PRE PAID LEGAL SERVICES INC
Form 10-Q
May 15, 2001

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

FORM 10-Q

(Mark One)

(X) QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the quarterly period ended March 31, 2001

or

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

For the transition period from __________ to __________

Commission File Number: 1-9293

PRE-PAID LEGAL SERVICES, INC.
(Exact name of registrant as specified in its charter)

Oklahoma	73-1016728
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
321 East Main Street Ada, Oklahoma	74821-0145
(Address of principal executive offices)	(Zip Code)

(580) 436-1234
(Registrants' telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes _______ No X _______

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of May 10, 2001:

Common Stock	$.01 par value	21,343,141

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ITEM 1. FINANCIAL STATEMENTS OF REGISTRANT

PRE-PAID LEGAL SERVICES, INC.
CONSOLIDATED BALANCE SHEETS
(Amounts in 000's, except par values)

ASSETS

Current assets:
Cash and cash equivalents...
Available-for-sale investments, at fair value...................................
Membership income receivable...
Inventories...

Amount due from coinsurer...
Membership commission advance receivables.............................

Total current assets..
Available-for-sale investments, at fair value.........................
Investments pledged...
Membership commission advance receivables, net........................
Property and equipment, net...
Deferred member and associate service costs...........................
Other assets..

Total assets..

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:
Membership benefits...
Deferred Membership revenue and fees and associate fees...............
Accident and health reserves..
Life insurance reserves...
Deferred income taxes...
Capital lease obligation..
Accounts payable and accrued expenses.................................

Total current liabilities...
Deferred income taxes...
Life insurance reserves...

Total liabilities...

Stockholders' equity: Common stock, $.01 par value; 100,000 shares authorized; 24,740 issued .
Capital in excess of par value..
Retained earnings...
Accumulated other comprehensive income (loss):
Unrealized gain (losses) on investments...............................
Unrealized loss from foreign currency translation.....................
Treasury stock, at cost; 3,254 and 2,480 shares held at March 31, 2001 and December 31, 2000, respectively..

Total stockholders' equity..

Total liabilities and stockholders' equity............................

The accompanying notes are an integral part of these financial statements.

PRE-PAID LEGAL SERVICES, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Amounts in 000's, except per share amounts)
(Unaudited)

Three months end
March 31,

	2001	2
		(Rest
Revenues:		
Membership fees	$ 59,495	$ 46
Associate services	10,137	6
Other	1,186	2
	70,818	55
Costs and expenses:		
Membership benefits	20,398	15
Commissions	14,432	11
Provision for estimated uncollectible Membership commission advance receivables	1,112	
Associate services and direct marketing	8,109	4
General and administrative	6,379	5
Life insurance benefits	278	
Other, net	104	
	50,812	39
Income before income taxes	20,006	16
Provision for income taxes	6,840	5
Income before cumulative effect of change in accounting principle	13,166	10
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables	-	(4
Net income	13,166	6
Less dividends on preferred shares	-	
Net income applicable to common stockholders	$ 13,166	$ 6
Basic earnings per common share before cumulative effect of change in method of accounting for Membership commission advance receivables	$ .60	$
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables	-	
Basic earnings per common share	$ .60	$
Diluted earnings per common share before cumulative effect of change in method of accounting for Membership commission advance receivables	$ .60	$
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables	-	
Diluted earnings per common share	$ .60	$

The accompanying notes are an integral part of these financial statements.

PRE-PAID LEGAL SERVICES, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Amounts in 000's)
(Unaudited)

	Three months end March 31,	
	2001	2
		(Rest
Net income	$ 13,166	$ 6
Other comprehensive income (loss), net of tax:		
Foreign currency translation adjustment	(92)	
Unrealized gains on investments:		
Unrealized holding gains arising during period,	416	
Less: reclassification adjustment for gains included in net income	(12)	
Other comprehensive income, net of income taxes of $168 and $11	312	
Comprehensive income	$ 13,478	$ 6

The accompanying notes are an integral part of these financial statements.

