
	=====	=====

See accompanying notes to unaudited condensed consolidated financial statements.

2

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)  
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	THREE MONTHS ENDED SEPTEMBER 30,	
	2001	2000
	-----	-----
Net revenue .....	\$ 93,762	\$ 102,762
Cost of service .....	68,651	75,000
	-----	-----
Gross profit .....	25,111	27,762
Operating expenses:		
Selling, general and administrative expenses .....	19,383	22,000
Provision for estimated uncollectible accounts .....	2,859	3,000
Amortization of goodwill .....	2,424	2,000
Restructuring cost recovery .....	--	--
	-----	-----
Total operating expenses .....	24,666	28,000
	-----	-----
Operating income (loss) from continuing operations .....	445	(1,238)
Other income (expense):		
Interest income .....	113	113
Interest expense (excluding post-petition contractual interest of \$3.5 million and \$10.4 million for the three and nine months ended September 30, 2001, respectively) .....	(4,072)	(6,000)

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Gains on sales of businesses .....	--	18
Equity in net income of unconsolidated joint ventures .....	259	
Other income (expense), net .....	9	
	-----	-----
Income (loss) from continuing operations before reorganization expenses, income taxes and minority interests .....	(3,246)	11
Reorganization expenses, net .....	(3,739)	(1)
	-----	-----
Income (loss) from continuing operations before income taxes and minority interests .....	(6,985)	9
Income tax expense .....	50	
Minority interests in net income of consolidated joint ventures .....	75	
	-----	-----
Income (loss) from continuing operations .....	(7,110)	9
Income (loss) from disposal of discontinued operations .....	--	
	-----	-----
Net income (loss) .....	\$ (7,110)	\$ 9
	=====	=====
Basic Income (Loss) Per Share		
Income (loss) from continuing operations .....	\$ (0.14)	\$
Income (loss) from discontinued operations .....	--	
	-----	-----
Net income (loss) .....	\$ (0.14)	\$
	=====	=====
Diluted Income (Loss) Per Share		
Income (loss) from continuing operations .....	\$ (0.14)	\$
Income (loss) from discontinued operations .....	--	
	-----	-----
Net income (loss) .....	\$ (0.14)	\$
	=====	=====

See accompanying notes to unaudited condensed consolidated financial statements.

3

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)  
(IN THOUSANDS)

	NINE MONTHS ENDED SEPTEMBER 30,	
	2001	2000
	-----	-----
Net cash provided by continuing operations before reorganization expenses .....	\$ 6,735	\$ 30,513
Net cash used by reorganization expenses .....	(6,962)	(1,001)
	-----	-----
Net cash provided by (used in) continuing operations (net of reorganization expenses) .....	(227)	29,512
	-----	-----
Cash flows from investing activities:		

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Purchases of property and equipment .....	(4,792)	(2,778)
Proceeds from sales of businesses .....	--	41,513
Proceeds from dispositions of property and equipment .....	69	60
	-----	-----
Net cash provided by (used in) investing activities .....	(4,723)	38,795
	-----	-----
Cash flows from financing activities:		
Borrowings on line of credit .....	--	1,500
Repayments of debt obligations .....	(277)	(55,376)
Payment of debtor-in-possession financing costs (post-petition) .....	--	(503)
Repayments of insurance note payable .....	(1,372)	--
Deposits to collateralize letters of credit .....	(2,095)	--
Cash distributions paid to minority interests .....	(308)	(850)
	-----	-----
Net cash used in financing activities .....	(4,052)	(55,229)
	-----	-----
Net increase (decrease) in cash from continuing operations ....	\$ (9,002)	\$ 13,078
	=====	=====
Net cash used in discontinued operations .....	\$ (27)	\$ (3,192)
	=====	=====

See accompanying notes to unaudited condensed consolidated financial statements.

4

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS  
SEPTEMBER 30, 2001

### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Business Activity. As of September 30, 2001, Coram Healthcare Corporation ("CHC") and its subsidiaries ("Coram" or the "company") were engaged primarily in the business of furnishing alternate site (outside the hospital) infusion therapy, including non-intravenous home health products such as durable medical equipment and respiratory services. Other services offered by Coram include centralized management, administration and clinical support for clinical research trials. Coram delivers its alternate site infusion therapy services through 76 branch offices located in 40 states and Ontario, Canada. CHC and its first tier wholly owned subsidiary, Coram, Inc. ("CI") (collectively the "Debtors"), filed voluntary petitions under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") on August 8, 2000. Since that date, the Debtors have been operating as debtors-in-possession subject to the jurisdiction of the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court"). None of the company's other subsidiaries is a debtor in the proceeding. See Note 2 for further details.

In December 1999, Coram announced that it was repositioning its business to focus on its core alternate site infusion therapy business and the clinical research business operated by its subsidiary, CTI Network, Inc. Accordingly, Coram's primary business strategy is to focus its efforts on the delivery of its

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

core infusion therapies, including nutrition, anti-infective therapies and intravenous immunoglobulin ("IVIG") therapy for persons receiving transplants and coagulant and blood clotting therapies for persons with hemophilia. Coram has also implemented programs focused on the reduction and control of the costs of providing services and operating expenses, assessment of under-performing branches and review of branch efficiencies. Pursuant to this review, several branches have been closed or scaled back to serve as satellites for other branches and personnel have been eliminated. See Note 6 for further details. Most of the company's net revenue is derived from third-party payers such as private indemnity insurers, managed care organizations and governmental payers.

Prior to August 1, 2000, the company delivered pharmacy benefit management and specialty mail-order pharmacy services for chronically ill patients through its Coram Prescription Services ("CPS") business from one primary mail order facility, four satellite mail order facilities and one retail pharmacy. The pharmacy benefit management service provided on-line claims administration, formulary management and certain drug utilization review services through a nationwide network of retail pharmacies. CPS's specialty mail-order pharmacy services were delivered through its six facilities, which provided distribution, compliance monitoring, patient education and clinical support to a wide variety of patients. On July 31, 2000, Coram completed the sale of its CPS business to a management-led group financed by GTCR Golder Rauner, L.L.C. for a one-time payment of approximately \$41.3 million. See Note 4 for further details.

Prior to January 1, 2000, the company provided ancillary network management services through its subsidiaries, Coram Resource Network, Inc. and Coram Independent Practice Association, Inc. (collectively the "Resource Network Subsidiaries" or "R-Net"), which managed networks of home healthcare providers on behalf of HMOs, PPOs, at-risk physician groups and other managed care organizations. R-Net served its customers through two primary call centers and three satellite offices. In April 1998, the company entered into a five-year capitated agreement with Aetna U.S. Healthcare, Inc. ("Aetna") (the "Master Agreement") for the management and provision of certain home health services, including home infusion, home nursing, respiratory therapy, durable medical equipment, hospice care and home nursing support for several of Aetna's disease management programs. Effective July 1, 1998, the company began receiving capitated payments on a monthly basis for members covered under the Master Agreement, assumed financial risk for certain home health services and began providing management services for a network of home health providers through R-Net. The agreements that R-Net had for the provision of ancillary network management services have been terminated and R-Net is no longer providing any ancillary network management services. Coram and Aetna were previously involved in litigation over the Master Agreement; however, the litigation was amicably resolved and the case was dismissed on April 20, 2000. The Resource Network Subsidiaries filed voluntary bankruptcy petitions on November 12, 1999 with the Bankruptcy Court under Chapter 11 of the United States Bankruptcy Code and the Resource Network Subsidiaries are being liquidated pursuant to such proceedings.

5

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

Basis of Presentation. The accompanying unaudited condensed consolidated financial statements have been prepared by the company pursuant to the rules and regulations of the Securities and Exchange Commission (the "Commission") and

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

reflect all adjustments and disclosures (consisting of normal recurring accruals and, effective August 8, 2000, all adjustments pursuant to the adoption of SOP 90-7, Financial Reporting by Entities in Reorganization under the Bankruptcy Code ("SOP 90-7")) that are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows as of and for the interim periods presented herein. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the applicable Commission regulations. The results of operations for the interim periods ended September 30, 2001 are not necessarily indicative of the results for the full fiscal year. For further information, refer to the audited consolidated financial statements and notes thereto included in the company's Annual Report on Form 10-K for the year ended December 31, 2000.

The accompanying condensed consolidated financial statements have been prepared on a going concern basis, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the ordinary course of business. However, as a result of the Debtors' bankruptcy filings and circumstances relating thereto, including the company's leveraged financial structure and cumulative losses from operations, such realization of assets and liquidation of liabilities are subject to significant uncertainty. During the pendency of the Debtors' Chapter 11 bankruptcy proceedings, the company may sell or otherwise dispose of assets and liquidate or settle liabilities for amounts other than those reflected in the Condensed Consolidated Financial Statements. Further, a confirmed plan of reorganization in the Chapter 11 bankruptcy proceedings could materially change the amounts reported in the Condensed Consolidated Financial Statements, which do not give effect to any adjustments of the carrying value of assets or liabilities that might be necessary as a consequence of a confirmed plan of reorganization (see Note 2 for further details). The company's ability to continue as a going concern is dependent upon, among other things, confirmation of a plan of reorganization, future profitable operations, the ability to comply with the terms of the company's financing agreements, the ability to remain in compliance with the physician ownership and referral provisions of the Omnibus Budget Reconciliation Act of 1993 (commonly known as "Stark II") and the ability to generate sufficient cash from operations and/or financing arrangements to meet its obligations.

Reclassifications. Certain amounts in the 2000 condensed consolidated financial statements have been reclassified to conform to the 2001 presentation.

Provision for Estimated Uncollectible Accounts. Management regularly reviews the collectibility of accounts receivable utilizing system-generated reports which track collection and write-off activity. Estimated write-off percentages are then applied to each aging category by payer classification to determine the allowance for estimated uncollectible accounts. Additionally, the company establishes appropriate additional reserves for accounts that are deemed uncollectible due to occurrences such as bankruptcy filings by the payers. The allowance for estimated uncollectible accounts is adjusted as needed to reflect current collection, write-off and other trends, including changes in assessment of realizable value. While management believes the resulting net carrying amounts for accounts receivable are fairly stated at each quarter-end and that the company has made adequate provision for uncollectible accounts based on all information available, no assurances can be given as to the level of future provisions for uncollectible accounts, or how they will compare to the levels experienced in the past. The company's ability to successfully collect its accounts receivable depends, in part, on its ability to adequately supervise and train personnel in billing and collections, and minimize losses related to branch consolidations and system changes.

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

Earnings per Share. Basic income (loss) per share excludes any dilutive effects of options, warrants and convertible securities. The company experienced losses from continuing operations for the three and nine months ended September 30, 2001 and, in accordance with the provisions of Financial Accounting Standards Board ("FASB") Statement No. 128, Earnings Per Share, the denominator utilized to calculate earnings (loss) per share does not increase when losses from continuing operations are in evidence because to do so would be anti-dilutive. However, the company experienced income from continuing operations for the three and nine months ended September 30, 2000. The following table sets forth the computations of basic and diluted income (loss) per share for the three and nine months ended September 30, 2001 and 2000 (in thousands, except per share amounts):

	THREE MONTHS ENDED SEPTEMBER 30,	
	2001	2000
	-----	-----
Numerator for basic and diluted income (loss) per share		
Income (loss) from continuing operations .....	\$ (7,110)	\$ 9,200
Income (loss) from discontinued operations .....	--	324
	-----	-----
Net income (loss) .....	\$ (7,110)	\$ 9,524
	=====	=====
Weighted average shares - denominator for basic		
Income (loss) per share .....	49,638	49,638
Effects of other dilutive securities:		
Stock options .....	--	--
Warrants .....	--	3,136
	-----	-----
Denominator for diluted income (loss) per share - adjusted		
Weighted average shares and assumed conversion .....	49,638	52,774
	=====	=====
Basic income (loss) per share:		
Income (loss) from continuing operations .....	\$ (0.14)	\$ 0.18
Income (loss) from discontinued operations .....	--	0.01
	-----	-----
Net income (loss) .....	\$ (0.14)	\$ 0.19
	=====	=====
Diluted income (loss) per share:		
Income (loss) from continuing operations .....	\$ (0.14)	\$ 0.17
Income (loss) from discontinued operations .....	--	0.01
	-----	-----
Net income (loss) .....	\$ (0.14)	\$ 0.18
	=====	=====

Derivatives and Hedging Activities. In June 1998, the FASB issued Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments



## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

and Hedging Activities ("Statement 133"), which requires the recognition of all derivative instruments as assets or liabilities, measured at fair value. Statement 133 was effective for fiscal years beginning after June 15, 2000. Accordingly, the company adopted the new accounting pronouncement effective January 1, 2001; however, it had no effect on the company's financial position or operating results.

Business Combinations. In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141, Business Combinations ("Statement 141"), which requires the use of the purchase method of accounting for all business combinations initiated after June 30, 2001, establishes specific criteria for the recognition of intangible assets separately from goodwill and requires unallocated negative goodwill to be written off immediately as an extraordinary gain. Statement 141 is effective for the company's financial statements for the year ending December 31, 2002. The adoption of this accounting pronouncement is not currently anticipated to have a material impact on the company's financial position or results of operations.

Goodwill and Other Intangible Assets. In July 2001, the FASB issued Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets ("Statement 142"), which primarily addresses the accounting for goodwill and intangible assets subsequent to their acquisition. Statement 142 requires that goodwill and indefinite long-lived intangible assets no longer be amortized to earnings, but instead be reviewed periodically for impairment. Statement 142 is effective for the company's financial statements for the year ending December 31, 2002. Management is currently evaluating the impact that the adoption of this accounting pronouncement will have on the company's financial position and results of operations.

7

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

### 2. REORGANIZATION UNDER CHAPTER 11 OF THE UNITED STATES BANKRUPTCY CODE

On August 8, 2000, CHC and CI filed voluntary petitions under Chapter 11 of the Bankruptcy Code. Following the filing of the voluntary Chapter 11 petitions, the Debtors have been operating as debtors-in-possession subject to the jurisdiction of the Bankruptcy Court. None of the company's other subsidiaries is a debtor in the proceeding. The Debtors' need to seek the relief afforded by the Bankruptcy Code was due, in part, to their requirement to remain in compliance with the physician ownership and referral provisions of the Omnibus Budget Reconciliation Act of 1993 (commonly referred to as "Stark II") after December 31, 2000 (see discussion of Stark II in Note 10) and the scheduled May 27, 2001 maturity of the Series A Senior Subordinated Unsecured Notes. Accordingly, the Debtors sought advice and counsel from a variety of sources and, in connection therewith, the Board of Directors unanimously concluded that the bankruptcy and restructuring were the only viable alternatives.

On August 9, 2000, the Bankruptcy Court approved the Debtors' motions for: (i) payment of employee wages and salaries and certain benefits and other employee obligations; (ii) payment of critical trade vendors, utilities and insurance in the ordinary course of business for both pre and post-petition expenses; (iii) access to a debtor-in-possession financing arrangement (see Note 7 for details of the executed agreement); and (iv) use of all company bank

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

accounts for normal business operations. In September 2000, the Bankruptcy Court approved the Debtors' motion to reject four unexpired, non-residential real property leases and any associated subleases. The rejected leases include underutilized locations in: (i) Allentown, Pennsylvania; (ii) Denver, Colorado; (iii) Philadelphia, Pennsylvania; and (iv) Whippany, New Jersey. The successful rejection of the Whippany, New Jersey lease caused the company to reverse certain reserves that had previously been established related to closure of its discontinued operations. Additionally, in September 2001 the Bankruptcy Court approved the Debtors' motion for an extension of the period of time in which the Debtors can reject unexpired leases of non-residential real property up to and including January 1, 2002. Certain other motions filed by the Debtors have been granted and others are presently pending.

In September 2000 and October 2000, the Bankruptcy Court approved payments of up to approximately \$2.6 million for retention bonuses to certain key employees. The bonuses were scheduled to be paid in two equal installments on (i) the later of the date of emergence from bankruptcy or December 31, 2000 and (ii) December 31, 2001. Due to events that have delayed the emergence from bankruptcy, the Bankruptcy Court approved early payment of the first installment to most individuals within the retention program and such payments, aggregating approximately \$0.7 million, were made on March 15, 2001. The remaining portion of the first installment of approximately \$0.5 million, which relates to the company's Chief Executive Officer and Executive Vice President, is scheduled for payment upon approval of a plan of reorganization by the Bankruptcy Court, and the second installment remains scheduled to be paid on December 31, 2001. The company is accruing monthly amounts as earned pursuant to the provisions of the retention plan.

On September 7, 2001, the Bankruptcy Court approved payments of up to \$2.7 million for management incentive compensation bonuses (the "MIP Plan") related to the year ended December 31, 2000 for all individuals participating in the MIP Plan, except for the company's Chief Executive Officer. In connection therewith, payments were made to those individuals in September 2001.

On or about May 9, 2001, the Bankruptcy Court approved the Debtors' motion requesting authorization to enter into an insurance premium financing agreement with AICCO, Inc. (the "Financing Agreement") to finance the payment of premiums under certain of the Debtors' insurance policies. Under the terms of the Financing Agreement, the Debtors made a down payment of approximately \$1.1 million. The amount financed is approximately \$2.1 million and is secured by the unearned premiums and loss payments under the insurance policies covered by the Financing Agreement. The amount financed is being paid in eight monthly installments of approximately \$0.3 million each, including interest at a per annum rate of 7.85%. In addition, AICCO, Inc. has the right to terminate the insurance policies and collect the unearned premiums (as administrative expenses) if the Debtors do not make the monthly payments called for by the Financing Agreement.

On October 29, 2001, the Debtors filed a motion with the Bankruptcy Court requesting approval of a proposed asset purchase agreement which would provide the authority for a non-debtor subsidiary of the company to sell certain durable medical equipment presently located at its New Orleans branch to a third party. A hearing on the motion will be held in November 2001; however, no assurances can be given that the Bankruptcy Court will approve the proposed transaction or that the parties will ultimately agree on a final asset purchase agreement.

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

### NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)

The Debtors are currently paying the post-petition claims of their vendors in the ordinary course of business and are, pursuant to an order of the Bankruptcy Court, causing their subsidiaries to pay their own debts in the ordinary course of business. Even though the filing of the Chapter 11 cases constituted defaults under the company's principal debt instruments, the Bankruptcy Code imposes an automatic stay that will generally preclude the creditors and other interested parties under such arrangements from taking remedial action in response to any such resulting default without prior Bankruptcy Court approval.

