

AMSURG

2002 Annual Report

Expanding the Base for Continued Profitable Growth



20
02

AMERICA'S SINGLE SPECIALTY SURGERY CENTER LEADER

LOCATIONS AT DECEMBER 31, 2002

ALABAMA

Dothan
Montgomery

ARIZONA

Mesa
Peoria
Phoenix
Sun City

ARKANSAS

Fayetteville
Rogers

CALIFORNIA

Burbank
Glendale
Inglewood
La Jolla
Sebastopol
Tarzana
Torrance
Westlake

COLORADO

Denver

CONNECTICUT

Bloomfield

DELAWARE

Dover
Lewes
Newark

FLORIDA

Boca Raton
Cape Coral
Coral Gables
Crystal River
Ft. Lauderdale
Ft. Myers (3)
Hialeah
Inverness
Melbourne (3)
Miami
Mount Dora
Naples
Ocala
Panama City
Sarasota (2)
Tamarac
Winter Haven
Zephyrhills

INDIANA

Evansville
Indianapolis

KANSAS

Hutchinson
Shawnee
Topeka
Wichita

KENTUCKY

Crestview Hills
Louisville (2)
Paducah

LOUISIANA

Alexandria
New Orleans
West Monroe

MARYLAND

Baltimore
Bel Air
Chevy Chase
Waldorf

MINNESOTA

Minneapolis (3)

MISSOURI

Independence
Kansas City

NEVADA

Las Vegas (2)

NEW JERSEY

Egg Harbor
Florham Park
Lawrenceville
Oakhurst

NEW MEXICO

Santa Fe

NORTH CAROLINA

Greensboro

OHIO

Akron
Cincinnati
Cleveland
Lorain
Middletown
Sidney
Toledo
Willoughby

OKLAHOMA

Oklahoma City
Tulsa

PENNSYLVANIA

Hillmont
Kingston
Seneca

SOUTH CAROLINA

Clemson
Columbia

TENNESSEE

Chattanooga
Columbia (2)
Jackson
Knoxville (2)
Maryville
Nashville (2)

TEXAS

Abilene (2)
Beaumont
El Paso
Harlingen
Weslaco

UTAH

Salt Lake City

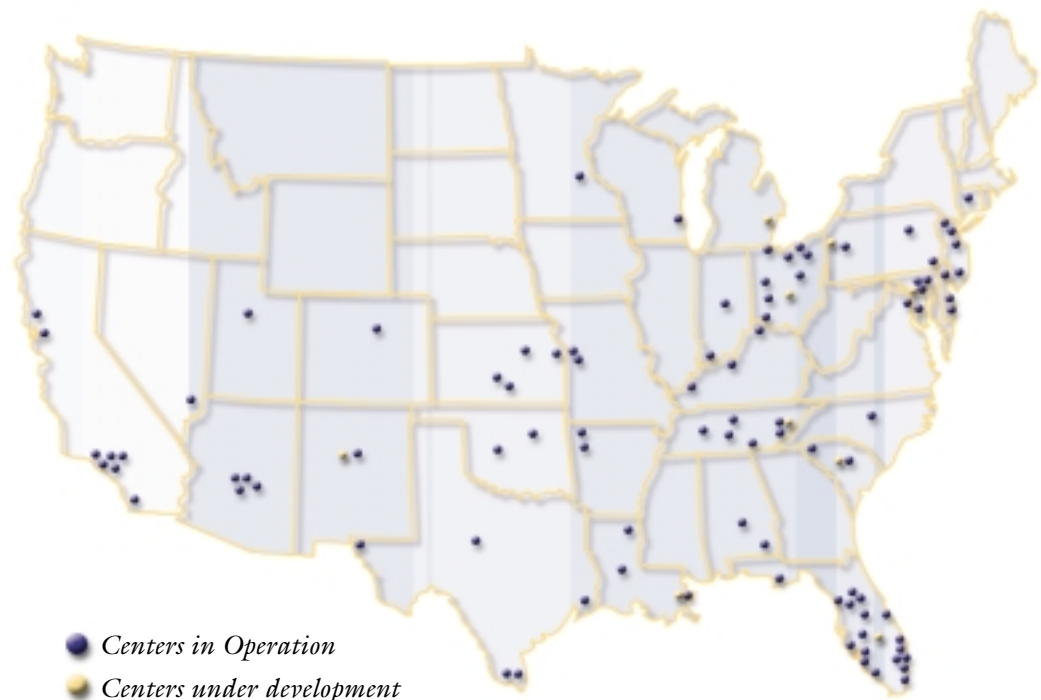
Washington, D.C.

WISCONSIN

Milwaukee

These are the centers under development at December 31, 2002:

Sebring, FL
New Orleans, LA
Columbia, MD
Southfield, MI
Los Alamos, NM
Columbus, OH
Johnstown, PA
Columbia, SC
Knoxville, TN



COMPANY PROFILE

AmSurg Corp. develops, acquires and operates practice-based ambulatory surgery centers in partnership with surgical and other group physician practices. Headquartered in Nashville, Tennessee, AmSurg operated 107 ambulatory surgery centers at December 31, 2002. By focusing on the delivery of low cost, high quality, high patient satisfaction surgery services, AmSurg Corp. creates value for the three constituencies involved in every surgical procedure: the patient, the physician and the payer.

FINANCIAL HIGHLIGHTS

	For the Years Ended December 31,	
	2002	2001
	<i>(In thousands, except per share and center data)</i>	
Operating Results:		
Revenues	\$ 251,525	\$ 202,312
Net earnings	24,022	14,905
Earnings per share (diluted)	\$ 1.16	\$ 0.78
Weighted average common shares outstanding (diluted)	20,728	19,021
Financial Position at Year End:		
Cash and cash equivalents	\$ 13,320	\$ 11,074
Working capital	37,414	34,909
Total assets	299,814	241,383
Long-term debt	27,884	12,685
Minority interest	29,869	25,047
Shareholders' equity	216,364	185,569
Center Data:		
Centers at end of year	107	95
Procedures performed during year	471,155	389,431

LETTER TO SHAREHOLDERS



Ken P. McDonald
President and
Chief Executive Officer

Claire M. Gulmi
Senior Vice President,
Chief Financial Officer and Secretary

Last year, this letter celebrated AmSurg's first decade in business, a 10-year period of consistent and substantial revenue growth and outstanding profitability. This year, after extending our record performance to an eleventh consecutive year, this letter focuses on the future. The theme of this report, "Expanding the Base for Continued Profitable Growth", sums up how we approach our jobs each day. Despite all that we have achieved over the past 11 years, we are fully confident that AmSurg's greatest opportunities for profitable growth lie ahead.

Before analyzing the basis for this confidence, let us put the discussion in context by reviewing our operating and financial performance for 2002. AmSurg produced record financial results for 2002 with revenues of \$251.5 million, up 24% from 2001. Net earnings per diluted share grew 49% to \$1.16 for 2002 from \$0.78 for 2001, which includes a positive impact of \$0.16 for 2002 from the adoption of Statement of Financial Accounting Standards ("SFAS") No. 142, "*Goodwill and Other Intangible Assets*." This performance exceeded our goals for 2002, which we stated in last year's letter as revenues of \$237 million to \$243 million and net earnings per diluted share, after the adoption of SFAS No. 142, of \$1.12 to \$1.14. In achieving these results, we generated same-center revenue growth for 2002 of 13%, adding a fifth year to our record of consecutive annual double-digit

increases in same-center revenues since we became public in December 1997.

In addition to same-center revenue growth, our results primarily reflected the steady expansion of our base of centers in operation. As anticipated, we added 12 new centers during 2002, crossing the 100th-center milestone and ending the year with 107 centers in operation, up 13% from 95 centers at the end of 2001. Consistent with our continuous efforts to prepare for future profitable growth, we also completed 2002 with one of the strongest development pipelines we have enjoyed. At year end, we had a total of 17 centers in the pipeline. Nine of these centers were de novo centers under construction. Six of these centers were under letter of intent and were split evenly between de novo centers and acquisitions. Two of these centers were de novo centers awaiting approval of a certificate of need, both of which were received in the first quarter of 2003.

As a result of this pipeline, we believe AmSurg is well positioned to meet its development goal for 2003 of adding 12 to 15 new centers through either de novo development or acquisition. In addition, we expect to achieve another year of significant same-center revenue expansion with a goal for 2003 of 9% to 11%. Primarily because of this combination of new development and

Celebrating over

100

CENTERS



CENTERS GRAPH
AT YEAR END



AmSurg expects to open 12 to 15 new surgery centers during 2003 that are either de novo centers or acquisitions.

Expanding the Base for Continued

Profitable

GROWTH



same-center revenue growth, our guidance as of the end of the first quarter of 2003 is for revenues for the full year in a range of \$300 million to \$310 million, representing growth of 20% to 24% over 2002. We also expect earnings per diluted share to increase 22% to 25% for 2003 over 2002 to a range of \$1.41 to \$1.45.

Key Factors Supporting AmSurg's Ability to Drive Continued Profitable Growth

Leadership position in a large and growing industry – AmSurg is the unchallenged leader in the single-specialty surgery center industry. The overall ambulatory surgery center industry continues to grow as medical and technological advances enable more procedures to be performed on an outpatient basis and as strong demographic trends drive utilization. Approximately 72% of surgical procedures today are performed on an outpatient basis and are expected to increase to more than 80% in the coming years. Concurrently, the aging of the baby boom generation is driving significant growth in the types of procedures performed in AmSurg's gastroenterology centers and ophthalmology centers.

As we have grown into the leading single-specialty surgery center company, we have created a critical mass of operations that sustains this leadership position. Through this critical mass we have achieved substantial economies of scale and skill, while developing a proven record and a well-known brand name among potential physician partners as a successful operator of single-specialty centers. Recognizing the consistent performance reflected by the opening of our 100th center in our 11th year of operations, we believe AmSurg is positioned to continue its clear leadership position for the foreseeable future.

Proven business model – Although we continuously analyze and refine the Company's business model, we believe five consecutive years of double-digit same-center revenue growth demonstrates its core strengths.

This record reflects AmSurg's ability to serve the needs of the three parties to every healthcare procedure – the patient, the physician and the payer – by consistently providing high quality, low cost services that generate high patient satisfaction.

Our business model contributes to this “win, win, win” formula through the physical design of our centers, which promotes physician convenience, minimizes patient anxiety and, through its single-specialty focus, reduces costs. Because our single-specialty centers are designed and equipped to perform a high volume of a limited variety of procedures, our surgical teams develop outstanding procedure experience, accounting for our consistently outstanding quality. In addition, this high volume, combined with low variable costs per incremental procedure, contributes substantially to our strong center economic profile.

We also attribute the business model's success to the strong physician practices with which we partner. Through their significant ownership interest in the surgery centers, our premiere physician partners are substantially invested in the success of the center and motivated to work with us to implement a customized strategic plan for each center, the goal of which is the delivery of high quality surgical services to achieve local market share dominance.

Sustainable growth strategy – As the leading operator of single-specialty surgery centers, AmSurg has a unique opportunity to pursue consistent, long-term profitable growth in a growing yet highly fragmented market. Despite the strength of our market position, however, superior performance in each and every center is critical to our continued success. Therefore, we continue to believe that a moderate, controlled growth strategy is the best way in which we can expand our market presence without losing focus on the quality of our existing operations.

