ALICO INC
Form 10-Q
May 11, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

R Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2015

or

£ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _____________ to _____________

Commission File Number: 0-261

Alico, Inc.

(Exact name of registrant as specified in its charter)

Florida	**59-0906081**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
10070 Daniels Interstate Court, Fort Myers, FL	**33913**
(Address of principal executive offices)	*(Zip Code)*

Registrant's telephone number, including area code: **239-226-2000**

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. R Yes £ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). R Yes £ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated file £	Accelerated filer R	Non-accelerated filer £	Smaller reporting company £
	(Do not check if a smaller reporting company)		

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

£ Yes R No

There were 8,277,513 shares of common stock, par value $1.00 per share, outstanding as of May 7, 2015.

ALICO, INC.

INDEX TO FORM 10-Q

2

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements.

ALICO, INC. AND SUBSIDIARIES
CONDENSED COMBINED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)
(in thousands, except per share amounts)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2015	2014	2015	2014
Operating revenues:				
Citrus Groves	$50,371	$22,590	$63,289	$28,223
Agricultural Supply Chain Management	3,296	6,135	4,479	8,241
Improved Farmland	982	10,750	2,074	17,282
Ranch and Conservation	309	910	1,145	1,441
Other Operations	164	257	313	444
Total operating revenue	55,122	40,642	71,300	55,631
Operating expenses:				
Citrus Groves	40,349	14,699	50,476	18,243
Agricultural Supply Chain Management	2,740	5,844	4,111	8,169
Improved Farmland	1,286	8,865	2,077	14,395
Ranch and Conservation	623	1,171	1,368	1,547
Other Operations	45	90	93	507
Total operating expenses	45,043	30,669	58,125	42,861
Gross profit	10,079	9,973	13,175	12,770
Corporate general and administrative	3,381	1,834	9,294	5,622
Income from operations	6,698	8,139	3,881	7,148
Other income (expense), net:				
Interest and investment income, net	-	(9)	2	27
Interest expense	(2,285)	(396)	(3,588)	(665)
Loss on extinguishment of debt	(17)	-	(964)	-
Gain (loss) on sale of real estate	(116)	(1)	16,424	(1)
Asset impairment	(541)	-	(541)	-

Other income (loss), net	5	(44)	24	(72)
Total other income (expense), net	(2,954)	(450)	11,357	(711)
Income before income taxes	3,744	7,689	15,238	6,437
Income taxes	950	2,992	4,713	2,445
Net income **attributable to common shareholders**	2,794	4,697	10,525	3,992
Comprehensive income, net of tax effect	-	-	-	-
Comprehensive income **attributable to common shareholders**	$2,794	$4,697	$10,525	$3,992
Weighted-average number of shares outstanding:				
Basic	8,272	7,345	7,815	7,313
Diluted	8,272	7,349	7,815	7,349
Earnings **per common share:**				
Basic	$0.34	$0.64	$1.35	$0.55
Diluted	$0.34	$0.64	$1.35	$0.54
Cash dividends declared per common share	$0.06	$-	$0.12	$0.12

See accompanying notes to condensed combined consolidated financial statements (unaudited)

3

ALICO, INC. AND SUBSIDIARIES
CONDENSED COMBINED CONSOLIDATED BALANCE SHEETS (UNAUDITED)
(dollars in thousands, except share and per share amounts)

	March 31, 2015 (unaudited)	September 30, 2014 (unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 2,775	$ 31,020
Investments	264	263
Accounts receivable, net	21,206	8,724
Inventories	58,539	25,469
Deferred tax asset	71	-
Assets held for sale	1,509	59,513
Other current assets	1,511	721
Total current assets	85,875	125,710
Investment in Magnolia Fund	998	1,435
Investments, deposits and other non-current assets	6,269	2,905
Goodwill	1,146	-
Cash surrender value of life insurance	688	695
Property, buildings and equipment, net	383,446	126,833
Total assets	$ 478,422	$ 257,578
LIABILITIES & STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 4,966	$ 2,052
Long-term debt, current portion	4,511	3,196
Accrued expenses	8,685	1,934
Income taxes payable	4,085	4,572
Dividend payable	442	442
Accrued ad valorem taxes	930	1,850
Capital lease obligation	258	259

Other current liabilities	751	6,365
Total current liabilities	24,628	20,670
Long-term debt, net of current portion	205,500	58,444
Line of credit	21,975	3,160
Other liability, noncurrent	3,633	-
Deferred gain on sale	29,140	-
Capital lease obligation, noncurrent	839	839
Deferred income taxes, net of current portion	11,966	5,738
Deferred retirement benefits, net of current portion	3,883	6,877
Total liabilities	301,564	95,728
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, no par value. Authorized 1,000,000 shares; issued and outstanding, none	-	-
Common stock, $1 par value; 15,000,000 shares authorized; 8,300,363 shares issued and 8,284,173 and 7,361,340 shares outstanding at March 31, 2015 and September 30, 2014, respectively	8,300	7,377
Additional paid in capital	21,173	3,742
Treasury stock at cost 16,190 and 15,766 shares held at March 31, 2015 and September 30, 2014, respectively	(771)	(650)
Member's equity	-	15,768
Retained earnings	143,222	135,613
Total Alico stockholders' equity	171,924	161,850
Noncontrolling interest	4,934	-
Total liabilities and stockholders' equity	$ 478,422	$ 257,578

See accompanying notes to condensed combined consolidated financial statements (unaudited).

4

ALICO, INC. AND SUBSIDIARIES
CONDENSED COMBINED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(in thousands)

	Six Months Ended March 31,	
	2015	2014
Net cash (used in) provided by operating activities	$(6,261)	$4,626
Cash flows from investing activities:		
Purchases of property and equipment	(23,239)	(8,758)
Acquisition of citrus business, net of cash acquired	(264,586)	-
Proceeds from disposals of property and equipment	103,445	700
Return on investment in Magnolia	474	2,555
Collections of mortgages and notes receivable	(2)	-
Net cash used in investing activities	(183,908)	(5,503)
Cash flows from financing activities:		
Principal payments on term loan	(11,629)	(1,001)
Payoff of term loan	(34,000)	-
Borrowings on revolving line of credit	63,671	300
Repayments on revolving line of credit	(44,856)	-
Proceeds from term loans	193,500	-
Payment of loan origination fees	(3,364)	-
Treasury stock purchases	(512)	(4,713)
Capital lease payments	(2)	-
Dividends paid	(884)	(2,005)
Net cash provided by (used in) financing activities	161,924	(7,419)
Net decrease in cash and cash equivalents	(28,245)	(8,296)
Cash and cash equivalents at beginning of period	31,020	27,252
Cash and cash equivalents at end of period	$2,775	$18,956
Supplemental cash flow information:		
Cash paid for interest, net of amount capitalized	$1,213	$580
Cash paid for income taxes	$5,200	$925

See accompanying notes to condensed combined consolidated financial statements (unaudited).

ALICO, INC. AND SUBSIDIARIES

NOTES TO CONDENSED COMBINED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1. Description of Business and Basis of Presentation

Description of Business and Basis of Presentation

Alico Inc. (“Alico”), and its subsidiaries (collectively, the “Company”), are an agribusiness and land management company. The Company owns approximately 121,000 acres of land in twelve Florida counties (Alachua, Charlotte, Collier, Desoto, Glades, Hardee, Hendry, Highlands, Lee, Martin, Osceola and Polk) and includes approximately 90,000 acres of mineral rights. In addition to principal lines of business in citrus groves, improved farmland, leasing, cattle ranching and conservation, and related support operations, we also receive royalties from rock mining and oil production.

Common Control Acquisition between the Company and 734 Citrus Holdings, LLC

Effective February 28, 2015, the Company completed the merger (“Merger”) with 734 Citrus Holdings, LLC (“Silver Nip Citrus”) pursuant to an Agreement and Plan of Merger (the “Merger Agreement”) with 734 Sub, LLC, a wholly owned subsidiary of the Company (“Merger Sub”), Silver Nip Citrus and, solely with respect to certain sections thereof, the equity holders of Silver Nip Citrus. The ownership of Silver Nip Citrus was held by 734 Agriculture, 74.89%, Mr. Clay Wilson, Chief Executive Officer of the Company, 5% and an entity controlled by Mr. Clay Wilson owned, 20.11%.

On November 19, 2013, 734 Agriculture and its affiliates, including 734 Investors, acquired approximately 51% of the Company’s common stock. 734 Agriculture is the sole managing member of 734 Investors. By virtue of their ownership percentage, 734 Agriculture is able to elect all of the Directors and, consequently, control Alico.

734 Agriculture has control over both Silver Nip Citrus and the Company, and therefore the Merger was treated as a common control acquisition.

At closing of the Merger, Merger Sub merged with and into Silver Nip Citrus, with Silver Nip Citrus surviving the Merger as a wholly owned subsidiary of the Company. Pursuant to the Merger Agreement, at closing, the Company issued 923,257 shares (the “Stock Issuance”) of the Company’s common stock, par value $1.00 per share (the “Common Stock”), to the holders of membership interests in Silver Nip Citrus. Silver Nip Citrus’ outstanding net indebtedness at the closing of the Merger was approximately $40,278,000 and other liabilities totaled $6,952,000. The Company acquired assets at net book value of $65,739,000 and total net assets of $18,509,000. The shares issued were recorded at the carrying amount of the net assets transferred. The holders of membership interests in Silver Nip Citrus will also receive additional Company shares based on the value of the proceeds received by the Company from the sale of citrus fruit harvested on Silver Nip Citrus’ real property following the conclusion of the 2014-2015 citrus harvest season.

The Company expensed $811,000 in professional and legal fees in connection with the Merger in the six months ended March 31, 2015.

Basis of Presentation

Because the Company and Silver Nip Citrus were under common control, we are required under generally accepted accounting principles in the United States (“GAAP”) to account for this Common Control Acquisition in a manner similar to the pooling of interest method of accounting. Under this method of accounting, our balance sheet reflects Silver Nip Citrus’ historical carryover basis in the assets and liabilities instead of reflecting the fair market value of the assets and liabilities. We have also retrospectively recast our financial statements to combine the operating results of the Company and Silver Nip Citrus from the date common control began, November 19, 2013.

The accompanying (a) condensed combined consolidated balance sheet as of September 30, 2014, which has been derived from financial statements, and (b) unaudited condensed combined consolidated interim financial statements (the “Financial Statements”) of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). The Financial Statements include all adjustments, consisting of normal and recurring adjustments, which in the opinion of management were necessary for a fair presentation of the financial position, results of operations and cash flows for the periods presented. The results of the interim period are not necessarily indicative of the results for any other interim periods or the entire fiscal year.

Due to the fact Silver Nip Citrus' fiscal year end is June 30, the Company's condensed combined consolidated financial condition as of March 31, 2015 includes the financial condition of Silver Nip Citrus as of December 31, 2014, and the Company's condensed combined consolidated results of operations for the six months ended March 31, 2015 includes the Silver Nip Citrus results of operations for the six months ended December 31, 2014. The Company's combined consolidated financial condition as of March 31, 2014 reflects the financial condition of Silver Nip Citrus as of December 31, 2013, and the Company's condensed combined consolidated results of operations for the six months ended March 31, 2014 includes Silver Nip Citrus' results of operations from November 19, 2013 (the initial date of common control) through December 31, 2013.

The Financial Statements have been presented according to the rules and regulations of the Securities and Exchange Commission ("SEC"), instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Certain information, footnotes and disclosures normally included in annual financial statements, prepared in accordance with GAAP, have been condensed or omitted in accordance with those rules and regulations. The Company believes that the disclosures made are adequate to make the information not misleading. The Financial Statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended September 30, 2014.