On September 11, 2000, the Resource Network Subsidiaries filed a motion in the Debtors' Chapter 11 proceedings seeking, among other things, to have the two separate bankruptcy proceedings substantively consolidated into one proceeding. The Resource Network Subsidiaries and the Debtors engaged in discovery related to this substantive consolidation motion and, in connection therewith, the parties reached a settlement agreement in November 2000, which was approved by an order of the Bankruptcy Court. See Note 10 for further details.

On the same day that the Chapter 11 cases were filed, the Debtors filed their joint plan of reorganization (the "Joint Plan") and their joint disclosure statement with the Bankruptcy Court. The Joint Plan was subsequently amended and restated (the "Restated Joint Plan") and, on or about October 10, 2000, the Restated Joint Plan and the First Amended Disclosure Statement with respect to the Restated Joint Plan were authorized for distribution by the Bankruptcy Court. Among other things, the Restated Joint Plan provided for: (i) a conversion of all of the CI obligations represented by the company's Series A Senior Subordinated Unsecured Notes (the "Series A Notes") and the Series B Senior Subordinated Unsecured Convertible Notes (the "Series B Notes") into (a) a four-year, interest only note in the principal amount of \$180 million, that would bear interest at the rate of 9% per annum and (b) all of the equity in the reorganized CI; (ii) the payment in full of all secured, priority and general unsecured debts of CI; (iii) the payment in full of all secured and priority claims against CHC; (iv) the impairment of certain general unsecured debts of CHC, including, among others, CHC's obligations under the Series A Notes and the Series B Notes; and (v) the complete elimination of the equity interests of CHC. Furthermore, pursuant to the Restated Joint Plan, CHC would be dissolved as soon as practicable after the effective date of the Restated Joint Plan and the stock of CHC would no longer be publicly traded. Therefore, under the Debtors' Restated Joint Plan, as filed, the existing stockholders of CHC would have received no value for their shares and all of the outstanding equity of CI as the surviving entity would be owned by the holders of the company's Series A Notes and Series B Notes. Representatives of the company negotiated the principal aspects of the Joint Plan with representatives of the holders of the company's Series A Notes and Series B Notes and Senior Credit Facility prior to the filing of such Joint Plan.

On or about October 20, 2000, the Restated Joint Plan and First Amended Disclosure Statement were distributed for a vote among persons holding impaired claims that were entitled to a distribution under the Restated Joint Plan. The Debtors did not send ballots to the holders of other types of claims and interested parties, including equity holders, as the holders of such claims and interested parties were deemed to reject the Restated Joint Plan. The tabulated vote of the unsecured creditors was in favor of the company's Restated Joint Plan. However, culminating at a confirmation hearing on December 21, 2000, the Restated Joint Plan was not approved by the Bankruptcy Court. On April 25, 2001 and July 11, 2001, the Bankruptcy Court extended the period during which the Debtors have the exclusive right to file a plan or plans before the Bankruptcy Court to July 11, 2001 and August 1, 2001, respectively. Additionally, on August

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

2, 2001, the Bankruptcy Court extended the Debtors' exclusivity period to solicit acceptances of any filed plan or plans to November 9, 2001 (the date to solicit acceptances of the plan for CHC's equity holders was subsequently extended to November 12, 2001). On or about November 7, 2001, the company filed a motion seeking to extend the exclusivity dates to file a plan or plans and solicit acceptances thereof to December 31, 2001 and March 4, 2002, respectively. A hearing on the motion is scheduled for December 2001.

In order for the company to remain compliant with the requirements of Stark II, on December 29, 2000, pursuant to an order of the Bankruptcy Court, CI exchanged approximately \$97.7 million of the Series A Notes and approximately \$11.6 million of accrued but unpaid interest on the Series A Notes and the Series B Notes for 905 shares of CI Series A Cumulative Preferred Stock (see Notes 7 and 9 for further details). This transaction generated an extraordinary gain on troubled debt restructuring of approximately \$107.8 million, net of tax, which was recorded in the fourth quarter of the year ended December 31, 2000. At December 31, 2000, the company's stockholders' equity exceeded the minimum Stark II requirement necessary to comply with the public company exemption. See Note 10 for further discussion regarding Stark II.

9

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

On or about February 6, 2001, the Official Committee of the Equity Security Holders (the "Equity Committee") filed a motion with the Bankruptcy Court seeking permission to bring a derivative lawsuit directly against the company's Chief Executive Officer, a former member of the Board of Directors and Cerberus Partners, L.P. (a party to the company's debtor-in-possession financing agreement, Senior Credit Facility and Securities Exchange Agreement). On February 26, 2001, the Bankruptcy Court ruled that the Equity Committee's motion would not be productive at that time and, accordingly, the motion was denied without prejudice. On the same day, the Bankruptcy Court approved the Debtors' motion and appointed Goldin Associates, L.L.C. ("Goldin") as independent restructuring advisors to the Independent Committee of the Board of Directors (the "Independent Committee"). Among other things, the scope of Goldin's services include (i) reporting its findings to the Independent Committee, including its assessment of the appropriateness of the Restated Joint Plan, and advising the Independent Committee respecting an appropriate course of action calculated to bring the Debtors' bankruptcy proceedings to a fair and satisfactory conclusion, (ii) preparing a written report as may be required by the Independent Committee and/or the Bankruptcy Court and (iii) appearing before the Bankruptcy Court to provide testimony, as needed. Goldin was also appointed as a mediator among the Debtors, the Equity Committee and other parties in interest.

Based upon Goldin's findings and recommendations, as set forth in the Report of Independent Restructuring Advisor, Goldin Associates, L.L.C. (the "Goldin Report"), on July 31, 2001, the Debtors filed with the Bankruptcy Court a Second Joint Disclosure Statement, as amended (the "Second Disclosure Statement"), with respect to their Second Joint Plan of Reorganization, as amended (the "Second Joint Plan"). The Second Joint Plan, which was also filed on July 31, 2001, provides for terms of reorganization similar to those described in the Restated Joint Plan; however, utilizing Goldin's recommendations, as set forth in the Goldin Report, the following substantive modifications are included in the Second Joint Plan:

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

- o the payment of up to \$3.0 million to the holders of allowed general unsecured claims of CHC;
- o the payment of up to \$10.0 million to the holders of CHC equity interests (contingent upon such holders voting in favor of the Second Joint Plan);
- o cancellation of the issued and outstanding CI Series A Cumulative Preferred Stock; and
- o a \$7.5 million reduction in certain performance bonuses payable to Daniel D. Crowley, the company's Chief Executive Officer.

Under certain circumstances, as more fully discussed in the Second Disclosure Statement, the general unsecured claim holders may be entitled to receive a portion of the \$10.0 million cash consideration allocated to the holders of CHC equity interests.

In order to become effective, the Second Joint Plan is subject to a vote by certain impaired creditors and equity holders and final approval of the Bankruptcy Court. On September 6, 2001 and September 10, 2001, hearings before the Bankruptcy Court considered the adequacy of the Second Disclosure Statement and, in connection therewith, the Second Disclosure Statement was approved for distribution to holders of certain claims in interests who are entitled to vote on the Second Joint Plan. On or about September 21, 2001, the Debtors mailed ballots to those parties entitled to vote on the Second Joint Plan.

Among other things, the Equity Committee's motion to terminate the Debtors' exclusivity periods and file its own plan of reorganization was denied by the Bankruptcy Court on August 1, 2001. The Equity Committee also filed a motion protesting and objecting to the Debtors' Second Joint Plan. Moreover, the Official Committee of the Equity Security Holders and Official Committee of Unsecured Creditors in the Resource Network Subsidiaries' bankruptcy proceedings filed objections to confirmation of the Second Joint Plan and a motion to lift the automatic stay to pursue their claims against the company. Management of the company cannot predict what impact the Equity Committee or any other interested parties, including those parties associated with the Resource Network Subsidiaries' bankruptcy proceedings, will have on the Second Joint Plan.

The tabulation of the ballots distributed to the holders of certain claims in interests who were entitled to vote on the Second Joint Plan resulted in the CHC equity holders voting against confirmation of the Second Joint Plan and all other classes of claimholders voting in favor of the Second Joint Plan. The Bankruptcy Court may ultimately confirm a plan of reorganization notwithstanding the non-acceptance of the plan by an impaired class of creditors or equity holders if certain conditions of the Bankruptcy Code are satisfied; however, no assurances can be given regarding the confirmation of the Second Joint Plan. Bankruptcy Court confirmation hearings for final confirmation of the Second Joint Plan have commenced and will continue through early December 2001.

Under the Bankruptcy Code, certain claims against the Debtors in existence prior to the filing date are stayed while the Debtors continue their operations as debtors-in-possession. These claims are reflected in the Condensed Consolidated Balance Sheets as liabilities subject to compromise. Additional Chapter 11 bankruptcy claims have arisen and may continue to arise subsequent to the filing date resulting from the rejection of executory contracts, including certain leases, and from the determination by the Bankruptcy

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

CORAM HEALTHCARE CORPORATION  
 (DEBTOR-IN-POSSESSION)  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
 FINANCIAL STATEMENTS - (CONTINUED)

Court of allowed claims for contingencies and other disputed amounts. Parties affected by the rejections may file claims with the Bankruptcy Court in accordance with the provisions of the Bankruptcy Code and applicable rules. Claims secured by the Debtors' assets also are stayed, although the holders of such claims have the right to petition the Bankruptcy Court for relief from the automatic stay and foreclose on the property securing their claims. Additionally, certain claimants have sought relief from the Bankruptcy Court to remove the automatic stay and continue pursuit of their claims against the Debtors or the Debtors' insurance carriers.

The principal categories and balances of Chapter 11 bankruptcy claims accrued in the Condensed Consolidated Balance Sheets and included in liabilities subject to compromise are summarized as follows (in thousands) (December 31, 2000 liabilities subject to compromise have been adjusted from amounts previously reported to reflect the proposed \$7.5 million reduction in performance bonuses payable to the company's Chief Executive Officer):

	SEPTEMBER 30 2001 -----
Series A and Series B Notes in default and other long-term debt obligations .....	\$153,422
Management incentive compensation liability .....	7,500
Liabilities of discontinued operations subject to compromise .....	2,936
Earn-out obligation .....	1,268
Accounts payable .....	1,113
Accrued merger and restructuring costs (primarily severance liabilities) .....	468
Legal and professional liabilities .....	98
Other .....	805
	-----
Total liabilities subject to compromise .....	\$167,610 =====

Subsequent to December 31, 2000, one of the Debtors' creditors issued pre-petition credits of approximately \$1.1 million. These credits have been filed as claims against the Debtors' estates in the bankruptcy proceedings and have therefore been recorded as liabilities subject to compromise in the company's Condensed Consolidated Financial Statements.

In addition to the amounts disclosed in the table above, the holders of Coram, Inc.'s Series A Cumulative Preferred Stock continue to maintain a claim position within the Debtors' bankruptcy proceedings in the aggregate amount of their cumulative liquidation preference. Notwithstanding the debt to equity exchange, the aforementioned holders' priority in the Debtors' bankruptcy proceedings will be no less than it was immediately prior to said exchange.

Schedules were filed with the Bankruptcy Court setting forth the assets and liabilities of the Debtors as of the filing date as shown by the Debtors' accounting records. Differences between amounts shown by the Debtors and claims filed by creditors are being investigated and resolved. The ultimate amount and

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

the settlement terms for such liabilities will be subject to the Second Joint Plan, which, as discussed above, has been voted on and is now subject to confirmation by the Bankruptcy Court. Therefore, it is not possible to fully or completely estimate the fair value of the liabilities subject to compromise at September 30, 2001 due to the Debtors' Chapter 11 cases and the uncertainty surrounding the ultimate amount and settlement terms for such liabilities.

Reorganization expenses are items of expense or income that are incurred or realized by the company as a result of the reorganization. These items include, but are not limited to, professional fees, expenses related to key employee retention plans, United States Trustee fees and other expenditures incurred relating to the Chapter 11 proceedings, offset by interest earned on cash accumulated related to the Debtors not paying their pre-petition liabilities and other expenditures incurred relating to the Chapter 11 proceedings. The principal components of reorganization expenses for the three and nine months ended September 30, 2001 are as follows (in thousands):

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS SEPTEMBER
	2001	2000	2001
	-----	-----	-----
Legal, accounting and consulting fees .....	\$ 3,525	\$ 1,554	\$ 8,771
Key employee retention plan expenses .....	413	310	1,498
United States Trustee fees .....	12	10	31
Interest income .....	(211)	(13)	(297)
	-----	-----	-----
Total reorganization expenses, net .....	\$ 3,739	\$ 1,861	\$ 10,003

11

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

### 3. DISCONTINUED OPERATIONS

In November 1999, following the filing of voluntary bankruptcy petitions for the Resource Network Subsidiaries and the plan to liquidate the R-Net division, Coram disclosed as Net Liabilities of Discontinued Operations in the Condensed Consolidated Financial Statements the excess of R-Net's liabilities over its assets. Coram also separately reflected R-Net's operating results in the Condensed Consolidated Statements of Operations as Discontinued Operations.

For the three and nine months ended September 30, 2001, no Losses from Operations of Discontinued Operations of R-Net were reflected in the company's Condensed Consolidated Statements of Operations. The \$3.2 million Loss from Disposal of Discontinued Operations for the nine months ended September 30, 2000 includes additional reserves for litigation and other wind-down costs resulting from R-Net's Chapter 11 bankruptcy proceedings. The components of the net liabilities of discontinued operations included in the Condensed Consolidated Balance Sheets are summarized as follows (in thousands):

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

	SEPTEMBER 30, 2001
Cash .....	\$ 1,401
Intercompany receivable (payable) .....	(34)
Accounts payable .....	(29,461)
Accrued expenses .....	(1,348)
Other long-term liabilities .....	--
	-----
Net liabilities subject to compromise under Debtors' Chapter 11 case ....	2,936
	-----
Net liabilities of Discontinued Operations .....	\$(26,506)
	=====

As of September 30, 2001, approximately \$27.5 million of the liabilities related to the discontinued operations were subject to compromise under the R-Net Chapter 11 bankruptcy proceedings.

All of the R-Net locations have been closed in connection with the pending liquidation of R-Net. Additionally, Coram employees who were members of the Resource Network Subsidiaries' Board of Directors resigned during the year ended December 31, 2000 and currently only the Chief Restructuring Officer appointed by the Bankruptcy Court remains on the Board of Directors to manage and operate the liquidation of the R-Net business.

4. SALE OF CPS AND OTHER BUSINESSES

On July 31, 2000, the company completed the sale of substantially all of the assets and assignment of certain related liabilities of the CPS business to Curascript Pharmacy, Inc. and Curascript PBM Services, Inc. (collectively the "Buyers") for a one-time cash payment of approximately \$41.3 million. The Buyers were effectively a management-led group that was financed by GTCR Golder Rauner, L.L.C. During the quarter ended September 30, 2000, the company recorded a gain of approximately \$18.1 million related to the sale of the CPS business. The cash proceeds, after related expenses, were applied to the remaining principal balance under the company's revolving line of credit of \$28.5 million and an additional \$9.5 million was applied to the principal balance of the Series A Senior Subordinated Unsecured Notes. See Note 7 for further details.

Pursuant to a contingent consideration arrangement related to one of the company's operating subsidiaries, approximately \$0.4 million was recognized as incremental proceeds during the three months ended September 30, 2000. The contingency related to the operating activities of the subsidiary through June 30, 2000. Upon payment of the contingent consideration, substantially all conditions of the initial sale and purchase agreement were satisfied.

5. RELATED PARTY TRANSACTIONS

The company's current Chairman, Chief Executive Officer and President,



## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Daniel D. Crowley, owns a consulting company (Dynamic Healthcare Solutions, LLC ("DHS")) from which the company purchased services. Effective with the Debtors' Chapter 11 filings in the Bankruptcy Court, DHS employees who were serving as consultants to Coram terminated their employment with DHS and became fulltime Coram employees. Subsequent to December 31, 2000 and through November 16, 2001, approximately \$0.2 million was paid to Mr. Crowley's company for overhead costs of the consulting company's Sacramento, California location that are directly attributable to the duties that Mr. Crowley performed on behalf of Coram in 2001. For the three and nine months ended September 30, 2000, the company paid approximately \$0.1 million and \$0.4 million, respectively, to Mr. Crowley's consulting company for consulting services and reimbursable expenses.

Effective August 2, 2000, the company's Board of Directors approved a contingent bonus to Mr. Crowley. Under the agreement, subject to certain material terms and conditions, Mr. Crowley is to be paid \$1.8 million following the successful refinancing of the company's debt. In connection therewith and the debt to preferred stock exchange discussed in Notes 2 and 7, the company recorded a \$1.8 million reorganization expense for the success bonus in 2000. Such success bonus will not be payable until such time as the Debtors' or another interested party's plan of reorganization is fully approved by the Bankruptcy Court.

As more fully discussed in Note 2, Mr. Crowley's incentive compensation may be reduced by \$7.5 million in connection with the Debtors' Second Joint Plan. Such amount is recorded as current liabilities subject to compromise in the accompanying Condensed Consolidated Balance Sheets.

Effective August 1, 1999, Mr. Crowley and Cerberus Capital Management, L.P. (an affiliate of Cerberus Partners, L.P. ("Cerberus"), a party to the company's debtor-in-possession financing agreement, Senior Credit Facility and Securities Exchange Agreement), executed an agreement whereby Mr. Crowley is paid by Cerberus approximately \$1 million per annum plus the potential of performance related bonus opportunities, equity options and fringe benefits. The services rendered by Mr. Crowley to Cerberus include, but are not limited to, providing business and strategic healthcare investment advice to executive management at Cerberus and its affiliates. Moreover, Mr. Crowley is the Chairman of the Board of Directors of Winterland Productions, Inc. ("Winterland"), a privately held affinity merchandise company in which an interest is owned by an affiliate of Cerberus. On January 2, 2001, Winterland voluntarily filed for protection under Chapter 11 of the United States Bankruptcy Code in the Northern District of California.