We expect to have significant opportunities to expand our base of centers in operation through de novo center development and acquisition for the foreseeable future. In our current 28-state market, which generally includes states with little or no certificate of need regulations, we estimate there are approximately 3,000 de novo and acquisition opportunities. Our 17-center development pipeline at the end of 2002 provides us a strong foundation on which to build toward our new center goals for 2003 and 2004. We remain confident of our prospects for significant, sustained growth thereafter.

Strong financial position – AmSurg has continued to maintain its strong financial position, even after a relatively active pace of acquisitions in 2002. With capital expenditures for acquired, de novo and existing centers for 2002 of \$63.5 million, we ended the year with cash and cash equivalents totaling \$13.3 million, long-term debt of \$27.9 million and shareholders' equity of \$216.4 million. The Company has substantial financial capacity, with access to a \$100 million, five-year credit facility and strong cash flow from operations, which was \$46.9 million for 2002.

Summary

Our Board of Directors recently displayed its confidence in AmSurg's ability to expand its base for continuing profitable growth through the declaration of a \$25 million stock repurchase program. As we have described in this letter, our confidence is based not only on AmSurg's historical success, but also, looking to the future, on its leadership in an industry with compelling growth dynamics, on its proven business model and growth strategies and on its strong financial position. More fundamentally, AmSurg has demonstrated its consistent ability to achieve profitable growth while delivering both high quality care and high patient satisfaction at a lower cost. We believe demand for this capability will only increase.

We have always been committed to managing AmSurg to the exacting standards that every one of our physician partners applies in every surgical procedure. With the recent focus on corporate accountability, we have formalized this commitment by adopting our Corporate Governance Guidelines, which embody many of our longstanding practices and incorporate new policies and procedures that strengthen our commitment to best practices. We aspire to the highest standards of ethical conduct: doing what we say, reporting results with accuracy and transparency, and maintaining full compliance with the laws, rules and regulations that govern our business. These principles are embodied in our Code of Conduct and Compliance Program governing all employees and affiliates of AmSurg.

We wish to recognize the people most responsible for AmSurg's success, our employees throughout the country and our physician partners. We also thank our Board for its vote of confidence in AmSurg and for its many continuing contributions to the Company's success. Finally, we thank you, our fellow shareholders, for your past and future support of the Company. We remain dedicated to leveraging the Company's opportunities and resources to achieve its operating and financial goals and to increase its shareholder value.

Sincerely,

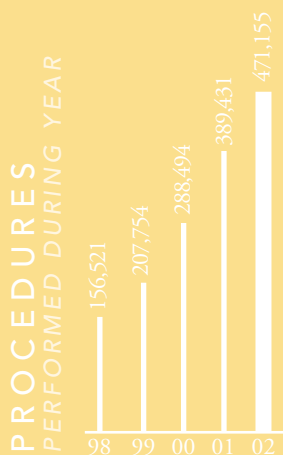


Ken P. McDonald
President and Chief Executive Officer

Performing over

470,000

PROCEDURES



Procedure growth accounts for virtually all of AmSurg's five consecutive years of double-digit annual growth in same-center revenues.

SELECTED FINANCIAL DATA

	Years Ended December 31,				
	2002	2001	2000	1999	1998
	<i>(Dollars in thousands, except per share data)</i>				
Consolidated Statement of Operations Data:					
Revenues	\$ 251,525	\$ 202,312	\$ 143,261	\$ 101,446	\$ 80,322
Operating expenses	159,202	135,023	96,114	69,428	63,370 ⁽¹⁾
Operating income	92,323	67,289	47,147	32,018	16,952
Minority interest	51,096	39,599	27,702	19,431	13,645
Interest and other expenses	1,190	2,844	4,703	1,122	1,499
Earnings before income taxes and cumulative effect of an accounting change	40,037	24,846	14,742	11,465	1,808
Income tax expense	16,015	9,941	5,676	4,414	1,047
Net earnings before cumulative effect of an accounting change	24,022	14,905	9,066	7,051	761
Cumulative effect of a change in the method in which pre-opening costs are recorded	—	—	—	(126)	—
Net earnings	\$ 24,022	\$ 14,905	\$ 9,066	\$ 6,925	\$ 761
Basic earnings per common share:					
Net earnings before cumulative effect of an accounting change	\$ 1.18	\$ 0.81	\$ 0.62	\$ 0.49	\$ 0.06
Net earnings	\$ 1.18	\$ 0.81	\$ 0.62	\$ 0.48	\$ 0.06
Diluted earnings per common share:					
Net earnings before cumulative effect of an accounting change	\$ 1.16	\$ 0.78	\$ 0.60	\$ 0.48	\$ 0.06
Net earnings	\$ 1.16	\$ 0.78	\$ 0.60	\$ 0.47	\$ 0.06
Weighted average number of shares and share equivalents outstanding:					
Basic	20,390	18,428	14,594	14,429	12,247
Diluted	20,728	19,021	15,034	14,778	12,834
Operating and Other Financial Data:					
Centers at end of year	107	95	81	63	52
Procedures performed during year	471,155	389,431	288,494	207,754	156,521
Same-center revenue increase	13%	10%	10%	10%	12%
Cash flows from operating activities	\$ 46,919	\$ 37,301	\$ 18,493	\$ 16,768	\$ 11,339
Cash flows from investing activities	(43,832)	(64,685)	(44,004)	(32,567)	(24,528)
Cash flows from financing activities	(841)	30,770	23,676	19,252	15,852
	At December 31,				
	2002	2001	2000	1999	1998
	<i>(In thousands)</i>				
Consolidated Balance Sheet Data:					
Cash and cash equivalents	\$ 13,320	\$ 11,074	\$ 7,688	\$ 9,523	\$ 6,070
Working capital	37,414	34,909	26,589	21,029	12,954
Total assets	299,814	241,383	190,652	137,868	98,421
Long-term debt and other long-term obligations	27,884	12,685	71,832	34,901	12,483
Minority interest	29,869	25,047	21,063	17,358	11,794
Shareholders' equity	216,364	185,569	83,145	72,708	64,369

⁽¹⁾ Includes a loss attributable to the sale of two partnership interests in two physician practices of approximately \$5.4 million, for the year ended December 31, 1998. We held no ownership in physician practices beyond 1998.

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

Forward-Looking Statements

This report contains certain forward-looking statements (all statements other than with respect to historical fact) within the meaning of the federal securities laws, which are intended to be covered by the safe harbors created thereby. Investors are cautioned that all forward-looking statements involve known and unknown risks and uncertainties including, without limitation, those described below, some of which are beyond our control. Although we believe that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate. Therefore there can be no assurance that the forward-looking statements included in this report will prove to be accurate. Actual results could differ materially and adversely from those contemplated by any forward-looking statement. In light of the significant risks and uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved. We undertake no obligation to publicly release any revisions to any forward-looking statements in this discussion to reflect events and circumstances occurring after the date hereof or to reflect unanticipated events.

Forward-looking statements and our liquidity, financial condition and results of operations may be affected by the following, as well as other unknown risks and uncertainties:

- our ability to enter into partnership or operating agreements for new practice-based ambulatory surgery centers;
- our ability to identify suitable acquisition candidates and negotiate and close acquisition transactions, including centers under letter of intent;
- our ability to obtain the necessary financing or capital on terms satisfactory to us in order to execute our expansion strategy;
- our ability to generate and manage growth;
- our ability to contract with managed care payors on terms satisfactory to us for our existing centers and our centers that are currently under development;
- our ability to obtain and retain appropriate licensing approvals for our existing centers and centers currently under development;
- our ability to minimize start-up losses of our development centers;
- our ability to maintain favorable relations with our physician partners;
- updates by the Department of Health and Human Services, or DHHS, to the ratesetting methodology, payment rates, payment policies and the list of covered surgical procedures for ambulatory surgery centers;
- risks associated with our status as a general partner of the limited partnerships;
- our ability to maintain our technological capabilities in compliance with regulatory requirements;
- risks associated with the valuation and tax deductibility of goodwill, as well as potential losses on disposal of goodwill associated with a disposition of an individual center;
- risks of legislation or regulatory changes that would prohibit physician ownership in ambulatory surgery centers; and
- our ability to obtain the necessary financing to fund the purchase of our physician partners' minority interest in the event of a regulatory change that would require such a purchase.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS — CONTINUED

Overview

We develop, acquire and operate practice-based ambulatory surgery centers in partnership with physician practice groups. As of December 31, 2002, we owned a majority interest (51% or greater) in 107 surgery centers.

The following table presents the changes in the number of surgery centers in operation, under development and under letter of intent for the years ended December 31, 2002, 2001 and 2000. A center is deemed to be under development when a partnership or limited liability company has been formed with the physician group partner to develop the center.

	2002	2001	2000
Centers in operation, beginning of the year	95	81	63
New center acquisitions placed in operation	10	15	9
New development centers placed in operation	2	1	9
Centers disposed ⁽¹⁾	—	(2)	—
Centers in operation, end of the year	107	95	81
Centers under development, end of the year	9	5	4
Development centers awaiting CON approval, end of year	2	1	1
Average number of centers in operation, during year	98	89	69
Centers under letter of intent, end of year	6	1	5

⁽¹⁾ We sold our interests in two surgery centers in 2001 for their approximate book value.

Of the surgery centers in operation as of December 31, 2002, 61 centers perform gastrointestinal endoscopy procedures, 38 centers perform ophthalmology surgery procedures, three centers perform orthopedic procedures and five centers perform procedures in more than one specialty. The other partner or member in each partnership or limited liability company is generally an entity owned by physicians who perform procedures at the center. We intend to expand primarily through the development and acquisition of additional practice-based ambulatory surgery centers in targeted surgical specialties and through future same-center growth. Our growth targets for 2003 include the acquisition or development of 12 to 15 additional surgery centers and the achievement of same-center revenue growth of 9% to 11%.

While we generally own 51% of the entities that own the surgery centers, and up to 67% in certain instances, our consolidated statements of operations include 100% of the results of operations of the entities, reduced by the minority partners' share of the net earnings or loss of the surgery center entities.

Sources of Revenues

Substantially all of our revenue is derived from facility fees charged for surgical procedures performed in our surgery centers. This fee varies depending on the procedure, but usually includes all charges for operating room usage, special equipment usage, supplies, recovery room usage, nursing staff and medications. Facility fees do not include the charges of the patient's surgeon, anesthesiologist or other attending physicians, which are billed directly by the physicians. Our revenues are recorded net of estimated contractual allowances from third-party medical service payors.

Practice-based ambulatory surgery centers, such as those in which we own a majority interest, depend upon third-party reimbursement programs, including governmental and private insurance programs, to pay for services rendered to patients. The amount of payment a surgery center receives for its services may be adversely affected by market and cost factors, as well as other factors over which we have no control, including Medicare and Medicaid regulations and the cost containment and utilization decisions of third-party payors. We derived approximately 40%, 38% and 37% of our revenues in the years ended December 31, 2002, 2001 and 2000, respectively, from governmental healthcare programs, primarily Medicare. The Medicare program currently pays ambulatory surgery centers in accordance with predetermined fee schedules.

Critical Accounting Policies

Our accounting policies are described in note 1 of the consolidated financial statements. We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States, which require us to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. We consider the following policies to be

most critical in understanding the judgments that are involved in preparing our financial statements and the uncertainties that could impact our results of operations, financial condition and cash flows.