Principles of Consolidation

The Financial Statements include the accounts of Alico, Inc. and its subsidiaries. The Company's subsidiaries include: Alico Land Development, Inc., Alico-Agri, Ltd., Alico Plant World, LLC, Alico Fruit Company, LLC (formerly Bowen Brothers Fruit Company, LLC"), Alico Citrus Nursery, LLC, 734 Citrus LLC and Citree Holdings 1, LLC. All significant intercompany accounts and transactions have been eliminated in consolidation.

Noncontrolling Interests in Consolidated Affiliate

The condensed combined consolidated financial statements include all assets and liabilities of the less-than-100%-owned affiliate the Company controls, Citree Holdings I, LLC ("Citree"). Accordingly, the Company has recorded noncontrolling interests in the equity of such entity. Citree did not have any income or loss for the quarter ended March 31, 2015, and therefore there is no allocation of income or loss to the noncontrolling interest holders based upon the portion of the subsidiary they own.

Business Combinations

The Company accounts for its business acquisitions under the acquisition method of accounting as indicated in ASC No. 805, Business Combinations, which requires the acquiring entity in a business combination to recognize the fair value of all assets acquired, liabilities assumed and any noncontrolling interest in the acquiree, and establishes the acquisition date as the fair value measurement point. Accordingly, the Company recognizes assets acquired and liabilities assumed in business combinations, including contingent assets and liabilities and noncontrolling interest in the acquiree, based on fair value estimates as of the date of acquisition. In accordance with ASC No. 805, the Company recognizes and measures goodwill, if any, as of the acquisition date, as the excess of the fair value of the consideration paid over the fair value of the identified net assets acquired.

When we acquire a business from an entity under common control, whereby the companies are ultimately controlled by the same party or parties both before and after the transaction, it is treated similar to the pooling of interest method of accounting, whereby the assets and liabilities are recorded at the transferring entity’s historical cost instead of reflecting the fair market value of assets and liabilities.

Reclassifications

Certain reclassifications have been made to the prior years’ consolidated financial statements to conform to the fiscal year 2015 presentation. These reclassifications had no impact on working capital, net income, stockholders’ equity or cash flows as previously reported.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States (“GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses 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 based upon future events. The Company periodically evaluates the estimates. The estimates are based on current and expected economic conditions, historical experience and various other specific assumptions that the Company believes to be reasonable.

Seasonality

The Company is primarily engaged in the production of fruit for sale to citrus markets, which is of a seasonal nature and subject to the influence of natural phenomena and wide price fluctuations. Historically, the second and third quarters of our fiscal year generally produce the majority of our annual revenue, and our working capital requirements are typically greater in the first and fourth quarters of our fiscal year. The results of the reported period herein are not necessarily indicative of the results for any other interim periods or the entire fiscal year.

Note 2. Inventories

A summary of the Company's inventories consisted of the following at March 31, 2015 and September 30, 2014:

(in thousands)	March 31, 2015	September 30, 2014
Unharvested fruit crop on the trees	$52,139	$23,502
Beef cattle	2,538	1,022
Nursery	1,876	516
Other	1,986	429
Total Inventories	$58,539	$25,469

Note 3. Property, Buildings and Equipment, Net

Property, buildings and equipment consisted of the following at March 31, 2015 and September 30, 2014:

(in thousands)	March 31, 2015	September 30, 2014

Breeding herd	$10,897	$11,558
Buildings	21,010	16,052
Citrus trees	242,278	66,886
Equipment and other facilities	58,412	55,696
Total depreciable properties	332,597	150,192
Less accumulated depreciation and depletion	(72,158)	(63,031)
Net depreciable properties	260,439	87,161
Land and land improvements	123,007	39,672
Net property, buildings and equipment	$383,446	$126,833

Land Purchase

Silver Nip Citrus purchased approximately 1,500 acres of citrus groves that included land, trees and fruit inventory as well as irrigation and other equipment on September 4, 2014. The purchase price was approximately $17,600,000 which was funded through cash plus additional financing of $11,000,000 in term debt (see “Note 7. Long -Term Debt” in the Notes to the Condensed Combined Consolidated Financial Statements (Unaudited)).

Land Sale

Certain Silver Nip Citrus land with a cost of $2,832,159 was classified as held for sale as of September 30, 2014. It was sold during the six month period ended March 31, 2015 resulting in a gain on sale of assets of $2,926,553.

Asset Impairment

The Company recorded an impairment loss of approximately $541,000 during the quarter ended March 31, 2015 on property classified as Assets Held for Sale. The Company entered into a sales contract on February 17, 2015, which triggered the impairment of the property based on the negotiated sales price. The property was closed on April 3, 2015 and the Company received approximately $1,509,000 in net sales proceeds.

Note 4. Orange-Co Acquisition

On December 2, 2014, the Company completed the acquisition of certain citrus and related assets of Orange-Co, LP (“Orange-Co”) pursuant to an Asset Purchase Agreement, which we refer to as the Orange-Co Purchase Agreement, dated as of December 1, 2014 and 51% of the ownership interests of Citree Holdings 1, LLC. The assets Alico purchased include approximately 20,263 acres of citrus groves in DeSoto and Charlotte Counties, Florida, which comprise one of the largest contiguous citrus grove properties in the state of Florida. The total purchase price was approximately $276,673,300, net of $2,060,000 in cash acquired, including: (1) $147,500,000 in initial cash consideration funded from the proceeds of the sugarcane disposition (see “Note 5. Assets held for sale” in the Notes to the Condensed Combined Consolidated Financial Statements (Unaudited)) and new term debt; (2) up to $7,500,000 in additional cash consideration to be released from escrow in equal parts, subject to certain limitations, on December 1, 2015 and June 1, 2016; (3) the refinancing of Orange-Co’s outstanding debt including approximately $91,371,000 in term debt and a working capital facility of approximately $27,775,000 and (4) the assumption of certain other liabilities totaling $4,587,000. On December 1, 2014, Alico deposited an irrevocable standby letter of credit issued by Rabo Agrifinance, Inc., or Rabo, in the aggregate amount of $7,500,000 into an escrow account to fund the additional cash consideration.

The Company acquired Orange-Co to transform our citrus business and meaningfully enhance the Company’s position in the citrus industry. The Company has included the financial results of Orange-Co in the consolidated financial statements from the date of acquisition in the Citrus Groves operating segment. These results include approximately $37,625,000 in revenue and $7,786,000 in gross profit.

This acquisition was accounted for under the acquisition method of accounting. Accordingly, the Company recognized amounts for identifiable assets acquired and liabilities assumed at their estimated acquisition date fair values, while transaction and integration costs associated with the acquisition were expensed as incurred. The excess of the purchase price over the fair value of assets acquired, net of liabilities assumed, and noncontrolling interests is recognized as goodwill. All goodwill recognized will be deductible for income tax purposes. The initial accounting for the business combination is not complete and adjustments to provisional amounts, or recognition of additional assets acquired or liabilities assumed, may occur as more detailed analyses are completed and additional information is obtained about the facts and circumstances that existed as of the acquisition date.

The Company expensed $3,037,000 in professional and legal fees in connection with the Orange-Co acquisition, in the six months ended March 31, 2015.

The following table summarizes the consideration paid for the acquired assets and the preliminary acquisition accounting for the fair values of the assets recognized and liabilities assumed in the Condensed Combined Consolidated Balance Sheets at the acquisition date. These balances are subject to change when final asset valuations are obtained and the potential for liabilities has been evaluated.

Asset acquisition

(in thousands)	Amount
Assets	
Accounts receivable	$888
Other current assets	845
Inventories	35,562
Property, Buildings and Equipment:	
Equipment and other facilities	13,432
Land	63,337
Citrus trees	164,053
Goodwill	1,146
Other assets	2,344
Total assets, net of cash acquired	$281,607
Liabilities	
Accounts payable and accrued liabilities	$4,087
Term loan	500
Payable to seller	7,500
Total liabilities assumed	$12,087
Assets acquired less liabilities assumed	$269,520
Less: fair value attributable to noncontrolling interest	(4,933)
Total purchase consideration	$264,587

The fair value of the consideration paid for the acquisition of the net assets was as follows:

Cash proceeds from sugarcane disposition	$97,126
Working capital line of credit	27,775
Term loans	139,686
Total purchase consideration	$264,587

The unaudited pro-forma information below for the three and six months ended March 31, 2015 and 2014 gives effect to this acquisition as if the acquisitions had occurred on October 1, 2013. The pro-forma financial information is not necessarily indicative of the results of operations if the acquisition had been effective as of this date.

(in thousands except per share amount)	Three Months Ended March 31, 2015	2014	Six Months Ended March 31, 2015	2014
Revenues	$55,122	$66,326	$71,828	$89,856
Income from operations	$6,698	$17,073	$3,865	$17,641
Net income attributable to common shareholder	$2,794	$9,902	$10,065	$9,435
Basic earnings per common share	$0.34	$1.35	$1.29	$1.29
Diluted earnings per common share	$0.34	$1.35	$1.29	$1.28

Note 5. Assets Held for Sale

Sugarcane land

On November 21, 2014, the Company completed the sale of approximately 36,000 acres of land used for sugarcane production and land leasing in Hendry County, Florida to Global Ag Properties, LLC ("Global Ag Properties") for $97,913,921 in cash. We had previously leased approximately 30,600 of these acres to United States Sugar Corporation (the "USSC Lease"). The USSC Lease was assigned to Global Ag Properties in conjunction with the land sale.

Net proceeds from the sugarcane land sale of $97,126,000 were deposited with a Qualified Intermediary in anticipation of the Orange-Co asset acquisition in a tax deferred like kind exchange pursuant to Internal Revenue Code Section §1031 (see "Note 4. Orange-Co Acquisition" in the Notes to the Condensed Combined Consolidated Financial Statements (Unaudited)).

The sales price is subject to post-closing adjustments over a ten (10)-year period. The Company realized a gain of $42,753,000 on the sale. However, $29,140,000 of the gain has been deferred due to the Company's continuing involvement in the property pursuant to a post-closing agreement and the potential price adjustments. The deferral represents the Company's estimate of the maximum exposure to loss as a result of the continuing involvement. A net gain of $13,613,000 was recognized in the financial statements as of and for the six months ended March 31, 2015.

As a result of the disposition of our sugarcane land, we are no longer involved in sugarcane operations, and, as of November 21, 2014, the Improved Farmland segment was no longer material to our business, however, the sugarcane operation has not been classified as a discontinued operation due to the post-closing adjustments, amongst other involvement, as described above.

Our sugarcane land was classified as assets held for sale as of September 30, 2014.

Asset held for sale

(in thousands)	March 31, 2015
Land and land improvements	$2,050
Impairment	(541)
Assets held for sale	$1,509

Note 6. Income Taxes

The Company's effective tax rates were 31.0% and 38% for the six months ended March 31, 2015 and 2014, respectively.

The Company applies a "more likely than not" threshold to the recognition and nonrecognition of tax positions. A change in judgment related to prior years' tax positions is recognized in the quarter of such change. The Company had no reserve for uncertain tax positions at March 31, 2015 and September 30, 2014. The Company recognizes interest and/or penalties related to income tax matters in income tax expense and in income taxes payable.

The Internal Revenue Service ("IRS") is currently auditing Alico's tax return for the fiscal year ended September 30, 2013.