### 6. ACQUISITIONS AND RESTRUCTURING

**Acquisitions.** Certain agreements related to previously acquired businesses or interests therein provide for additional contingent consideration to be paid by the company. The amount of additional consideration, if any, is generally based on the financial performance levels of the acquired companies. As of September 30, 2001, the company may be required to pay approximately \$1.3 million under such contingent obligations. However, payment of such amounts has been stayed by the Debtors' bankruptcy proceedings. Subject to certain elections by the company or the sellers, \$0.6 million of these contingent obligations may be paid in cash. In the period these payments become probable, they are recorded as additional goodwill. No payments were made during the nine months ended September 30, 2001 but approximately \$0.1 million was paid during the nine months ended September 30, 2000. See Note 10 for further details concerning contingencies relative to earn-out payments.

**Merger and Restructuring.** As a result of the formation of Coram and the May 1995 acquisition of substantially all of the assets of the alternate site infusion business of Caremark, Inc., a subsidiary of Caremark International, Inc., the company initiated a restructuring plan (the "Caremark Business

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Consolidation Plan") and charged approximately \$25.8 million to operations as a restructuring cost.

13

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

During December 1999, the company initiated an organizational restructure and strategic repositioning plan (the "Coram Restructure Plan") and charged approximately \$4.8 million to operations as a restructuring cost. The Coram Restructure Plan resulted in the closing of additional facilities and reduction of personnel. In connection therewith, the company reserved for (i) personnel reduction costs relating to severance payments, fringe benefits and taxes for employees that have been or may be terminated and (ii) facility closing costs that consist of rent, common area maintenance and utility costs for fulfilling lease commitments of approximately fifteen branch and corporate facilities that have been or may be closed or downsized. Reserves for facility closing costs are offset by amounts arising from sublease arrangements, but not until such arrangements are in the form of signed and executed contracts. As part of the Coram Restructure Plan, the company informed certain reimbursement sites of their estimated closure dates. Such operations were closed during the first half of 2001 and, in connection therewith, approximately 80 related employees were terminated.

Under the Caremark Business Consolidation Plan and the Coram Restructure Plan, the total charges through September 30, 2001, the estimate of total future cash expenditures and the estimated total charges are as follows (in thousands):

	CHARGES THROUGH SEPTEMBER 30, 2001			BAL
	CASH EXPENDITURES	NON-CASH CHARGES	TOTAL	
Caremark Business Consolidation Plan:				
Personnel reduction costs .....	\$ 11,300	\$ --	\$ 11,300	
Facility reduction costs .....	10,250	3,900	14,150	
Subtotal .....	21,550	3,900	25,450	
Coram Restructure Plan:				
Personnel reduction costs .....	2,361	--	2,361	
Facility reduction costs .....	995	--	995	
Subtotal .....	3,356	--	3,356	
Totals .....	\$ 24,906	\$ 3,900	\$ 28,806	
Restructuring costs subject to compromise .....				
Accrued Merger and Restructuring Costs				
Per the Condensed Consolidated Balance Sheets ...				

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

During the nine months ended September 30, 2001, significant items impacting the restructuring reserves that were not subject to compromise are summarized as follows (in thousands):

Balance at December 31, 2000 .....	\$ 2,301
Activity during the nine months ended September 30, 2001:	
Payments under the plans .....	(904)
Reversals principally due to changes in estimates attributable to leased facilities (lease assumption by a third party) and severance obligations .....	(583)
	-----
Balance at September 30, 2001 .....	\$ 814
	=====

The company estimates that the future cash expenditures related to the restructuring plans stated above will be made in the following periods: 66% through September 30, 2002, 18% through September 30, 2003, 9% through September 30, 2004 and 7% thereafter.

14

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

### 7. DEBT OBLIGATIONS

Debt obligations are as follows (in thousands):

Debtor-In-Possession Financing Agreement .....	
Senior Credit Facility .....	
Series A Senior Subordinated Unsecured Notes in default .....	
Series B Senior Subordinated Unsecured Convertible Notes in default .....	
Insurance and accreditation notes payable .....	
Other obligations, including capital leases, at interest rates ranging from 7.5% to 13.1% ....	
Less: Debt obligations subject to compromise .....	
Less: Current scheduled maturities .....	

As a result of the Debtors' Chapter 11 Bankruptcy Court filings, substantially all short and long-term debt obligations at the August 8, 2000 filing date have been classified as liabilities subject to compromise in the accompanying Condensed Consolidated Balance Sheets in accordance with SOP 90-7.

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Under the United States Bankruptcy Code, actions against the Debtors to collect pre-petition indebtedness are subject to an automatic stay. As of August 8, 2000, the company's principal credit and debt agreements included (i) a Securities Exchange Agreement (the "Securities Exchange Agreement"), dated May 6, 1998, with Cerberus Partners, L.P., Goldman Sachs Credit Partners, L.P. and Foothill Capital Corporation (collectively the "Holders") and the related Series A Senior Subordinated Unsecured Notes (the "Series A Notes") and the Series B Senior Subordinated Unsecured Convertible Notes (the "Series B Notes") and (ii) a Senior Credit Facility with Foothill Income Trust L.P., Cerberus Partners, L.P. and Goldman Sachs Credit Partners, L.P. (collectively the "Lenders") and Foothill Capital Corporation as agent thereunder. Subsequent to the petition date, the Debtors entered into a secured debtor-in-possession financing agreement with an affiliate of Cerberus Partners, L.P. Pursuant to the terms and conditions of the aforementioned credit and debt agreements, the company is precluded from paying cash dividends or making other capital distributions. Moreover, the Debtors' voluntary Chapter 11 filings caused events of default to occur under the Securities Exchange Agreement and the Senior Credit Facility, thereby terminating the Debtors' ability to make additional borrowings under the Senior Credit Facility through its expiration on February 6, 2001.

The recognition of interest expense pursuant to SOP 90-7 is appropriate during the Chapter 11 proceedings if it is probable that such interest will be an allowed priority, secured or unsecured claim. The Debtors' Second Joint Plan (see Note 2), if approved, will effectively eliminate all post-petition interest on pre-petition borrowings. Accordingly, no interest expense is being recorded on pre-petition unsecured indebtedness. The ultimate confirmed plan put forth by the Debtors or any other party in interest may have a similar effect on post-petition interest; however, appropriate approvals in accordance with the Bankruptcy Code will be required.

Exit Financing Facility. In connection with the Chapter 11 cases, on October 26, 2001, CI filed a draft of the Exit Financing Facility with the Bankruptcy Court together with other draft documents relating to the Second Joint Plan. The proposed lenders under the Exit Financing Facility would include the Holders or affiliates thereof. The agreement contemplates that CI could access, as necessary, a revolving credit facility of up to \$40 million for use in connection with payments under the Second Joint Plan and for general working capital and corporate purposes of the company and its subsidiaries. If approved, the Exit Financing Facility will mature the earlier of December 2004 or the date on which the revolving loans shall become due and payable in accordance with the terms of the agreement. No assurances can be given that the parties will ultimately agree to the terms and conditions as set forth in the proposed Exit Financing Facility agreement or that such agreement will be approved by the Bankruptcy Court.

Debtor-In-Possession ("DIP") Financing Agreement. In connection with the Chapter 11 Bankruptcy Court filings, effective August 30, 2000, the Debtors entered into a secured debtor-in-possession financing agreement with Madeleine L.L.C. ("Madeleine"), an affiliate of Cerberus Partners, L.P. Prior to entering into the DIP financing agreement, management and the Board of Directors solicited advice from the company's financial advisors. Such advisors indicated that the terms and conditions of the DIP financing agreement were generally favorable when compared to a company with Coram's financial history. The agreement provided that the Debtors could access, as necessary, a line of credit of up to \$40 million for use in connection with the operation of their businesses and the businesses of their subsidiaries. On September 12, 2000, the Bankruptcy Court issued an order approving the DIP financing agreement.

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

The DIP financing agreement expired by its terms on August 31, 2001. The DIP financing agreement provided for maximum borrowings generally equal to the product of: (i) 65% of Net Eligible Accounts Receivable, as defined in the underlying agreement, and (ii) 95%. During the term of the DIP financing agreement, no borrowings had been made thereunder. The DIP financing agreement was secured by the capital stock of the Debtors' subsidiaries, as well as, the accounts receivable and certain other assets held by the Debtors and their subsidiaries. Under the DIP financing agreement, among other nominal fees, the Debtors paid a fee of 1% or \$0.4 million and were liable for commitment fees on the unused facility at a rate of 0.5% per annum, payable monthly in arrears.

Management is currently negotiating a renewal of the DIP financing agreement; however, no assurances can be given that the parties will ultimately agree to the terms and conditions of such renewal or that a renewal will be approved by the Bankruptcy Court.

Senior Credit Facility. On August 20, 1998, the company entered into the Senior Credit Facility, which provided for the availability of up to \$60.0 million for acquisitions, working capital, letters of credit and other corporate purposes. The terms of the agreement also provided for the issuance of letters of credit of up to \$25.0 million provided that available credit would not fall below zero. In connection with the sale of CPS, effective July 31, 2000, the company reduced its outstanding borrowings under the Senior Credit Facility by \$28.5 million, leaving only irrevocable letter of credit obligations totaling \$2.7 million outstanding. Furthermore, on September 21, 2000 and January 29, 2001, the company permanently reduced the Senior Credit Facility commitment to \$2.7 million and \$2.1 million, respectively, in order to reduce the fees related to commitments on which the company was not able to borrow against due to the Debtors' bankruptcy proceedings. Effective February 6, 2001, the Lenders and the company terminated the Senior Credit Facility. In connection with the termination of the Senior Credit Facility and pursuant to orders of the Bankruptcy Court, the company established new letters of credit through Wells Fargo Bank Minnesota, NA ("Wells Fargo") and such new letters of credit are fully secured by interest bearing cash deposits of the company held by Wells Fargo.

The Senior Credit Facility provided for interest on outstanding indebtedness at the rate of prime plus 1.5%, payable in arrears. Additionally, the terms of the agreement provided for a fee of 1.0% per annum on the outstanding letter of credit obligations, also payable in arrears. The Senior Credit Facility further provided for additional fees to be paid on demand to any letter of credit issuer pursuant to the application and related documentation under which such letters of credit are issued. The Senior Credit Facility was secured by the capital stock of the company's subsidiaries, as well as, the accounts receivable and certain other assets held by the company and its subsidiaries. The Senior Credit Facility contained other customary covenants and events of default.

Among other fees, the company incurred approximately \$0.8 million upon consummation of the Senior Credit Facility and was thereafter liable for commitment fees on the unused facility at 0.375% per annum, due quarterly in arrears. Additionally, the terms of the agreement provided for the issuance of warrants to purchase up to 1.9 million shares of the company's common stock at \$0.01 per share, subject to customary anti-dilution adjustments (the "1998 Warrants"). The estimated fair value of the 1998 Warrants was determined on the

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

date of issuance and capitalized as deferred debt issuance costs. Such costs were amortized ratably to interest expense over the life of the Senior Credit Facility; however, contemporaneous with the permanent reduction of the borrowing capacity on September 21, 2000, the company charged to interest expense approximately \$1.1 million of remaining deferred debt issuance costs related to the Senior Credit Facility. The 1998 Warrants expired on February 6, 2001 when the Senior Credit Facility was terminated.

Securities Exchange Agreement. On May 6, 1998, the company entered into the Securities Exchange Agreement with the Holders of its subordinated rollover note (the "Rollover Note"). While the Rollover Note was outstanding, the Holders had the right to receive warrants to purchase up to 20% of the outstanding common stock of the company (the "Rollover Note Warrants") on a fully diluted basis. Effective April 13, 1998, the Securities Exchange Agreement provided for the cancellation of the Rollover Note, including deferred interest and fees, and the Rollover Note Warrants in an exchange for the payment of \$4.3 million in cash and the issuance by the company to the Holders of (i) \$150.0 million in principal amount of Series A Notes and (ii) \$87.9 million in principal amount of 8.0% Series B Notes. Additionally, the Holders of the Series A Notes and the Series B Notes were given the right to approve certain new debt and the right to name one director to the company's Board of Directors. Such director was elected to the Board of Directors in June 1998 and reelected in August 1999; however, the designated board member resigned in July 2000 and has not been replaced.

16

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

On April 9, 1999, the company entered into Amendment No. 2 (the "Note Amendment") to the Securities Exchange Agreement with the Holders. Pursuant to the Note Amendment, the outstanding principal amount of Series B Notes is convertible into shares of the company's common stock at a conversion price of \$2.00 per share (subject to customary anti-dilution adjustments). Prior to entering into the Note Amendment, the Series B Notes were convertible into common stock at a conversion price of \$3.00 per share, which was subject to downward (but not upward) adjustment based on prevailing market prices for the company's common stock on April 13, 1999 and October 13, 1999. Based on reported market closing prices for the company's common stock prior to April 13, 1999, this conversion price would have been adjusted to below \$2.00 on such date had the company not entered into the Note Amendment. Pursuant to the Note Amendment, the parties also increased the interest rate applicable to the Series A Notes from 9.875% to 11.5% per annum.

On December 28, 2000, the Debtors announced the Bankruptcy Court's approval of their request to exchange a sufficient amount of debt and related accrued interest for equity in the form of Coram, Inc. Series A Cumulative Preferred Stock in order to maintain compliance with the physician ownership and referral provisions of the Omnibus Budget Reconciliation Act of 1993 (commonly referred to as "Stark II"). On December 29, 2000, the Securities Exchange Agreement was amended ("Amendment No. 4") and an Exchange Agreement was simultaneously executed among the Debtors and the Holders. Pursuant to such arrangements, the Holders agreed to exchange approximately \$97.7 million aggregate principal amount of the Series A Notes and \$11.6 million of aggregate unpaid accrued contractual interest on the Series A Notes and the Series B Notes as of December 29, 2000 for 905 shares of Coram, Inc. Series A Cumulative Preferred Stock (see

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Note 9 for further details regarding the preferred stock). Following the exchange, the Holders retain approximately \$61.2 million aggregate principal amount of the Series A Notes and \$92.1 million aggregate principal amount of the Series B Notes. Pursuant to Amendment No. 4, the per annum interest rate on both the Series A Notes and the Series B Notes has been adjusted to 9.0%. Moreover, the Series A Notes' and Series B Notes' original scheduled maturity dates of May 2001 and April 2008, respectively, have both been modified to June 30, 2001. Due to the Holders receipt of consideration with a fair value less than the face value of the exchanged principal and accrued interest, the exchange transactions qualified as a troubled debt restructuring pursuant to Statement of Financial Accounting Standards No. 15, Accounting by Debtors and Creditors for Troubled Debt Restructurings ("SFAS No. 15"). In connection therewith, the company recognized an extraordinary gain during the fourth quarter of the year ended December 31, 2000 of approximately \$107.8 million, net of tax.

Although the principal amounts under the Series A Notes and Series B Notes were not paid on June 30, 2001 and the company is in technical default of the Securities Exchange Agreement, the Holders are stayed from any remedies pursuant to the provisions of the United States Bankruptcy Code.

The Securities Exchange Agreement, pursuant to which the Series A Notes and the Series B Notes were issued, contains customary covenants and events of default. Upon the Debtors' Chapter 11 bankruptcy filings, the company was in violation of certain covenants and conditions thereunder; however, such bankruptcy proceedings have stayed any remedial actions by either the Debtors or the Holders. Additionally, the company was not in compliance with other covenants relating to certain contractual relationships its wholly-owned Resource Network Subsidiaries had with certain parties that were contracted to provide services pursuant to the Aetna Master Agreement, effective May 1, 1998, and to other covenants relating to the capitalization of subsidiaries. The company received waivers from its lenders regarding such events of noncompliance. The voluntary filing of Chapter 11 bankruptcy petitions by the Resource Network Subsidiaries caused further defaults under the Securities Exchange Agreement; however, such defaults were waived by the Holders. In connection with these waivers and the waivers provided for certain matters of noncompliance under the Senior Credit Facility, the company and the Holders entered into an amendment on November 15, 1999 pursuant to which the Holders agreed that no interest on the Series A Notes and the Series B Notes would be due for the period from November 15, 1999 through the earlier of (i) final resolution of the litigation with Aetna or (ii) May 15, 2000. The Aetna litigation was settled on April 20, 2000 and, as a result, the obligation to pay interest on the Series A Notes and the Series B Notes resumed on such date. However, due to the Debtors' Chapter 11 bankruptcy filings no interest is being paid subsequent to August 8, 2000.

Other than the aforementioned default for non-payment of principal on June 30, 2001, management believes that at September 30, 2001 the company was in compliance with all other covenants of the Securities Exchange Agreement. There can be no assurance as to whether further covenant violations or defaults will occur in future periods and whether any necessary waivers would be granted.

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

At the election of the company, the Series A Notes and the Series B Notes are scheduled to pay interest quarterly in arrears in cash or through the issuance of pari passu debt securities, except that Holders can require the company to pay interest in cash if the company exceeds a predetermined interest coverage ratio. Notwithstanding the contractual terms of the Securities Exchange Agreement, no interest is being paid subsequent to August 8, 2000 due to the Debtors' ongoing bankruptcy proceedings. Pursuant to the troubled debt restructuring rules promulgated under SFAS No. 15 and other accounting rules under SOP 90-7, no interest expense was recognized in the company's consolidated financial statements relative to the Series A Notes and the Series B Notes from December 29, 2000 through September 30, 2001.

The Series A Notes and the Series B Notes are callable, in whole or in part, at the option of the Holders in connection with any change of control of the company (as defined in the Securities Exchange Agreement), if the company ceases to hold and control certain interests in its significant subsidiaries, or upon the acquisition of the company or certain of its subsidiaries by a third party. In such instances, the notes are callable at 103% of the then outstanding principal amount, plus accrued interest. The Series B Notes are also redeemable at the option of the Holders thereof upon maturity of the Series A Notes at the outstanding principal amount thereof, plus accrued interest. In addition, the Series A Notes are redeemable at 103% of the then outstanding principal amount, plus accrued interest at the option of the company.

In connection with the disposition of CPS, effective July 31, 2000, the company applied \$9.5 million of the net cash proceeds derived therefrom to prepay a portion of the principal amount outstanding under the Series A Notes. The Holders of the Series A Notes waived the 103% prepayment premium thereby permitting the company to reduce the then outstanding principal balance by the full amount of the payment.