Principles of Consolidation. The consolidated financial statements include the accounts of AmSurg and our subsidiaries and the majority owned limited partnerships and limited liability companies in which we are the general partner or majority member. Consolidation of such partnerships and limited liability companies is necessary, as we have 51% or more of the financial interest, are the general partner or majority member with all the duties, rights and responsibilities thereof and are responsible for the day-to-day management of the partnership or limited liability company. The limited partner or minority member responsibilities are to supervise the delivery of medical services, with their rights being restricted to those that protect their financial interests, such as approval of the acquisition of significant assets or the incurrence of debt which they, as physician limited partners or members, are required to guarantee on a pro rata basis based upon their respective ownership interests. Intercompany profits, transactions and balances have been eliminated.

We operate in one reportable business segment, the ownership and operation of ambulatory surgery centers.

Revenue Recognition. Center revenues consist of billing for the use of the centers' facilities, or facility fees, directly to the patient or third-party payor, and in limited instances, billing for anesthesia services. Such revenues are recognized when the related surgical procedures are performed. Revenues exclude any amounts billed for physicians' surgical services, which are billed separately by the physicians to the patient or third-party payor.

Allowance for Contractual Adjustments and Bad Debt Expense. Our revenues are recorded net of estimated contractual allowances from third-party medical service payors, which we estimate based on historical trends of the surgery centers' cash collections and contractual and bad debt write-offs, accounts receivable agings, established fee schedules, relationships with payors and procedure statistics. In addition, we must estimate allowances for bad debt expense using similar information and analysis. While we believe that our allowances for contractual adjustments and bad debt expense are adequate, if the actual write-offs are in excess of our estimates, our results of operations may be overstated. At December 31, 2002 and 2001, net accounts receivable reflected allowances for contractual adjustments of \$25.5 million and \$25.1 million, respectively, and allowances for bad debt expense of \$4.0 million and \$3.5 million, respectively.

Goodwill. In July 2001, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standards, or SFAS, No. 141, "*Business Combinations*," and SFAS No. 142, "*Goodwill and Other Intangible Assets*." The provisions of SFAS No. 141 require all business combinations to be accounted for by the purchase method. SFAS No. 142 requires that, upon adoption, amortization of goodwill and indefinite life intangible assets will cease and instead, the carrying value of goodwill and indefinite life intangible assets will be evaluated for impairment at least on an annual basis; impairment of carrying value will be evaluated more frequently if certain indicators are encountered. Identifiable intangible assets with a determinable useful life will continue to be amortized over that period and reviewed for impairment in accordance with SFAS No. 144 (discussed in "– Recent Accounting Pronouncements" below). SFAS No. 142 is effective for fiscal years beginning after December 15, 2001, except for goodwill and intangible assets acquired after June 30, 2001, which were subject immediately to the nonamortization provisions of this statement.

We fully adopted SFAS No. 142 on January 1, 2002, and accordingly, ceased to amortize goodwill, which previously had been amortized over 25 years. SFAS No. 142 requires that goodwill be tested at the reporting unit level, defined as an operating segment or one level below an operating segment (referred to as a component), with the fair value of the reporting unit being compared to its carrying amount, including goodwill. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is not considered to be impaired. We have determined that we have one operating as well as one reportable segment. Our centers each qualify as components of that operating segment and have similar economic characteristics, and therefore, should be aggregated and deemed a single reporting unit. We completed the transitional goodwill impairment test and have determined that no potential impairment exists. As a result, we have recognized no transitional impairment loss in fiscal year 2002 in connection with the adoption of SFAS No. 142.

Purchase Price Allocation. We allocate the respective purchase price of our acquisitions in accordance with SFAS No. 141. The allocation of purchase price involves first, determining the fair value of net tangible and identifiable intangible assets acquired. Secondly, the excess amount of purchase price is to be allocated to unidentifiable intangible assets (goodwill). A significant portion of each surgery center's purchase price has historically been allocated to goodwill due to the nature of the businesses acquired, the pricing and structure of our acquisitions and the absence of other factors indicating any significant value which could be attributable to separately identifiable intangible assets. Our resulting goodwill, in accordance with SFAS No. 142 as described above, is no longer amortized, but will be tested for impairment at least annually.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS — CONTINUED

Results of Operations

Our revenues are directly related to the number of procedures our surgery centers perform. Our overall growth in procedure volume is directly impacted by the increase in the number of surgery centers in operation and the growth in procedure volume at existing centers. Procedure growth at any existing center may result from additional contracts entered into with third-party payors, increased market share of the associated medical practice of our physician partners, new physician partners and/or scheduling and operating efficiencies gained at the surgery center.

Expenses directly related to such procedures include clinical and administrative salaries and benefits, supply cost and other variable expenses such as linen cost, repair and maintenance of equipment, billing fees and bad debt expense. The majority of our corporate salary and benefits cost is directly associated with the number of centers we own and manage and tends to grow in proportion to the growth of our centers in operation. Our centers and corporate offices also incur costs which are more fixed in nature, such as lease expense, legal fees, property taxes, utilities and depreciation and amortization.

Surgery center profits are allocated to our minority partners in proportion to their individual ownership percentages and reflected in the aggregate as minority interest. Our interest expense results primarily from our borrowings used to fund acquisition and development activity, as well as interest incurred on capital leases.

We file a consolidated federal income tax return and numerous state income tax returns with varying tax rates. Our income tax expense reflects the blending of these rates.

The following table shows certain statement of earnings items expressed as a percentage of revenues for the years ended December 31, 2002, 2001 and 2000:

	2002	2001	2000
Revenues	100.0%	100.0%	100.0%
Operating expenses:			
Salaries and benefits	26.4	26.8	27.8
Supply cost	11.9	11.8	11.6
Other operating expenses	21.0	21.0	20.5
Depreciation and amortization	4.0	7.1	7.2
Total operating expenses	63.3	66.7	67.1
Operating income	36.7	33.3	32.9
Minority interest	20.3	19.6	19.3
Interest expense, net of interest income	0.5	1.4	3.3
Earnings before income taxes	15.9	12.3	10.3
Income tax expense	6.3	4.9	4.0
Net earnings	9.6%	7.4%	6.3%

Year Ended December 31, 2002 Compared to Year Ended December 31, 2001

Revenues increased \$49.2 million, or 24%, to \$251.5 million in 2002 from \$202.3 million in 2001, primarily due to the following two factors:

- 12 additional surgery centers in operation at year end, primarily resulting from acquisitions, with an average number of centers in operation throughout the year of 98 in 2002 compared to 89 in 2001; and
- Same-center procedure growth resulting in 13% revenue growth (79 centers included in the same-center group).

The additional surgery centers in operation and same-center procedure growth resulted in a 21% increase in procedure volume in 2002 over 2001. In order to appropriately staff our surgery centers for these additional procedures, as well as provide appropriate corporate management for the additional centers in operation, salaries and benefits increased proportionately by 22% to \$66.3 million in 2002 from \$54.2 million in 2001.

Supply cost was \$30.1 million in 2002, an increase of \$6.2 million, or 26%, over supply cost in 2001. This increase resulted primarily from additional procedure volume.

Other operating expenses increased \$10.2 million to \$52.8 million, or 24%, in 2002 from 2001, primarily as a result of the additional surgery centers in operation and additional corporate overhead.

Depreciation and amortization expense decreased \$4.4 million, or 31%, in 2002 from 2001, primarily due to the non-amortization of goodwill starting in 2002 as a result of our adoption of SFAS No. 142 (see note 1(f) to the consolidated financial statements and “– Critical Accounting Policies – *Goodwill*”).

We anticipate further increases in operating expenses in 2003, primarily due to additional start-up centers and acquired centers expected to be placed in operation, as well as insurance cost and scheduled property rent increases at our existing centers. Typically, a start-up center will incur start-up losses while under development and during its initial months of operations and will experience lower revenues and operating margins than an established center until its case load grows to a more optimal operating level, which generally is expected to occur within the 12 months after a center opens. At December 31, 2002, we had nine centers under development and two centers that had been open for less than one year.

Operating income margin increased by 3.4%, which is primarily the result of the elimination of goodwill as described above, as well as the leverage we achieve from having a high but consistent fixed cost component from year to year at each center. Because each incremental procedure generates only a variable cost component, same-center procedure growth generally contributes to operating income at a rate higher than the average operating income margin of the center.

Minority interest in earnings in 2002 increased \$11.5 million, or 29%, from 2001, primarily as a result of minority partners' interest in earnings at surgery centers recently added to operations and from increased same-center profitability. As a percentage of revenues, minority interest increased due to the fact that our minority partners participate in the increased profitability of our centers. Additionally, all of the acquired and developed centers in 2002 have a 49% minority ownership, which diluted the impact on minority interest of those existing centers that have less than 49% minority ownership.

Interest expense decreased \$1.7 million in 2002, or 58%, from 2001. Prior to April 2001, our debt level had grown to approximately \$92.5 million, primarily due to acquisition-related borrowings. However, net proceeds from our public offering, as further discussed in “– Liquidity and Capital Resources,” were used to repay a significant portion of our outstanding debt. Additionally, we experienced lower interest rates in 2002 than in 2001.

We recognized income tax expense of \$16.0 million in 2002 compared to \$9.9 million in 2001. Our effective tax rate in 2002 and 2001 was 40.0% of net earnings before income taxes and differed from the federal statutory income tax rate of 35%, primarily due to the impact of state income taxes. Because we continue to deduct goodwill amortization for tax purposes, a larger portion of our overall income tax expense is considered deferred income taxes, which result in a continuing increase in our deferred tax liability.

Year Ended December 31, 2001 Compared to Year Ended December 31, 2000

Revenues increased \$59.1 million, or 41%, to \$202.3 million in 2001 from \$143.3 million in 2000, primarily due to the following three factors:

- 14 additional surgery centers in operation at year end, primarily resulting from acquisitions, with an average number of centers in operation throughout the year of 89 in 2001 compared to 69 in 2000;
- Same-center procedure growth resulting in 10% revenue growth (61 centers included in the same-center group); and
- A larger percentage of ophthalmology procedures performed, which have a larger average reimbursement rate per procedure than our average rate experienced in 2000.

The additional surgery centers in operation and same-center procedure growth resulted in a 35% increase in procedure volume in 2001 over 2000. In order to appropriately staff our surgery centers for these additional procedures, as well as provide appropriate corporate management for the additional centers in operation, salaries and benefits increased proportionately by 36% to \$54.2 million in 2001 from \$39.8 million in 2000.

Supply cost was \$23.8 million in 2001, an increase of \$7.2 million, or 44%, over supply cost in 2000. This increase resulted primarily from the additional procedure volume and an increased mix of ophthalmology procedures, which require more costly supplies than gastroenterology procedures, our predominant procedure type.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS — CONTINUED

Other operating expenses increased \$13.1 million to \$42.6 million, or 45%, in 2001 from 2000, primarily as a result of the additional surgery centers in operation and additional corporate overhead.

Depreciation and amortization expense increased \$4.1 million, or 40%, in 2001 from 2000, primarily due to the additional surgery centers in operation as well as a full year of amortization of additional goodwill from acquisitions completed throughout 2000 and the amortization of goodwill acquired from January 1, 2001 to June 30, 2001. In accordance with SFAS No. 142, we did not amortize goodwill for eight acquisitions completed after June 30, 2001 (see “- Critical Accounting Policies - *Goodwill*” and note 1(f) to the consolidated financial statements). This change had no material impact on our consolidated financial statements, however.