Note 7. Long-Term Debt

Outstanding debt under the Company's various loan agreements is presented in the table below:

(in thousands)

	March 31, 2015	September 30, 2014
Long-term debt, net of current portion:		
Metropolitan Life Insurance Company and New England Life Insurance Company fixed rate term loans in the original principal amount of $125 million: the loans bear interest at the rate of 4.15%. The loans are collateralized by real estate and mature in November 2029.	$ 114,688	$ -
Metropolitan Life Insurance Company and New England Life Insurance Company variable rate term loans in the original principal amounts of $57.5 million: the variable interest rate was 1.75% at March 31, 2015. The loans are collateralized by real estate and mature in November 2029.	56,781	-
Metropolitan Life Insurance Company term loan: the loan bears interest at the initial rate of 5.49%. A final advance of $4.5 million is scheduled for December 1, 2015 subject to certain performance conditions. The interest rate is subject to adjustment on the date of the final advance. The loan is secured by real estate and matures in February 2029.	500	-
Rabo Agrifinance, Inc. variable rate term loan: the variable interest rate on this loan was 2.40% at September 30, 2014. The loan was secured by real estate and had a maturity date of October 2020. The loan was refinanced on December 3, 2014.	-	34,000
Prudential Mortgage Capital Company, LLC fixed rate term loans: the loans bear interest at the rate of 5.35%. The loans are collateralized by real estate and mature in June 2033.	26,970	27,550
Prudential Mortgage Capital Company, LLC fixed rate term loan: the loan bears interest at the rate of 3.85%. The loan is collateralized by real estate and matures in September 2021.	5,500	-
Prudential Mortgage Capital Company, LLC fixed rate term loan: the loan bears interest at the rate of 3.45%. The loan is collateralized by real estate and matures in September 2039.	5,500	-
Note payable to a financing company secured by equipment and maturing in December 2016	72	90
	210,011	61,640
Less current portion	4,511	3,196

Long-term debt	$ 205,500	$ 58,444

12

(in thousands)

	March 31, 2015	September 30, 2014
Lines of Credit:		
Metropolitan Life Insurance Company and New England Life Insurance Company revolving line of credit: this $25 million line bears interest at a variable rate which was 1.75% at March 31, 2015. The line is secured by real estate and matures in November 2019.	$-	$ -
Rabo Agrifinance, Inc. working capital line of credit: this $70 million line bears interest at a variable rate which was 1.92% at March 31, 2015. The line is secured by personal property and matures in November 2016. Availability under the line was $36.3 million at March 31, 2015.	16,239	-
Rabo Agrifinance, Inc. revolving line of credit: this $60 million line bore interest at a variable rate which was 2.10% at September 30, 2014. The entire $60 million balance was available at September 30, 2014. The line was secured by real estate and had a maturity date of October 2020. The loan was refinanced on December 3, 2014.	-	-
Prudential Mortgage Capital Company, LLC revolving line of credit: this $6 million line bears interest at a variable rate which was 3.00% at December 31, 2014 and 2.98% at June 30, 2014, respectively. The line is secured by real estate and matures in June 2018. Availability under the line was $264,000 at December 31, 2014 and $2,840,000 at June 30, 2014.	5,736	3,160
Lines of Credit	$21,975	$ 3,160

Refinancing on December 3, 2014

The Company refinanced its outstanding debt on December 3, 2014 in connection with the Orange-Co acquisition (see "Note 4. Orange-Co Acquisition" in the Notes to the Condensed Combined Consolidated Financial Statements (Unaudited)). The debt facilities include $114,688,000 in fixed rate term loans, $56,781,000 in variable rate term loans and a $25,000,000 revolving line of credit ("RLOC") with Metropolitan Life Insurance Company and New England Life Insurance Company (collectively "Met") and a $70,000,000 working capital line of credit ("WCLC") with Rabo Agrifinance, Inc. ("Rabo").

The term loans and RLOC are secured by approximately 38,700 gross acres of citrus groves and 14,000 gross acres of farmland. The WCLC is secured by current assets and certain other personal property owned by the Company.

The term loans are subject to quarterly principal payments of $2,281,250 and mature November 1, 2029. The fixed rate term loans bear interest at 4.15%, and the variable rate term loans bear interest at a rate equal to 90 day LIBOR plus 150 basis points (the "LIBOR spread"). The LIBOR spread is subject to adjustment by the lender on May 1, 2017 and every two years thereafter. Interest on the term loans is payable quarterly.

The Company may prepay up to $8,750,000 of the fixed rate term loan principal annually without penalty, and any such prepayments shall be applied to reduce subsequent mandatory principal payments. The maximum annual prepayment has been made for the current fiscal year. The variable rate term loans may be prepaid without penalty.

The RLOC bears interest at a floating rate equal to 90 day LIBOR plus 150 basis points payable quarterly. The LIBOR spread is subject to adjustment by the lender on May 1, 2017 and every two years thereafter. Outstanding principal, if any, is due at maturity on November 1, 2019. The RLOC is subject to an annual commitment fee of 25 basis points on the unused portion of the line. The RLOC is available for funding general corporate needs.

The WCLC is a revolving credit facility and is available for funding working capital and general corporate needs. The interest rate on the WCLC is based on the one month LIBOR plus a spread. The spread is adjusted quarterly based on our debt service coverage ratio for the preceding quarter and can vary from 175 to 250 basis points. The rate is currently at LIBOR plus 175 basis points. The WCLC facility matures November 1, 2016.

The WCLC is subject to a quarterly commitment fee on the daily unused availability under the line computed as the commitment amount less the aggregate of the outstanding loans and outstanding letters of credit. The commitment fee is adjusted quarterly based on our debt service coverage ratio for the preceding quarter and can vary from 20 to 30 basis points.

The WCLC agreement provides for Rabo to issue up to $20,000,000 in letters of credit on our behalf. At March 31, 2015, there was $17,498,500 in outstanding letters of credit which correspondingly reduced our availability under the line of credit.

The Company capitalized approximately $2,834,000 of debt issuance costs and recognized a loss on extinguishment of debt of approximately $585,000.

The facilities above are subject to various covenants including the following financial covenants (1) minimum debt service coverage ratio of 1.10 to 1.00, (2) tangible net worth of at least $160,000,000 increased annually by 10% of consolidated net income for the preceding year, (3) minimum current ratio of 1.50 to 1.00 (4) debt to total assets ratio not greater than .625 to 1.00, and, solely in the case of the WCLC, (5) a limit on capital expenditures of $30,000,000 per fiscal year. The Company is in compliance with all covenants at March 31, 2015.

Debt Prior to Refinancing

Prior to the December 3, 2014 refinancing, the Company had a $34,000,000 term loan and a $60,000,000 revolving line of credit (“Old RLOC”) with Rabo.

The term loan required quarterly payments of interest at a floating rate of one month LIBOR plus 225 basis points and quarterly principal payments of $500,000. The term loan was refinanced in connection with the Orange-Co acquisition.

The Old RLOC had an interest rate based on one month LIBOR plus a spread. The spread was determined based upon our debt service coverage ratio for the preceding fiscal year and could vary from 195 to 295 basis points. The rate was LIBOR plus 195 basis points at the date of the refinancing and September 30, 2014. Interest on the Old RLOC was payable quarterly. The Old RLOC was subject to an unused commitment fee of 20 basis points on the annual average unused availability. There was no balance outstanding at the time of the refinancing or September 30, 2014.

Loan origination fees incurred as a result of entry into the Rabo credit facility loan agreement, including appraisal fees, document stamps, legal fees and lender fees of approximately $1,202,000 were capitalized in fiscal year 2010 and were being amortized over the term of the loan agreement. The unamortized balance of the loan origination fees at the time of December 3, 2014 refinancing was approximately $697,000 of which approximately $396,000 was expensed as a loss on extinguishment of debt and approximately $301,000 will be amortized over the applicable terms of the new loans.

At September 30, 2014, the Company was in compliance with the financial debt covenants and terms of the Rabo loan agreement.

Silver Nip Citrus Debt

Silver Nip Citrus has five loans payable to Prudential Mortgage Capital Company, LLC (“Prudential”) as described below.

There are two fixed rate term loans with total outstanding balances of $26,970,000 and $27,550,000 at December 31, 2014 and June 30, 2014, respectively. Principal of $290,000 is payable quarterly. Interest accrues at 5.35% and is also payable quarterly. The Company may prepay up to $5,000,000 of principal without penalty. The loan is secured by real estate in Collier, Hardee, Hendry, Highlands, Martin, Osceola and Polk Counties, Florida.

In connection with the purchase of 1,500 acres of citrus grove on September 4, 2014 (see “Note 3. Property, Buildings and Equipment, Net” in the Notes to the Condensed Combined Consolidated Financial Statements (Unaudited)), Silver Nip Citrus has a fixed rate term loan with Prudential with an outstanding balance of $5,500,000 at December 31, 2014 that bears interest at the rate of 3.85%. Principal in the amount of $55,000 is payable quarterly together with accrued interest. The loan is secured by real estate in Charlotte County, Florida.

Silver Nip Citrus also has a fixed rate term loan with Prudential with an outstanding balance of $5,500,000 at December 31, 2014 that bears interest at the rate of 3.45%. The rate is subject to adjustment on September 1, 2019 and every five years thereafter until maturity. Principal of $55,000 is payable quarterly together with accrued interest. The loan is secured by real estate in Charlotte County, Florida.

Silver Nip Citrus has a $6,000,000 revolving line of credit with Prudential. Outstanding balances were $5,736,000 and $3,160,000 at December 31, 2014 and June 30, 2014, respectively. The interest rate on the line is based the three month LIBOR rate plus 275 basis points. Interest is payable semi-annually with outstanding principal due at maturity.

The Silver Nip Citrus facilities are subject to a financial covenant requiring a current ratio of at least 2.00 to 1.00 measured at the end of each fiscal year. The Company was in compliance with all covenants related to the Silver Nip debt at June 30, 2014.

The Silver Nip Citrus facilities are personally guaranteed by George Brokaw, Remy Trafelet and Clayton Wilson.

Debt Maturities

Maturities of the Company's debt were as follows at March 31, 2015:

(in thousands)	
Due within one year	$4,511
Due between one and two years	24,504
Due between two and three years	10,750
Due between three and four years	16,586
Due between four and five years	10,938
Due beyond five years	164,697
Total	$231,986

Interest costs expensed and capitalized to property, buildings and equipment were as follows:

(in thousands)	Three Months Ended March 31,		Six Months Ended March 31,	
	2015	2014	2015	2014

Interest expense	$2,285	$396	$3,588	$665
Interest capitalized	159	40	212	69
Total	$2,444	$436	$3,800	$734

Note 8. Disclosures about reportable segments

The Company manages its land based upon its primary usage and reviews its performance based upon three primary classifications – Citrus Groves, Improved Farmland and Ranch and Conservation. In addition, it operates an Agricultural Supply Chain Management business that is not tied directly to its land holdings and Other Operations that include a citrus nursery and leasing mines and oil extraction rights to third parties. The Company presents its financial results and the related discussions based upon these five segments (Citrus Groves, Improved Farmland, Ranch and Conservation, Agricultural Supply Chain Management and Other Operations). A description of the Company's business segments is as follows:

- Citrus Groves include activities related to planting, owning, cultivating and/or managing citrus groves in order to produce fruit for sale to fresh and processed citrus markets.

- Agricultural Supply Chain Management and Support includes activities related to the purchase and resale of fruit, as well as, to value-added services which include contracting for the harvesting, marketing and hauling of citrus.

- Improved Farmland includes activities related to owning and/or leasing improved farmland. Improved farmland is acreage that has been converted, or is permitted to be converted, from native pasture and which has various improvements including irrigation, drainage and roads.

- Ranch and Conservation includes activities related to cattle grazing, sod, native plant and animal sales, leasing, management and/or conservation of unimproved native pasture land.

- Other Operations include activities related to rock mining royalties, oil exploration, a citrus nursery and other insignificant lines of business.

Intersegment sales and transfers are accounted by the Company as if the sales or transfers were to third parties at current market prices. Goods and services produced by these segments are sold to wholesalers and processors in the United States who prepare the products for consumption. The Company evaluates the segments performance based on direct margins from operations before general and administrative costs, interest expense and income taxes not including nonrecurring gains and losses.