### 8. INCOME TAXES

During the nine months ended September 30, 2001 and 2000, the company recorded income tax expense of approximately \$0.2 million and \$0.3 million, respectively. The effective income tax rate for the nine-month period ended September 30, 2001 is higher than the statutory rate because the company is not recognizing the deferred income tax benefits potentially generated by the current period loss. The effective income tax rate for the nine-month period ended September 30, 2000 is lower than the statutory rate because the company is able to utilize net operating loss carryforwards ("NOLs") which are fully reserved in the valuation allowance. As of September 30, 2001, deferred tax assets were net of a \$146.5 million valuation allowance. Realization of deferred tax assets is dependent upon the company's ability to generate taxable income in the future. Deferred tax assets have been limited to amounts expected to be recovered, net of deferred tax liabilities that would otherwise become payable in the carryforward period. As management believes that realization of the balance of deferred tax assets is sufficiently uncertain at this time, the balances were fully offset by valuation allowances at both September 30, 2001 and December 31, 2000.

Deferred taxes relate primarily to temporary differences consisting, in part, of accrued restructuring costs, the charge for goodwill and other long-lived assets, allowances for doubtful accounts, R-Net reserves and other accrued liabilities that are not deductible for income tax purposes until paid or realized and NOLs that may be deductible against future taxable income. As of September 30, 2001, the company had NOLs of approximately \$174.0 million that are available to offset future federal taxable income and expire in varying amounts in the years 2002 through 2019. This NOL balance includes approximately \$36.4 million generated prior to the creation of Coram through the merger by and among T2 Medical, Inc., Curaflex Health Services, Inc., HealthInfusion, Inc. and Medisys, Inc. Such pre-merger NOL amounts are subject to an annual usage



## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

limitation of approximately \$4.5 million. The ability to utilize the full amount of the \$174.0 million of NOLs is uncertain due to income tax rules related to changes in ownership.

As a result of the issuance of Coram, Inc. Series A Cumulative Preferred Stock in December 2000 (see Note 9), the company effectuated a deconsolidation of its group for federal income tax purposes. Accordingly, subsequent income tax returns will be filed with Coram, Inc. as the parent company of the new consolidated group and Coram Healthcare Corporation will file its own separate income tax returns. The issuance of the preferred stock also caused an ownership change at Coram, Inc. for federal income tax purposes. However, Coram, Inc. currently operates as a debtor-in-possession under the jurisdiction of the Bankruptcy Court and it meets certain other bankruptcy related conditions of the Internal Revenue Code ("IRC"). The bankruptcy provisions of IRC Section 382 impose limitations on the utilization of NOLs and other tax attributes.

18

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

In January 1999, the Internal Revenue Service ("IRS") completed an examination of the company's federal income tax return for the year ended September 30, 1995 and proposed substantial adjustments to the prior tax liabilities. The company previously agreed to adjustments of \$24.4 million that only affect available NOLs. The issues involve the deductibility of warrants, write-off of goodwill and the ability of the company to categorize certain NOLs as specified liability losses and offset income in prior years. The alleged deficiency totaled approximately \$12.7 million (obtained from federal tax refunds), plus interest and penalties to be determined. In May 1999, the company received a statutory notice of deficiency with respect to the proposed adjustments seeking to recover the amount of taxes previously refunded. In August 1999, the company filed a petition with the United States Tax Court ("Tax Court") contesting the notice of deficiency. The IRS responded to the petition and requested the petition be denied. The Tax Court proceeding is currently stayed by reason of the Debtors' bankruptcy proceedings.

Pursuant to standard IRS procedures, the resolution of the issues contained in the Tax Court petition were assigned to the administrative appeals function of the IRS. The company has tentatively reached a settlement agreement with the IRS Appeals office on the aforementioned issues. The settlement, if approved by the Joint Committee of Taxation and, if necessary, the Bankruptcy Court, would result in a federal tax liability of approximately \$9.9 million, plus interest. In connection therewith, the accompanying Condensed Consolidated Financial Statements include reserves for the proposed liabilities, including approximately \$5.5 million of incremental interest expense for the nine months ended September 30, 2001. The federal income tax adjustments would also give rise to additional state tax liabilities. If the company is not able to negotiate an installment plan with the IRS with respect to the proposed settlement amount or if either the Joint Committee of Taxation or the Bankruptcy Court do not approve the proposed settlement amount, the financial position and liquidity of the company could be materially adversely affected.

### 9. MINORITY INTERESTS

The following summarizes the minority interests in consolidated joint

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

ventures and preferred stock issued by a subsidiary (in thousands):

	SEPTEMBER 30, 2001	DECEMBER 31, 2000
	-----	-----
Series A Cumulative Preferred Stock of Coram, Inc. ....	\$ 5,522	\$5,522
Majority-owned companies .....	557	456
	-----	-----
Total minority interests .....	\$ 6,079	\$5,978
	=====	=====

On December 29, 2000, Coram, Inc. ("CI"), a wholly-owned subsidiary of Coram Healthcare Corporation, executed the Exchange Agreement with the Holders of CI's Securities Exchange Agreement (see Note 7 for further details) to exchange approximately \$97.7 million of the Series A Notes and approximately \$11.6 million of accrued but unpaid interest on the Series A Notes and Series B Notes in exchange for 905 shares of CI Series A Cumulative Preferred Stock, \$0.001 par value per share, having an aggregate liquidation preference of approximately \$109.3 million (hereinafter referred to as the "Preferred Stock"). The Preferred Stock was issued to the Holders on a pro rata basis. Through an independent valuation, it was determined that the Preferred Stock had a fair value of approximately \$6.1 million and such amount, offset by certain legal and other closing costs, nets to approximately \$5.5 million.

The authorized CI Preferred Stock consists of 10,000 shares, and the only shares issued and outstanding at September 30, 2001 are those pursuant to the Exchange Agreement. So long as any shares of the Preferred Stock are outstanding, the Holders are entitled to receive preferential dividends at a rate of 15% per annum on the liquidation preference amount. Dividends are payable on a quarterly basis on the last business day of each calendar quarter. Prior to the effective date of the Debtors' plan of reorganization, dividends are to be paid in the form of additional shares of Preferred Stock having a liquidation preference amount equal to such dividend amount. Subsequent to the effective date of a plan of reorganization, at CI's election, dividends will be payable in cash or shares of common stock of CI having a fair value equal to such cash dividend payment, as determined by a consensus of investment banking firms acceptable to the Holders. In the event of default, the dividend rate shall increase to 16% per annum until such time that the event of default is cured. All dividends are to include tax indemnities and gross-up provisions (computed subsequent to the company's tax fiscal year end in connection with the preparation of the company's income tax returns) as are appropriate for transactions of this nature. In-kind dividends earned during the nine months ended September 30, 2001, exclusive of any tax indemnities and gross-up provisions, aggregated approximately 107 shares and had a liquidation preference of approximately \$12.9 million.

19

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

The agreements and bylaws underlying the Preferred Stock include usual and

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

customary affirmative and negative covenants for a security of this nature, including, but not limited to (i) providing timely access to certain financial and business information; (ii) authorization to communicate with independent certified public accountants with respect to the financial conditions and other affairs of the company; (iii) maintaining tax compliance; (iv) maintaining adequate insurance coverage; (v) adherence to limitations on transactions with affiliates; (vi) adherence to limitations on acquisitions or investments; (vii) adherence to limitations on the liquidation of assets or businesses; and (viii) adherence to limitations on entering into additional indebtedness.

Subsequent to the effective date of a plan of reorganization, each share of Preferred Stock will be entitled to one vote and shall vote together with the shares of CI's common stock on all matters submitted to a vote of stockholders. The Preferred Stock would have had 47.5% of CI's total voting power on December 31, 2000; however, such voting rights are temporarily suspended during the Debtors' bankruptcy proceedings. Subsequent to the effective date of a plan of reorganization, the Holders will have the right to appoint three directors out of a total of seven directors to CI's Board of Directors, and a quorum in meetings of the Board of Directors shall be constituted by the presence of a majority of the members, at least two of whom must be directors appointed by the Holders. During the pendency of CI's bankruptcy proceedings, the Holders have the right to appoint two directors to CI's Board of Directors. Alternatively, if no Board of Directors representation is elected by the Holders, they retain the right to appoint one observer.

The Preferred Stock is redeemable at the option of CI, in whole or in part, at any time, on not less than thirty days prior written notice, at the liquidation preference amount plus any accrued but unpaid dividends. Redemption may be made in the form of cash payments only. As of November 16, 2001, the aggregate Preferred Stock liquidation preference was approximately \$122.2 million.

The Debtors' Second Joint Plan (Note 2), if confirmed in its current form, would effectively retire all of the currently outstanding Preferred Stock on or before the Plan's effective date.

### 10. LITIGATION AND CONTINGENCIES

Bankruptcy Proceedings. On August 8, 2000, the Debtors filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code with the United States Bankruptcy Court for the District of Delaware, In Re: Coram Healthcare Corporation and Coram, Inc., Case Nos. 00-3299 (MFW) and 00-3300 (MFW) (collectively the "Chapter 11 Cases"), respectively. The proceedings have been consolidated for administrative purposes only by the United States Bankruptcy Court in Delaware and are being administered under the docket of In Re: Coram Healthcare Corporation, Case No. 00-3299 (MFW). None of the Debtors' other subsidiaries are a debtor in the proceeding. See Note 2 for further details.

Except as may otherwise be determined by the Bankruptcy Court overseeing the Chapter 11 Cases, the protection generally afforded by Chapter 11 automatically stays any litigation proceedings pending against either or both of the Debtors. All such claims will be addressed through the proceedings applicable to the Chapter 11 Cases. The automatic stay would not, however, apply to actions brought against the company's non-debtor subsidiaries.

Official Committee of the Equity Security Holders' Matters. A committee of persons claiming to own shares of the company's publicly-traded common stock (the "Equity Committee") filed motions objecting to the Restated Joint Plan and the Second Joint Plan of reorganization, contending, among other things, that the company's valuation upon which the Restated Joint Plan of reorganization was premised and the underlying projections and assumptions were flawed. On December

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

21, 2000, the Bankruptcy Court determined not to confirm the Restated Joint Plan. The company and the Equity Committee are involved in a review of certain company information regarding, among other things, the Equity Committee's contentions. Moreover, on July 30, 2001, the Equity Committee filed a motion to terminate the Debtors' exclusivity period and file its own plan or reorganization; however, the motion was denied by the Bankruptcy Court. The CHC equity holders, including the Equity Committee, voted against confirmation of the Second Joint Plan.

20

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

Additionally, on or about February 6, 2001, the Equity Committee filed a motion with the Bankruptcy Court seeking permission to bring a derivative lawsuit directly against the company's Chief Executive Officer, a former member of the Board of Directors and Cerberus Partners, L.P. (a party to the company's debtor-in-possession financing agreement, Senior Credit Facility and Securities Exchange Agreement). The Equity Committee's lawsuit alleged a collusive plan whereby the named parties conspired to devalue the company for the benefit of the company's creditors under the Securities Exchange Agreement. On February 26, 2001, the Bankruptcy Court ruled that the Equity Committee's motion would not be productive at that time and, accordingly, the motion was denied without prejudice.

Management cannot predict whether any future objections of the Equity Committee will be forthcoming or if they would prevent confirmation of the Second Joint Plan set forth by management. Management also cannot predict if any other actions of the Equity Committee will have adverse consequences to the company.

Resource Network Subsidiaries' Bankruptcy. On November 12, 1999, the Resource Network Subsidiaries filed voluntary petitions under Chapter 11 of the United States Code in the United States Bankruptcy Court for the District of Delaware, Case No. 99-2889 (MFW). On August 19, 1999, a small group of parties with claims against the Resource Network Subsidiaries filed an involuntary bankruptcy petition under Chapter 11 against Coram Resource Network, Inc. in the United States Bankruptcy Court for the District of Delaware. The two proceedings were consolidated by stipulation of the parties and the case is pending under the style, In Re Coram Resource Network, Inc. and Coram Independent Practice Association, Inc., Case No. 99-2889 (MFW). The Resource Network Subsidiaries are now being liquidated pursuant to the proceedings. The Chief Restructuring Officer of the Resource Network Subsidiaries had threatened suit on behalf of the estates against CHC. The draft complaint included claims for damages against CHC and certain of its former and current officers and directors in excess of \$41 million. The draft complaint included a threat to pierce the corporate veil of the Resource Network Subsidiaries to reach CHC and included claims of breaches by the officers and directors of their fiduciary duties to the Resource Network Subsidiaries and CHC.

On September 11, 2000, the Resource Network Subsidiaries filed a motion in the Debtor's Chapter 11 proceedings seeking, among other things, to have the two separate bankruptcy proceedings substantively consolidated into one proceeding. If granted, the Chapter 11 proceedings involving the Resource Network Subsidiaries and the Chapter 11 proceedings involving the Debtors would have been combined such that the assets and liabilities of the Resource Network

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Subsidiaries would be joined with the assets and liabilities of the Debtors, the liabilities of the combined entity would be satisfied from their combined funds and all intercompany claims would be eliminated. Furthermore, the creditors of both proceedings would have voted on any reorganization plan for the combined entities. The Resource Network Subsidiaries and the Debtors engaged in discovery related to this substantive consolidation motion and, in connection therewith, the parties reached a settlement agreement in November 2000. The settlement agreement was approved by the Bankruptcy Court in December 2000 and the Debtors made a payment of \$0.5 million to the Resource Network Subsidiaries in January 2001.

Notwithstanding the withdrawal of the substantive consolidation motion, the Resource Network Subsidiaries still maintain proofs of claim in excess of \$41 million against each of CHC's and CI's estates and the company maintains a reciprocal claim of approximately the same amount against the Resource Network Subsidiaries' estate. Additionally, the Official Committee of the Equity Security Holders and Official Committee of Unsecured Creditors in the Resource Network Subsidiaries' bankruptcy proceedings filed an objection to confirmation of the Second Joint Plan and a motion to lift the automatic stay to pursue their claims against the company. The ultimate outcome of these matters cannot be predicted with any degree of certainty, but management, in consultation with legal counsel, does not believe that the final resolution of these matters or other matters raised by the Resource Network Subsidiaries' Chief Restructuring Officer will have a material adverse impact on the company's financial position or results of operations.

Aetna U.S. Healthcare, Inc. On June 30, 1999, the company filed a complaint (the "Coram Complaint") against Aetna in the United States District Court for the Eastern District of Pennsylvania setting forth claims against Aetna for fraud, misrepresentation, breach of contract and rescission relating to the Master Agreement between the parties for ancillary network management services through the Resource Network Subsidiaries. On June 30, 1999, the company received a copy of a complaint (the "Aetna Complaint") that had been filed by Aetna on June 29, 1999 in the Court of Common Pleas of Montgomery County, Pennsylvania. The Aetna Complaint sought specific performance, injunctive relief and declaratory relief to compel the company to perform under the Master Agreement, including the payment of compensation to the healthcare providers that had rendered and continued to render services to Aetna's health plan members. As stated in the Aetna Complaint, Aetna disputed the company's right to terminate the Agreement. The company removed the Aetna Complaint to federal court. On July 20, 1999, Aetna filed a counterclaim against the company in the federal court lawsuit brought by the company. In its counterclaim, Aetna sued the company for, among other things, breach of the

21

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

Master Agreement and fraudulent misrepresentation, contending the company never intended to perform under the Master Agreement, defamation, interference with contractual relations with providers and interference with prospective contractual relations with other companies that allegedly bid for the Master Agreement.

On April 20, 2000, the company and Aetna reached an amicable resolution to

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

the then outstanding disputes and, in connection therewith, all claims and counterclaims amongst the parties were dismissed from the courts of appropriate jurisdiction. The final resolution of these matters did not have a material effect on the company's consolidated financial position or results of operations. The impact of this dispute resolution has been charged to discontinued operations in the accompanying condensed consolidated financial statements during the nine months ended September 30, 2000.

Apria Healthcare, Inc. Apria Healthcare, Inc. and one of its affiliates, Apria Healthcare of New York State, Inc., (collectively "Apria") filed suit against CHC and the Resource Network Subsidiaries in the Superior Court of Orange County, California. Apria's claims related to services that were rendered as part of certain home health provider networks managed by the Resource Network Subsidiaries. Apria's complaint alleged that, among other things, the Resource Network Subsidiaries operated as the alter ego of CHC and, as a result, CHC should be declared responsible for the alleged breaches of the contracts that the Resource Network Subsidiaries had with Apria. The complaint included requests for declaratory, compensatory and other relief in excess of \$1.4 million. On February 21, 2001, the company and Apria agreed to a "dismissal without prejudice" from the Superior Court of Orange County, California with each party responsible for its own legal fees.

TBOB Enterprises, Inc. On July 17, 2000, TBOB Enterprises, Inc. ("TBOB") filed an arbitration demand against CHC (TBOB Enterprises, Inc. f/k/a Medical Management Services of Omaha, Inc. against Coram Healthcare Corporation, in the American Arbitration Association office in Dallas, Texas). In its demand, TBOB claims that the company breached its obligations under an agreement entered into by the parties in 1996 relating to a prior earn-out obligation of the company that originated from the acquisition of the claimant's prescription services business in 1993 by a wholly-owned subsidiary of the company. The company operated the business under the name Coram Prescription Services ("CPS") and the assets of the CPS business were sold on July 31, 2000. See Note 4 for further details. TBOB alleges, among other things, that the company has impaired the earn-out payments due TBOB by improperly charging certain expenses to the CPS business and failing to fulfill the company's commitments to enhance the value of CPS by marketing its services. The TBOB demand alleges damages of more than \$0.9 million. TBOB contends that this amount must be paid in addition to the final scheduled earn-out payment of approximately \$1.3 million that was due in March 2001. Furthermore, pursuant to the underlying agreement with TBOB, additional liabilities related to post-petition interest on the final scheduled earn-out payment may result. In accordance with SOP 90-7, such interest, aggregating approximately \$0.1 million through September 30, 2001 based on an 18% interest rate, has not been recorded in the company's Condensed Consolidated Financial Statements because TBOB is an unsecured creditor in the Debtors' bankruptcy proceedings and the interest claim may not be sustainable. TBOB reiterated its monetary demand through a proof of claim filed against CHC's estate for the aggregate amount of approximately \$2.2 million (the scheduled earn-out payment plus the alleged damages). Any action relating to the final \$1.3 million earn-out payment that was scheduled for March 2001, the alleged damages of \$0.9 million and any interest accrued thereon have been stayed by operation of the Bankruptcy Code. On July 5, 2001, the company received a letter from TBOB's legal counsel requesting that the aforementioned arbitration remain in abeyance pending resolution of the bankruptcy proceedings. Management does not believe that final resolution of this matter will have a material adverse impact on the company's financial position or results of operations.