PRE-PAID LEGAL SERVICES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in 000's)
(Unaudited)

	Three months end March 31,	
	2001	2
		(Rest
Cash flows from operating activities:		
Net income	$ 13,166	$ 6
Adjustments to reconcile net income to net cash provided by operating activities:		
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables	-	4

Provision for deferred income taxes	3,164	3
Provision for uncollectible Membership commission advance receivables	1,112	
Depreciation and amortization	948	
Decrease (increase) in Membership income receivable	495	
Decrease (increase) in inventories	477	
Increase in amount due from coinsurer	(1,904)	
Increase in Membership commission advance receivables	(10,713)	(10
Increase in deferred member and associate service costs	(786)	(7
(Increase) decrease in other assets	(894)	
Increase in accrued Membership benefits	363	
Increase in deferred revenue and fees	1,365	9
Increase in accident and health reserves	1,904	
Increase in life insurance reserves	94	
Increase (decrease) in accounts payable and accrued expenses	1,994	(1
Net cash provided by operating activities	10,785	5
Cash flows from investing activities:		
Additions to property and equipment	(2,804)	(1
Purchases of investments - available for sale	(1,031)	
Maturities and sales of investments - available for sale	5,934	
Net cash provided by (used in) investing activities	2,099	(1
Cash flows from financing activities:		
Proceeds from sale of common stock	-	
Decrease in capital lease obligations	(84)	
Purchases of treasury stock	(12,804)	
Dividends paid on preferred stock	-	
Net cash used in financing activities	(12,888)	
Net (decrease) increase in cash and cash equivalents	(4)	3
Cash and cash equivalents at beginning of period	11,570	10
Cash and cash equivalents at end of period	$ 11,566	$ 13
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 1	$
Income taxes paid	$ 1,000	$ 1

The accompanying notes are an integral part of these financial statements.

PRE-PAID LEGAL SERVICES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. BASIS OF PRESENTATION

The consolidated balance sheet as of March 31, 2001, and the related consolidated statements of income, comprehensive income and cash flows for the three-month periods ended March 31, 2001 and 2000 are unaudited; in the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of such financial statements have been included. The results for the three months ended March 31, 2001 are not considered indicative of the results for the full year.

These financial statements and notes are prepared pursuant to the rules and regulations of the Securities and Exchange Commission for interim reporting and should be read in conjunction with the financial statements and notes included in the Company's 2000 Annual Report on Form 10-K.

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.

SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," ("SFAS 133") was issued in June 1998. This Statement, as amended, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives), and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. The accounting for changes in the fair value of a derivative (that is, gains and losses) depends on the intended use of the derivative and the resulting designation. SFAS 133, as amended, applies to all entities and is effective for all fiscal quarters of fiscal years beginning after June 15, 2000. The Company adopted SFAS 133, as amended, on January 1, 2001 as required. The Company did not hold any derivative instruments at January 1, 2001 and there was no effect on the consolidated financial statements upon the adoption of SFAS 133.

During 2000, the Company changed its methodology for evaluating the recoverability of its commission advance receivables from terminated or "D status" sales associates. "D status" associates are those that fail to meet the Company's established vesting requirements (by failing to sell at least three new Memberships per quarter or by not retaining a personal Membership). "D status" associates lose their right to any further commissions earned on Memberships previously sold at the time they are placed in "D status" and as a result, the Company is entitled to retain all commission earnings that would be otherwise payable to these terminated associates to recover their commission advance receivable balance.

Prior to 2000, the Company "pooled" the activity of this "D status" group of former associates and accounted for the group and evaluated the collectibility of their commission advance receivables as if it were a single associate rather than on an associate by associate basis. The Company determined that it would change its methodology in 2000 such that the Company now evaluates the collectibility of "D status" commission advance receivables on an individual associate basis, as it does the commission advance receivables of its active associates. The cumulative effect of this change on prior years is reflected separately in the consolidated statement of income for the three months ended March 31, 2000 and resulted in a reduction in income (net of applicable taxes of $2.2 million) of approximately $4.1 million ($.18 per basic and diluted share) for that quarter. The effect of the change on the three months ended March 31, 2000 resulted in a reduction of income (net of applicable income taxes of $217,000) of approximately $402,000 ($.02 per basic and diluted share).