The accounting policies of the segments are the same as those described in Note 1, Description of Business and Basis of Presentation. Total revenues represent sales to unaffiliated customers, as reported in the Company’s Condensed Combined Consolidated Statement of Comprehensive Income. All intercompany transactions have been eliminated.

16

Information by business segment is as follows:

(in thousands)	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014	Six Months Ended March 31, 2015	Six Months Ended March 31, 2014
Revenues:				
Citrus Groves	$50,371	$22,590	$63,289	$28,223
Agricultural Supply Chain Management	3,296	6,135	4,479	8,241
Improved Farmland	982	10,750	2,074	17,282
Ranch and Conservation	309	910	1,145	1,441
Other Operations	164	257	313	444
Intersegment Revenues	4,115	4,000	5,386	6,245
Eliminations	(4,115)	(4,000)	(5,386)	(6,245)
Total revenue	55,122	40,642	71,300	55,631
Operating expenses:				
Citrus Groves	40,349	14,699	50,476	18,243
Agricultural Supply Chain Management	2,740	5,844	4,111	8,169
Improved Farmland	1,286	8,865	2,077	14,395
Ranch and Conservation	623	1,171	1,368	1,547
Other Operations	45	90	93	507
Total operating expenses	45,043	30,669	58,125	42,861
Gross profit:				
Citrus Groves	10,022	7,891	12,813	9,980
Agricultural Supply Chain Management	556	291	368	72
Improved Farmland	(304)	1,885	(3)	2,887
Ranch and Conservation	(314)	(261)	(223)	(106)
Other Operations	119	167	220	(63)
Total gross profit	$10,079	$9,973	$13,175	$12,770
Capital expenditures:				
Citrus Groves	$17,661	$2,083	$19,230	$4,026
Agricultural Supply Chain Management	119	38	329	71
Improved Farmland	-	212	-	3,685
Ranch and Conservation	14	33	190	776
Other Operations	3,396	196	3,411	200
Other Capital Expenditures	-	(343)	79	-
Total capital expenditures	$21,190	$2,219	$23,239	$8,758

Depreciation, depletion and amortization:				
Citrus Groves	$3,584	$525	$4,840	$1,054
Agricultural Supply Chain Management	93	53	145	82
Improved Farmland	-	1,285	-	2,622
Ranch and Conservation	242	329	485	662
Other Operations	270	21	398	109
Other Depreciation, Depletion and Amortization	36	214	200	400
Total depreciation, depletion and amortization	$4,225	$2,427	$6,068	$4,929

17

(in thousands)	March 31, 2015	September 30, 2014
Assets:		
Citrus Groves	$422,070	$121,399
Agricultural Supply Chain Management	3,097	2,498
Improved Farmland	119	57,726
Ranch and Conservation	13,384	13,920
Other Operations	31,292	26,356
Other Corporate Assets	8,460	35,679
Total assets	$478,422	$257,578

Note 9. Stockholders’ Equity

Effective January 27, 2015, the Company’s Board of Directors adopted the Stock Incentive Plan of 2015 (the “2015 Plan”) which provides for up to an additional 1,250,000 shares available for issuance to provide a long-term incentive plan for officers, employees, directors and/or consultants to directly link incentives to shareholders value. The 2015 Plan was approved by shareholders on February 25, 2015.

The adoption of the 2015 Plan superseded the 2013 Incentive Equity Plan (“2013 Plan”), which had been in place since April 2013.

There are no awards outstanding under the 2015 Plan or the 2013 Plan at March 31, 2015 or September 30, 2014.

In March 2015, the Board of Directors authorized the repurchase of up to 20,000 shares of the Company’s common stock beginning March 25, 2015 and continuing through March 25, 2016. The stock repurchases were made through open market transactions at times and in such amounts as the Company’s broker determined subject to the provisions of SEC Rule 10b-18. All repurchases were made on or subsequent to March 25, 2015. The following table illustrates the Company’s treasury stock purchases and issuances for the six months ended March 31, 2015:

(in thousands, except share amounts)	Shares	Cost
Balance at September 30, 2014	15,766	$650
Purchased	9,907	512

Issued to Directors and Named Executive Officers	(9,483)	(391)
Balance at March 31, 2015	16,190	$771

Stock-based compensation expense recognized in the Condensed Combined Consolidated Statements of Comprehensive Income in general and administrative expenses was $254,000 and $509,000 for the three and six months ended March 31, 2015, respectively, and $204,000 and $705,000 for the three and six months ended March 31, 2014, respectively. Stock-based compensation is recorded for Board of Directors fees paid in treasury stock and the Long Term Incentive Compensation Plan restricted common stock awards.

Note 10. Commitments and Contingencies

On March 11, 2015, a putative shareholder class action lawsuit was filed by Shiva Y. Stein in the Circuit Court of the Twentieth Judicial District in and for Lee County, Florida, against Alico, Inc. ("Alico"), its current and certain former directors, 734 Citrus Holdings, LLC d/b/a Silver Nip Citrus ("Silver Nip"), 734 Investors, LLC ("734 Investors"), 734 Agriculture, LLC ("734 Agriculture") and 734 Sub, LLC ("734 Sub") in connection with the acquisition of Silver Nip by Alico (the "Acquisition"). The complaint alleges that Alico's directors at the time of the Acquisition, 734 Investors and 734 Agriculture breached fiduciary duties to Alico stockholders in connection with the Acquisition and that Silver Nip and 734 Sub aided and abetted such breaches. The lawsuit seeks, among other things, monetary and equitable relief, costs, fees (including attorneys' fees) and expenses. We believe that this lawsuit is without merit and intend to contest it vigorously.

From time to time, we may be involved in litigation relating to claims arising out of our operations in the normal course of business. There are no current legal proceedings to which we are a party to or which any of our property is subject to that we believe will have a material adverse effect on our business, financial condition or results of operations.

Note 11. Related Party Transactions

Change in Control Transaction

On November 19, 2013, 734 Agriculture, LLC (“734 Agriculture”) and its affiliates, including 734 Investors, LLC (“734 Investors”), completed the previously announced purchase from Alico Holding, LLC, a company wholly owned by Atlantic Blue Group, Inc. (“Atlanticblue”), of 3,725,457 shares of our common stock (the “Share Purchase”).

The common stock acquired by 734 Agriculture and its affiliates, including 734 Investors, represented approximately 51% of the Company’s outstanding voting securities. On November 15, 2013, 734 Investors amended and restated its LLC operating agreement (the “LLC Agreement”) to admit new members and to designate 734 Agriculture as the managing member, with authority to administer the affairs of 734 Investors, including the voting and disposition of shares of common stock, subject to certain restrictions set forth therein. As a result, upon the consummation of the Share Purchase, 734 Agriculture and its affiliates, including 734 Investors, acquired the voting power to control the election of the Company’s Directors and any other matter requiring the affirmative vote or consent of the Company’s shareholders. Messrs. Remy W. Trafelet and George R. Brokaw are the two controlling persons of 734 Agriculture.

Appointment of Mr. Wilson as the Company’s Chief Executive Officer

Upon the Closing of the Share Purchase, Mr. JD Alexander ceased to be the Company’s CEO pursuant to his previously disclosed resignation. On November 22, 2013, the Board appointed Mr. Wilson to serve as the CEO, effective immediately.

Silver Nip Merger Agreement

Effective February 28, 2015, the Company completed the merger ("Merger") with 734 Citrus Holdings, LLC ("Silver Nip Citrus") pursuant to an Agreement and Plan of Merger (the "Merger Agreement") with 734 Sub, LLC, a wholly owned subsidiary of the Company ("Merger Sub"), Silver Nip Citrus and, solely with respect to certain sections thereof, the equity holders of Silver Nip Citrus. The ownership of Silver Nip Citrus was held by 734 Agriculture, 74.89%, Mr. Clay Wilson, Chief Executive Officer of the Company, 5% and an entity controlled by Mr. Clay Wilson owned, 20.11%.

On November 19, 2013, 734 Agriculture and its affiliates, including 734 Investors, acquired approximately 51% of the Company's common stock. 734 Agriculture is the sole managing member of 734 Investors. By virtue of their ownership percentage, 734 Agriculture is able to elect all of the Directors and, consequently, control Alico.

734 Agriculture has control over both Silver Nip Citrus and the Company and therefore the Merger was treated as a common control acquisition.

At closing of the Merger, Merger Sub merged with and into Silver Nip Citrus, with Silver Nip Citrus surviving the Merger as a wholly owned subsidiary of the Company. Pursuant to the Merger Agreement, at closing, the Company issued 923,257 shares (the "Stock Issuance") of the Company's common stock, par value $1.00 per share (the "Common Stock"), to the holders of membership interests in Silver Nip Citrus. Silver Nip Citrus' outstanding net indebtedness at the closing of the Merger was approximately $40,278,000 and other liabilities totaled $6,952,000. The Company acquired assets at net book value of $65,739,000 and total net assets of $18,509,000. The shares issued were recorded at the carrying amount of the net assets transferred. The holders of membership interest in Silver Nip Citrus will also receive additional Company shares based on the value of the proceeds received by the Company from the sale of citrus fruit harvested on Silver Nip Citrus' real property following the conclusion of the 2014-2015 citrus harvest season.

The Company expensed $811,000 in professional and legal fees in connection with the Merger in the six months ended March 31, 2015.

JD Alexander

On November 6, 2013, JD Alexander tendered his resignation as Chief Executive Officer and as an employee of the Company, subject to and effective immediately after the Closing of the Share Purchase transaction on November 19, 2013. Mr. Alexander's resignation includes a waiver of any rights to any payments under his Change-in-Control Agreement with the Company. On November 6, 2013, the Company and Mr. Alexander also entered into a Consulting and Non-Competition Agreement under which (i) Mr. Alexander will provide consulting services to the Company during the two-year period after the Closing, (ii) Mr. Alexander agreed to be bound by certain non-competition covenants relating to the Company's citrus operations and non-solicitation and non-interference covenants for a period of two years after the Closing, and (iii) the Company will pay Mr. Alexander for such services and covenants $2,000,000 in twenty-four monthly installments. Mr. Alexander also agreed, in a separate side letter with the Company, not to sell or transfer the shares that were awarded pursuant to his Restricted Stock Award Agreement (other than to a family trust) for a period of two years after the Closing. Mr. Alexander also executed a general release in favor of the Company.

Ken Smith

On March 20, 2015, Ken Smith tendered his resignation as Chief Operating Officer and as an employee of the Company. Mr. Smith's resignation includes a waiver of any rights to any payments under his Change-in-Control Agreement with the Company. On March 20, 2015, the Company and Mr. Smith also entered into a Consulting and Non-Competition Agreement under which (i) Mr. Smith will provide consulting services to the Company during the three-year period after the resignation date, (ii) Mr. Smith agreed to be bound by certain non-competition covenants relating to the Company's citrus operations and non-solicitation and non-interference covenants for a period of two years after the resignation date, and (iii) the Company will pay Mr. Smith up to $1,225,000 for such services and covenants.

Note 12. Subsequent Events

Modification of Credit Agreements

The Silver Nip Citrus line of credit with Prudential was paid in full and terminated on April 28, 2015. Rabo has agreed, subject to certain conditions, that the Company may loan Silver Nip Citrus up to $7,000,000 on a revolving basis. These advances would be funded from either cash on hand or draws on the Company's $70,000,000 Rabo working capital line of credit.

Silver Nip has provided a $7,000,000 limited guaranty and a security agreement granting Rabo a security interest in crops, accounts receivable, inventory and certain other assets.

This modification required the amendment of various Prudential and Rabo loan documents and mortgages.