Internal Revenue Service Negotiations. CHC is contesting a notice of deficiency issued by the Internal Revenue Service through administrative proceedings and litigation. See Note 8 for further details.

Alan Furst et al. v. Stephen Feinberg, et al. A complaint was filed in the United States District Court for the Third District of New Jersey on November 8,

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

2000 and an Amended Class Action Complaint was filed on November 15, 2000, alleging that certain current and former officers and directors of the company and the company's principal lenders, Cerberus Partners, L.P., Foothill Capital Corporation and Goldman Sachs & Co., implemented a scheme to perpetrate a fraud upon the stock market regarding the common stock of CHC. A second Amended Class Action Complaint (the "Second Amended Complaint") was filed on March 21, 2001, which removed all of the officers and directors of the company as defendants, except the company's Chief Executive Officer and another current member of the Board of Directors and continued to name Cerberus Partners, L.P., Foothill Capital Corporation and Goldman Sachs & Co. as defendants. The plaintiffs alleged that the defendants artificially depressed the trading price of the company's publicly traded shares and created the false impression that stockholders' equity was decreasing in value and was ultimately worthless. The plaintiffs further alleged that members of the class sustained total investment losses of \$50 million or more. On June 14, 2001, a third

22

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

Amended Class Action Complaint (the "Third Amended Complaint") was filed naming the same defendants as the Second Amended Complaint. The plaintiffs' allegations in the Third Amended Complaint were substantially similar to the allegations in the Second Amended Complaint; however, the Third Amended Complaint eliminated references to the corporate assets of Coram. The defendants filed a motion to dismiss the Third Amended Complaint, as they believe the claims are inadequately pleaded and meritless. That motion has not yet been adjudicated. The company notified its insurance carrier of the lawsuit and intends to avail itself of any appropriate insurance coverage for its directors and officers, who are vigorously contesting the allegations. The company cannot predict the outcome of this case nor can it predict the scope and nature of any indemnification that the directors and officers may have with the company's insurance carrier.

General. Management of the company and its subsidiaries intends to vigorously defend the company in the matters described above. Nevertheless, due to the uncertainties inherent in litigation, including possible indemnification against other parties, the ultimate disposition of such matters cannot presently be determined. Adverse outcomes in some or all of the proceedings could have a material adverse effect on the financial position, results of operations and liquidity of the company.

The company and its subsidiaries are also parties to various other legal actions arising out of the normal course of their businesses, including employee claims, reviews of cost reports submitted to Medicare and examinations by regulators such as Medicare and Medicaid fiscal intermediaries and the Centers for Medicare and Medicaid Services (formerly the Health Care Financing Administration). Management believes that the ultimate resolution of such other actions will not have a material adverse effect on the financial position, results of operations or liquidity of the company.

PricewaterhouseCoopers LLP. On July 7, 1997, the company filed suit against Price Waterhouse LLP (now known as PricewaterhouseCoopers LLP) in the Superior Court of San Francisco, California, seeking damages in excess of \$165.0 million. As part of the settlement that resolved a case filed by the company against Caremark International, Inc. and Caremark, Inc. (collectively "Caremark"),

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Caremark assigned and transferred to the company all of Caremark's claims and causes of action against Caremark's independent auditors, PricewaterhouseCoopers LLP, related to the lawsuit filed by the company against Caremark. This assignment of claims includes claims for damages sustained by Caremark in defending and settling its lawsuit with the company. The case was dismissed from the California court because of inconvenience to witnesses with a right to re-file in Illinois. The company re-filed the lawsuit in state court in Illinois and PricewaterhouseCoopers LLP filed a motion to dismiss the company's lawsuit on several grounds, but its motion was denied on March 15, 1999. PricewaterhouseCoopers LLP filed an additional motion to dismiss the lawsuit in May 1999, and that motion was dismissed on January 28, 2000. On April 19, 2001, PricewaterhouseCoopers LLP filed a motion for partial summary judgement with regard to a portion of Caremark's claims; however, this motion was subsequently denied. The lawsuit is currently in the discovery stage and a trial is scheduled to commence after June 22, 2002. There can be no assurance of any recovery from PricewaterhouseCoopers LLP.

Government Regulation. Under the physician ownership and referral provisions of the Omnibus Budget Reconciliation Act of 1993 (commonly referred to as "Stark II"), it is unlawful for a physician to refer patients for certain designated health services reimbursable under the Medicare or Medicaid programs to an entity with which the physician and/or the physician's family, as defined under Stark II, has a financial relationship, unless the financial relationship fits within an exception enumerated in Stark II or regulations promulgated thereunder. A "financial relationship" under Stark II is defined broadly as an ownership or investment interest in, or any type of compensation arrangement in which remuneration flows between the physician and the provider. The company has financial relationships with physicians and physician owned entities in the form of medical director agreements and service agreements pursuant to which the company provides pharmacy products. In each case, the relationship has been structured, based upon advice of legal counsel, using an arrangement management believes to be consistent with the applicable exceptions set forth in Stark II.

23

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

In addition, the company is aware of certain referring physicians (or their immediate family members) that have had financial interests in the company through ownership of shares of the company's common stock. The Stark II law includes an exception for the ownership of publicly traded stock in companies with equity above certain levels. This exception of Stark II requires the issuing company to have stockholders' equity of at least \$75 million either as of the end of its most recent fiscal year or on average over the last three fiscal years. Due principally to the extraordinary gain on troubled debt restructuring (see Note 7) and the disposition of the CPS business, at December 31, 2000 the company's stockholders' equity was above the required level. However, as of September 30, 2001, the company's total stockholders' equity was approximately \$65.5 million. As a result, the company will no longer qualify for the Stark II exception without a significant increase in stockholders' equity effective January 1, 2002. The penalties for failure to comply with Stark II include, among other things, non-payment of claims and civil penalties that could be imposed upon the company and, in some instances upon the referring physician, regardless of whether the company intended to violate the law.



## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Management has been advised by counsel that a company whose stock is publicly traded has, as a practical matter, no reliable way to implement and maintain an effective compliance plan for addressing the requirements of Stark II other than complying with the public company exception. Accordingly, if the company's common stock remains publicly traded and its stockholders' equity falls below the required levels, the company would be forced to cease accepting referrals of patients covered by the Medicare or Medicaid programs or run a significant risk of noncompliance with Stark II. Because referrals of the company's patients with such government-sponsored benefit programs comprise approximately 25% and 23% of the company's consolidated net revenue (excluding CPS) for the nine months ended September 30, 2001 and the year ended December 31, 2000, respectively, discontinuing the acceptance of patients with government-sponsored benefit programs would have a material adverse effect on the financial condition, results of operations and cash flows of the company. Additionally, ceasing to accept such referrals could materially adversely affect the company's business reputation in the market as it may cause the company to be a less attractive provider to which a physician could refer his or her patients. The company previously requested a Stark II waiver from the Health Care Financing Administration, but such waiver request was denied.

### 11. INDUSTRY SEGMENT AND GEOGRAPHIC AREA OPERATIONS

Management regularly evaluates the operating performance of the company by reviewing results on a product or service basis. The company's reportable segments are Infusion and CPS. Infusion is the company's base business, which derives its revenue primarily from alternate site infusion therapy and related services (including non-intravenous home health products such as durable medical equipment and respiratory therapy services). CPS, which was divested by the company on July 31, 2000, primarily provided specialty mail-order pharmacy and pharmacy benefit management services. The other non-reportable segment principally represents centralized management, administration and clinical support for clinical research trials.

Management uses earnings before interest expense, income taxes, depreciation and amortization ("EBITDA") for purposes of performance measurement. For the three and nine months ended September 30, 2001 and 2000, corporate costs were allocated on a revenue basis. For the three and nine months ended September 30, 2000, EBITDA has been reclassified to conform to the 2001 presentation. EBITDA excludes net reorganization expenses, merger and restructuring charges and results from discontinued operations. The measurement basis for segment assets includes net accounts receivable, inventories, net property and equipment and other current assets.

24

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

Summary information by segment is as follows (in thousands):

AS OF AND FOR THE THREE MONTHS ENDED SEPTEMBER 30,	
-----	
2001	2000

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

	-----	-----
INFUSION		
Revenue from external customers .....	\$ 93,547	\$ 94,108
Intersegment revenue .....	28	(53)
Interest income .....	22	18
Equity in net income of unconsolidated joint ventures .....	259	322
Segment EBITDA profit .....	5,770	5,072
Segment assets .....	118,866	104,607
Segment asset expenditures .....	1,385	578
CPS		
Revenue from external customers .....	\$ --	\$ 8,353
Intersegment revenue .....	--	--
Interest income .....	--	10
Equity in net income of unconsolidated joint ventures .....	--	--
Segment EBITDA loss .....	--	(461)
Segment assets .....	--	--
Segment asset expenditures .....	--	6
ALL OTHER		
Revenue from external customers .....	\$ 215	\$ 405
Intersegment revenue .....	--	--
Interest income .....	--	4
Equity in net income of unconsolidated joint ventures ....	--	--
Segment EBITDA profit (loss) .....	131	154
Segment assets .....	130	284
Segment asset expenditures .....	--	--

A reconciliation of the company's segment revenue, segment EBITDA profit (loss) and segment assets to the corresponding amounts in the Condensed Consolidated Financial Statements are as follows (in thousands):

	AS OF AND FOR THE THREE MONTH ENDED SEPTEMBER 30,	
	2001	2000
	-----	-----
NET REVENUE		
Total for reportable segments .....	\$ 93,575	\$ 102,408
Other revenue .....	215	531
Elimination of intersegment revenue (expense) .....	(28)	53
Total consolidated revenue .....	\$ 93,762	\$ 102,866
	=====	=====
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND MINORITY INTERESTS		
Total EBITDA profit for reportable segments .....	\$ 5,770	\$ 4,611
Other EBITDA profit (loss) .....	131	154
Goodwill amortization expense .....	(2,424)	(2,562)
Depreciation and other amortization expense .....	(2,512)	(2,277)
Interest expense .....	(4,072)	(6,866)
Gains on sales of businesses .....	--	18,456
Reorganization expenses, net .....	(3,739)	(1,861)
All other income (loss), net .....	(139)	(251)
	-----	-----
Income (loss) from continuing operations before income taxes and Minority interests .....	\$ (6,985)	\$ 9,404
	=====	=====

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

ASSETS		
Total assets for reportable segments .....	\$ 118,866	\$ 104,607
Other assets .....	224,391	239,732
	-----	-----
Consolidated total assets .....	\$ 343,257	\$ 344,339
	=====	=====

For each of the periods presented, the company's primary operations and assets were within the United States. The company maintains an infusion operation in Canada; however, the assets and revenue generated from this business are not material to the company's consolidated operations.

Sales to Aetna U.S. Healthcare ("Aetna") and its affiliated payers for the company's Infusion and CPS segments represented approximately 2% of the company's consolidated net revenue from continuing operations both the three months ended September 30,

25

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

2001 and 2000, and 2% and 4% for the nine months ended September 30, 2001 and 2000, respectively. The National Ancillary Services Agreement with Aetna applicable to the company's home infusion business was terminated effective April 12, 2000. The company and Aetna have agreed to use their good faith efforts to negotiate new local agreements for home infusion services. As of September 30, 2001, four such agreements for home infusion services have been entered into by Coram subsidiaries and local Aetna plans.

Net revenue from the Medicare and Medicaid programs represented approximately 25% of the company's consolidated net revenue for both the three months ended September 30, 2001 and 2000 and 23% of the company's consolidated net revenue for both the nine months ended September 30, 2001 and 2000.

Accounts receivable under the Medicare program represented approximately 35% and 30% of the company's consolidated accounts receivable as of September 30, 2001 and December 31, 2000, respectively. No other individual payer exceeded 5% of consolidated accounts receivable at those dates.

12. DEBTOR/NON-DEBTOR FINANCIAL STATEMENTS

In accordance with SOP 90-7, the Debtors are presenting the following Condensed Consolidating Financial Statements as of and for the nine months ended September 30, 2001 (in thousands):

CONDENSED CONSOLIDATING BALANCE SHEET

	DEBTORS	NON-DEBTOR
	-----	-----
ASSETS		
Current assets:		
Cash and cash equivalents .....	\$ 17,894	\$ 336

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Cash limited as to use .....	161	159
Accounts receivable, net .....	--	90,286
Inventories .....	--	12,092
Deferred income taxes, net .....	--	365
Other current assets .....	3,864	2,028
	-----	-----
Total current assets .....	21,919	105,266
Property and equipment, net .....	2,161	12,769
Deferred income taxes, net .....	--	1,612
Other deferred costs and intangible assets, net .....	295	6,610
Goodwill, net .....	--	186,582
Investments in and advances to wholly-owned subsidiaries, net .....	243,816	--
Other assets .....	4,600	1,443
	-----	-----
Total assets .....	\$272,791	\$314,282
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities not subject to compromise:		
Accounts payable .....	\$ 11,984	\$ 12,165
Accrued compensation and related liabilities .....	9,157	5,209
Current maturities of long-term debt .....	--	8
Insurance and accreditation notes payable .....	876	--
Income taxes payable .....	199	338
Deferred income taxes .....	--	956
Accrued merger and restructuring costs .....	481	333
Accrued reorganization costs for administrative professionals .....	7,836	--
Other accrued liabilities, including interest payable .....	3,457	4,247
	-----	-----
Total current liabilities not subject to compromise .....	33,990	23,256
Total current liabilities subject to compromise .....	167,610	--
	-----	-----
Total current liabilities .....	201,600	23,256
Long-term liabilities not subject to compromise:		
Long-term debt, less current maturities .....	152	18
Minority interests in consolidated joint ventures and preferred stock issued by a subsidiary .....	5,522	557
Other liabilities .....	--	19,108
Deferred income taxes .....	--	1,021
Net liabilities of discontinued operations .....	--	26,506
	-----	-----
Total liabilities .....	207,274	70,466
Net assets, including amounts due to Debtors .....	--	243,816
Total stockholders' equity .....	65,517	--
	-----	-----
Total liabilities and stockholders' equity .....	\$272,791	\$314,282
	=====	=====

CORAM HEALTHCARE CORPORATION  
(DEBTOR-IN-POSSESSION)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS - (CONTINUED)

CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

	DEBTORS -----	NON-DEBTOR -----
Net revenue .....	\$ --	\$ 287,44
Cost of service .....	--	207,30
Gross profit .....	--	80,13
Operating expenses:		
Selling, general and administrative expenses .....	12,202	48,92
Provision for estimated uncollectible accounts .....	--	8,78
Amortization of goodwill .....	--	7,27
Restructuring cost recovery .....	--	(58)
Total operating expenses .....	12,202	64,39
Operating income (loss) from continuing operations .....	(12,202)	15,74
Other income (expense):		
Interest income .....	955	11
Interest expense .....	(747)	(5,53)
Equity in net income of wholly-owned subsidiaries .....	10,532	-
Equity in net income of unconsolidated joint ventures .....	--	72
Other income, net .....	1	4
Income (loss) from continuing operations before reorganization expenses, income taxes and minority interests .....	(1,461)	11,09
Reorganization expenses, net .....	(10,003)	-
Income (loss) from continuing operations before income taxes and minority interests .....	(11,464)	11,09
Income tax expense .....	--	15
Minority interests in net income of consolidated joint ventures .....	--	40
Net income (loss) from continuing operations .....	\$ (11,464)	\$ 10,53

CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

	DEBTORS -----	NON-DEBTORS -----	CO -----
Net cash provided by (used in) continuing operations before reorganization expenses .....	\$ (8,186)	\$ 14,921	
Net cash used by reorganization expenses .....	(6,962)	--	
Net cash provided by (used in) continuing operations (net of reorganization expenses) .....	(15,148)	14,921	
Cash flows from investing activities:			
Purchases of property and equipment .....	(1,301)	(3,491)	
Cash advances from wholly-owned subsidiaries .....	11,073	(11,073)	
Proceeds from dispositions of property and equipment .....	6	63	
Net cash provided by (used in) investing activities .....	9,778	(14,501)	
Cash flows from financing activities:			
Repayments of debt obligations .....	(100)	(177)	
Repayments of insurance note payable .....	(1,372)	--	

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Deposits to collateralize letters of credit .....	(2,095)	--
Cash distributions paid to minority interests .....	--	(308)
	-----	-----
Net cash used in financing activities .....	(3,567)	(485)
	-----	-----
Net decrease in cash from continuing operations .....	\$ (8,937)	\$ (65)
	=====	=====
Net cash used in discontinued operations .....	\$ --	\$ (27)
	=====	=====

27

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

This Quarterly Report on Form 10-Q contains certain "forward-looking" statements (as such term is defined in the Private Securities Litigation Reform Act of 1995) and information relating to Coram Healthcare Corporation ("CHC") and its subsidiaries ("Coram" or the "company") that is based on the beliefs of the management of Coram, as well as, assumptions made by and information currently available to the management of Coram. The company's actual results may vary materially from the forward-looking statements made in this report due to important factors such as the outcome of the bankruptcy proceedings of CHC and its first tier wholly owned subsidiary, Coram, Inc. ("CI") (collectively the "Debtors") and certain other factors, which are described in greater detail later in this Item 2 under the caption "Risk Factors." When used in this report, the words "estimate," "project," "believe," "anticipate," "intend," "expect" and similar expressions are intended to identify forward-looking statements. Such statements reflect the current views of management with respect to future events based on currently available information and are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Management does not undertake any obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

The accompanying Condensed Consolidated Financial Statements have been prepared on a going concern basis, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the ordinary course of business. However, as a result of the Debtors' bankruptcy filings and circumstances relating thereto, including the company's leveraged financial structure and cumulative losses from operations, such realization of assets and liquidation of liabilities are subject to significant uncertainty. During the pendency of the Debtors' Chapter 11 bankruptcy proceedings, the company may sell or otherwise dispose of assets and liquidate or settle liabilities for amounts other than those reflected in the Condensed Consolidated Financial Statements. Further, the Debtors' Second Joint Plan of Reorganization, as amended (the "Second Joint Plan"), filed in the Chapter 11 proceedings could materially change the amounts reported in the Condensed Consolidated Financial Statements, which do not give effect to any adjustments of the carrying value of assets or liabilities that might be necessary as a consequence of a plan of reorganization (see Note 2 to the company's Condensed Consolidated Financial Statements for further details). The company's ability to continue as a going concern is dependent upon, among other things, confirmation of a plan of reorganization, future profitable operations, the ability to comply with the terms of the

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

company's financing agreements, the ability to remain in compliance with the physician ownership and referral provisions of the Omnibus Budget Reconciliation Act of 1993 (commonly known as "Stark II") and the ability to generate sufficient cash from operations and/or financing arrangements to meet its obligations.