2. CONTINGENCIES

Subsequent to December 31, 2000, the Company and various of its executive officers were named in multiple putative securities class action complaints filed in both the United States District Courts for the Eastern and Western Districts of Oklahoma seeking damages on the basis of allegations that the Company issued false and misleading financial information, primarily related to the method the Company uses to account for commission advance receivables from sales associates. These complaints have been transferred to Western District of Oklahoma where motions to consolidate them into a single proceeding are pending. As of May 13, 2001, these cases were in the preliminary procedural stages relating to selection of lead counsel and lead plaintiffs as required by the Private Securities Litigation Reform Act of 1995 ("PSLRA"). After the selection of lead plaintiffs and lead counsel, the Company expects that an amended and consolidated complaint will be filed. The Company expects to file a motion to dismiss the complaint. Under PSLRA, discovery is stayed during the pendency of a motion to dismiss. Costs of defense of these cases through the motion to dismiss stage are not expected to be material. While the outcome of these cases is uncertain, the Company believes these actions are without merit and will vigorously defend these actions. However, an unfavorable decision in this litigation could have a material adverse effect on the Company's financial condition, results of operations and cash flows.

In January 2001, the Company received inquiries from the Division of Enforcement of the Securities and Exchange Commission ("SEC") requesting information relating primarily to the Company's accounting policies for commission advance receivables from sales associates. The Division of Enforcement's inquiry is informal and does not constitute a formal investigation or proceeding. At present, the Company is unable to determine the ultimate outcome of this inquiry.

Also, in January 2001 and May 2001, the staff of the SEC's Division of Corporation Finance reveiewed the Company's 1999 and 2000 Forms 10-K, respectively. On May 11, 2001, the Company received a letter from the staff of the Division of Corporation Finance advising that, after reveiwing the Company's Forms 10-K, it was the position of the Division that the Company's accounting for commission advance receivables is not in accordance with GAAP. The Company has determined that it intends to appeal the position of Division of Corporation Finance to the SEC's Office of Chief Accountant. The Company is not able to predict what the outcome of this appeal may be or when it will be resolved, but will continue to cooperate with the staff of the SEC to resolve these matters. While the Company continues to believe that its accounting for commission advance receivables conforms to generally accepted accounting principles in all material respects, there is significant risk that the SEC's Office of Chief Accountant will not agree with the Company's position. If the appeal to the Office of Chief Accountant is resolved adversely to the Company, it could have material adverse effect on the Company's financial condition and results of operations.

The Company is a named defendant in certain other lawsuits arising in the ordinary course of the Company's business. While the outcome of these lawsuits cannot be predicted with certainty, the Company does not expect these matters to have a material adverse effect on the Company's financial condition, liquidity or results of operations.

3. STOCK REPURCHASES

The Company announced on April 6, 1999, a stock repurchase program authorizing management to reacquire up to 500,000 shares of the Company's common stock. The Board of Directors has increased such authorization from 500,000 shares to 3,000,000 shares during subsequent board meetings. At March 31, 2001, the Company had repurchased 2,456,991 shares under these authorizations for a total consideration of $56.4 million, an average price of $22.94 per share.

Stock repurchases will be made at prices that are considered attractive by management and at such times that management believes will not unduly impact the Company's liquidity. No time limit has been set for completion of the repurchase program.

4. EARNINGS PER SHARE

Basic earnings per common share are computed by dividing net income applicable to common stockholders by the weighted average number of shares of common stock outstanding during the respective periods.

Diluted earnings per common share are computed by dividing net income applicable to common stockholders by the weighted average number of shares of common stock and common stock equivalents outstanding during the period. The $3.00 cumulative convertible preferred stock and the special preferred stock are considered to be dilutive common stock equivalents for the fiscal year 2000. The weighted average number of common shares is also increased by the number of shares issuable on the exercise of options less the number of common shares assumed to be purchased with the proceeds from the exercise of the options pursuant to the treasury stock method; those purchases are assumed to have been made at the average price of the common stock during the respective period.