Operating income margin increased by 0.4%, which reflects the leverage we achieve from having a high but consistent fixed cost component from year to year at each center. Because each incremental procedure generates only a variable cost component, procedure growth generally contributes to operating income at a rate higher than the average operating income margin of the center.

Minority interest in earnings in 2001 increased \$11.9 million, or 43%, from 2000, primarily as a result of minority partners' interest in earnings at surgery centers recently added to operations and from increased same-center profitability. As a percentage of revenues, minority interest increased due to the fact that our minority partners participate in the increased profitability of our centers. Additionally, nearly all of the acquired and developed centers in 2001 have a 49% minority ownership, which diluted the impact on minority interest of those existing centers that have less than 49% minority ownership.

Interest expense decreased \$1.9 million in 2001, or 40%, from 2000. Prior to April 2001, our debt level had grown to approximately \$92.5 million, primarily due to acquisition-related borrowings. However, net proceeds from our public offering, as further discussed in “- Liquidity and Capital Resources,” were used to repay a significant portion of our outstanding debt. Additionally, we experienced lower interest rates in 2001 than in 2000.

We recognized income tax expense of \$9.9 million in 2001 compared to \$5.7 million in 2000. Our effective tax rate in 2001 and 2000 was 40.0% and 38.5%, respectively, of net earnings before income taxes and differed from the federal statutory income tax rate of 35% and 34%, respectively, primarily due to the impact of state income taxes.

Liquidity and Capital Resources

At December 31, 2002, we had working capital of \$37.4 million compared to \$34.9 million at December 31, 2001. Operating activities for 2002 generated \$46.9 million in cash flow from operations compared to \$37.3 million in 2001. The increase in operating cash flow activity resulted primarily from an additional \$9.1 million in net earnings, resulting primarily from additional centers in operation and growth in same-center revenue. Cash and cash equivalents at December 31, 2002 and 2001 were \$13.3 million and \$11.1 million, respectively.

During 2002, we used approximately \$29.4 million to acquire interests in practice-based ambulatory surgery centers, including \$8.4 million for the payment of contingent purchase obligations, primarily as a result of the discontinuance of a proposed rulemaking action by DHHS described below. In addition, we issued notes payable of \$19.6 million for the acquisition of interests in practice-based ambulatory surgery centers, which were paid in January 2003 with cash provided from additional borrowings under our revolving credit facility. We made capital expenditures primarily for new start-up surgery centers and for new or replacement property at existing centers totaling approximately \$14.5 million in 2002, which included the purchase of the land and building of a surgery center previously leased. Included in this amount were maintenance capital expenditures of \$8.5 million. In addition, we entered into capital lease arrangements for replacement equipment of \$107,000. We used our cash flow from operations to fund our acquisition cash obligations and development activity, and we received approximately \$1.5 million from capital contributions of our minority partners to fund their proportionate share of development activity. At December 31, 2002, we and our partnerships and limited liability companies had unfunded construction and equipment purchase commitments for centers under development or under renovation of approximately \$1.9 million, which we intend to fund through additional borrowings of long-term debt, operating cash flow and capital contributions by minority partners.

During 2002, we were able to make net payments on long-term debt of \$5.6 million, including \$2.6 million on our revolving credit facility. At December 31, 2002, we had \$4.7 million outstanding under our revolving credit facility, as most recently amended on March 4, 2003, which permits us to borrow up to \$100.0 million to finance our acquisition and development projects at a rate equal to, at our option, the prime rate or LIBOR plus a spread of

1.5% to 2.25%, depending upon borrowing levels. The loan agreement also provides for a fee of 0.50% of unused commitments. The loan agreement prohibits the payment of dividends and contains covenants relating to the ratio of debt to net worth, operating performance and minimum net worth. We were in compliance with all covenants at December 31, 2002. Borrowings under the credit facility are due in March 2008 and are secured primarily by a pledge of the stock of our subsidiaries and our membership interests in the limited liability companies.

In 2002, we received approximately \$3.3 million from the exercise of options and issuance of common stock under our employee stock option plans. Tax benefits received from the exercise of those options was \$3.5 million.

In April 2001, we completed a public offering of 4,600,000 shares of Class A Common Stock, including 74,000 shares offered by selling shareholders, for net proceeds to us of approximately \$76.6 million. The net proceeds were used to repay borrowings under our revolving credit facility.

In July 2001, after receiving shareholder approval, we reclassified our Class A and Class B Common Stock into one class of common stock, having the rights of the Class A Common Stock. The Class A and Class B shares were reclassified into one class of common stock using a one-to-one conversion ratio, and, as a result, there was no increase in the total number of shares or book value of common stock outstanding.

In February 2003, we announced that our Board of Directors authorized a stock repurchase program for up to \$25.0 million of our outstanding shares of common stock over the subsequent 18 months, which we intend to fund through borrowings under our credit facility.

In May 2002, DHHS listed as a “discontinued action” the June 12, 1998 proposed rule that would update the rate setting methodology, payment rates, payment policies and the list of covered surgical procedures for ambulatory surgery centers. If implemented, the proposed rule would have reduced the rates paid for certain ambulatory surgery center procedures reimbursed by Medicare, including a number of endoscopy and ophthalmology procedures performed at our centers. Although this action has been discontinued, DHHS may propose a new rule at any time that could adversely impact surgery center reimbursement. Upon the announcement of the discontinuance of this proposed rule, we paid the remaining purchase price commitments of approximately \$7.7 million that were contingent on certain outcomes or resolutions of DHHS’s proposed rule.

A purchase price obligation of \$1.3 million related to a prior year acquisition remains contingent at December 31, 2002, and is not currently reflected in our financial statements. We expect to fund such obligation, if such obligation becomes due, with borrowings under our revolving credit facility or from operating cash flow.

In August 2002, the OIG published its work plan for the 2003 fiscal year. The work plan identified several projects related to our industry, including a project identified as “Financial Arrangements Between Physicians and Ambulatory Surgical Centers.” This project will focus on determining if physician ownership in ambulatory surgery centers affects utilization and the cost of outpatient surgeries. While we believe physician ownership of ambulatory surgery centers as structured within our partnerships and limited liability companies is in compliance with applicable law, there can be no assurance that the outcome of this work plan project would not generate legislative or regulatory changes that would have an adverse impact on us or obligate us to purchase some or all of the minority interests of physician entities affiliated with us as discussed in “Forward-Looking Statements.”

The following schedule summarizes all of our contractual obligations by period as of December 31, 2002 (in thousands):

	Total	Less than 1 Year	1-3 Years	3-5 Years	After 5 Years
Long-term debt ⁽¹⁾	\$ 28,633	\$ 1,289	\$ 1,404	\$ 675	\$ 25,265
Capital lease obligations	1,658	1,118	540	—	—
Operating leases	59,285	11,705	19,387	12,687	15,506
Construction in progress commitments	1,861	1,861	—	—	—
Other long-term obligations ⁽²⁾	1,253	—	1,253	—	—
Total contractual cash obligations	\$ 92,690	\$ 15,973	\$ 22,584	\$ 13,362	\$ 40,771

⁽¹⁾ Our long-term debt may increase based on acquisition activity expected to occur in the future and our stock repurchase program for up to \$25.0 million of our outstanding shares of common stock. We may use our operating cash flow to repay existing long-term debt under our credit facility prior to its maturity date.

⁽²⁾ Other long-term obligations consist of purchase price commitments that are contingent upon certain events.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS — CONTINUED

In addition, as of December 31, 2002, we have available under our revolving credit facility \$95.3 million for acquisition borrowings. Our credit facility, as recently amended on March 4, 2003, matures on March 4, 2008.

Foregoing any significant adverse impact on our future operating results, we believe that our operating cash flow and borrowing capacity will provide us with adequate liquidity for the next five years to conduct our business and further implement our growth strategy.

Recent Accounting Pronouncements

In June 2001, the FASB issued SFAS No. 143, "*Accounting for Asset Retirement Obligations*." SFAS No. 143 addresses accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This statement is effective for fiscal years beginning after June 15, 2002. SFAS No. 143 establishes accounting standards for recognition and measurement of liability for an asset retirement obligation and the associated retirement costs. This statement applies to all entities and to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or the normal operation of a long-lived asset, except for certain obligations of lessees. The implementation of SFAS No. 143 will not have a material effect on our consolidated financial position or consolidated results of operations.

On August 1, 2001, the FASB issued SFAS No. 144 "*Accounting for the Impairment or Disposal of Long-Lived Assets*." This statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes SFAS No. 121, "*Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets To Be Disposed Of*," and the accounting and reporting provisions of Accounting Principles Board, or APB, Opinion No. 30, "*Reporting the Results of Operations – Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*," for the disposal of a segment of a business. This statement also amends Accounting Research Bulletin No. 51, "*Consolidated Financial Statements*," to eliminate the exception to consolidation for a subsidiary for which control is likely to be temporary. The provisions of this statement are effective for financial statements issued for fiscal years beginning after December 15, 2001. The provisions are generally to be applied prospectively. There was no impact on our results of operations from the adoption of this standard.

In July 2002, the FASB issued SFAS No. 146, "*Accounting for Costs Associated with Exit or Disposal Activities*." The standard requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Examples of costs covered by the standard include lease termination costs and certain employee severance costs that are associated with a restructuring, discontinued operations, plant closings, or other exit or disposal activities. The provisions of this statement are effective for exit or disposal activities initiated after December 31, 2002.

In November 2002, the FASB issued Interpretation No., or FIN, 45, "*Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an Interpretation of FASB Statements No. 5, 57 and 107 and Rescission of FASB Interpretation No. 34*." The interpretation requires that upon issuance of a guarantee, the entity must recognize a liability for the fair value of the obligation it assumes under that obligation. This interpretation is intended to improve the comparability of financial reporting by requiring identical accounting for guarantees issued with separately identified consideration and guarantees issued without separately identified consideration. The initial recognition and measurement provisions of FIN 45 are applicable to guarantees issued or modified after December 31, 2002. We are currently evaluating what impact, if any, adoption of FIN 45 will have on our consolidated financial position and consolidated results of operations. The disclosure requirements of FIN 45 are effective for us as of December 31, 2002. The required disclosures are included in the notes to the consolidated financial statements.

In January 2003, the FASB issued FIN 46, "*Consolidation of Variable Interest Entities*." FIN 46 addresses consolidation by business enterprises of variable interest entities that have certain characteristics. This interpretation applies immediately to variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. It applies in the first fiscal year beginning after June 15, 2003 to variable interest entities in which an enterprise holds a variable interest that it acquired before February 1, 2003. We have not yet determined the impact, if any, the adoption of FIN 46 will have on our financial position and results of operations.

In December 2002, the FASB issued SFAS No. 148, “*Accounting for Stock-Based Compensation – Transition and Disclosure – an Amendment of FASB Statement No. 123.*” SFAS No. 148 amends SFAS No. 123, “*Accounting for Stock-Based Compensation,*” to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 is effective for annual and interim periods beginning after December 15, 2002. We have elected not to change to the fair value based method of accounting for stock-based employee compensation. Accordingly, the adoption of SFAS No. 148 will not have an impact on our consolidated financial position or consolidated results of operations. We have included the disclosures in accordance with SFAS No. 148 in Note 1(j) to our consolidated financial statements.