Background. During 2000, Coram and its subsidiaries were engaged primarily in two principal lines of business: (i) alternate site (outside the hospital) infusion therapy, including non-intravenous home health products such as durable medical equipment and respiratory therapy services, and (ii) pharmacy benefit management and specialty mail-order pharmacy services. Effective July 31, 2000, the company sold its pharmacy benefit management and specialty mail-order pharmacy services business to Curascript Pharmacy, Inc. and Curascript PBM Services, Inc. (collectively the "Buyers"). The Buyers were a management-led group that was financed by GTCR Golder Rauner, L.L.C. Other services offered by Coram include centralized management, administration and clinical support for clinical research trials. See Note 4 to the company's Condensed Consolidated Financial Statements for further details.

Additionally, Coram's R-Net subsidiaries are being liquidated through proceedings that are currently pending in the United States Bankruptcy Court for the District of Delaware. These proceedings originated in August 1999 following the filing of an involuntary bankruptcy petition against Coram Resource Network, Inc. in such court. All of the R-Net locations have been closed in connection with the pending liquidation of R-Net. Additionally, Coram employees who were members of the Resource Network Subsidiaries' Board of Directors resigned during the year ended December 31, 2000 and currently only the Chief Restructuring Officer appointed by the Bankruptcy Court remains on the Board of Directors to manage and operate the liquidation of the R-Net business. See Note 3 to the company's Condensed Consolidated Financial Statements for further details.

Reorganization. On August 8, 2000, CHC and CI filed voluntary petitions under Chapter 11 of the Bankruptcy Code. Following the filing of the voluntary Chapter 11 petitions, the Debtors have been operating as debtors-in-possession subject to the jurisdiction of the Bankruptcy Court. None of the company's other subsidiaries is a debtor in the proceeding. The Debtors' need to seek the relief afforded by the Bankruptcy Code was due, in part, to their requirement to remain in compliance with the physician ownership and referral provisions of the Omnibus Budget Reconciliation Act of 1993 (commonly referred to as "Stark II") after December 31, 2000 (see discussion of Stark II in Note 10 to the company's Condensed Consolidated Financial Statements) and the scheduled May 27, 2001 maturity of the Series A Senior Subordinated Unsecured Notes. Accordingly, the Debtors sought advice and counsel from a variety of sources and, in connection therewith, the Board of Directors unanimously concluded that the bankruptcy and restructuring were the only viable alternatives.

28

On August 9, 2000, the Bankruptcy Court approved the Debtors' motions for: (i) payment of employee wages and salaries and certain benefits and other employee obligations; (ii) payment of critical trade vendors, utilities and insurance in the ordinary course of business for both pre and post-petition expenses; (iii) access to a debtor-in-possession financing arrangement (see Note 7 to the company's Condensed Consolidated Financial Statements for details of the executed agreement); and (iv) use of all company bank accounts for normal business operations. In September 2000, the Bankruptcy Court approved the Debtors' motion to reject four unexpired, non-residential real property leases and any associated subleases. The rejected leases include underutilized locations in: (i) Allentown, Pennsylvania; (ii) Denver, Colorado; (iii)

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Philadelphia, Pennsylvania; and (iv) Whippany, New Jersey. The successful rejection of the Whippany, New Jersey lease caused the company to reverse certain reserves that had previously been established related to closure of its discontinued operations. Additionally, in September 2001 the Bankruptcy Court approved the Debtors' motion for an extension of the period of time in which the Debtors can reject unexpired leases of non-residential real property up to and including January 1, 2002. Certain other motions filed by the Debtors have been granted and others are presently pending.

In September 2000 and October 2000, the Bankruptcy Court approved payments of up to approximately \$2.6 million for retention bonuses to certain key employees. The bonuses were scheduled to be paid in two equal installments on (i) the later of the date of emergence from bankruptcy or December 31, 2000 and (ii) December 31, 2001. Due to events that have delayed the emergence from bankruptcy, the Bankruptcy Court approved early payment of the first installment to most individuals within the retention program and such payments, aggregating approximately \$0.7 million, were made on March 15, 2001. The remaining portion of the first installment of approximately \$0.5 million, which relates to the company's Chief Executive Officer and Executive Vice President, is scheduled for payment upon approval of a plan of reorganization by the Bankruptcy Court, and the second installment remains scheduled to be paid on December 31, 2001. The company is accruing monthly amounts as earned pursuant to the provisions of the retention plan.

On September 7, 2001, the Bankruptcy Court approved payments of up to \$2.7 million for management incentive compensation bonuses (the "MIP Plan") related to the year ended December 31, 2000 for all individuals participating in the MIP Plan, except the company's Chief Executive Officer. In connection therewith, payments were made to those individuals in September 2001.

On October 29, 2001, the Debtors filed a motion with the Bankruptcy Court requesting approval of a proposed asset purchase agreement which would provide the authority for a non-debtor subsidiary of the company to sell certain durable medical equipment presently located at its New Orleans branch to a third party. A hearing on the motion will be held in November 2001; however, no assurances can be given that the Bankruptcy Court will approve the proposed transaction or that the parties will ultimately agree on a final asset purchase agreement.

The Debtors are currently paying the post-petition claims of their vendors in the ordinary course of business and are, pursuant to an order of the Bankruptcy Court, causing their subsidiaries to pay their own debts in the ordinary course of business. Even though the filing of the Chapter 11 cases constituted defaults under the company's principal debt instruments, the Bankruptcy Code imposes an automatic stay that will generally preclude the creditors and other interested parties under such arrangements from taking remedial action in response to any such resulting default without prior Bankruptcy Court approval.

On September 11, 2000, the Resource Network Subsidiaries filed a motion in the Debtors' Chapter 11 proceedings seeking, among other things, to have the two separate bankruptcy proceedings substantively consolidated into one proceeding. The Resource Network Subsidiaries and the Debtors engaged in discovery related to this substantive consolidation motion and, in connection therewith, the parties reached a settlement agreement in November 2000, which was approved by an order of the Bankruptcy Court. See Note 10 to the company's Condensed Consolidated Financial Statements for further details.

On the same day that the Chapter 11 cases were filed, the Debtors filed their joint plan of reorganization (the "Joint Plan") and their joint disclosure statement with the Bankruptcy Court. The Joint Plan was subsequently amended and restated (the "Restated Joint Plan") and, on or about October 10, 2000, the Restated Joint Plan and the First Amended Disclosure Statement with respect to



## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

the Restated Joint Plan were authorized for distribution by the Bankruptcy Court. Among other things, the Restated Joint Plan provided for: (i) a conversion of all of the CI obligations represented by the company's Series A Senior Subordinated Unsecured Notes (the "Series A Notes") and the Series B Senior Subordinated Unsecured Convertible Notes (the "Series B Notes") into (a) a four-year, interest only note in the principal amount of \$180 million, that would bear interest at the rate of 9% per annum and (b) all of the equity in the reorganized CI; (ii) the payment in full of all secured, priority and general unsecured debts of CI; (iii) the payment in full of all secured and priority claims against CHC; (iv) the impairment of certain general unsecured debts of CHC, including, among others, CHC's obligations under the Series A Notes and the Series B Notes; and (v) the complete elimination of the equity interests of CHC. Furthermore, pursuant to the Restated Joint Plan, CHC would be dissolved as soon as practicable after the effective date of the

29

Restated Joint Plan and the stock of CHC would no longer be publicly traded. Therefore, under the Debtors' Restated Joint Plan, as filed, the existing stockholders of CHC would have received no value for their shares and all of the outstanding equity of CI as the surviving entity would be owned by the holders of the company's Series A Notes and Series B Notes. Representatives of the company negotiated the principal aspects of the Joint Plan with representatives of the holders of the company's Series A Notes and Series B Notes and Senior Credit Facility prior to the filing of such Joint Plan.

On or about October 20, 2000, the Restated Joint Plan and First Amended Disclosure Statement were distributed for a vote among persons holding impaired claims that were entitled to a distribution under the Restated Joint Plan. The Debtors did not send ballots to the holders of other types of claims and interested parties, including equity holders, as the holders of such claims and interested parties were deemed to reject the Restated Joint Plan. The tabulated vote of the unsecured creditors was in favor of the company's Restated Joint Plan. However, culminating at a confirmation hearing on December 21, 2000, the Restated Joint Plan was not approved by the Bankruptcy Court. On April 25, 2001 and July 11, 2001, the Bankruptcy Court extended the period during which the Debtors have the exclusive right to file a plan or plans before the Bankruptcy Court to July 11, 2001 and August 1, 2001, respectively. Additionally, on August 2, 2001, the Bankruptcy Court extended the Debtors' exclusivity period to solicit acceptances of any filed plan or plans to November 9, 2001 (the date to solicit acceptances of the plan for CHC's equity holders was subsequently extended to November 12, 2001). On or about November 7, 2001, the company filed a motion seeking to extend the exclusivity dates to file a plan or plans and solicit acceptances thereof to December 31, 2001 and March 4, 2002, respectively. A hearing on the motion is scheduled for December 2001.

In order for the company to remain compliant with the requirements of Stark II, on December 29, 2000, pursuant to an order of the Bankruptcy Court, CI exchanged approximately \$97.7 million of the Series A Notes and approximately \$11.6 million of accrued but unpaid interest on the Series A Notes and the Series B Notes for 905 shares of CI Series A Cumulative Preferred Stock (see Notes 7 and 9 to the company's Condensed Consolidated Financial Statements for further details). This transaction generated an extraordinary gain on troubled debt restructuring of approximately \$107.8 million, net of tax, which was recorded in the fourth quarter of the year ended December 31, 2000. At December 31, 2000, the company's stockholders' equity exceeded the minimum Stark II requirement necessary to comply with the public company exemption. See Note 10 to the company's Condensed Consolidated Financial Statements for further discussion regarding Stark II.

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

On or about February 6, 2001, the Official Committee of the Equity Security Holders (the "Equity Committee") filed a motion with the Bankruptcy Court seeking permission to bring a derivative lawsuit directly against the company's Chief Executive Officer, a former member of the Board of Directors and Cerberus Partners, L.P. (a party to the company's debtor-in-possession financing agreement, Senior Credit Facility and Securities Exchange Agreement). On February 26, 2001, the Bankruptcy Court ruled that the Equity Committee's motion would not be productive at that time and, accordingly, the motion was denied without prejudice. On the same day, the Bankruptcy Court approved the Debtors' motion and appointed Goldin Associates, L.L.C. ("Goldin") as independent restructuring advisors to the Independent Committee of the Board of Directors (the "Independent Committee"). Among other things, the scope of Goldin's services include (i) reporting its findings to the Independent Committee, including its assessment of the appropriateness of the Restated Joint Plan, and advising the Independent Committee respecting an appropriate course of action calculated to bring the Debtors' bankruptcy proceedings to a fair and satisfactory conclusion, (ii) preparing a written report as may be required by the Independent Committee and/or the Bankruptcy Court and (iii) appearing before the Bankruptcy Court to provide testimony, as needed. Goldin was also appointed as a mediator among the Debtors, the Equity Committee and other parties in interest.

Based upon Goldin's findings and recommendations, as set forth in the Report of Independent Restructuring Advisor, Goldin Associates L.L.C. (the "Goldin Report"), on July 31, 2001 the Debtors filed with the Bankruptcy Court a Second Joint Disclosure Statement, as amended (the "Second Disclosure Statement"), with respect to their Second Joint Plan. The Second Joint Plan, which was also filed on July 31, 2001, provides for terms of reorganization similar to those described in the Restated Joint Plan; however, utilizing Goldin's recommendations, as set forth in the Goldin Report, the following substantive modifications are included in the Second Joint Plan:

- o the payment of up to \$3.0 million to the holders of allowed general unsecured claims of CHC;
- o the payment of up to \$10.0 million to the holders of CHC equity interests (contingent upon such holders voting in favor of the Second Joint Plan);
- o cancellation of the issued and outstanding CI Series A Cumulative Preferred Stock; and
- o a \$7.5 million reduction in certain performance bonuses payable to Daniel D. Crowley, the company's Chief Executive Officer.

30

Under certain circumstances, as more fully discussed in the Second Disclosure Statement, the general unsecured claim holders may be entitled to receive a portion of the \$10.0 million cash consideration allocated to the holders of CHC equity interests.

In order to become effective, the Second Joint Plan is subject to a vote by certain impaired creditors and equity holders and final approval of the Bankruptcy Court. On September 6, 2001 and September 10, 2001, hearings before the Bankruptcy Court considered the adequacy of the Second Disclosure Statement and, in connection therewith, the Second Disclosure Statement was approved for distribution to holders of certain claims in interests who are entitled to vote

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

on the Second Joint Plan. On or about September 21, 2001, the Debtors mailed ballots to those parties entitled to vote on the Second Joint Plan.

Among other things, the Equity Committee's motion to terminate the Debtors' exclusivity periods and file its own plan of reorganization was denied by the Bankruptcy Court on August 1, 2001. The Equity Committee also filed a motion protesting and objecting to the Debtors' Second Joint Plan. Moreover, the Official Committee of the Equity Security Holders and Official Committee of Unsecured Creditors in the Resource Network Subsidiaries' bankruptcy proceedings filed objections to confirmation of the Second Joint Plan. Management of the company cannot predict what impact the Equity Committee or any other interested parties, including those parties associated with the Resource Network Subsidiaries' bankruptcy proceedings, will have on the Second Joint Plan.

The tabulation of the ballots distributed to the holders of certain claims in interests who were entitled to vote on the Second Joint Plan resulted in the CHC equity holders voting against confirmation of the Second Joint Plan and all other classes of claimholders voting in favor of the Second Joint Plan. The Bankruptcy Court may ultimately confirm a plan of reorganization notwithstanding the non-acceptance of the plan by an impaired class of creditors or equity holders if certain conditions of the Bankruptcy Code are satisfied; however, no assurances can be given regarding the confirmation of the Second Joint Plan. Bankruptcy Court confirmation hearings for final confirmation of the Second Joint Plan have commenced and will continue through early December 2001.

Under the Bankruptcy Code, certain claims against the Debtors in existence prior to the filing date are stayed while the Debtors continue their operations as debtors-in-possession. These claims are reflected in the Condensed Consolidated Balance Sheets as liabilities subject to compromise. Additional Chapter 11 bankruptcy claims have arisen and may continue to arise subsequent to the filing date resulting from the rejection of executory contracts, including certain leases, and from the determination by the Bankruptcy Court of allowed claims for contingencies and other disputed amounts. Parties affected by the rejections may file claims with the Bankruptcy Court in accordance with the provisions of the Bankruptcy Code and applicable rules. Claims secured by the Debtors' assets also are stayed, although the holders of such claims have the right to petition the Bankruptcy Court for relief from the automatic stay and foreclose on the property securing their claims. Additionally, certain claimants have sought relief from the Bankruptcy Court to remove the automatic stay and continue pursuit of their claims against the Debtors or the Debtors' insurance carriers.

The holders of Coram, Inc.'s Series A Cumulative Preferred Stock continue to maintain a claim position within the Debtors' bankruptcy proceedings in the aggregate amount of their cumulative liquidation preference. Notwithstanding the debt to equity exchange, the aforementioned holders' priority in the Debtors' bankruptcy proceedings will be no less than it was immediately prior to said exchange.

Schedules were filed with the Bankruptcy Court setting forth the assets and liabilities of the Debtors as of the filing date as shown by the Debtors' accounting records. Differences between amounts shown by the Debtors and claims filed by creditors are being investigated and resolved. The ultimate amount and the settlement terms for such liabilities will be subject to the Second Joint Plan, which, as discussed above, has been voted on and is now subject to confirmation by the Bankruptcy Court. Therefore it is not possible to fully or completely estimate the fair value of the liabilities subject to compromise at September 30, 2001 due to the Debtors' Chapter 11 cases and the uncertainty surrounding the ultimate amount and settlement terms for such liabilities.

RESULTS OF OPERATIONS

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

As discussed in Note 3 to the company's Condensed Consolidated Financial Statements, the company considers R-Net's operating results as part of discontinued operations; however, for the three and nine months ended September 30, 2001 and 2000 the Resource Network Subsidiaries had no operations.

Three Months Ended September 30, 2001 Compared to Three Months Ended September 30, 2000

**Net Revenue.** Net revenue decreased \$9.1 million or 8.8% to \$93.8 million in the three months ended September 30, 2001 from \$102.9 million in the three months ended September 30, 2000. The decrease is primarily due to a permanent reduction, effective July 1, 2001, in the Average Wholesale Price ("AWP") for, among others, the antibiotic drug Vancomycin. The direct impact of the AWP reduction resulted in an

31

unfavorable pricing variance of \$3.2 million for the three months ended September 30, 2001 compared to the three months ended September 30, 2000 (see "Risk Factors" for further AWP discussion), the sale of CPS on July 31, 2000 (CPS had net revenue of \$8.4 million during the three months ended September 30, 2000) and a \$0.2 million decline in net revenue attributable to the company's subsidiary, CTI Network, Inc. ("CTI"). These decreases are partially offset by net revenue increases from initiatives to focus on core infusion therapies.