5. SEGMENT INFORMATION

The Company derived approximately 99% and 98%, respectively of its revenues and net income from the sale of legal service plans and directly related activities during the three months ended March 31, 2001 and 2000. Revenues and net income from the Company's other operating segment (life insurance, through UFL) were approximately 1% and 2% each of the respective consolidated totals for the three months ended March 31, 2001 and 2000. UFL markets primarily to individuals, age 65 and over, in New Mexico, Oklahoma and Texas. The following table sets forth the composition of the segments and total Company revenues, net income and identifiable assets for the three months ended March 31, 2001 and 2000.

	Three months ende	
	March 31,	
	2001	2
Revenues:		
Legal service plans and directly related activities:		
Legal service plan Membership fees....................	$ 59,495	$
Associate services....................................	10,137	
Product sales...	20	
Other...	881	
Total..	$ 70,533	$
Life insurance segment (UFL):		
Life premiums and other income........................	285	
Total..	$ 285	$
Total..	$ 70,818	$

Interest Income:		
Legal service plans and directly related activities...	$ 1,126	$
Life insurance segment (UFL).........................	363	
Interest income.................................	$ 1,489	$
Net Income:		
Legal service plans and directly related activities...	$ 12,988	$
Life insurance segment (UFL).........................	178	
Net Income......................................	$ 13,166	$
Assets:		
Legal service plans and directly related activities...	$ 229,597	$ 1
Life insurance segment (UFL).........................	27,475	
Total assets....................................	$ 257,072	$ 2

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

Results of Operations

The Company reported net income applicable to common shares of $13.2 million, or $.60 per diluted common share, for the three months ended March 31, 2001, up 91% from net income applicable to common stockholders of $6.9 million, or $.30 per diluted common share, for the comparable period of the prior year after an after-tax charge of $4.1 million relating to the cumulative effect on prior years of changing the accounting for Membership commission advance receivables. The increase in the net income applicable to common shares for the 2001 period is primarily the result of increases in Membership fees for 2001 as compared to 2000.

Membership fees totaled $59.5 million during 2001 compared to $47.0 million for 2000, an increase of 27%. Membership fees and their impact on total revenues in any period are determined directly by the number of active Memberships in force during any such period. The active Memberships in force are determined by both the number of new Memberships sold in any period together with the renewal rate of existing Memberships. New Membership sales increased 12% during the three months ended March 31, 2001 to 183,712 from 163,341 during the comparable period of 2000. At March 31, 2001, there were 1,114,437 active Memberships in force compared to 890,264 at March 31, 2000, an increase of 25%. Additionally, the average annual fee per Membership has increased from $237 for all Memberships in force at March 31, 2000 to $246 for all Memberships in force at March 31, 2001, a 4% increase. This increase is a result of a higher portion of active Memberships containing the additional pre-trial hours benefit at an additional cost and increased sales of the Business Owners' Legal Solutions plan.

Associate services revenue increased 63% from $6.2 million for the first three months of 2000 to $10.1 million during the same period of 2001 primarily as a result of more new associates recruited and of the Fast Start program which generated training fees of approximately $6.0 million during the first three months of 2001 compared to $3.5 million for the comparable period of 2000. The field training program, titled Fast Start to Success ("Fast Start") is aimed at increasing the level of new Membership sales per associate. Fast Start requires a training fee of $184 per new associate and upon successful completion of the program provided for the payment of certain training bonuses through March 31, 2001. The $6.0 million and $3.5 million for the three month periods ending March 31, 2001 and 2000, respectively, in training fees was comprised of $184 from each of approximately 32,790 new sales associates who elected to participate in Fast Start during the first three months of 2001 compared to 19,240 that participated during the comparable quarter of 2000. New associates enrolled during the first three months of 2001 were 34,286 compared to 21,238 for the same period of 2000, an increase of 61%. Effective April 2001, the Company modified its compensation plan to consolidate the lower four levels of its compensation structure into two levels. At the same time, the Company implemented a two-year advance at the lowest commission level for associates who participate in the training program. Associates who do not participate in the training program receive only earned commissions until they meet the advancement qualification requiring them to produce 50 new memberships in their organization in order to advance to the next compensation level and qualify for up to 3 years commission advance.

Other income decreased from $2.7 million for the first three months of 2000 to $1.2 million during the same period of 2001, primarily due to a reduction in product sales and UFL's claims processing revenue.