For a discussion of additional recent accounting pronouncements, see “– Critical Accounting Policies – *Goodwill* and – *Purchase Price Allocation*” above.

Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risk from exposure to changes in interest rates based on our financing, investing and cash management activities. We utilize a balanced mix of maturities along with both fixed-rate and variable-rate debt to manage our exposures to changes in interest rates. Our debt instruments are primarily indexed to the prime rate or LIBOR. Although there can be no assurances that interest rates will not change significantly, we do not expect changes in interest rates to have a material effect on income or cash flows in 2003.

The table below provides information as of December 31, 2002 and 2001 about our long-term debt obligations based on maturity dates that are sensitive to changes in interest rates, including principal cash flows and related weighted average interest rates by expected maturity dates (*in thousands, except percentage data*):

	Years Ended December 31,							Value at
	2003	2004	2005	2006	2007	2008	Total	December 31, 2002
Fixed rate	\$ 1,908	\$ 1,026	\$ 405	\$ 283	\$ 301	\$ 18	\$ 3,941	\$ 4,072
Average interest rate	7.43%	7.37%	6.80%	7.84%	7.96%	6.00%		
Variable rate	\$ 499	\$ 370	\$ 143	\$ 44	\$ 47	\$ 25,247	\$ 26,350	\$ 26,350
Average interest rate	5.03%	4.94%	4.50%	4.50%	4.50%	2.96%		

	Years Ended December 31,							Fair Value at December 31,
	2002	2003	2004	2005	2006	2007	Total	2001
Fixed rate	\$ 2,456	\$ 2,014	\$ 1,223	\$ 656	\$ 355	\$ 225	\$ 6,929	\$ 6,929
Average interest rate	8.23%	8.06%	8.28%	8.25%	8.09%	7.84%		
Variable rate	\$ 444	\$ 7,707	\$ 404	\$ 101	\$ –	\$ –	\$ 8,656	\$ 8,656
Average interest rate	5.05%	3.66%	5.04%	4.50%	–	–		

The difference in maturities of long-term obligations and overall increase in total borrowings principally resulted from our borrowings associated with our acquisition activity and the extension of the maturity date of our revolving credit facility. The average interest rates on these borrowings at December 31, 2002 decreased as compared to December 31, 2001 due to an overall decrease in market rates and the repayment of debt with higher average interest rates.

CONSOLIDATED BALANCE SHEETS

	December 31,	
	2002	2001
	<i>(Dollars in thousands)</i>	
Assets		
Current assets:		
Cash and cash equivalents	\$ 13,320	\$ 11,074
Accounts receivable, net of allowance of \$3,986 and \$3,475, respectively	29,597	28,069
Supplies inventory	3,762	3,298
Deferred income taxes (note 8)	797	537
Prepaid and other current assets	5,688	5,030
Total current assets	53,164	48,008
Long-term receivables and deposits (note 2)	2,969	3,069
Property and equipment, net (notes 3, 5 and 6)	48,862	42,134
Intangible assets, net (notes 2 and 4)	194,819	148,172
Total assets	\$ 299,814	\$ 241,383
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt (note 5)	\$ 2,407	\$ 2,900
Accounts payable	5,203	4,348
Accrued salaries and benefits	6,188	4,395
Other accrued liabilities	1,368	1,456
Current income taxes payable	584	–
Total current liabilities	15,750	13,099
Long-term debt (notes 2 and 5)	27,884	12,685
Deferred income taxes (note 8)	9,947	4,983
Minority interest	29,869	25,047
Preferred stock, no par value, 5,000,000 shares authorized	–	–
Shareholders' equity:		
Common stock, no par value, 39,800,000 shares authorized, 20,548,235 and 20,116,892 shares outstanding, respectively (note 7)	158,585	151,812
Retained earnings	57,779	33,757
Total shareholders' equity	216,364	185,569
Commitments and contingencies (notes 2, 5, 6, 9 and 11)		
Total liabilities and shareholders' equity	\$ 299,814	\$ 241,383

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF EARNINGS

	Years Ended December 31,		
	2002	2001	2000
	<i>(In thousands, except earnings per share)</i>		
Revenues	\$ 251,525	\$ 202,312	\$ 143,261
Operating expenses:			
Salaries and benefits (note 9)	66,332	54,190	39,770
Supply cost	30,060	23,835	16,598
Other operating expenses (note 9)	52,815	42,572	29,445
Depreciation and amortization	9,995	14,426	10,301
Total operating expenses	159,202	135,023	96,114
Operating income	92,323	67,289	47,147
Minority interest	51,096	39,599	27,702
Interest expense, net of interest income of \$227, \$216 and \$230, respectively	1,190	2,844	4,703
Earnings before income taxes	40,037	24,846	14,742
Income tax expense (note 8)	16,015	9,941	5,676
Net earnings	\$ 24,022	\$ 14,905	\$ 9,066
Earnings per common share (note 7):			
Basic	\$ 1.18	\$ 0.81	\$ 0.62
Diluted	\$ 1.16	\$ 0.78	\$ 0.60
Weighted average number of shares and share equivalents outstanding (note 7):			
Basic	20,390	18,428	14,594
Diluted	20,728	19,021	15,034

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Years Ended December 31, 2002, 2001 and 2000			
	<i>(In thousands)</i>			
	Common Stock		Retained	Total
	Shares	Amount	Earnings	
Balance December 31, 1999	14,547	\$ 62,922	\$ 9,786	\$ 72,708
Issuance of common stock	30	172	—	172
Stock options exercised	162	695	—	695
Tax benefit related to exercise of stock options	—	504	—	504
Net earnings	—	—	9,066	9,066
Balance December 31, 2000	14,739	64,293	18,852	83,145
Issuance of common stock	4,528	76,661	—	76,661
Stock options exercised	850	3,264	—	3,264
Tax benefit related to exercise of stock options	—	7,594	—	7,594
Net earnings	—	—	14,905	14,905
Balance December 31, 2001	20,117	151,812	33,757	185,569
Issuance of common stock	2	66	—	66
Stock options exercised	429	3,218	—	3,218
Tax benefit related to exercise of stock options	—	3,489	—	3,489
Net earnings	—	—	24,022	24,022
Balance December 31, 2002	20,548	\$ 158,585	\$ 57,779	\$ 216,364

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2002	2001	2000
	<i>(In thousands)</i>		
Cash flows from operating activities:			
Net earnings	\$ 24,022	\$ 14,905	\$ 9,066
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Minority interest	51,096	39,599	27,702
Distributions to minority partners	(49,468)	(38,560)	(27,416)
Depreciation and amortization	9,995	14,426	10,301
Deferred income taxes	4,704	1,409	957
Increase (decrease) in cash and cash equivalents, net of effects of acquisitions and dispositions, due to changes in:			
Accounts receivable, net	(575)	(782)	(3,141)
Supplies inventory	(58)	(22)	(182)
Prepaid and other current assets	447	(2,894)	(460)
Other assets	—	—	278
Accounts payable	727	1,647	56
Accrued expenses and other liabilities	5,757	7,445	1,447
Other, net	272	128	(115)
Net cash flows provided by operating activities	46,919	37,301	18,493
Cash flows from investing activities:			
Acquisition of interest in surgery centers	(29,443)	(57,589)	(30,714)
Acquisition of property and equipment	(14,489)	(7,007)	(13,457)
(Increase) decrease in long-term receivables	100	(89)	167
Net cash flows used in investing activities	(43,832)	(64,685)	(44,004)
Cash flows from financing activities:			
Proceeds from long-term borrowings	27,497	44,861	37,345
Repayment on long-term borrowings	(33,098)	(96,805)	(14,145)
Net proceeds from issuance of common stock	3,284	79,925	695
Proceeds from capital contributions by minority partners	1,491	2,807	704
Financing cost incurred	(15)	(18)	(923)
Net cash flows provided by (used in) financing activities	(841)	30,770	23,676
Net increase (decrease) in cash and cash equivalents	2,246	3,386	(1,835)
Cash and cash equivalents, beginning of year	11,074	7,688	9,523
Cash and cash equivalents, end of year	\$ 13,320	\$ 11,074	\$ 7,688

See accompanying notes to the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

a. Principles of Consolidation

AmSurg Corp. (the “Company”), through its wholly owned subsidiaries, owns majority interests, primarily 51% and up to 67% in certain instances, in limited partnerships and limited liability companies (“LLCs”) which own and operate practice-based ambulatory surgery centers (“centers”). The Company also has majority ownership interests in other partnerships and LLCs formed to develop additional centers. The consolidated financial statements include the accounts of the Company and its subsidiaries and the majority owned limited partnerships and LLCs in which the Company is the general partner or majority member. Consolidation of such partnerships and LLCs is necessary as the Company has 51% or more of the financial interest, is the general partner or majority member with all the duties, rights and responsibilities thereof and is responsible for the day-to-day management of the partnership or LLC. The limited partner or minority member responsibilities are to supervise the delivery of medical services, with their rights being restricted to those that protect their financial interests, such as approval of the acquisition of significant assets or the incurrence of debt which they, as physician limited partners or members, are required to guarantee on a pro rata basis based upon their respective ownership interests. Intercompany profits, transactions and balances have been eliminated. All subsidiaries and minority owners are herein referred to as partnerships and partners, respectively.

The Company operates in one reportable business segment, the ownership and operation of ambulatory surgery centers.

b. Cash and Cash Equivalents

Cash and cash equivalents are comprised principally of demand deposits at banks and other highly liquid short-term investments with maturities of less than three months when purchased.

c. Supplies Inventory

Supplies inventory consists of medical and drug supplies and is recorded at cost on a first-in, first-out basis.

d. Prepaid and Other Current Assets

Prepaid and other current assets are comprised of prepaid expenses and other receivables.

e. Property and Equipment

Property and equipment are stated at cost. Equipment held under capital leases is stated at the present value of minimum lease payments at the inception of the related leases. Depreciation for buildings and improvements is recognized under the straight-line method over 20 years, or for leasehold improvements, over the remaining term of the lease plus renewal options. Depreciation for movable equipment is recognized over useful lives of three to ten years.

f. Intangible Assets

Goodwill

In July 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (“SFAS”) No. 141, “*Business Combinations*,” and SFAS No. 142, “*Goodwill and Other Intangible Assets*.” The provisions of SFAS No. 141 require all business combinations to be accounted for by the purchase method. SFAS No. 142 requires that, upon adoption, amortization of goodwill and indefinite life intangible assets will cease and instead, the carrying value of goodwill and indefinite life intangible assets will be evaluated for impairment at least on an annual basis; impairment of carrying value will be evaluated more frequently if certain indicators are encountered. Identifiable intangible assets with a determinable useful life will continue to be amortized over that period and reviewed for impairment in accordance with SFAS No. 144 (discussed below). SFAS No. 142 is effective

for fiscal years beginning after December 15, 2001, except for goodwill and intangible assets acquired after June 30, 2001, which were subject immediately to the nonamortization provisions of this statement.