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

The following discussion and analysis should be read in conjunction with the unaudited condensed combined consolidated financial statements and related notes included elsewhere in this Form 10-Q. Additional context can also be found in our Form 10-K for the fiscal year ended September 30, 2014, as filed with the Securities and Exchange Commission ("SEC") on December 12, 2014.

Cautionary Statement Regarding Forward-Looking Information

We provide forward-looking information in this Quarterly Report, particularly in this Management's Discussion and Analysis, pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Any statements in this Quarterly Report that are not historical facts are forward-looking statements. Forward-looking statements include, but are not limited to, statements that express our intentions, beliefs, expectations, strategies, predictions or any other statements relating to our future activities or other future events or conditions. These statements are based on our current expectations, estimates and projections about our business based, in part, on assumptions made by our management. Factors which may cause future outcomes to differ materially from those foreseen in forward-looking statements include, but are not limited to: changes in laws, regulation and rules; weather conditions that affect production, transportation, storage, demand, import and export of fresh product and their by-products, increased pressure from disease, insects and other pests; disruption of water supplies or changes in water allocations; pricing and supply of raw materials and products; market responses to industry volume pressures; pricing and supply of energy; changes in interest rates; availability of financing for land development activities and other growth opportunities; onetime events; acquisitions and divestitures; seasonality; labor disruptions; inability to pay debt obligations; inability to engage in certain transactions due to restrictive covenants in debt instruments; government restrictions on land use; changes in agricultural land values; changes in dividends; and market and pricing risks due to concentrated ownership of stock. These assumptions are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in the forward-looking statements due to numerous factors, including those risks factors described in our Annual Report on Form 10-K for the year ended September 30, 2014 and our Quarterly Reports on Form 10-Q.

Overview

We manage our land based upon its primary usage and review its performance based upon three primary classifications – Citrus Groves, Improved Farmland and Ranch and Conservation. In addition, we operate an Agricultural Supply Chain Management business that is not tied directly to our land holdings and Other Operations that include leases for mining and oil extraction rights to third parties. We present our financial results and the related discussions based upon these five segments (Citrus Groves, Improved Farmland, Ranch and Conservation, Agricultural Supply Chain Management and Other Operations).

In connection with our pursuit of growth opportunities consistent with our mission, we intend to regularly evaluate potential acquisitions and divestitures and other business opportunities, some of which are material in nature. If appropriate opportunities present themselves, we may engage in selected acquisitions, divestitures and other business growth initiatives or undertakings. To the extent we engage in such opportunities it could, among other things, change our revenue mix, require us to obtain additional debt or equity financing and have a material impact on our business and financial condition.

Segments

We own approximately 121,000 acres of land in twelve Florida counties (Alachua, Charlotte, Collier, DeSoto, Glades, Hardee, Hendry, Highlands, Lee, Martin Osceola and Polk), and includes approximately 90,000 acres of mineral rights, and operate five segments.

- Citrus Groves include activities related to planting, owning, cultivating and/or managing citrus groves in order to produce fruit for sale to fresh and processed citrus markets.

- Agricultural Supply Chain Management and Support includes activities related to the purchase and resale of fruit, as well as, to value-added services which include contracting for the harvesting, marketing and hauling of citrus.

- Improved Farmland includes activities related to owning and/or leasing improved farmland. Improved Farmland is acreage that has been converted, or is permitted to be converted, from native pasture and which may have various improvements including irrigation, drainage and roads.

- Ranch and Conservation includes activities related to cattle grazing, sod, native plant and animal sales, leasing, management and/or conservation of unimproved native pasture land.

- Other Operations include activities related to a citrus nursery, rock mining royalties, oil exploration and other insignificant lines of business.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our unaudited condensed combined consolidated financial statements which have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. We base these estimates on historical experience, available current market information and on various other assumptions that management believes are reasonable under the circumstances. Additionally we evaluate the results of these estimates on an on-going basis. Management's estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The Company accounts for its business acquisitions under the acquisition method of accounting as indicated in ASC No. 805, Business Combinations, which requires the acquiring entity in a business combination to recognize the fair value of all assets acquired, liabilities assumed and any noncontrolling interest in the acquiree, and establishes the acquisition date as the fair value measurement point. Accordingly, the Company recognizes assets acquired and liabilities assumed in business combinations, including contingent assets and liabilities and noncontrolling interest in the acquiree, based on fair value estimates as of the date of acquisition. In accordance with ASC No. 805, the Company recognizes and measures goodwill, if any, as of the acquisition date, as the excess of the fair value of the consideration paid over the fair value of the identified net assets acquired.

When we acquire a business from an entity under common control, whereby the companies are ultimately controlled by the same party or parties both before and after the transaction, it is treated similar to the pooling of interest method of accounting, whereby the assets and liabilities are recorded at the transferring entity's historical cost instead of reflecting the fair market value of assets and liabilities.

There have been no significant changes during this reporting period to the policies and disclosures set forth in Part II, Item 7 in our Annual Report on Form 10-K for the fiscal year ended September 30, 2014.

Recent Events

Orange-Co Acquisition

On December 2, 2014, we completed the acquisition of certain citrus and related assets of Orange-Co, LP ("Orange-Co") pursuant to an Asset Purchase Agreement, which we refer to as the Orange-Co Purchase Agreement, dated as of December 1, 2014. The assets we purchased include approximately 20,263 acres of citrus groves in DeSoto and Charlotte Counties, Florida, which comprise one of the largest contiguous citrus grove properties in the state of Florida. The purchase price was approximately $276,673,000, net of cash acquired, including: (1) $147,500,000 in initial cash consideration funded from the proceeds of the sugarcane disposition and new term debt; (2) up to $7,500,000 in additional cash consideration to be released from escrow in equal parts, subject to certain limitations, on December 1, 2015 and June 1, 2016; (3) the refinancing of Orange-Co's outstanding debt including approximately $91,371,000 in term debt and a working capital facility of approximately $27,775,000 and (4) the assumption of certain other liabilities totaling $4,587,000. On December 1, 2014, we deposited an irrevocable standby letter of credit issued by Rabo Agrifinance, Inc., or Rabo, in the aggregate amount of $7,500,000 into an escrow account to fund the additional cash consideration.

Sugarcane Land Disposition

On November 21, 2014, the Company completed the sale of approximately 36,000 acres of land used for sugarcane production and land leasing in Hendry County, Florida to Global Ag Properties, LLC ("Global Ag Properties") for $97,913,921 in cash. We had previously leased approximately 30,600 of these acres to United States Sugar Corporation (the "USSC Lease"). The USSC Lease was assigned to Global Ag Properties in conjunction with the land sale.

Net proceeds from the sugarcane land sale of $97,126,000 were deposited with a Qualified Intermediary in anticipation of the Orange-Co asset acquisition in a tax deferred like kind exchange pursuant to Internal Revenue Code Section §1031 (see "Note 4. Orange-Co Acquisition" in the Notes to the Condensed Combined Consolidated Financial Statements (Unaudited)).

The sales price is subject to post-closing adjustments over a ten (10)-year period. The Company realized a gain of $42,753,000 on the sale. However, $29,140,000 of the gain has been deferred due to the Company's continuing involvement in the property pursuant to a post-closing agreement and the potential price adjustments. The deferral represents the Company's estimate of the maximum exposure to loss as a result of the continuing involvement. A net gain of $13,613,000 was recognized in the financial statements as of and for the six months ended March 31, 2015.

As a result of the disposition of our sugarcane land, we are no longer involved in sugarcane, and, as of November 21, 2014, the Improved Farmland segment was no longer material to our business.

Our sugarcane land was classified as assets held for sale as of September 30, 2014. The sugarcane operation has not been classified as a discontinued operation due to the Company's continuing involvement pursuant to the post-closing agreement described above.

Water Storage Contract Approval

In December 2012, the South Florida Water Management District ("SFWMD") issued a solicitation request for projects to be considered for the Northern Everglades Payment for Environmental Services Program. In March 2013, the Company submitted its response proposing a dispersed water management project on a portion of its ranch land.

On December 11, 2014, the SFWMD approved a contract with the Company. The contract term is eleven years and allows up to one year for implementation (design, permitting, construction and construction completion certification) and ten years of operation whereby the Company will provide water retention services. Payment for these services includes an amount not to exceed $4,000,000 of reimbursement for implementation. In addition, it provides for an annual fixed payment of $12,000,000 for operations and maintenance costs as long as the project is in compliance with the contract and subject to annual SFWMD Governing Board ("Board") approval of funding. The contract specifies that the Board has to approve the payments annually, and there can be no assurance that it will approve the annual fixed payments.

Silver Nip Merger Agreement

Effective February 28, 2015, the Company completed the merger ("Merger") with 734 Citrus Holdings, LLC ("Silver Nip Citrus") pursuant to an Agreement and Plan of Merger (the "Merger Agreement") with 734 Sub, LLC, a wholly owned subsidiary of the Company ("Merger Sub"), Silver Nip Citrus and, solely with respect to certain sections thereof, the equity holders of Silver Nip Citrus. The ownership of Silver Nip Citrus was held by 734 Agriculture, 74.89%, Mr. Clay Wilson, Chief Executive Officer of the Company, 5% and an entity controlled by Mr. Clay Wilson owned, 20.11%.

On November 19, 2013, 734 Agriculture and its affiliates, including 734 Investors, acquired approximately 51% of the Company's common stock. 734 Agriculture is the sole managing member of 734 Investors. By virtue of their ownership percentage, 734 Agriculture is able to elect all of the Directors and, consequently, control Alico.

734 Agriculture has control over both Silver Nip Citrus and the Company and therefore the Merger was treated as a common control acquisition.

At closing of the Merger, Merger Sub merged with and into Silver Nip Citrus, with Silver Nip Citrus surviving the Merger as a wholly owned subsidiary of the Company. Pursuant to the Merger Agreement, at closing, the Company issued 923,257 shares (the "Stock Issuance") of the Company's common stock, par value $1.00 per share (the "Common Stock"), to the holders of membership interests in Silver Nip Citrus. Silver Nip Citrus' outstanding net indebtedness at the closing of the Merger was approximately $40,278,000 and other liabilities totaled $6,952,000. The Company acquired assets at net book value of $65,739,000 and total net assets of $18,509,000. The shares issued were recorded at the carrying amount of the net assets transferred. The holders of membership interest in Silver Nip Citrus will also receive additional Company shares based on the value of the proceeds received by the Company from the sale of citrus fruit harvested on Silver Nip Citrus' real property following the conclusion of the 2014-2015 citrus harvest season.

The Company expensed $811,000 in professional and legal fees in connection with the Merger in the six months ended March 31, 2015.

Because the Company and Silver Nip Citrus were under common control, we are required under generally accepted accounting principles in the United States ("GAAP") to account for this Common Control Acquisition in a manner similar to the pooling of interest method of accounting. Under this method of accounting, our balance sheet reflects Silver Nip Citrus' historical carryover basis in the assets and liabilities instead of reflecting the fair market value of the assets and liabilities. We have also retrospectively recast our financial statements to combine the operating results of the Company and Silver Nip Citrus from the date common control began, November 19, 2013.

Due to the fact Silver Nip Citrus' fiscal year end is June 30, the Company's condensed combined consolidated financial condition as of March 31, 2015 includes the financial condition of Silver Nip Citrus as of December 31, 2014, and the Company's condensed combined consolidated results of operations for the six months ended March 31, 2015 includes the Silver Nip Citrus results of operations for the six months ended December 31, 2014. The Company's combined consolidated financial condition as of March 31, 2014 reflects the financial condition of Silver Nip Citrus as of December 31, 2013, and the Company's condensed combined consolidated results of operations for the six months ended March 31, 2014 includes Silver Nip Citrus' results of operations from November 19, 2013 (the initial date of common control) through December 31, 2013.