Primarily as a result of the increase in Membership fees and associate services, total revenues increased to $70.8 million for the three months ended March 31, 2001 from $55.9 million during the comparable period of 2000, an increase of 27%.

Membership benefits totaled $20.4 million for the three months ended March 31, 2001 compared to $15.5 million for the comparable period of 2000, and represented 34.3% and 33.1% of Membership fees for 2001 and 2000, respectively. This Membership benefit ratio (Membership benefits as a percentage of Membership fees) should remain near 35% as substantially all active Memberships provide for a capitated benefit.

Commission expense was $14.4 million for the three months ended March 31, 2001 compared to $11.7 million for the comparable period of 2000, and represented 24.3% and 25.0% of Membership fees for such periods. Commission expense, as a percentage of Membership fees, should remain at or near 25% of Membership fees based on the existing commission structure.

The provision for estimated uncollectible Membership commission advance receivables was $1.1 million for the three months ended March 31,2001 compared to $619,000 for the comparable period of 2000, and represented 1.9% and 1.3% of Membership fees, respectively.

Associate services and direct marketing expenses increased to $8.1 million for the three months ended March 31, 2001 from $4.3 million for the comparable period of 2000. Fast Start bonuses incurred were approximately $3.6 million during the first three months of 2001 compared to $1.8 million in the same period of 2000. Additional costs due to increased enrollment of new associates and purchases of marketing and promotional supplies by associates also contributed to the increase. These expenses also include marketing costs, other than commissions, that are directly associated with new Membership sales.

General and administrative expenses during the three months ended March 31, 2001 and 2000 were $6.4 million and $5.9 million, respectively, and represented 10.7% and 12.6% of Membership fees for such years. Management expects further gradual decreases in general and administrative expenses when expressed as a percentage of Membership fees as a result of certain economies of scale.

Other expenses decreased 84% from $668,000 for the first three months of

2000 to $104,000 for the comparable period of 2001. Fee income on certain commission advance receivables was $582,000 for the first three months of 2001 compared to $357,000 for the comparable period in 2000. Depreciation and amortization increased to $948,000 for the first three months of 2001 from $603,000 for the comparable period of 2000. Product costs declined by approximately $542,000 from the first three months of 2000.

The Company has recorded a provision for income taxes of $6.8 million (34.2% of pretax income) for the first three months of 2001 compared to $5.9 million (35% of pretax income) for the same period of 2000.

The Company did not pay dividends during the first three months of 2001 due to the fact that during the second quarter of 2000, all shares of preferred stock were converted into shares of common stock or repurchased by the Company. Dividends paid on outstanding preferred stock were $2,000 for the three-month period ended March 31, 2000.

The Company and several of its officers and directors have been named as defendants in numerous putative class actions pending in the United States District Court for the Western District of Oklahoma, alleging violations of the federal securities laws in connection with the Company's accounting policies with respect to payments made to sales associates as commission advances. See Note 2 (Contingencies) to Consolidated Financial Statements. If the class actions are resolved adversely to the Company, there could be a material adverse effect on the Company's financial condition, results of operations and liquidity.

In January 2001, the Company received inquiries from the Division of Enforcement of the Securities and Exchange Commission ("SEC") requesting information relating primarily to the Company's accounting policies for commission advance receivables from sales associates. The Division of Enforcement's inquiry is informal and does not constitute a formal investigation or proceeding. At present, the Company is unable to determine the ultimate outcome of this inquiry.

Also, in January 2001 and May 2001, the staff of the SEC's Division of Corporation Finance reveiewed the Company's 1999 and 2000 Forms 10-K, respectively. On May 11, 2001, the Company received a letter from the staff of the Division of Corporation Finance advising that, after reveiwing the Company's Forms 10-K, it was the position of the Division that the Company's accounting for commission advance receivables is not in accordance with GAAP. The Company has determined that it intends to appeal the position of Division of Corporation Finance to the SEC's Office of Chief Accountant. The Company is not able to predict what the outcome of this appeal may be or when it will be resolved, but will continue to cooperate with the staff of the SEC to resolve these matters. While the Company continues to believe that its accounting for commission advance receivables conforms to generally accepted accounting principles in all material respects, there is significant risk that the SEC's Office of Chief Accountant will not agree with the Company's position. If the appeal to the Office of Chief Accountant is resolved adversely to the Company, it could have material adverse effect on the Company's financial condition and results of operations.