**Gross Profit.** Gross profit decreased \$2.1 million to \$25.1 million or a gross margin of 26.8% in the three months ended September 30, 2001 from \$27.2 million or a gross margin of 26.4% in the three months ended September 30, 2000. The gross margin percentage increase is primarily due to a more favorable product/therapy mix and the sale of CPS, which had a lower gross margin percentage than that of the infusion business segment, thereby causing a lower blended consolidated percentage during the three months ended September 30, 2000. However, commencing on July 1, 2001, there was an offsetting decrease in gross profit due to reductions in the AWP reimbursement rates for Vancomycin and certain other drugs used in the company's operations. The components of gross profit are as follows (in millions):

	FOR THE THREE MONTHS ENDED SEPTEMBER 30,	
	2001	2000
	-----	-----
Infusion .....	\$24,921	\$25,877
CPS .....	--	934
CTI .....	190	388
	-----	-----
Total gross profit ....	\$25,111	\$27,199
	=====	=====

**Selling, General and Administrative ("SG&A") Expenses.** SG&A expenses decreased \$2.7 million or 12.2% to \$19.4 million in the three months ended September 30, 2001 from \$22.1 million in the three months ended September 30, 2000. The decrease during the three months ended September 30, 2001 is primarily due a decrease in expenses related to management incentive compensation of \$4.4

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

million and approximately \$0.4 million of SG&A expenses directly related to CPS personnel and other CPS related activities that were eliminated upon the divestiture of the CPS business segment. The aforementioned expense decreases are partially offset by costs incurred by the company to enhance its risk-management profile and expand its sales force.

**Provision for Estimated Uncollectible Accounts.** The provision for estimated uncollectible accounts is \$2.9 million or 3.0% of net revenue in the three months ended September 30, 2001 compared to \$3.4 million or 3.3% of net revenue in the three months ended September 30, 2000. The percentage decrease is primarily attributable to a higher level of bad debt write-offs in the three months ended September 30, 2000.

**Interest Expense.** Interest expense decreased \$2.8 million to \$4.1 million in the three months ended September 30, 2001 from \$6.9 million in the three months ended September 30, 2000. The decrease is primarily due to (i) reduced outstanding borrowings on revolving credit arrangements and (ii) the non-recognition of interest expense related to the Series A Senior Subordinated Unsecured Notes (the "Series A Notes") and the Series B Senior Subordinated Unsecured Convertible Notes (the "Series B Notes") in connection with the execution of the Exchange Agreement on December 29, 2000, which qualified as a troubled debt restructuring (see Notes 7 and 9 to the company's Condensed Consolidated Financial Statements for further details). These decreases are partially offset by the recognition of approximately \$4.1 million of interest expense on the proposed settlement of a dispute with the Internal Revenue Service, which is more fully described in Note 8 to the company's Condensed Consolidated Financial Statements.

**Gains on Sales of Businesses.** During the three months ended September 30, 2000, the company recorded gains on sales of businesses of approximately \$18.5 million consisting primarily of the gain on the sale of the CPS business and an earn-out payment relating to one of the company's operating subsidiaries. See Note 4 to the company's Condensed Consolidated Financial Statements for further details.

**Reorganization Expenses, Net.** In the three months ended September 30, 2001, the company recognized \$3.7 million in net reorganization expenses compared to \$1.9 million during the three months ended September 30, 2000 related to the Debtors' Chapter 11 bankruptcy proceedings. The principal reason for the increased reorganization expenses is the commencement of the company's bankruptcy proceedings in the middle of the three month period ended September 30, 2000 and the continuation of such proceedings during the entire three month period ended September 30, 2001. These expenses include, but are not limited to, professional fees, expenses related to employee retention plans, United States Trustee fees and other expenditures during the Chapter 11 proceedings, offset by interest earned on accumulated cash due to the Debtors not paying their liabilities subject to compromise. See Note 2 to the company's Condensed Consolidated Financial Statements for further details.

32

**Income Tax Expense.** See Note 8 to the company's Condensed Consolidated Financial Statements for discussion of the variance between the statutory income tax rate and the company's effective income tax rate.

**Income from Disposal of Discontinued Operations.** During the three months ended September 30, 2000, Coram recognized income in the aggregate amount of \$0.3 million related to proceeds from certain insurance recoveries. See Note 3 to the company's Condensed Consolidated Financial Statements for further

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

discussion of the discontinued operations.

Nine Months Ended September 30, 2001 Compared to Nine Months Ended September 30, 2000

**Net Revenue.** Net revenue decreased \$80.4 million or 21.9% to \$287.5 million in the nine months ended September 30, 2001 from \$367.9 million in the nine months ended September 30, 2000. The decrease is primarily due to the sale of CPS on July 31, 2000 (CPS had net revenue of \$61.4 million during the nine months ended September 30, 2000), a \$1.9 million decline in net revenue attributable to CTI and a permanent reduction, effective July 1, 2001, in the AWP for, among others, the antibiotic drug Vancomycin. The direct impact of the AWP reduction resulted in an unfavorable pricing variance of \$1.0 million for the nine months ended September 30, 2001 compared to the nine months ended September 30, 2000 (see "Risk Factors" for further AWP discussion). Additionally, a decrease in infusion net revenue of approximately \$17 million is due, in part, to the termination of the Aetna National Ancillary Services Agreement, effective April 12, 2000.

**Gross Profit.** Gross profit decreased \$15.4 million to \$80.1 million or a gross margin of 27.9% in the nine months ended September 30, 2001 from \$95.5 million or a gross margin of 26.0% in the nine months ended September 30, 2000. The gross margin percentage increase is primarily due to a more favorable product/therapy mix and the sale of CPS, which had a lower gross margin percentage than that of the infusion business segment, thereby causing a lower blended consolidated percentage during the nine months ended September 30, 2000. However, commencing on July 1, 2001, there was an offsetting decrease in gross profit due to reductions in the AWP reimbursement rates for Vancomycin and certain other drugs used in the company's operations. The components of gross profit are as follows (in millions):

	FOR THE NINE MONTHS ENDED SEPTEMBER 30,	
	2001	2000
	-----	-----
Infusion .....	\$79,716	\$86,017
CPS .....	--	8,059
CTI .....	421	1,419
	-----	-----
Total gross profit ....	\$80,137	\$95,495
	=====	=====

**Selling, General and Administrative ("SG&A") Expenses.** SG&A expenses decreased \$9.5 million or 13.5% to \$61.1 million in the nine months ended September 30, 2001 from \$70.6 million in the nine months ended September 30, 2000. The decrease during the nine months ended September 30, 2001 is primarily due to approximately \$4.5 million of SG&A expenses directly related to CPS personnel and other CPS related activities that were eliminated upon the divestiture of the CPS business segment and a decrease in expenses related to management incentive compensation of \$8.4 million (in connection with the plans approved by the company's Compensation Committee of the Board of Directors and filed with the Bankruptcy Court, the company recorded management incentive compensation expenses of \$1.5 million and \$9.9 million for the nine months ended September 30, 2001 and 2000, respectively). The aforementioned expense decreases are partially offset by costs incurred by the company to enhance its risk-management profile and expand its sales force.

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Provision for Estimated Uncollectible Accounts. The provision for estimated uncollectible accounts is \$8.8 million or 3.1% of net revenue in the nine months ended September 30, 2001 compared to \$10.1 million or 2.8% of net revenue in the nine months ended September 30, 2000. The percentage increase is primarily attributable to the sale of CPS, which had a lower bad debt experience rate than that of the infusion business segment, thereby causing a lower blended consolidated effective rate during the nine months ended September 30, 2000. Additionally, the company experienced a bad debt recovery of \$0.3 million during the nine months ended September 30, 2000.

Restructuring Cost Recovery. During the nine months ended September 30, 2001, the company recognized restructuring cost recoveries of approximately \$0.6 million related to the assumption of one of the company's real property leases by a third party and certain changes in estimates attributable to severance liabilities. Such items were previously reserved for as part of accrued merger and restructuring costs.

33

Interest Expense. Interest expense decreased \$14.0 million to \$6.3 million in the nine months ended September 30, 2001 from \$20.3 million in the nine months ended September 30, 2000. The decrease is primarily due to (i) reduced outstanding borrowings on revolving credit arrangements and (ii) the non-recognition of interest expense related to the Series A Notes and the Series B Senior Notes in connection with the execution of the Exchange Agreement on December 29, 2000, which qualified as a troubled debt restructuring (see Notes 7 and 9 to the company's Condensed Consolidated Financial Statements for further details). These decreases are partially offset by the recognition of approximately \$5.5 million of interest expense on the proposed settlement of a dispute with the Internal Revenue Service, which is more fully described in Note 8 to the company's Condensed Consolidated Financial Statements.

Gains on Sales of Businesses. During the nine months ended September 30, 2000, the company recorded gains on sales of businesses of approximately \$18.5 million consisting primarily of the gain on the sale of the CPS business and an earn-out payment relating to one of the company's operating subsidiaries. See Note 4 to the company's Condensed Consolidated Financial Statements for further details.

Reorganization Expenses, Net. In the nine months ended September 30, 2001, the company recognized \$10.0 million in net reorganization expenses compared to \$1.9 million in the nine months ended September 30, 2000 related to the Debtors' Chapter 11 bankruptcy proceedings. The principal reason for the increased reorganization expenses is the commencement of the company's bankruptcy proceedings late in the nine month period ended September 30, 2000 and the continuation of such proceedings during the entire nine month period ended September 30, 2001. These expenses include, but are not limited to, professional fees, expenses related to employee retention plans, United States Trustee fees and other expenditures during the Chapter 11 proceedings, offset by interest earned on accumulated cash due to the Debtors not paying their pre-petition liabilities. See Note 2 to the company's Condensed Consolidated Financial Statements for further details.

Income Tax Expense. See Note 8 to the company's Condensed Consolidated Financial Statements for discussion of the variance between the statutory income tax rate and the company's effective income tax rate.

Loss on Disposal of Discontinued Operations. During the nine months ended

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

September 30, 2000, Coram recorded charges in the aggregate amount of \$3.5 million, which includes additional reserves for litigation and other wind-down costs of the Resource Network Subsidiaries. These charges are partially offset by \$0.3 million in proceeds related to certain insurance recoveries. See Note 3 to the company's Condensed Consolidated Financial Statements for further discussion of the discontinued operations.

### LIQUIDITY AND CAPITAL RESOURCES

**Bankruptcy Proceedings.** The Debtors filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code on August 8, 2000. Since that date, the Debtors have been operating as debtors-in-possession subject to the jurisdiction of the Bankruptcy Court. None of the company's other subsidiaries is a debtor in the proceeding. Although the filing of the Chapter 11 cases constitutes defaults under the company's principal debt instruments, Section 362 of the Bankruptcy Code imposes an automatic stay that will generally preclude creditors and other interested parties under such arrangements from taking remedial action in response to any such default without prior Bankruptcy Court approval. In addition, the Debtors may reject executory contracts and unexpired leases. Parties affected by the rejections may file claims with the Bankruptcy Court in accordance with the provisions of the Bankruptcy Code and applicable rules. See Note 2 to the company's Condensed Consolidated Financial Statements for further details.

Schedules were filed with the Bankruptcy Court setting forth the assets and liabilities of the Debtors as of the filing date as shown by the Debtors' accounting records. Differences between amounts shown by the Debtors and claims filed by creditors are being investigated and resolved. The ultimate amount and the settlement terms for such liabilities will be subject to the Debtors' Second Joint Plan, which, as discussed above, has been voted on and is now subject to confirmation by the Bankruptcy Court. Therefore, it is not possible to fully or completely estimate the fair value of the liabilities subject to compromise at September 30, 2001 due to the Debtors' Chapter 11 cases and the uncertainty surrounding the ultimate amount and settlement terms for such liabilities.

**Credit Facilities.** On August 20, 1998, the company entered into the Senior Credit Facility, which provided for the availability of up to \$60.0 million for acquisitions, working capital, letters of credit and other corporate purposes. The terms of the agreement also provided for the issuance of letters of credit of up to \$25.0 million provided that available credit would not fall below zero. In connection with the sale of CPS, effective July 31, 2000, the company reduced its outstanding borrowings under the Senior Credit Facility by \$28.5 million, leaving only irrevocable letter of credit obligations of \$2.7 million outstanding. Furthermore, on September 21, 2000 and January 29, 2001, the company permanently reduced the Senior Credit Facility commitment to \$2.7 million and \$2.1 million, respectively, in order to reduce the fees related to commitments on which the company was not be able to borrow against due

to the Debtors' bankruptcy proceedings. Effective February 6, 2001, the Senior Credit Facility lenders and the company terminated the Senior Credit Facility. In connection with the termination of the Senior Credit Facility and pursuant to orders of the Bankruptcy Court, the company established new letters of credit aggregating \$2.1 million through Wells Fargo Bank Minnesota, NA ("Wells Fargo") and such new letters of credit are fully secured by interest bearing cash deposits of the company held by Wells Fargo. Due to certain hemophilia and intravenous immunoglobulin product shortages and the pendency of the Debtors' bankruptcy proceedings, the company may be required to enhance exiting letters



## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

of credit or establish new letters of credit in order to ensure the availability of such products for its patients' medical needs.

The Debtors entered into a secured debtor-in-possession ("DIP") financing agreement with Madeleine L.L.C., an affiliate of Cerberus Partners, L.P. (a party to the Senior Credit Facility and the Securities Exchange Agreement), as of August 30, 2000. Prior to entering into the DIP financing agreement, management and the Board of Directors solicited advice from the company's financial advisors. Such advisors indicated that the terms and conditions of the DIP financing agreement were generally favorable when compared to a company with Coram's financial history. The agreement provided that the Debtors could access, as necessary, up to \$40 million depending upon borrowing base availability, for use in connection with the operations of their businesses and the businesses of their subsidiaries. On September 12, 2000, the Bankruptcy Court approved the DIP agreement. The DIP financing agreement expired by its terms on August 31, 2001 with the company making no draw-downs thereunder through the term of the financing. See Note 7 to the company's Condensed Consolidated Financial Statements for further details.

Management is currently negotiating a renewal of the DIP financing agreement; however, no assurances can be given that the parties will ultimately agree to the terms and conditions of such renewal or that a renewal will be approved by the Bankruptcy Court.

On December 29, 2000, the Securities Exchange Agreement was amended ("Amendment No. 4") and an Exchange Agreement was simultaneously executed among the Debtors and Cerberus Partners, L.P., Goldman Sachs Credit Partners, L.P. and Foothill Capital Corporation (collectively the "Holders"). Pursuant to such arrangements, the Holders agreed to exchange approximately \$97.7 million aggregate principal amount of the Series A Notes and \$11.6 million of aggregate unpaid accrued contractual interest on the Series A Notes and the Series B Notes as of December 29, 2000 for 905 shares of Coram, Inc. Series A Cumulative Preferred Stock (see Note 9 to the company's Condensed Consolidated Financial Statements for further details regarding the preferred stock). Following the exchange, the Holders retain approximately \$61.2 million aggregate principal amount of the Series A Notes and \$92.1 million aggregate principal amount of the Series B Notes. Pursuant to Amendment No. 4, the per annum interest rate on both the Series A Notes and the Series B Notes has been adjusted to 9.0%. Moreover, the Series A Notes' and Series B Notes' original scheduled maturity dates of May 2001 and April 2008, respectively, have both been modified to June 30, 2001. See Note 7 to the company's Condensed Consolidated Financial Statements for discussion of certain continuing defaults under the Securities Exchange Agreement. Due to the Holders' receipt of consideration with a fair value less than the face value of the exchanged principal and accrued interest, the exchange transactions qualified as a troubled debt restructuring pursuant to Statement of Financial Accounting Standards No. 15, Accounting by Debtors and Creditors for Troubled Debt Restructurings. In connection therewith, the company recognized an extraordinary gain during the fourth quarter of the year ended December 31, 2000 of approximately \$107.8 million, net of tax. As of November 16, 2001, the aggregate Preferred Stock liquidation preference was approximately \$122.2 million.

Exit Financing Facility. In connection with the Chapter 11 cases, on October 26, 2001, CI filed a draft of the Exit Financing Facility with the Bankruptcy Court together with other draft documents relating to the Second Joint Plan. The proposed lenders under the Exit Financing Facility would include the Holders or affiliates thereof. The agreement contemplates that CI could access, as necessary, a revolving credit facility of up to \$40 million for use in connection with payments under the Second Joint Plan and for general working capital and corporate purposes of the company and its subsidiaries. If approved, the Exit Financing Facility will mature the earlier of December 2004 or the date on which the revolving loans shall become due and payable in accordance with the

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

terms of the agreement. No assurances can be given that the parties will ultimately agree to the terms and conditions as set forth in the proposed Exit Financing Facility agreement or that such agreement will be approved by the Bankruptcy Court.

The money necessary for CI to make payments pursuant to the Second Joint Plan is expected to be obtained from the company's available cash balances and cash flow from operations of reorganized CI and may also include funds from the Exit Financing Facility.

General. The company's Consolidated Financial Statements have been prepared on a going concern basis, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the ordinary course of business. However, as a result of the Debtors' bankruptcy filings and circumstances relating thereto, including the company's leveraged financial structure and cumulative losses from operations, such realization of assets and liquidation of liabilities is subject to significant uncertainty. During the pendency of the Debtors' Chapter 11 bankruptcy proceedings, the company may sell or otherwise dispose of assets and liquidate or settle liabilities for amounts other than those reflected in the Condensed Consolidated Financial Statements. Further, a confirmed plan

35

of reorganization in the Chapter 11 proceedings could materially change the amounts reported in the Condensed Consolidated Financial Statements, which do not give effect to any adjustments of the carrying value of assets or liabilities that might be necessary as a consequence of a confirmed plan of reorganization. The company's ability to continue as a going concern is dependent upon, among other things, confirmation of a plan of reorganization, future profitable operations, the ability to comply with the terms of the company's financing agreements, the ability to remain in compliance with the physician ownership and referral provisions of Stark II and the ability to generate sufficient cash from operations and/or financing arrangements to meet its obligations.