Results of Operations

The following table sets forth a comparison of results of operations for the three and six months ended March 31, 2015 and 2014:

(in thousands)	Three Months Ended				Six Months Ended			
	March 31,		Change		March 31,		Change	
	2015	2014	$	%	2015	2014	$	%
Operating revenues:								
Citrus Groves	$50,371	$22,590	$27,781	123.0 %	$63,289	$28,223	$35,066	124.3 %
Agricultural Supply Chain Management	3,296	6,135	(2,839)	(46.3)%	4,479	8,241	(3,762)	(45.6)%
Improved Farmland	982	10,750	(9,768)	(90.9)%	2,074	17,282	(15,208)	(88.0)%
Ranch and Conservation	309	910	(601)	(66.1)%	1,145	1,441	(296)	(20.5)%
Other Operations	164	257	(93)	(36.2)%	313	444	(131)	(29.5)%
Total operating revenues	55,122	40,642	14,480	35.7 %	71,300	55,631	15,669	28.2 %
Gross Profit:								
Citrus Groves	10,022	7,891	2,131	27.0 %	12,813	9,980	2,833	28.4 %
Agricultural Supply Chain Management	556	291	265	91.1 %	368	72	296	NM
Improved Farmland	(304)	1,885	(2,189)	(116.2)%	(3)	2,887	(2,890)	(100.1)%
Ranch and Conservation	(314)	(261)	(53)	20.3 %	(223)	(106)	(117)	110.4 %
Other Operations	119	167	(48)	(28.8)%	220	(63)	283	NM
Total gross profit	10,079	9,973	106	1.1 %	13,175	12,770	405	3.2 %
Corporate, general and administrative expenses	3,381	1,834	1,547	84.4 %	9,294	5,622	3,672	65.4 %
Income from operations	6,698	8,139	(1,441)	(17.7)%	3,881	7,148	(3,267)	(45.7)%
Other income (expense), net	(2,954)	(450)	(2,504)	NM	11,357	(711)	12,068	NM

Income before income taxes	3,744	7,689	(3,945)	(51.3)%	15,238	6,437	8,801	136.8 %
Income taxes	950	2,992	(2,042)	(68.3)%	4,713	2,445	2,268	92.8 %
Net income	$2,794	$4,697	$(1,903)	(40.6)%	$10,525	$3,992	$6,533	163.7 %

A discussion of our segment results of operations follows.

24

Citrus Groves

The table below presents key operating measures for the three and six months ended March 31, 2015 and 2014:

(in thousands, except per box and per pound solid data)

	Three Months Ended March 31,		Change		Six Months Ended March 31,		Change	
	2015	2014	$	%	2015	2014	$	%
Revenue From:								
Early and Mid Season	$ 36,052	$ 17,927	$ 18,125	101.1 %	$ 47,927	$ 22,366	$ 25,561	114.3 %
Valencias	12,037	3,438	8,599	250.2 %	12,037	3,438	8,599	250.1 %
Fresh Fruit	1,621	1,205	416	34.6 %	2,541	1,859	692	36.7 %
Other	661	20	641	NM	784	560	224	40.0 %
Total	$ 50,371	$ 22,590	$ 27,781	123.0 %	$ 63,289	$ 28,223	$ 35,066	124.3 %
Boxes Harvested:								
Early and Mid Season	3,117	1,381	1,736	125.7 %	4,251	1,828	2,423	132.6 %
Valencias	887	245	642	262.1 %	888	245	643	262.5 %
Total Processed	4,004	1,626	2,378	146.3 %	5,139	2,073	3,066	147.9 %
Fresh Fruit	117	110	7	6.4 %	179	160	19	11.9 %
Total	4,121	1,736	2,385	137.4 %	5,318	2,233	3,085	138.2 %
Pound Solids Produced:								
Early and Mid Season	18,694	8,644	10,050	116.3 %	24,941	11,255	13,686	121.6 %
Valencias	5,610	1,528	4,082	NM	5,610	1,528	4,082	NM
Fresh Fruit	85	37	48	129.8 %	84	37	47	127.1 %
Total	24,389	10,209	14,180	138.9 %	30,635	12,820	17,815	139.0 %

Pound Solids per Box:								
Early and Mid Season	6.00	6.26	(0.26)	(4.3)%	5.87	6.16	(0.29)	(4.7)%
Valencias	6.32	6.24	0.08	1.3%	6.32	6.24	0.08	1.3%
Price per Pound Solid:								
Early and Mid Season	$ 1.93	$2.07	$ (0.15)	(7.2)%	$1.92	$ 1.99	$(0.07)	(3.6)%
Valencias	$ 2.15	$2.25	$ (0.10)	(4.5)%	$2.15	$ 2.25	$(0.10)	(4.5)%
Price per Box:								
Fresh Fruit	$ 13.85	$10.95	$ 2.90	26.5%	$14.20	$ 11.62	$2.58	22.2%
Operating Expenses:								

								(25,946)
Change in net unrealized gain (loss) on securities, net of taxes of $6,304					(11,709)		(11,709)	
Comprehensive loss							(37,655)	
Issuance of common stock	467	1	4				5	
Stock option forfeiture			(1,033)				(1,033)	
Purchase of treasury stock (1,121,500 shares, at cost)						(7,488)	(7,488)	
Balance at December 31, 1999	16,653,646	16,654	187,952	33,626	(10,464)	(7,488)	220,280	
Comprehensive income:								
Net income				2,669			2,669	
Change in net unrealized gain (loss) on securities, net of taxes of $3,508					6,516		6,516	
Comprehensive income							9,185	

Issuance of common stock	669		4				4
Purchase of treasury stock (1,261,870 shares, at cost)						(8,292)	(8,292)
Balance at December 31, 2000	16,654,315	16,654	187,956	36,295	(3,948)	(15,780)	221,177
Comprehensive income:							
Net income				4,175			4,175
Change in net unrealized gain (loss) on securities, net of taxes of $3,150					5,851		5,851
Comprehensive income							10,026
Issuance of common stock			(29)			442	413
Purchase of treasury stock (367,262 shares, at cost)						(2,216)	(2,216)
Balance at December 31, 2001	16,654,315	16,654	187,927	40,470	1,903	(17,554)	229,400
(Unaudited):							
Comprehensive income:							
Net income				5,430			5,430
Change in net unrealized gain (loss) on securities, net of taxes of $1,064					(1,977)		(1,977)
Comprehensive income							3,453
Issuance of common stock			(35)			297	262
Purchase of treasury stock (1,400,000 shares, at cost)						(19,540)	(19,540)
Balance at March 31, 2002 (unaudited)	16,654,315	$ 16,654	$ 187,892	$ 45,900	$ (74)	$ (36,797)	$ 213,575

See accompanying Notes to Consolidated Financial Statements

F-6

American Medical Security Group, Inc.

Notes to Consolidated Financial Statements

1. Organization and Significant Accounting Policies

Organization

American Medical Security Group, Inc., together with its subsidiary companies (the "Company"), is a provider of individual and small employer group insurance products. The Company's principal product offering is health insurance for small employer groups and health insurance for individuals and families ("MedOne^{SM}"). The Company also offers life, dental, prescription drug, disability and accidental death insurance, and provides self-funded benefit administration. The Company's products are marketed in 32 states and the District of Columbia through independent agents. Approximately 75 Company sales managers located in sales offices throughout the United States support the independent agents. The Company's products generally provide discounts to insureds that utilize preferred provider organizations ("PPOs"). The Company owns a preferred provider network and also contracts with other networks to ensure cost-effective health care choices to its members.

Basis of Presentation

The consolidated financial statements include the accounts of the Company and all of its majority-owned subsidiaries. Significant intercompany accounts and transactions have been eliminated. The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates are based on knowledge of current events and anticipated future events, and accordingly, actual results may differ from those estimates.

The accompanying unaudited interim consolidated financial statements reflect, in the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for fair presentation. Operating results for the three months ended March 31, 2002 are not necessarily indicative of the results that may be expected for the year ending December 31, 2002.

Cash and Cash Equivalents

Cash and cash equivalents include operating cash and short-term investments with original maturities of three months or less. These amounts are recorded at cost, which approximates market value.

Investments

The Company's investments are classified in three categories. Investments that the Company has the positive intent and ability to hold to maturity are classified as held-to-maturity securities and are reported at amortized cost. Assets which are invested for the purpose of supporting the Company's nonqualified executive retirement plan are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings as net investment income. All other investments are classified as available-for-sale securities and are reported at fair value based on quoted market prices. Unrealized gains and losses on available-for-sale securities are excluded from earnings and reported as a separate component of shareholders' equity as accumulated other comprehensive income or loss, net of income tax effects. Realized gains and losses from the sale or write-down for

other-than-temporary impairments of available-for-sale debt and equity securities are calculated using the specific identification method.

Fair Value of Financial Instruments

The fair values of investments are reported in Note 4. The fair values of all other financial instruments approximate their December 31, 2001 and 2000 carrying values.

Property and Equipment

Property and equipment are recorded at cost. Depreciation and amortization are provided using the straight-line method over the estimated useful lives, which are 20 to 30 years for land improvements, 10 to 40 years for buildings and building improvements, three to five years for computer equipment and software and three to 10 years for furniture and other equipment.

Goodwill and Other Intangibles

Goodwill represents the excess of cost over the fair market value of net assets acquired. Goodwill and other intangible assets are currently being amortized on a straight-line basis over a period of 40 years or less. Accumulated amortization was $20,089,000 and $16,461,000 at December 31, 2001 and 2000, respectively. The Company periodically evaluates whether events and circumstances have occurred that may affect the estimated useful life or the recoverability of the remaining balance of its intangibles. Based on accounting standards in effect at December 31, 2001, the Company measures impairment of goodwill and other intangibles using undiscounted cash flows, and on that basis, believes that no impairment of goodwill or other intangible assets exists at December 31, 2001. As discussed in more detail in Note 2, "Recent Accounting Pronouncements," the Financial Accounting Standards Board issued new statements during 2001, which will impact the Company's accounting for goodwill and other intangibles in future periods.

Policy Acquisition Costs

Policy acquisition costs consist of commissions and other administrative costs that the Company incurs to acquire new business. The Company currently does not defer policy acquisition costs. Premium is collected and billed and commissions and other administrative costs are incurred on a month-to-month basis. Policy acquisition costs are expensed in the period incurred.

Reinsurance

Reinsurance premiums, commissions and expense reimbursements on reinsured business are accounted for on a basis consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts. Premiums and benefits ceded to other companies have been reported as a reduction of premium revenue and benefits. Reinsurance receivables and prepaid reinsurance premium amounts are reported as assets.

The Company limits the maximum net loss that can arise from certain lines of business by reinsuring (ceding) a portion of these risks with other insurance organizations (reinsurers) on an excess of loss or

quota share basis. The Company's retention limit per covered life is $500,000 per policy year for medical claims and $50,000 for life claims. The Company is liable on reinsurance ceded in the event that the reinsurers do not meet their contractual obligations.

A summary of reinsurance assumed and ceded is as follows**:**

	Year ended December 31,		
	2001	**2000**	**1999**
		(In thousands)	
Reinsurance assumed:			
Insurance premiums	$ 1,515	$ 8,725	$ 58,924
Medical and other benefits	1,395	9,921	52,137
Reinsurance ceded:			
Insurance premiums	$ 2,532	$ 2,523	$ 4,916
Medical and other benefits	1,910	3,250	7,897

Medical and Other Benefits Payable

The liabilities for medical and other benefits represent estimates of the ultimate net cost of all reported and unreported claims that are unpaid at year end. These estimates are developed using actuarial methods based upon historical data for payment patterns, cost trends, product mix, seasonality, utilization of health care services and other relevant factors. The estimates are reviewed periodically and, as adjustments to the liabilities become necessary, the adjustments are reflected in current operations. Management believes that the amount of medical and other benefits payable is adequate to cover the Company's liability for unpaid claims as of December 31, 2001.