Liquidity and Capital Resources

General

Consolidated net cash provided by operating activities was $10.8 million for the first three months of 2001 compared to cash provided of $5.2 million for the 2000 period. The increase of $5.6 million in cash provided by operating activities during the first three months of 2001 compared to the same period of 2000 resulted primarily from the increase in net income of $6.3 million.

Consolidated net cash provided by investing activities was $2.1 million for the first three months of 2001 compared to net cash used in investing activities of $1.9 million for the comparable period of 2000. This $4.0 million increase in cash provided by investing activities resulted primarily from the $5.8 million change in the maturities and sales of investments offset by a $400,000 increase in the purchases of investments and the $1.3 million increase in net additions to property and equipment.

Net cash used in financing activities during the first three months of 2001 was $12.9 million compared to $15,000 for the comparable period of 2000. This $12.9 million change was primarily comprised of the $12.8 million used to reacquire treasury stock during the first three months of 2001.

The Company had a consolidated working capital surplus of $21.2 million at March 31, 2001, a decrease of $5.1 million compared to a consolidated working capital of $26.3 million at December 31, 2000. The $5.1 million decrease in working capital during the first three months of 2001 was primarily the result of a $1.4 million increase in deferred Membership revenue and fees and associate fees, and a $2.1 million increase in accounts payable and accrued expenses.

At March 31, 2001 the Company reported $37.0 million in cash and investments (after utilizing more than $12.8 million to repurchase approximately 774,000 shares of its common stock during the three months ending March 31, 2001) compared to $41.3 million at December 31, 2000. The Company's investments consist of common stocks, investment grade (rated Baa or higher) preferred stocks and investment grade bonds primarily issued by corporations, the United States Treasury, federal agencies, federally sponsored agencies and enterprises as well as mortgage-backed securities and state and municipal tax-exempt bonds.

The Company generally advances significant commissions at the time a Membership is sold. During the three months ended March 31, 2001, the Company advanced commissions of $25.2 million on new Membership sales compared to $22.7 million for the same period of 2000. Since approximately 94% of Membership premiums are collected on a monthly basis, a significant cash flow deficit is created at the time a Membership is sold. This deficit is reduced as monthly premiums are remitted and commissions payable on those Memberships are withheld to recover the advance. Commission advance receivables were reduced by earned commissions payable of $14.4 million and $11.7 million for the three-month periods ended March 31, 2001 and 2000, respectively. The Company assesses collectibility of its commission advance receivables quarterly and has recorded an allowance of $12.8 million to provide for estimated uncollectible balances.

Commission advance receivable activity for three months ended March 31, 2001 is as follows:

Beginning commission advance receivables.....	$ 167,193
Commission advances...	25,200
Recovery of advanced commissions.............................	(14,487)
Write-offs..	(540)
Ending commission advance receivables.........................	177,366
Allowance for unrecoverable commission advance receivables......	(11,627)
Ending commission advance receivables, net....................	$ 165,739

Commission advance receivables as of March 31, 2001 are as follows:

Active sales associates.....................................	$ 155,065
"D status" sales associates..................................	22,301
Allowance for unrecoverable commission advance receivables......	(11,627)
Commission advance receivables, net.........	

$ 165,739

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The Company believes that it has significant ability to finance expected future growth in Membership sales based on its existing amount of cash and cash equivalents and unpledged investments at March 31, 2001 of $31.0 million. The Company expects to maintain cash and investment balances on an on-going basis of approximately $30 to $40 million in order to meet expected working capital needs and regulatory capital requirements. Cash balances in excess of this amount would be used for discretionary purposes such as stock repurchases. The Company continues to consider incurring indebtedness in order to continue or increase the rate of stock repurchases, including financing its new corporate headquarters in order to allow cash flow from operations to continue to be used to repurchase stock.