The Company fully adopted SFAS No. 142 on January 1, 2002, and accordingly, ceased to amortize goodwill, which previously had been amortized over 25 years. SFAS No. 142 requires that goodwill be tested at the reporting unit level, defined as an operating segment or one level below an operating segment (referred to as a component), with the fair value of the reporting unit being compared to its carrying amount, including goodwill. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is not considered to be impaired. Management has determined that the Company has one operating as well as one reportable segment. The Company's centers each qualify as components of that operating segment and have similar economic characteristics, and therefore, should be aggregated and deemed a single reporting unit. The Company completed the transitional goodwill impairment test and has determined that no potential impairment exists. As a result, the Company has recognized no transitional impairment loss in fiscal year 2002 in connection with the adoption of SFAS No. 142.

As required by SFAS No. 142, the results for periods prior to its adoption have not been restated. The following reconciles the reported net earnings per share to that which would have resulted had SFAS No. 142 been applied to the years ended December 31, 2002, 2001 and 2000 (in thousands, except earnings per share):

	2002	2001	2000
Net earnings:			
As reported	\$ 24,022	\$ 14,905	\$ 9,066
Goodwill amortization, net of income tax expense	–	3,413	2,408
As adjusted	\$ 24,022	\$ 18,318	\$ 11,474
Basic earnings per share:			
As reported	\$ 1.18	\$ 0.81	\$ 0.62
As adjusted	1.18	0.99	0.79
Diluted earnings per share:			
As reported	\$ 1.16	\$ 0.78	\$ 0.60
As adjusted	1.16	0.96	0.76

Other Intangible Assets

Other intangible assets consist primarily of deferred financing costs of the Company and the entities included in the Company's consolidated financial statements and non-compete agreements, which are amortized over the term of the related debt as interest expense and the contractual term (five years) of the non-compete agreements as amortization expense, respectively.

g. Revenue Recognition

Center revenues consist of billing for the use of the centers' facilities (the "facility fee") directly to the patient or third-party payor, and in limited instances, billing for anesthesia services. Such revenues are recognized when the related surgical procedures are performed. Revenues exclude any amounts billed for physicians' surgical services, which are billed separately by the physicians to the patient or third-party payor.

Revenues from centers are recognized on the date of service, net of estimated contractual allowances from third-party medical service payors including Medicare and Medicaid (see note 1 (l)). During the years ended December 31, 2002, 2001 and 2000, approximately 40%, 38%, and 37%, respectively, of the Company's revenues were derived from the provision of services to patients covered under Medicare and Medicaid. Concentration of credit risk with respect to other payors is limited due to the large number of such payors.

h. Income Taxes

The Company files a consolidated federal income tax return. Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

i. Earnings Per Share

Basic earnings per share is computed by dividing net earnings available to common shareholders by the combined weighted average number of common shares, while diluted earnings per share is computed by dividing net earnings available to common shareholders by the weighted average number of such common shares and dilutive share equivalents.

j. Stock-Based Compensation

The Company accounts for its stock option plan in accordance with the provisions of Accounting Principles Board (“APB”) Opinion No. 25, “*Accounting for Stock Issued to Employees*,” and related interpretations. Compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. No stock-based employee compensation cost is reflected in net earnings for the years ended December 31, 2002, 2001 and 2000. Disclosure in accordance with SFAS No. 123, “*Accounting for Stock-Based Compensation*,” to reflect the pro forma earnings per share as if the fair value of all stock-based awards on the date of grant are recognized over the vesting period is presented below.

The estimated weighted average fair values of the options at the date of grant using the Black-Scholes option pricing model as promulgated by SFAS No. 123 in 2002, 2001 and 2000 were \$6.94, \$15.23 and \$4.65 per share, respectively. In applying the Black-Scholes model, the Company assumed no dividends, an expected life for the options of four years in 2002 and seven years in 2001 and 2000, a forfeiture rate of 15% in 2002 and 3% in 2001 and 2000 and an average risk free interest rate of 4.1%, 4.8% and 6.7% in 2002, 2001 and 2000, respectively. The Company also assumed a volatility rate of 46%, 66% and 70% in 2002, 2001 and 2000, respectively. Had the Company used the Black-Scholes estimates to determine compensation expense for the options granted in the years ended December 31, 2002, 2001 and 2000, net earnings and net earnings per share attributable to common shareholders would have been reduced to the following pro forma amounts (*in thousands, except per share amounts*):

	2002	2001	2000
Net earnings available to common shareholders:			
As reported	\$ 24,022	\$ 14,905	\$ 9,066
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(3,263)	(4,238)	(959)
Pro forma	\$ 20,759	\$ 10,667	\$ 8,107
Basic earnings per share available to common shareholders:			
As reported	\$ 1.18	\$ 0.81	\$ 0.62
Pro forma	1.02	0.58	0.56
Diluted earnings per share available to common shareholders:			
As reported	\$ 1.16	\$ 0.78	\$ 0.60
Pro forma	1.00	0.56	0.54

k. Fair Value of Financial Instruments

Cash and cash equivalents, receivables and payables are reflected in the financial statements at cost, which approximates fair value. The fair value of fixed-rate long-term debt, with a carrying value of \$3,941,000, is \$4,072,000. Management believes that the carrying amounts of variable-rate long-term debt approximate market value, because it believes the terms of its borrowings approximate terms which it would incur currently.

l. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The determination of contractual and bad debt allowances constitutes a significant estimate. Some of the factors considered by management in determining the amount of allowances to establish are the historical trends of the centers' cash collections and contractual and bad debt write-offs, accounts receivable agings, established fee schedules, relationships with payors and procedure statistics. Accordingly, net accounts receivable at December 31, 2002 and 2001, reflect allowances for contractual adjustments of \$25,451,000 and \$25,069,000, respectively, and allowance for bad debt expense of \$3,986,000 and \$3,475,000, respectively.

m. Recent Accounting Pronouncements

In June 2001, the FASB issued SFAS No. 143, "*Accounting for Asset Retirement Obligations*." SFAS No. 143 addresses accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This statement is effective for fiscal years beginning after June 15, 2002. SFAS No. 143 establishes accounting standards for recognition and measurement of liability for an asset retirement obligation and the associated retirement costs. This statement applies to all entities and to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and (or) the normal operation of a long-lived asset, except for certain obligations of lessees. The implementation of SFAS No. 143 will not have a material effect on the Company's consolidated financial position or consolidated results of operations.

On August 1, 2001, the FASB issued SFAS No. 144 "*Accounting for the Impairment or Disposal of Long-Lived Assets*." This statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes SFAS No. 121, "*Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets To Be Disposed Of*," and the accounting and reporting provisions of APB Opinion No. 30, "*Reporting the Results of Operations – Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*," for the disposal of a segment of a business. This statement also amends Accounting Research Bulletin No. 51, "*Consolidated Financial Statements*," to eliminate the exception to consolidation for a subsidiary for which control is likely to be temporary. The provisions of this statement are effective for financial statements issued for fiscal years beginning after December 15, 2001. The provisions are generally to be applied prospectively. There was no impact on the Company's results of operations from the adoption of this standard.

In July 2002, the FASB issued SFAS No. 146, "*Accounting for Costs Associated with Exit or Disposal Activities*." The standard requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Examples of costs covered by the standard include lease termination costs and certain employee severance costs that are associated with a restructuring, discontinued operations, plant closings, or other exit or disposal activities. The provisions of this statement are effective for exit or disposal activities initiated after December 31, 2002.

In November 2002, the FASB issued Interpretation No. ("FIN") 45, "*Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an Interpretation of FASB Statements No. 5, 57 and 107 and Rescission of FASB Interpretation No. 34*." The interpretation requires that upon

issuance of a guarantee, the entity must recognize a liability for the fair value of the obligation it assumes under that obligation. This interpretation is intended to improve the comparability of financial reporting by requiring identical accounting for guarantees issued with separately identified consideration and guarantees issued without separately identified consideration. The initial recognition and measurement provision of FIN 45 are applicable to guarantees issued or modified after December 31, 2002. The Company is currently evaluating what impact, if any, adoption of FIN 45 will have on its consolidated financial position and consolidated results of operations. The disclosure requirements of FIN 45 are effective for the Company as of December 31, 2002.

In January 2003, the FASB issued FIN 46, *“Consolidation of Variable Interest Entities.”* FIN 46 addresses consolidation by business enterprises of variable interest entities that have certain characteristics. This interpretation applies immediately to variable interest entities created in January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. It applies in the first fiscal year beginning after June 15, 2003 to variable interest entities in which an enterprise holds a variable interest that it acquired before February 1, 2003. The Company has not yet determined the impact, if any, the adoption of FIN 46 will have on its financial position and results of operations.

In December 2002, the FASB issued SFAS No. 148, *“Accounting for Stock-Based Compensation – Transition and Disclosure – an Amendment of FASB Statement No. 123.”* SFAS No. 148 amends SFAS No. 123, *“Accounting for Stock-Based Compensation,”* to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 is effective for annual and interim periods beginning after December 15, 2002. As the Company has elected not to change to the fair value based method of accounting for stock-based employee compensation, the adoption of SFAS No. 148 will not have an impact on the Company’s consolidated financial position or consolidated results of operation. The Company has included the disclosures in accordance with SFAS No. 148 in Note 1(j).

2. Acquisitions and Dispositions

a. Acquisitions

The Company, through wholly owned subsidiaries and in separate transactions, acquired a majority interest in ten, fifteen and nine practice-based surgery centers during 2002, 2001 and 2000, respectively. Consideration paid for the acquired interests consisted of cash, common stock and notes payable at rates ranging from 4.3% in 2002 to 9.5% in 2000, due within 30 days from issuance. Total acquisition price and cost in 2002, 2001 and 2000 was \$49,018,000, \$47,113,000, and \$41,563,000, respectively, of which the Company assigned \$47,161,000, \$43,929,000 and \$38,149,000, respectively, to goodwill. Such amounts in 2002 included an aggregate of \$8,403,000 in contingent purchase price payments associated with prior year acquisitions, primarily related to a discontinuance of a proposed rule to update reimbursement by Medicare as discussed below. The goodwill is expected to be fully deductible for tax purposes. At December 31, 2002, the Company had notes payable associated with recent acquisitions of \$19,575,000. All notes payable outstanding as of December 31, 2002 were funded in January 2003 through long-term borrowings on the Company’s credit facility (see note 5). All acquisitions were accounted for as purchases, and the accompanying consolidated financial statements include the results of their operations from the dates of acquisition.

In May 2002, the Department of Health and Human Services (“DHHS”) listed as a “discontinued action” the June 12, 1998 proposed rule that would update the rate setting methodology, payment rates, payment policies and the list of covered surgical procedures for ambulatory surgery centers. If implemented, the proposed rule would have reduced the rates paid for certain ambulatory surgery center procedures reimbursed by Medicare, including a number of endoscopy and ophthalmology procedures performed at the Company’s centers. Upon the announcement of the discontinuance of this proposed rule, the Company paid purchase price commitments of \$7,742,000 that were contingent on certain outcomes or resolutions of DHHS’s proposed rule. Such amounts are included in the acquisition transaction amounts above.

b. Pro Forma Information

The unaudited consolidated pro forma results for the years ended December 31, 2002 and 2001, assuming all 2002 and 2001 acquisitions had been consummated on January 1, 2001, are as follows (*in thousands, except per share data*):

	2002	2001
Revenues	\$ 272,398	\$ 240,722
Net earnings	26,043	16,902
Earnings per common share:		
Basic	\$ 1.28	\$ 0.92
Diluted	1.26	0.89
Weighted average number of shares and share equivalents:		
Basic	20,390	18,428
Diluted	20,728	19,021

c. Dispositions

In 2001, the Company sold its interests in two surgery centers and a portion of its interest in a third surgery center. Combined proceeds of these sales approximated the book value of the assets sold and included notes receivable totaling \$1,119,000, bearing interest at 7.0%, due in installments through 2005 and secured by the assets of a surgery center and certain personal guarantees by the buyers.