Premium Deficiency Reserves

The Company recognizes premium deficiency reserves on an existing group of insurance contracts when the sum of expected future claim costs, claim adjustment expenses and related maintenance expenses exceeds the expected future premium revenue and investment income. Insurance contracts are grouped as relating to highly regulated markets or all other markets consistent with the Company's manner of acquiring, servicing and measuring the profitability of its business. Highly regulated markets are identified based on significant rating restrictions, states' general legislative and regulatory environments, and the Company's ability to effectively underwrite risk. The Company continues to evaluate assumptions used in the premium deficiency reserve analysis and records or adjusts premium deficiency reserves as necessary.

During 1999, the Company established a premium deficiency reserve of $19,200,000 for its highly regulated markets. Premium deficiency reserves are included in medical and other benefits payable in the Company's consolidated balance sheets. At December 31, 2000, the Company had a remaining recorded premium deficiency reserve of $1,142,000, which was fully amortized during 2001 leaving no remaining recorded premium deficiency reserve at December 31, 2001.

Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial statement purposes and the amounts used for income tax purposes. A valuation allowance is recognized when, based on available evidence, it is more likely than not that the deferred tax asset may not be realized.

Revenue Recognition

Premiums for health and life policies are recognized ratably over the period that insurance coverage is provided. Other revenue, including administrative fee income from claim processing and other administrative services, is recognized in the period the service is provided.

Related Parties

The Company has deferred compensation payable to employees of $3,167,000 and $3,388,000 at December 31, 2001 and 2000, respectively.

Comprehensive Income (Loss)

Comprehensive income (loss) is defined as net income (loss) plus or minus other comprehensive income (loss). For the Company, under existing accounting standards, other comprehensive income (loss) includes unrealized gains and losses, net of income tax effects, on certain investments in debt and equity securities. Comprehensive income (loss) is reported by the Company in the consolidated statements of changes in shareholders' equity and comprehensive income (loss). For the three months ended March 31, 2001 (not separately presented in the Statements of Changes in Shareholders' Equity), unaudited comprehensive loss was $1,748,000, comprised of net loss of $5,140,000 and unrealized gain on available for sale securities of $3,392,000.

Earnings (Loss) Per Common Share

A reconciliation of the numerator and denominator of the basic and diluted earnings (loss) per common share ("EPS") is as follows:

	Three Months Ended March 31,		**Year ended December 31,**		
	2002	**2001**	**2001**	**2000**	**1999**
	(unaudited)				
Numerator (in thousands):					
Net income (loss)	$ 5,430	$ (5,140)	$ 4,175	$ 2,669	$ (25,946)

	Three Months Ended March 31,		Year ended December 31,		
Denominator:					
Denominator for basic EPS weighted average shares	13,802,666	14,210,643	14,048,545	14,898,652	16,470,096
Effect of dilutive securities employee stock options	688,875		179,143	150,651	
Denominator for diluted EPS	14,491,541	14,210,643	14,227,688	15,049,303	16,470,096
Earnings (loss) per common share:					
Basic	$ 0.39	$ (0.36)	$ 0.30	$ 0.18	$ (1.58)
Diluted	$ 0.37	$ (0.36)	$ 0.29	$ 0.18	$ (1.58)

Options to purchase 3,243,767 and 3,460,130 shares of common stock were outstanding at December 31, 2001 and 2000, respectively. Of those shares, 1,914,313 and 2,030,170 were excluded from the computation of diluted earnings (loss) per common share for the respective years because the option's exercise price was greater than the average market price of common shares and, therefore, the effect would be antidilutive. There was no effect of dilutive securities for 1999 and the three months ended March 31, 2001 because employee stock options were antidilutive during those periods.

2. Recent Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ("Statement 142"), effective for fiscal years beginning after December 15, 2001. The new rules will impact the Company in two ways. First, goodwill and intangible assets deemed to have indefinite lives will no longer be amortized. Other intangible assets will continue to be amortized over their useful lives. Second, goodwill and intangible assets with indefinite lives will be subject to an initial impairment test in accordance with Statement 142, and any remaining balance of goodwill and intangible assets will be subject to future annual impairment testing.

The Company will apply the new rules on accounting for goodwill and other intangible assets beginning in the first quarter of 2002. Application of the nonamortization provisions of Statement 142 is expected to result in an increase in net income of approximately $2,700,000 per year. The Company will perform the first of the required impairment tests of goodwill and intangible assets deemed to have indefinite lives in 2002, effective as of January 1, 2002, by comparing the fair value of the Company's reporting units to their carrying amounts (book value), including goodwill. In determining the fair value of the

Company's reporting units, management will consider valuation techniques such as the quoted market price of the Company's stock, the present value of future cash flows and market comparison of similar assets and liabilities.

At December 31, 2001, the Company's book value per share was $16.30 and was significantly higher than the $12.45 quoted market price per share. As of December 31, 2001 and March 31, 2002, the Company has not yet determined what the effect of these tests will be on the earnings and financial position of the Company. If management determines that the quoted market price per share is the appropriate measure of the Company's fair value, the resulting impairment would be greater than 50% of the amount of goodwill on the Company's December 31, 2001 balance sheet. If it is determined that an impairment exists as of January 1, 2002, the charge would be reported as the cumulative effect of a change in accounting principle in the Company's consolidated financial statements and would have no impact on cash flows or the statutory-basis capital and surplus of the Company's insurance subsidiaries.

March 31, 2002 Update (unaudited)

On January 1, 2002, the Company adopted Statement 142. Effective January 1, 2002, in accordance with Statement 142, the Company reclassified an intangible asset, net of related deferred taxes, into goodwill because it did not meet the new recognition criteria for an intangible asset to be recognized apart from goodwill. The amortization period used prior to 2002 for this intangible asset was the same as the amortization period for goodwill.

The Company's other intangible asset will continue to be amortized on a straight-line basis over its remaining useful life of five years. This intangible asset had a gross carrying amount of $7.3 million and accumulated amortization of $3.7 million at December 31, 2001. Future amortization expense for this intangible asset is expected to be approximately $0.7 million for each of the next five years.

F-12

The following unaudited table illustrates net income (loss) and net income (loss) per share adjusted to exclude the effects of adopting Statement 142:

	Three months ended March 31,		Year ended December 31,		
	2002	2001	2001	2000	1999
	(In thousands, except share and per share data)				
Reported net income (loss)	$ 5,430	$ (5,140)	$ 4,175	$ 2,669	$ (25,946)
Add back: Goodwill amortization		671	2,685	2,685	2,827
Adjusted net income (loss)	$ 5,430	$ (4,469)	$ 6,860	$ 5,354	$ (23,119)
Basic earnings (loss) per common share:					
Reported net income (loss)	$ 0.39	$ (0.36)	$ 0.30	$ 0.18	$ (1.58)
Goodwill amortization		0.05	0.19	0.18	0.17
Adjusted net income (loss)	$ 0.39	$ (0.31)	$ 0.49	$ 0.36	$ (1.40)
Diluted earnings (loss) per common share:					
Reported net income (loss)	$ 0.37	$ (0.36)	$ 0.29	$ 0.18	$ (1.58)
Goodwill amortization		0.05	0.19	0.18	0.17
Adjusted net income (loss)	$ 0.37	$ (0.31)	$ 0.48	$ 0.36	$ (1.40)

Goodwill amortization for 1998 and 1997 was $2,827,000 or $0.17 per share and $2,618,000 or $0.16 per share, respectively.

F-13

3. Medical and Other Benefits Payable

Activity related to liabilities for unpaid claims included in medical and other benefits payable is summarized as follows:

	December 31,		
	2001	2000	1999
	(In thousands)		
Balance at January 1	$ 134,690	$ 141,177	$ 101,700
Less reinsurance recoverables	476	992	1,058

	December 31,		
Net balance at January 1	134,214	140,185	100,642
Incurred related to:			
Current year	612,491	720,897	792,105
Prior years	(12,026)	(3,397)	10,398
Total incurred	600,465	717,500	802,503
Paid related to:			
Current year	487,400	587,828	651,941
Prior years	120,300	135,643	111,019
Total paid	607,700	723,471	762,960
Net balance at December 31	126,979	134,214	140,185
Plus reinsurance recoverables	1,351	476	992
Balance at December 31	$ 128,330	$ 134,690	$ 141,177

The incurred amounts related to prior years represent the differences between the Company's estimated medical and other benefits payable for prior years' claims and the actual amounts required to satisfy such claims. Actual amounts differ from previously recorded liabilities due to inherent variabilities associated with estimating health insurance benefits payable. The liabilities for unpaid claims at December 31, 2000 and 1999 developed redundant in subsequent years by $12,026,000 and $3,397,000, respectively. The developed redundancy on the liability as of December 31, 2000 was due to an improvement in the Company's average medical claims cost per member in late 2000. The liability for unpaid claims at December 31, 1998, developed deficient by $10,398,000 in the subsequent year as a result of an increase in medical claims trends that was higher than anticipated in late 1998. No additional premiums are collected or returned as a result of incurred claims from prior years.

In determining the liability for unpaid claims at December 31, 2001, management considered the potential impact of the September 11, 2001 events. Although the events of September 11, 2001 did not have a direct material effect on the Company, management anticipated an indirect impact including, but not limited to, increased utilization by the general population of mental health services for stress, anxiety, depression and similar conditions in the fourth quarter. Also, subsequent bio-terrorism threats and attacks were anticipated to result in increased utilization of health care services including office visits, laboratory tests and prescription drugs for flu-like symptoms in the fourth quarter. While the impact of these claims cannot be predicted with certainty, management believes adequate provision has been made for such claims as of December 31, 2001. Accordingly, the outcome of these matters is not expected to have a material adverse effect on the financial position of the Company.

4. Investments

Net investment income and net realized investment losses include the following:

	Year ended December 31,		
	2001	2000	1999
	(In thousands)		
Net investment income:			
Interest on fixed maturities	$ 15,728	$ 17,867	$ 18,731
Dividends on equity securities	148	148	134
Unrealized loss on trading securities	(34)	(21)	
Interest on cash equivalents and other investment income	2,223	1,629	1,581

	Year ended December 31,		
Investment expenses	(622)	(616)	(680)
Net investment income	$ 17,443	$ 19,007	$ 19,766
Net realized investment losses:			
Realized investment losses	$ (2,323)	$ (436)	$ (2,205)
Realized investment gains	1,544	111	1,351
Net realized investment losses	$ (779)	$ (325)	$ (854)

Unrealized gains (losses) are computed as the difference between estimated fair value and amortized cost for fixed maturities and equity securities classified as available for sale. A summary of the net change in unrealized gains (losses), which is included in accumulated other comprehensive income (loss), is as follows:

	Year ended December 31,		
	2001	2000	1999
	(In thousands)		
Fixed maturities	$ 8,847	$ 9,854	$ (17,753)
Equity securities	154	170	(260)
Net change in unrealized gains (losses)	$ 9,001	$ 10,024	$ (18,013)

Changes in accumulated other comprehensive income (loss) related to changes in unrealized gains and losses on securities are as follows:

	Year ended December 31,		
	2001	2000	1999
	(In thousands)		
Change in net unrealized gain (loss) on securities, net of taxes	$ 6,357	$ 6,727	$ (12,264)
Less: reclassification adjustment for losses included in net income (loss), net of tax benefit of $273,000, $114,000 and $299,000 in 2001, 2000 and 1999 respectively	(506)	(211)	(555)
Change in net unrealized gain (loss) on securities, net of taxes	$ 5,851	$ 6,516	$ (11,709)

The amortized cost and estimated fair values of investments are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(In thousands)			

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
At December 31, 2001:				
Available for sale:				
Fixed maturities:				
U.S. Treasury securities	$ 47,869	$ 283	$ (1)	$ 48,151
Corporate debt securities	115,263	2,447	(1,068)	116,642
Foreign government securities	12,391	442	(2)	12,831
Government agency mortgage-backed securities	77,966	691	(101)	78,556
Municipal securities	13,351	223	(1)	13,573
	266,840	4,086	(1,173)	269,753
Equity securities preferred	708	14		722
Held to maturity:				
U.S. Treasury securities	4,286	73		4,359
	$ 271,834	$ 4,173	$ (1,173)	$ 274,834

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
		(In thousands)		
At December 31, 2000:				
Available for sale:				
Fixed maturities:				
U.S. Treasury securities	$ 51,657	$ 160	$ (340)	$ 51,477
Corporate debt securities	145,817	213	(5,142)	140,888
Foreign government securities	15,614	82	(356)	15,340
Government agency mortgage-backed securities	37,718	45	(513)	37,250
Municipal securities	17,556	6	(89)	17,473
	268,362	506	(6,440)	262,428
Equity securities preferred	2,508		(140)	2,368
Held to maturity:				
U.S. Treasury securities	4,320	10	(16)	4,314
	$ 275,190	$ 516	$ (6,596)	$ 269,110

The amortized cost and estimated fair values of debt securities at December 31, 2001 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations.