Coram used cash generated from operations and cash reserves to fund its reorganization activities, working capital requirements and operations for the nine months ended September 30, 2001. Coram's working capital deficit as of September 30, 2001 was \$97.7 million as compared to a working capital deficit of \$97.1 million at December 31, 2000. The working capital deficits at such dates are primarily due to (i) liabilities subject to compromise classified as current liabilities, including the full amount of the company's Series A Notes and the Series B Notes aggregating \$153.3 million, (ii) accruals for management incentive compensation and (iii) accruals for administrative costs of the Debtors' bankruptcy proceedings. Events impacting the net working capital deficit during the nine months ended September 30, 2001 were the requisite deposit of \$2.1 million needed to collateralize certain letters of credit and obligations to purchase new financial and human resource software packages. As discussed above under Credit Facilities, the company may be required to provide additional cash collateral or new and/or enhanced letters of credit. Changes in current assets related to (i) a decrease in cash and cash equivalents of \$9.0 million, (ii) an increase in accounts receivable of \$12.9 million primarily due to unfavorable effects resulting from the consolidation of the company's reimbursement sites, (iii) a decrease in inventories of \$0.7 million and (iv) an increase in other current assets of \$1.1 million. Total current liabilities changed primarily due to (i) an increase in accrued compensation and related liabilities of \$2.7 million, (ii) a decrease in merger and restructuring costs of \$1.5 million (including a non-cash reserve reversal of \$0.6 million), (iii)

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

an increase in accrued reorganization costs for administrative professionals of \$3.0 million and (iv) an increase in other accrued liabilities of \$0.8 million.

Management throughout the company is continuing to concentrate on enhancing timely reimbursement by emphasizing improved billing and cash collection methods, continued assessment of systems support for reimbursement and concentration of the company's expertise and managerial resources into certain reimbursement locations. In December 2000, Coram announced that as part of its continuing efforts to improve efficiency and overall performance, several Patient Financial Service Centers (reimbursement sites) were being consolidated and the related reimbursement positions were to be eliminated. By consolidating to fewer sites, management expects to implement improved training, more easily standardize "best demonstrated practices," enhance specialization related to payers such as Medicare and achieve more consistent and timely cash collections. Management does not expect this change to affect Coram's patients or payers, but believes, instead, that in the long-term they will receive better, more consistent service. The transition was accomplished in stages, commencing April 1, 2001 and ending July 2001. Management had taken certain actions to mitigate the potential shortfall in cash collections during and after the transition period, including, but not limited to, offering incentives for personnel to stay with the company until the completion of their corresponding regional consolidation. Notwithstanding management's efforts, the company experienced deterioration in its days sales outstanding ("DSO") since the commencement of the reimbursement consolidation plan and a substantial growth in accounts receivable. No assurances can be given that the consolidation of the company's Patient Financial Service Centers will be successful in enhancing timely reimbursement, that the company will not continue to experience a significant shortfall in cash collections after the transition period or that the aforementioned deterioration in DSO and accounts receivable growth will not continue.

Management believes that the costs for the Debtors' reorganization and bankruptcy proceedings will result in significant use of cash for the year ending December 31, 2001 and thereafter. These items principally consist of professional fees and expenses and expenditures related to key employee success and retention plans. Management believes that such costs will primarily be funded through available cash balances, cash provided by operations and, if the terms of the Exit Financing Facility are approved by the Bankruptcy Court and if the parties ultimately agree to final terms and conditions, funds provided by the Exit Financing Facility.

36

The company sponsors a Management Incentive Plan ("MIP"), which provides for annual bonuses payable to certain key employees. The bonuses are predicated on overall corporate performance (principally cash collections and earnings before interest, taxes, reorganization expenses, restructuring costs, depreciation and amortization), as well as, individual performance targets and objectives. On March 20, 2001, the Compensation Committee of the company's Board of Directors approved an overall award of approximately \$13.6 million for the year ended December 31, 2000 for those individuals participating in the MIP. The Second Joint Plan, if approved, will reduce the MIP and other incentive compensation by \$7.5 million related to amounts payable to Daniel D. Crowley, the company's Chief Executive Officer. On September 7, 2001, the Bankruptcy Court approved payment of up to approximately \$2.7 million for the MIP related to the year ended December 31, 2000 to all individuals participating in the MIP, except for the amounts due to Mr. Crowley. In connection therewith, such payments to those individuals were made in September 2001. The \$7.5 million incentive compensation bonus for Mr. Crowley that is subject to potential

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

downward adjustment is recorded in current liabilities subject to compromise in the accompanying Condensed Consolidated Balance Sheets.

On or about May 9, 2001, the Bankruptcy Court approved the Debtors' motion requesting authorization to enter into an insurance premium financing agreement with AICCO, Inc. (the "Financing Agreement") to finance the payment of premiums under certain of the Debtors' insurance policies. Under the terms of the Financing Agreement, the Debtors made a down payment of approximately \$1.1 million. The amount financed is approximately \$2.1 million and is secured by the unearned premiums and loss payments under the insurance policies covered by the Financing Agreement. The amount financed is being paid in eight monthly installments of approximately \$0.3 million each, including interest at a per annum rate of 7.85%, which commenced on May 15, 2001. In addition, AICCO, Inc. has the right to terminate the insurance policies and collect the unearned premiums (as administrative expenses) if the Debtors do not make the monthly payments called for by the Financing Agreement.

The final liquidation of the Resource Network Subsidiaries through their bankruptcy proceedings may result in certain additional cash expenditures by the company beyond the cash accounts already deemed to be a part of R-Net's bankruptcy estate. While management does not expect that such amounts, if any, will be material to the financial condition or cash flows of the company, no assurances can be given as to the company's aggregate amount of expenditures anticipated related to the Resource Network Subsidiaries' bankruptcy. See Note 10 to the company's Condensed Consolidated Financial Statements for further details.

The Board of Directors approved management's request to upgrade Coram's company-wide information systems. In connection therewith, on May 17, 2001 the company entered into an agreement whereby new financial and human resource software packages and related licenses will be procured. The total purchase price for such software and licenses will be approximately \$1.2 million, of which \$0.5 million was paid on May 18, 2001 and the remaining balance is accrued in the accompanying Condensed Consolidated Balance Sheets. Additional internal and external costs will be incurred to implement this software. The company also entered into an agreement to purchase certain hardware necessary for the new information systems. The aggregate purchase price for the hardware will be approximately \$1.4 million, including \$0.3 million and \$0.9 million paid in September 2001 and October 2001, respectively. Additional hardware components will be required in order to make the new software fully functional and, in connection therewith, management is currently evaluating several alternatives. The company intends to fund its current and future capital commitments with its available cash balances, cash provided by operations and, if approved by the Bankruptcy Court and if the parties ultimately agree to final terms and conditions, funds from the Exit Financing Facility.

Coram is currently in negotiations to settle a dispute with the Internal Revenue Service regarding certain tax refunds previously received by the company. If the company is not able to negotiate an installment payment plan with the IRS with respect to the proposed settlement amount or if either the Joint Committee of Taxation or the Bankruptcy Court do not approve the proposed settlement amount, the financial position and liquidity of the company could be materially adversely affected. Furthermore, management cannot predict whether any future objections of the Official Committee of the Equity Security Holders or other interested parties in the Debtors' bankruptcy proceedings will be forthcoming or if they would prevent confirmation of the Debtors' Second Joint Plan. Outcomes unfavorable to the company or unknown additional actions could require the company and the Debtors to access significant additional funds. See Notes 8 and 10 to the company's Condensed Consolidated Financial Statements for further details.

RISK FACTORS

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

There can be no assurance regarding Coram's ability to continue operations in light of the Chapter 11 Proceedings.

The company's ability to continue operations is dependent upon, among other things, confirmation of a plan of reorganization, success of future operations after such confirmation and the ability to generate sufficient cash from operations and financing sources to meet obligations. There can be no assurances that the Debtors' Second Joint Plan or any other plan of reorganization will be approved by the Bankruptcy Court or that such a plan will allow the company to operate profitably. Any plan of reorganization and

37

other actions during the Chapter 11 proceedings could change materially the financial condition and/or outlook of the company. Furthermore, the future availability or terms of financing cannot be determined in light of the Chapter 11 filings and there can be no assurances that the amounts available through the proposed Exit Financing Facility will be sufficient to fund the operations of the company or that other financing instruments will not be necessary during the pendency of the Debtors' bankruptcy proceedings. In addition, the company may experience difficulty in attracting and maintaining patients and appropriate personnel as a result of the Chapter 11 proceedings.

Coram's common stock is subject to a high degree of risk and market volatility.

As a result of the Chapter 11 bankruptcy filings of the Debtors, the equity interests of the common stockholders are subject to a high degree of risk. Should a plan of reorganization similar to the Second Joint Plan of reorganization be approved, the complete elimination of the equity interests of CHC would occur in accordance with the terms of the Second Joint Plan. There can be no assurances that the Second Joint Plan will be approved by Bankruptcy Court. See Note 2 to the company's Condensed Consolidated Financial Statements for further details.

There has historically been and may continue to be significant volatility in the market price for Coram's common stock. Factors include, but not limited to, the Debtors' Chapter 11 bankruptcy proceedings, actual or anticipated fluctuations in Coram's operating results, new products or services introduced or new contracts entered into by the company or its competitors, conditions and trends in the healthcare industry including changes in government reimbursement policies, changes in financial estimates by securities analysts, general market conditions and other factors could cause the market price of Coram's common stock to fluctuate substantially. In addition, the stock market has from time to time experienced significant price and volume fluctuations that have particularly affected the market price for the common stock of healthcare companies. These broad market fluctuations may adversely affect the market price of the common stock. In the past, following periods of volatility in the market price of a particular company's securities, securities class action litigation has been brought against that company. There can be no assurances that such litigation will not occur in the future with respect to Coram. Such litigation could result in substantial costs and a diversion of management's attention and resources, which could have a material adverse effect upon Coram's business, financial condition and results of operations.

Under the Stark II law, Coram will need to maintain certain equity requirements in order to be able to avoid disruption in accepting referrals of certain patients from physicians who may own shares of Coram common stock.

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

Coram is aware that certain referring physicians (or their immediate family members) have, from time to time, owned shares of its common stock. A federal law, known as Stark II, prohibits a physician from making Medicare or Medicaid referrals for certain "designated health services," including durable medical equipment, parenteral and enteral nutrition therapy and outpatient prescription drugs, to entities with which the physician or an immediate family member has a financial relationship, unless an exception to the law is available. The Stark II law includes an exception for the ownership of publicly traded stock in companies with equity above certain levels. This exception of Stark II requires the issuing company to have stockholders' equity of at least \$75 million either as of the end of its most recent fiscal year or on average over the last three fiscal years. The company currently meets the public company exception based on stockholders' equity as of December 31, 2000. However, in light of the company's losses during the nine months ended September 30, 2001, management's ability to achieve an appropriate level of stockholders' equity as of January 1, 2002 cannot be reasonably assured. The penalties for failure to comply with Stark II include, among other things, non-payment of claims and civil penalties that could be imposed upon the company and, in some instances, upon the referring physician. Some of such penalties can be imposed regardless of whether the company intended to violate the law. Accordingly, if the company's common stock remains publicly traded and its stockholders' equity falls below the required levels, the company would be forced to cease accepting referrals of patients covered by the Medicare or Medicaid programs or run a significant risk on noncompliance with Stark II. Ceasing to accept such referrals could materially adversely affect the company's financial condition and business reputation in the market as it may cause the company to be a less attractive provider to which a physician could refer his or her patients. The company previously requested a Stark II waiver from the Health Care Financing Administration, but such waiver request was denied.

In the absence of the confirmation and effectuation of the Debtors' Second Joint Plan on or before December 31, 2001, management is considering certain alternatives in order to remain compliant with the provisions of Stark II. However, there can be no assurances that the company will be able to successfully implement any of management's plans or that the Bankruptcy Court would approve any such plans put forth by management or the company. Failure to comply with Stark II would have a material adverse impact on the company's operations and financial condition.

38

Coram may find itself unable to procure the products necessary to serve its patients.

Due to the nature of factor manufacturing processes, intermittent product shortages may be experienced from time to time, which may make it difficult for Coram to meet the needs of its patients and may have an adverse impact on Coram's future results of operations. Furthermore, limited allocations of products from manufacturers, including, but not limited to, recombinant factor VIII (rVIII), greatly impact the company's ability to expand its customer base. These shortages could be due to insufficient donor pools, failed production lots, contamination, regulations and other factors beyond Coram's control. The ability to acquire factor products under normal conditions is volatile, but currently the international demand for certain factor products far exceeds the supply. Availability of factor product from manufacturers is spotty, thereby requiring the company to purchase through the blood broker market wherein pricing may not be favorable to the company and product availability can change significantly from day to day. During times of such shortages, prices can rise

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

significantly with limited ability on the part of the company to pass these additional costs on to patients.

Average Wholesale Price ("AWP") changes may trend in a direction that is adverse to net revenue and profitability.

For most of the drugs that Coram provides to its patients, it is reimbursed by governmental and third party payers according to rate schedules that are based on the AWP of the drugs as published by commercial pricing services. For example, the Medicare program generally pays 95 percent of the published AWP of a drug. AWP is an industry term that is typically understood to represent a suggested resale price for wholesale sales to pharmacies. The AWP does not necessarily reflect the price paid by either wholesalers or other end-user purchasers.

In the last several years, state and federal government enforcement agencies have conducted an ongoing investigation of manufacturers' practices with respect to AWP in which they have suggested that "inflated" AWPs have led to excessive government payments for prescription drugs and biologicals. At least one private class action suit has also been filed against manufacturers based on similar allegations. As a byproduct of these investigations, federal and state policymakers have begun to question the appropriateness of continuing to reimburse for drugs and biologicals under federal programs using AWP-based methodologies.

For example, the Medicare, Medicaid and SCHIP Benefits and Improvement and Protection Act of 2000 ("BIPA") required the General Accounting Office ("GAO") to study Medicare reimbursement for drugs and biologicals and for related services. The Secretary of Health and Human Services is required to revise the current Medicare payment methodologies for covered drugs and biologicals and related services based on the GAO's recommendations. Similarly, on November 14, 2001, members of the House Commerce Committee outlined a proposal to the Centers for Medicare & Medicaid Services administrator for a proposed new methodology under which payments for drugs and biologicals would be based on a new "average sales price" concept, which would be intended to more accurately reflect providers' actual acquisition cost for drugs and biologicals.

In addition, as part of the government investigation of AWP described above, the Department of Justice and states' attorneys general developed "revised" AWPs for a number of drugs and biologicals which are generally lower than those published by commercial services. The Medicare program proposed that these revised AWPs be used in determining reimbursement amounts, but this proposal was withdrawn in light of the BIPA provisions described above. According to a recent report by the Department of Health and Human Services Office of Inspector General, however, approximately 30 state Medicaid programs are using the revised AWPs to establish reimbursement amounts for some of the listed drugs and biologicals.

There can be no assurances that government or private healthcare programs will continue to reimburse for drugs and biologicals based on current AWP-based methodologies, or that future AWPs or revised AWPs will reflect acquisition prices available to purchasers such as the company. If government or private health insurance programs discontinue or modify the use of AWP or otherwise implement payment methods that reduce the reimbursement for drugs and biologicals, the product margins that the company receives may be reduced, and may, in many cases be inadequate to cover the cost of clinical services and overhead expenses associated with the delivery and administration of the drugs. This could produce a material adverse impact on the company's overall profit margins.

In particular, effective July 1, 2001, the margin between Coram's reimbursement rate and the cost of the acquired drug Vancomycin has decreased as

## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

a result of the reduction in the AWP reimbursement rate. To possibly mitigate the decrease of net revenue from the resulting decrease in AWP reimbursement, the company has made modifications to its drug purchasing formulary. While the company is implementing changes to reduce the adverse effect on net revenue and the direct impact to profitability, no assurances can be made that the company will be successful in implementing these changes. See Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations" for further discussion.

For a discussion of other risks that have impacted or may impact the company, readers are instructed to review the discussion under the heading "Risk Factors" which appears in Item 7. of the company's Annual Report on Securities and Exchange Commission Form 10-K for the year ended December 31, 2000.

39

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

The following discusses the company's exposure to market risk related to changes in interest rates. This discussion contains forward-looking statements that are subject to risks and uncertainties. Actual results could vary materially as a result of a number of factors, including but not limited to, changes in interest rates.

As of September 30, 2001, the company had outstanding long-term debt of \$154.5 million of which \$153.3 million matured on June 30, 2001 and bore interest at 9.0% per annum; however, the \$153.3 million was not paid on such date and the creditors' remedies are currently stayed pursuant to the Debtors' bankruptcy proceedings. The company also had a debtor-in-possession ("DIP") financing agreement providing for the availability of up to \$40.0 million for use in connection with the operation of its businesses and the businesses of its subsidiaries. The DIP financing agreement expired on August 31, 2001. No borrowings were provided thereunder during its term. Management is currently negotiating a renewal of the DIP financing agreement; however, no assurances can be given that the parties will ultimately agree to the terms and conditions of such renewal or that a renewal will be approved by the Bankruptcy Court. Because substantially all of the interest on the company's debt is fixed, a hypothetical 10.0% change in interest rates would not have a material impact on the company. Increases in interest rates could, however, increase interest expense associated with future borrowings by the company, if any. The company does not hedge against interest rate changes.

The debt to equity exchange transaction described in Note 7 to the company's Condensed Consolidated Financial Statements qualified as a troubled debt restructuring pursuant to Statement of Financial Accounting Standards No. 15, Accounting by Debtors and Creditors for Troubled Debt Restructurings. In accordance therewith and the provisions of SOP 90-7, the Debtors did not recognize any interest expense on the Series A Notes and the Series B Notes during the nine months ended September 30, 2001.

## PART II

### OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS

Descriptions of the material legal proceedings to which the company is a party are set forth in Note 10 to the company's Condensed Consolidated Financial Statements.



## Edgar Filing: CORAM HEALTHCARE CORP - Form 10-Q

The company is also a party to various other legal actions arising out of the normal course of its business. Management believes that the ultimate resolution of such other actions will not have a material adverse effect on the financial position, results of operations or liquidity of the company. Nevertheless, due to the uncertainties inherent in litigation, the ultimate disposition of these actions cannot presently be determined.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

A discussion of defaults and certain matters of non-compliance with certain covenants contained in the company's principal debt agreements is set forth in Note 7 to the company's Condensed Consolidated Financial Statements.

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

(A) Exhibits

None

(B) Reports on Form 8-K.

None

40

### SIGNATURES

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

CORAM HEALTHCARE CORPORATION

By: /s/ SCOTT R. DANITZ

-----  
Scott R. Danitz  
Senior Vice President, Chief Financial Officer  
and Treasurer

November 19, 2001

41