3. Property and Equipment

Property and equipment at December 31, 2002 and 2001 are as follows (*in thousands*):

	2002	2001
Land and improvements	\$ 549	\$ 99
Building and improvements	30,705	25,315
Movable equipment	52,928	43,522
Construction in progress	1,502	574
	85,684	69,510
Less accumulated depreciation and amortization	36,822	27,376
Property and equipment, net	\$ 48,862	\$ 42,134

At December 31, 2002, the Company and its partnerships had unfunded construction and equipment purchases of approximately \$1,861,000 in order to complete construction in progress.

4. Intangible Assets

Amortizable intangible assets at December 31, 2002 and 2001 consist of the following (*in thousands*):

	2002			2001		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Deferred financing cost	\$ 1,026	\$ 881	\$ 145	\$ 1,017	\$ 558	\$ 459
Agreements not to compete	1,000	250	750	1,000	50	950
Total amortizable intangible assets	\$ 2,026	\$ 1,131	\$ 895	\$ 2,017	\$ 608	\$ 1,409

Amortization of intangible assets for the years ended December 31, 2002, 2001 and 2000 was \$529,000, \$6,066,000 and \$4,283,000, respectively. Estimated amortization of intangible assets for the four years subsequent to December 31, 2002 are \$345,000, \$200,000, \$200,000 and \$150,000.

The changes in the carrying amount of goodwill for the years ended December 31, 2002 and 2001 are as follows (*in thousands*):

	2002	2001
Balance, beginning of year	\$ 146,763	\$ 110,640
Goodwill acquired during year	47,161	43,929
Goodwill written off related to sale of business units	—	(2,117)
Amortization	—	(5,689)
Balance, end of year	\$ 193,924	\$ 146,763

5. Long-term Debt

Long-term debt at December 31, 2002 and 2001 is comprised of the following (*in thousands*):

	2002	2001
Notes payable at 2.9% (see note 2)	\$ 19,575	\$ —
\$100 million credit agreement at prime or LIBOR plus a spread of 1.5% to 2.25% (average rate of 2.9% at December 31, 2002), due March 2008	4,700	7,300
Other debt at an average rate of 6.0%, due through September 2022	4,358	4,487
Capitalized lease arrangements at an average rate of 7.8%, due through September 2005 (see note 6)	1,658	3,798
	30,291	15,585
Less current portion	2,407	2,900
Long-term debt	\$ 27,884	\$ 12,685

The borrowings under the credit facility are guaranteed by the wholly owned subsidiaries of the Company, and in some instances, the underlying assets of certain developed centers. The credit agreement, as most recently amended on March 4, 2003, permits the Company to borrow up to \$100,000,000 to finance the Company's acquisition and development projects at prime rate or LIBOR plus a spread of 1.50% to 2.25% or a combination thereof, provides for a fee of 0.50% of unused commitments, prohibits the payment of dividends and contains covenants relating to the ratio of debt to net worth, operating performance and minimum net worth. The Company was in compliance with all covenants at December 31, 2002.

Certain partnerships and LLCs included in the Company's consolidated financial statements have loans with local lending institutions which are collateralized by certain assets of the centers with a book value of approximately \$6,684,000. The Company and the partners or members have guaranteed payment of the loans in proportion to the relative partnership or membership interests.

Principal payments required on long-term debt in the five years subsequent to December 31, 2002 and thereafter are \$2,407,000, \$1,396,000, \$548,000, \$327,000, \$348,000 and \$25,265,000, respectively. These maturities reflect the funding of notes payable in January 2003 with borrowings under the credit facility and the amended terms of the credit facility.

6. Leases

The Company has entered into various building and equipment operating leases and equipment capital leases for its surgery centers in operation and under development and for office space, expiring at various dates through 2017. Future minimum lease payments at December 31, 2002 are as follows (*in thousands*):

Year Ended December 31,	Capitalized Equipment Leases	Operating Leases
2003	\$ 1,204	\$ 11,705
2004	547	10,440
2005	11	8,947
2006	—	7,032
2007	—	5,655
Thereafter	—	15,506
Total minimum rentals	1,762	\$ 59,285
Less amounts representing interest at rates ranging from 6.0% to 9.6%	104	
Capital lease obligations	<u>\$ 1,658</u>	

At December 31, 2002, equipment with a cost of approximately \$4,193,000 and accumulated amortization of approximately \$1,460,000 was held under capital lease. The Company and the partners have guaranteed payment of certain of these leases. Rental expense for operating leases for the years ended December 31, 2002, 2001, and 2000 was approximately \$11,323,000, \$9,757,000 and \$7,126,000, respectively (see note 9).

7. Shareholders' Equity

a. Common Stock

In April 2001, the Company completed a public offering of 4,526,000 shares of Class A Common Stock, for net proceeds of approximately \$76,600,000 to the Company. Net proceeds from the offering were used to repay borrowings under the Company's revolving credit facility.

In July 2001, after receiving shareholder approval, the Company reclassified its Class A and Class B Common Stock into one class of common stock, having the rights of the Class A Common Stock. The Class A and Class B shares were reclassified into one class of common stock using a one-to-one conversion ratio, resulting in no increase in the Company's total number of shares or book value of common stock outstanding.

b. Shareholder Rights Plan

In 1999, the Company's Board of Directors adopted a shareholder rights plan and declared a distribution of one stock purchase right for each outstanding share of the Company's common stock to shareholders of record on December 16, 1999 and for each share of common stock issued thereafter. Each right initially entitles its holder to purchase one one-hundredth of a share of Series C Junior Participating Preferred Stock, at \$48, subject to adjustment. With certain exceptions, each right will become exercisable only when a person or group acquires, or commences a tender or exchange offer for, 15% or more of the Company's outstanding common stock. Rights will also become exercisable in the event of certain mergers or asset sales involving more than 50% of the Company's assets or earning power. Upon becoming exercisable, each right will allow the holder (other than the person or group whose actions triggered the exercisability of the rights), under specified circumstances, to buy either securities of the Company or securities of the acquiring company (depending on the form of the transaction) having a value of twice the then current exercise price of the rights. The rights expire on December 2, 2009.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — CONTINUED

c. Earnings per Share

The following is a reconciliation of the numerator and denominators of basic and diluted earnings per share (*in thousands, except per share amounts*):

	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
For the year ended December 31, 2002:			
Basic earnings per share:			
Net earnings	\$ 24,022	20,390	\$ 1.18
Effect of dilutive securities options	—	338	
Diluted earnings per share:			
Net earnings	\$ 24,022	20,728	\$ 1.16
For the year ended December 31, 2001:			
Basic earnings per share:			
Net earnings	\$ 14,905	18,428	\$ 0.81
Effect of dilutive securities options	—	593	
Diluted earnings per share:			
Net earnings	\$ 14,905	19,021	\$ 0.78
For the year ended December 31, 2000:			
Basic earnings per share:			
Net earnings	\$ 9,066	14,594	\$ 0.62
Effect of dilutive securities options	—	440	
Diluted earnings per share:			
Net earnings	\$ 9,066	15,034	\$ 0.60

d. Stock Options

The Company has two stock option plans under which it has granted non-qualified options to purchase shares of common stock to employees and outside directors. Options are granted at market value on the date of the grant and vest ratably over four years. Options have a term of 10 years from the date of grant. At December 31, 2002, 4,217,333 shares were authorized for grant under the two stock option plans and 996,929 shares were available for future option grants. Stock option activity for the three years ended December 31, 2002 is summarized below:

	Number of Shares	Weighted Average Exercise Price
Outstanding at December 31, 1999	1,635,804	\$ 5.00
Options granted	377,059	6.82
Options exercised	(161,930)	4.29
Options terminated	(25,054)	7.62
Outstanding at December 31, 2000	1,825,879	5.40
Options granted	793,759	23.90
Options exercised	(849,915)	3.84
Options terminated	(115,961)	14.91
Outstanding at December 31, 2001	1,653,762	14.41
Options granted	502,378	24.95
Options exercised	(429,219)	7.50
Options terminated	(84,680)	20.56
Outstanding at December 31, 2002	1,642,241	\$ 19.13

The following table summarizes information concerning outstanding and exercisable options at December 31, 2002:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Life (Yrs.)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$ 3.00 - \$ 9.00	462,921	5.9	\$ 7.16	295,663	\$ 7.27
9.01 - 15.00	35,118	5.5	9.99	33,452	9.74
15.01 - 21.00	8,333	8.3	19.12	834	18.85
21.01 - 27.00	1,063,371	8.7	24.00	312,114	23.76
27.01 - 31.45	72,498	9.1	28.56	8,755	27.59
	<u>1,642,241</u>			<u>650,818</u>	
\$ 3.00 - \$31.45		7.9	\$ 19.13		\$ 15.59

8. Income Taxes

Total income tax expense for the years ended December 31, 2002, 2001 and 2000 was allocated as follows (*in thousands*):

	2002	2001	2000
Income from operations	\$ 16,015	\$ 9,941	\$ 5,676
Shareholders' equity, for compensation expense for tax purposes in excess of amounts recognized for financial reporting purposes	(3,489)	(7,594)	(504)
Total income tax expense	\$ 12,526	\$ 2,347	\$ 5,172

Income tax expense from operations for the years ended December 31, 2002, 2001 and 2000 is comprised of the following (*in thousands*):

	2002	2001	2000
Current:			
Federal	\$ 9,337	\$ 6,848	\$ 3,907
State	1,974	1,684	812
Deferred	4,704	1,409	957
Income tax expense	\$ 16,015	\$ 9,941	\$ 5,676

Income tax expense from operations for the years ended December 31, 2002, 2001 and 2000 differed from the amount computed by applying the U.S. Federal income tax rates of 35%, 35% and 34%, respectively, to earnings before income taxes as a result of the following (*in thousands*):

	2002	2001	2000
Statutory Federal income tax	\$ 14,013	\$ 8,696	\$ 5,012
State income taxes, net of Federal income tax benefit	2,004	1,066	662
Increase (decrease) in valuation allowance	(58)	58	(9)
Adjustment to beginning-of-the-year net deferred tax liability to reflect 35% U.S. Federal income tax rate	-	73	-
Other	56	48	11
Income tax expense	\$ 16,015	\$ 9,941	\$ 5,676

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — CONTINUED

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2002 and 2001 are as follows (*in thousands*):

	2002	2001
Deferred tax assets:		
Allowance for uncollectible accounts	\$ 906	\$ 546
State net operating losses	7	65
Accrued liabilities and other	160	120
Gross deferred tax assets	1,073	731
Valuation allowance	(7)	(65)
Net deferred tax assets	1,066	666
Deferred tax liabilities:		
Property and equipment, principally due to difference in depreciation	624	133
Goodwill, principally due to differences in amortization	9,323	4,850
Prepaid expenses	269	129
Gross deferred tax liabilities	10,216	5,112
Net deferred tax liabilities	\$ 9,150	\$ 4,446

The net deferred tax liability at December 31, 2002 and 2001, is recorded as follows (*in thousands*):

	2002	2001
Current deferred income tax assets	\$ 797	\$ 537
Noncurrent deferred income tax liability	9,947	4,983
Net deferred tax liability	\$ 9,150	\$ 4,446

The Company has provided a valuation allowance on its gross deferred tax asset primarily related to state net operating losses to the extent that management does not believe that it is more likely than not that such asset will be realized.