Parent Company Funding and Dividends

Although the Company is the operating entity in many jurisdictions, the Company's subsidiaries serve as operating companies in various states which regulate Memberships as insurance or specialized legal expense products. The most significant of these wholly owned subsidiaries are PPLCI, UFL and PPLSIF. The ability of PPLCI, UFL and PPLSIF to provide funds to the Company is subject to a number of restrictions under various insurance laws in the jurisdictions in which PPLCI, UFL and PPLSIF conduct business, including limitations on the amount of dividends and management fees that may be paid and requirements to maintain specified levels of capital and reserves. In addition PPLCI and UFL are required to maintain its stockholders' equity at levels sufficient to satisfy various state regulatory requirements, the most restrictive of which is currently $3 million for PPLCI. Additional capital requirements of PPLCI, UFL or PPLSIF, if needed, would be funded by the Company in the form of capital contributions or surplus debentures.

FORWARD - LOOKING STATEMENTS

All statements in this report concerning Pre-Paid Legal Services, Inc. (the "Company") other than purely historical information, including but not limited to, statements relating to the Company's future plans and objectives, expected operating results, and statements regarding accounting issues raised by the staff of the Division of Corporation Finance of the Securities and Exchange Commission (See Note 2 (Contingencies) to the Consolidated Financial Statements), and the assumptions on which such forward-looking statements are based, constitute "Forward-Looking Statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Such statements are based on the Company's historical operating trends and financial condition as of March 31, 2001 and other information currently available to management. The Company cautions that the Forward-Looking Statements are subject to all the risks and uncertainties incident to its business, including (among others) those listed in the Company's Annual Report on Form 10-K and in Note 2 to the Consolidated Financial Statements included herein. Please refer to page 30 of the Company's 2000 Annual Report on Form 10-K and page 8 herein for a more complete description of the factors that could cause actual results to differ materially from those described in the forward-looking statements. Moreover, the Company may make acquisitions or dispositions of assets or businesses, enter into new marketing arrangements or enter into financing transactions. None of these can be predicted with certainty and, accordingly, are not taken into consideration in any of the Forward-Looking Statements made herein. For all of the foregoing reasons, actual results may vary materially from the Forward-Looking Statements. The Company assumes no obligation to update the Forward-Looking Statements to reflect events or circumstances occurring after the date of the statement.

Risk Factors

As noted above there are a number of risk factors which could affect our financial condition or results of operations. The status of pending SEC inquiries with respect to certain of our accounting practices has been updated as described in Note 2 (Contingencies) and Item 1, Legal Proceedings. Please refer to page 30 and 31 of the Company's 2000 Annual Report on Form 10-K for a description of other risk factors.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's consolidated balance sheets include a certain amount of assets and liabilities whose fair values are subject to market risk. Due to the Company's significant investment in fixed-maturity investments, interest rate risk represents the largest market risk factor affecting the Company's consolidated financial position. Increases and decreases in prevailing interest rates generally translate into decreases and increases in fair values of those instruments. Additionally, fair values of interest rate sensitive instruments may be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, liquidity of the instrument and other general market conditions.

As of March 31, 2001, substantially all of the Company's investments were in investment grade (rated Baa or higher) fixed-maturity investments, interest-bearing money market accounts and a collateralized repurchase agreement. The Company does not hold any investments classified as trading account assets or derivative financial instruments.

The table below summarizes the estimated effects of hypothetical increases and decreases in interest rates on the Company's fixed-maturity investment portfolio. It is assumed that the changes occur immediately and uniformly, with no effect given to any steps that management might take to counteract that change. The hypothetical changes in market interest rates reflect what could be deemed best and worst case scenarios. The fair values shown in the following table are based on contractual maturities. Significant variations in market interest rates could produce changes in the timing of repayments due to prepayment options available. The fair value of such instruments could be affected and, therefore, actual results might differ from those reflected in the following table:

	Fair Value	Hypothetical change in inter rate (bp=basis point
		(Dollars in thousands
Fixed-maturity investments at March 31, 2001 (1)...........	$21,435	100 bp increase
		200 bp increase
		50 bp decrease
		100 bp decrease
Fixed-maturity investments at December 31, 2000 (1).........	$25,480	100 bp increase

200 bp increase
50 bp decrease
100 bp decrease

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(1) Excluding short-term investments with a fair value of $3.5 million and $3.9 million at March 31, 2001 and December 31, 2000, respectively.