9. Related Party Transactions

The Company leases space for certain surgery centers from its physician partners affiliated with its centers at rates the Company believes approximate fair market value. Payments on these leases were approximately \$6,963,000, \$5,937,000 and \$3,898,000 for the years ended December 31, 2002, 2001 and 2000, respectively.

The Company reimburses certain of its limited partners for salaries and benefits related to time spent by employees of their practices on activities of the centers. Total reimbursement of such salary and benefit costs totaled approximately \$23,512,000, \$21,114,000 and \$15,660,000 for the years ended December 31, 2002, 2001 and 2000, respectively.

The Company receives capitated reimbursement at one of its centers from a non-physician minority partner associated with the center. Total capitated revenue received was approximately \$1,320,000, \$1,337,000 and \$1,447,000 for the years ended December 31, 2002, 2001 and 2000, respectively.

The Company believes that the foregoing transactions are in its best interests. It is the Company's current policy that all transactions by the Company with officers, directors, five percent shareholders and their affiliates will be entered into only if such transactions are on terms no less favorable to the Company than could be obtained from unaffiliated third parties, are reasonably expected to benefit the Company and are approved by a majority of the disinterested independent members of the Company's Board of Directors.

10. Employee Benefit Programs

As of January 1, 1999, the Company adopted the AmSurg 401(k) Plan and Trust. This plan is a defined contribution plan covering substantially all employees of AmSurg Corp. and provides for voluntary contributions by

these employees, subject to certain limits. Company contributions are based on specified percentages of employee compensation. The Company funds contributions as accrued. The Company's contributions for the years ended December 31, 2002, 2001 and 2000 were approximately \$94,000, \$81,000 and \$76,000, respectively, and vest incrementally over four years.

As of January 1, 2000, the Company adopted the Supplemental Executive Retirement Savings Plan. This plan is a defined contribution plan covering all officers of the Company and provides for voluntary contributions up to 5% of employee annual compensation. Company contributions are at the discretion of the Compensation Committee of the Board of Directors and vest incrementally over four years. The employee and employer contributions are placed in a Rabbi Trust. Employer contributions to this plan for the years ended December 31, 2002, 2001 and 2000 were approximately \$446,000, \$387,000 and \$193,000, respectively.

11. Commitments and Contingencies

The Company and its partnerships are insured with respect to medical malpractice risk on a claims-made basis. The Company also maintains insurance for general liability, director and officer liability and property. Certain policies are subject to deductibles. In addition to the insurance coverage provided, the Company indemnifies certain officers and directors for actions taken on behalf of the Company and its partnerships. Management is not aware of any claims against it or its partnerships which would have a material financial impact.

The Company or its wholly owned subsidiaries, as general partners in the limited partnerships, are responsible for all debts incurred but unpaid by the partnership. As manager of the operations of the partnership, the Company has the ability to limit its potential liabilities by curtailing operations or taking other operating actions.

In the event of a change in current law which would prohibit the physicians' current form of ownership in the partnerships or LLCs, the Company is obligated to purchase the physicians' interests in the partnerships or LLCs. The purchase price to be paid in such event is determined by a predefined formula, as specified in the partnership agreements.

12. Supplemental Cash Flow Information

Supplemental cash flow information for the years ended December 31, 2002, 2001 and 2000 is as follows (*in thousands*):

	2002	2001	2000
Cash paid during the year for:			
Interest	\$ 1,071	\$ 3,171	\$ 4,507
Income taxes, net of refunds	5,983	3,350	3,376
Noncash investing and financing activities:			
Capital lease obligations incurred to acquire equipment	107	1,440	1,967
Notes received for sale of a partnership interest	–	1,119	–
Effect of acquisitions:			
Assets acquired, net of cash	51,805	50,296	45,090
Liabilities assumed	(2,787)	(3,183)	(4,008)
Issuance of common stock	–	–	(50)
Notes payable and other obligations	(19,575)	10,476	(10,318)
Payment for assets acquired	\$ 29,443	\$ 57,589	\$ 30,714

13. Subsequent Events

In February 2003, the Company announced that its Board of Directors authorized a stock repurchase program for up to \$25,000,000 of the Company's outstanding shares of common stock over the subsequent 18 months, which the Company intends to fund through borrowings under its credit facility.

In March 2003, the Company, through a wholly owned subsidiary, acquired a majority interest in a physician practice-based surgery center for approximately \$9,620,000.

INDEPENDENT AUDITORS' REPORT

Board of Directors and Shareholders
AmSurg Corp.
Nashville, Tennessee

We have audited the accompanying consolidated balance sheets of AmSurg Corp. and subsidiaries as of December 31, 2002 and 2001, and the related consolidated statements of earnings, changes in shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of AmSurg Corp. and its subsidiaries as of December 31, 2002 and 2001 and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1(f) to the consolidated financial statements, effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, "*Goodwill and Other Intangible Assets*," which resulted in the Company changing the method in which it accounts for goodwill and other intangible assets.

Deloitte & Touche LLP

Nashville, Tennessee
February 14, 2003, except for Notes 5 and 13,
as to which the date is March 26, 2003

SHAREHOLDER INFORMATION

Common Stock and Dividend Information

Prior to July 12, 2001, we had two classes of common stock, Class A Common Stock and Class B Common Stock, which traded under the symbols “AMSGA” and “AMSGB,” respectively, on the Nasdaq National Market. On July 12, 2001, after receiving shareholder approval, we reclassified our Class A and Class B Common Stock into one class of common stock, having the rights of the Class A Common Stock. The Class A and Class B shares were reclassified into one class of common stock using a one-to-one conversion ratio, resulting in no increase in our total number of shares or book value of common stock outstanding. The new class of common stock trades under the symbol “AMSG” on the Nasdaq National Market. See “Quarterly Earnings and Market Price Data” below for the high and low sales prices per share for the common stock for each of the quarters in 2001 and 2002, as reported on the Nasdaq National Market.

At March 21, 2003 there were approximately 6,250 holders of our common stock, including 121 shareholders of record. We have never declared or paid a cash dividend on our common stock. We intend to retain our earnings to finance the growth and development of our business and do not expect to declare or pay any cash dividends in the foreseeable future. The declaration of dividends is within the discretion of our Board of Directors, which will review this dividend policy from time to time. Presently, the declaration of dividends is prohibited by a covenant in our credit facility with lending institutions.

Quarterly Earnings and Market Price Data

The following table presents certain quarterly statement of earnings data for the years ended December 31, 2001 and 2002, as well as the high and low sales prices per share for the common stock for each of the quarters. The quarterly statement of earnings data set forth below was derived from our unaudited financial statements and includes all adjustments, consisting of normal recurring adjustments, which we consider necessary for a fair presentation thereof. Results of operations for any particular quarter are not necessarily indicative of results of operations for a full year or predictive of future periods. The results of operations for 2002 reflect the adoption of SFAS No. 142, “*Goodwill and Other Intangible Assets*.”

	2001				2002			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<i>(In thousands, except per share data)</i>								
Revenues	\$ 45,139	\$ 49,474	\$ 51,582	\$ 56,117	\$ 58,290	\$ 61,713	\$ 63,280	\$ 68,242
Earnings before income taxes	4,475	6,182	6,578	7,611	8,954	9,813	10,369	10,901
Net earnings	2,685	3,709	3,944	4,567	5,372	5,888	6,221	6,541
Diluted earnings per common share	\$ 0.17	\$ 0.19	\$ 0.19	\$ 0.22	\$ 0.26	\$ 0.28	\$ 0.30	\$ 0.31
Market prices per share:								
AMSGA:								
High	\$ 25.00	\$ 30.20	\$ 30.07	—	—	—	—	—
Low	\$ 14.13	\$ 17.63	\$ 27.07	—	—	—	—	—
AMSGB:								
High	\$ 22.88	\$ 29.75	\$ 30.00	—	—	—	—	—
Low	\$ 13.56	\$ 17.38	\$ 26.10	—	—	—	—	—
AMSG:								
High	—	—	\$ 30.36	\$ 31.13	\$ 27.87	\$ 32.70	\$ 33.85	\$ 32.44
Low	—	—	\$ 21.91	\$ 21.39	\$ 22.06	\$ 25.71	\$ 23.10	\$ 18.80

SHAREHOLDER INFORMATION

Corporate Office

AmSurg Corp.
20 Burton Hills Boulevard
Nashville, Tennessee 37215
615/665-1283

Form 10-K/Investor Contact

A copy of the AmSurg Corp. Annual Report on Form 10-K for Fiscal 2002 (without exhibits) filed with the Securities and Exchange Commission is available from the Company at no charge. These requests and other investor contacts should be directed to Claire M. Gulmi, Senior Vice President, Chief Financial Officer and Secretary, at the Company's corporate office.

Annual Shareholders' Meeting

The annual meeting of shareholders will be held on Thursday, May 22, 2003, at 9:00 a.m. in the Founders Room at the Nashville City Club, 30th Floor, 201 4th Avenue North, Nashville, Tennessee.

Registrar and Transfer Agent

SunTrust Bank, Atlanta
Corporate Trust Department
58 Edgewood Avenue, Room 225 Annex
Atlanta, Georgia 30303
800/568-3476

DIRECTORS AND OFFICERS

Ken P. McDonald

President, Chief Executive Officer
and Director

Thomas G. Cigarran ⁽¹⁾

Chairman;
Chairman, President and
Chief Executive Officer,
American Healthways, Inc.,
healthcare services

James A. Deal ⁽²⁾⁽³⁾

Director;
Chairman and Chief Executive Officer,
Geriatrics,
healthcare services

Steven I. Geringer ⁽³⁾

Director;
Former President and
Chief Executive Officer,
PCS Health Systems, Inc.,
pharmaceutical services

Debora A. Guthrie ⁽²⁾⁽³⁾

Director;
President and Chief Executive Officer
of the general partner of Capitol Health
Partners, L.P.,
healthcare venture capital

Henry D. Herr ⁽²⁾

Director;
Former Executive Vice President of Finance and
Administration and Chief Financial Officer,
American Healthways, Inc.,
healthcare services

Bergein F. Overholt, M.D. ⁽¹⁾

Director;
President,
Gastrointestinal Associates, P.C.
physician

Claire M. Gulmi

Senior Vice President,
Chief Financial Officer and Secretary

Royce D. Harrell

Senior Vice President,
Corporate Services

David L. Manning

Senior Vice President,
Development

Dennis J. Zamojski

Senior Vice President,
Operations

⁽¹⁾ Nominating and Corporate Governance Committee

⁽²⁾ Audit Committee

⁽³⁾ Compensation Committee



Executive Officers

Standing:

David L. Manning, Ken P. McDonald, Dennis J. Zamojski

Seated:

Claire M. Gulmi, Royce D. Harrell

AmSurg Corp.
20 Burton Hills Boulevard
Nashville, Tennessee 37215
615.665.1283
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