The table above illustrates, for example, that an instantaneous 200 basis point increase in market interest rates at March 31, 2001 would reduce the estimated fair value of the Company's fixed-maturity investments by approximately $1.7 million at that date. At December 31, 2000, an instantaneous 200 basis point increase in market interest rates would have reduced the estimated fair value of the Company's fixed-maturity investments by approximately $1.7 million at that date. The definitive extent of the interest rate risk is not quantifiable or predictable due to the variability of future interest rates, but the Company does not believe such risk is material.

The Company primarily manages its exposure to interest rate risk by purchasing investments that can be readily liquidated should the interest rate environment begin to significantly change.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

In January 2001, the Company received inquiries from the Division of Enforcement of the Securities and Exchange Commission ("SEC") requesting information relating primarily to the Company's accounting policies for commission advance receivables from sales associates. The Division of Enforcement's inquiry is informal and does not constitute a formal investigation or proceeding. At present, the Company is unable to determine the ultimate outcome of this inquiry.

Also, in January 2001 and May 2001, the staff of the SEC's Division of Corporation Finance reveiewed the Company's 1999 and 2000 Forms 10-K, respectively. On May 11, 2001, the Company received a letter from the staff of the Division of Corporation Finance advising that, after reveiwing the Company's Forms 10-K, it was the position of the Division that the Company's accounting for commission advance receivables is not in accordance with GAAP. The Company has determined that it intends to appeal the position of Division of Corporation Finance to the SEC's Office of Chief Accountant. The Company is not able to predict what the outcome of this appeal may be or when it will be resolved, but will continue to cooperate with the staff of the SEC to resolve these matters. While the Company continues to believe that its accounting for commission advance receivables conforms to generally accepted accounting principles in all material respects, there is significant risk that the SEC's Office of Chief Accountant will not agree with the Company's position. If the appeal to the Office of Chief Accountant is resolved adversely to the Company, it could have material adverse effect on the Company's financial condition and results of operations.

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

(a) Exhibits: The following exhibits are filed as part of this Form 10-Q:

No.	Description
11.1	Statement Regarding Computation of Per Share Earnings

(b) Reports on Form 8-K: The Company filed Form 8-K dated January 25, 2001 providing under Item 5 additional information pertaining to the Company's Membership commission advance receivables.

SIGNATURES

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

PRE-PAID LEGAL SERVICES, INC.

Date: May 15, 2001

/s/ Randy Harp

Randy Harp
Chief Operating Officer
(Duly Authorized Officer)

Date: May 15, 2001

/s/ Steve Williamson

Steve Williamson
Chief Financial Officer
(Principal Accounting Officer)

EXHIBIT INDEX

No.	Description
11.1	Statement Regarding Computation of Per Share Earnings

EXHIBIT 11.1

PRE-PAID LEGAL SERVICES, INC.
Statement re Computation of Per Share Earnings
(In 000's except per share amounts)
(Unaudited)

	Three months end March 31,	
	2001	2
		(Rest
Basic Earnings Per Share:		
Earnings:		
Income before cumulative effect of change in accounting principle...........	$ 13,166	$ 10
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables...............................	-	(4
Net income...	13,166	6
Less dividends on preferred shares..	-	
Net income applicable to common stockholders.............................	$ 13,166	$ 6
Shares:		
Weighted average shares outstanding..	22,002	22
Basic earnings per common share before cumulative effect of change in accounting method..	$ .60	$
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables...............................	-	
Basic earnings per common share..	$ .60	$
Diluted Earnings Per Share:		
Earnings:		
Income before cumulative effect of change in accounting principle...........	$ 13,166	$ 6
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables...............................	-	(4
Income available to common stockholders after assumed conversions...........	$ 13,166	$ 6

Shares:		
Weighted average shares outstanding	22,002	22
Assumed conversion of preferred stock	-	
Assumed exercise of options	31	
Weighted average number of shares, as adjusted	22,033	23
Diluted earnings per common share before cumulative effect on prior years of change in accounting method for Membership commission advance receivables	$ .60	$
Cumulative effect on prior years of change in method of accounting for Membership commission advance receivables	-	
Diluted earnings per common share	$ .60	$