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value

	Available-for-Sale		Held-to-Maturity	
	(In thousands)			
Due in one year or less	$ 9,370	$ 9,515	$ 2,228	$ 2,244
Due after one through five years	99,796	101,646	755	775
Due after five through ten years	56,392	56,559	1,303	1,340
Due after ten years	23,316	23,477		
	188,874	191,197	4,286	4,359
Government agency mortgage-backed securities	77,966	78,556		
	$ 266,840	$ 269,753	$ 4,286	$ 4,359

At December 31, 2001, the insurance subsidiaries had fixed securities and cash equivalents on deposit with various state insurance departments with carrying values of approximately $4,500,000.

5. Property and Equipment

Property and equipment are stated at cost and are summarized as follows:

	December 31,	
	2001	2000
	(In thousands)	
Land and land improvements	$ 3,893	$ 3,890
Building and building improvements	24,315	24,301
Computer equipment and software	18,121	13,024
Furniture and other equipment	13,559	13,495
	59,888	54,710
Less accumulated depreciation	(26,507)	(22,259)
	$ 33,381	$ 32,451

The Company recognized depreciation expense on property and equipment of $5,555,000, $4,656,000 and $4,544,000 in 2001, 2000 and 1999, respectively.

6. Debt

Notes payable consists of the following:

	December 31,	
	2001	2000
	(In thousands)	
	$ 35,158	$ 35,158

	December 31,	
Line of credit, commercial banks, adjusted periodically, interest payments due quarterly through February 2005		
Mortgage payable, commercial bank, 9.05% interest, monthly principal payments of $100,000 plus interest through January 1, 2004	4,900	6,100
	$ 40,058	$ 41,258

At December 31, 2001, the Company maintained a revolving bank line of credit agreement with a maximum commitment and outstanding balance of advances under the credit agreement of $35,158,000. Interest is charged on the outstanding balance based upon an indexed floating rate of interest. As collateral for the outstanding balance, the Company is required to maintain a minimum cash deposit of $2,500,000 in an account at the lender's institution. The credit agreement contains customary covenants which, among other matters, require the Company to achieve certain minimum financial results and restrict the Company's ability to incur additional debt, pay future cash dividends and dispose of assets outside the ordinary course of business. The Company was in compliance with all such covenants at December 31, 2001. Obligations under the credit agreement are secured by the stock of the Company's principal subsidiaries.

The credit agreement was amended in January 2001 and April 2001 to revise the minimum financial requirements of certain covenants. The April 2001 amendment also revised the Company's applicable interest rate on outstanding loans and the schedule of mandatory future commitment reductions including a $4,842,000 maximum commitment reduction from $40,000,000 to $35,158,000.

Future annual principal amounts due for all of the Company's debt, including the credit agreement, as of December 31, 2001 are $6,200,000 for 2002, $11,200,000 for 2003, $12,500,000 for 2004, and $10,158,000 for 2005. During 2001, 2000 and 1999, interest paid totaled $2,931,000, $4,005,000 and $3,547,000, respectively.

The mortgage payable is collateralized by the Company's home office property located in Green Bay, Wisconsin. The Company believes the carrying value of all notes payable approximates fair value.

March 31, 2002 Update (Unaudited)

At March 31, 2002, the outstanding balance and maximum commitment related to the credit agreement was $30.2 million.

7. Income Taxes

The Company and most of its subsidiaries file a consolidated federal income tax return. The Company and its subsidiaries file separate state franchise, income and premium tax returns as applicable.

The Company had a net current federal income tax payable of $4,012,000 and a net current federal income tax receivable of $2,094,000 at December 31, 2001 and 2000, respectively. The Company and its subsidiaries had state net business loss carryforwards totaling $92,327,000 at December 31, 2001, which

will begin to expire in the year 2008. The Company received net federal and state income tax refunds of $466,000 and $6,910,000 in 2001 and 2000, respectively and paid net federal and state income taxes of $1,496,000 in 1999.

The components of income tax expense (benefit) are as follows:

	Year ended December 31,		
	2001	2000	1999
	(In thousands)		
Current:			

	Year ended December 31,		
Federal	$ 5,410	$ (3,077)	$ (5,965)
State	238	495	34
	5,648	(2,582)	(5,931)
Deferred:			
Federal	313	5,673	(6,244)
State	296	356	(868)
	609	6,029	(7,112)
Income tax expense (benefit)	$ 6,257	$ 3,447	$ (13,043)

The differences between taxes computed at the federal statutory rate and recorded income taxes are as follows:

	Year ended December 31,		
	2001	**2000**	**1999**
		(In thousands)	
Income tax expense (benefit) at federal statutory rate	$ 3,651	$ 2,141	$ (13,658)
Goodwill amortization	829	829	879
State income and franchise taxes, net of federal benefit	571	415	(565)
Other, net	1,206	62	301
Income tax expense (benefit)	$ 6,257	$ 3,447	$ (13,043)

Significant components of the Company's federal and state deferred tax liabilities and assets are as follows:

	December 31, 2001		December 31, 2000	
	Federal	**State**	**Federal**	**State**
		(In thousands)		
Deferred tax assets:				
Insurance liabilities	$ 1,231	$ 63	$ 2,031	$ 137
Unearned income	782	56	1,348	82
Unrealized losses on investments			2,126	
Employee compensation and benefits	2,561	440	2,977	538
Accrued expenses	4,289	611	2,087	371
Specified policy acquisition costs	765	39	874	45
Net business loss carryforwards	1,082	6,384	1,082	6,176
Other deductible temporary differences	2,428	586	2,584	492
	13,138	8,179	15,109	7,841
Valuation allowances	(1,963)	(3,431)	(1,082)	(2,779)

	December 31, 2001		December 31, 2000	
	11,175	4,748	14,027	5,062
Deferred tax liabilities:				
Intangibles	6,457	1,459	6,790	1,533
Prepaid assets	1,145	115	1,346	151
Depreciation and amortization	1,889	361	1,462	278
Unrealized gain on investments	1,024			
Other taxable temporary differences	1,815	11	2,112	26
	12,330	1,946	11,710	1,988
Net deferred tax assets (liabilities)	$ (1,155)	$ 2,802	$ 2,317	$ 3,074

The federal deferred benefit arising from the deductibility of state deferred tax is included as a component of other federal deferred taxes. The net deferred taxes are included in other assets in the accompanying consolidated balance sheets.

8. Commitments and Contingencies

Skilstaf Litigation

On August 26, 1999, a $6,900,000 verdict was entered against the Company in a lawsuit involving allegations regarding the Company's administration of a self-funded benefit plan for Skilstaf, Inc., an employee leasing company. The Company appealed the verdict and expected the verdict to be reversed or substantially reduced following appeal. Based upon management's evaluation of the merits of the appeal, the facts of the case and consultation with outside legal counsel, management concluded that the likelihood of the appellate court affirming the verdict was not probable. As a result, the Company's accrual related to this case at the end of 1999 and 2000 was not material. Following an adverse decision from the Court of Appeals on March 12, 2001, the Company recognized an additional accrual during the first quarter of 2001 representing the full potential loss including punitive damages and other

expenses. In July 2001, at the direction of the district court, the Company paid the full amount of the verdict plus interest and the case is closed.

Health Administrators Litigation

On February 7, 2000, a $5,400,000 verdict was entered against the Company in a lawsuit filed by Health Administrators, Inc., an insurance agency owned and operated by a former agent of the Company, which alleged breach of contract involving commission amounts due to such agent. The Company appealed the verdict and on March 29, 2001, the Ohio Court of Appeals affirmed a portion of the verdict, with modifications, representing approximately $3,000,000 in damages. The affirmed portion of the verdict was paid by the Company during 2001 and is considered closed. The appeals court reversed and remanded the remaining issue in the case representing approximately $2,400,000 in damages. Briefs have been submitted for the remanded portion of the case and the parties are awaiting the trial court's decision.

Class Action Litigation Status at December 31, 2001

In February 2000, a complaint was filed against the Company in the Circuit Court for Palm Beach County, Florida, seeking certification of a statewide class action on behalf of certain individuals insured by or formerly insured by the Company. Plaintiffs allege the Company did not follow Florida law when it discontinued writing certain health insurance policies and offered new policies in 1998. Plaintiffs claim the Company wrongfully terminated policies, improperly notified insureds of conversion rights and charged improper premium for the new policies. Plaintiffs also assert that the Company's renewal rating methodology violates Florida law. Plaintiffs are seeking unspecified damages. A motion for class certification was granted by the Circuit Court and appealed to the Fourth District Court of Appeals of the State of Florida, which upheld the class certification in October 2001. The Company has an appeal pending with the Florida Supreme Court with the ultimate objective of seeking to vacate the finding of a certifiable class. The Company and plaintiffs filed cross motions for summary judgment in Circuit Court that were heard and denied in February 2002. A memorandum filed by plaintiffs in January 2002 in support of their motion for summary judgment raised new arguments that expanded the legal theory, scope and potential damages of the case. The trial is tentatively scheduled to commence as a bench trial in March 2002. Management believes the Company acted in compliance with applicable Florida law with regard to the discontinuance and replacement of and conversion of insurance policies and with regard to its renewal rating practices. Although the outcome of the case cannot be predicted with certainty, management believes this suit is without merit and is defending its position vigorously.

Class Action Litigation March 31, 2002 (Unaudited)

In March 2002, a bench trial on the liability issues of the case was held. On April 24, 2002, a judgment was rendered against the Company and the damages portion of the lawsuit is expected to be heard before a jury later this year. In a separate administrative proceeding based on similar facts with similar issues, the Florida Department of Insurance issued a complaint against the Company in May 2001, challenging the Company's rating and other practices in Florida. On April 25, 2002, the Administrative Law Judge found in favor of the Company and held that the evidence presented by the Florida Department of Insurance did not support a conclusion that the Company had violated any provisions of the Florida insurance statutes or regulations. The Administrative Law Judge recommended that the

administrative complaint be dismissed. The Commissioner of the Florida Department of Insurance must accept the Administrative Law Judge's findings of fact but may make modifications on the conclusions of law. In light of the conflicting findings in these cases, the Company intends to request that the court in the class action lawsuit reconsider its ruling. If the ruling is not reconsidered, the Company intends to appeal the ruling.

The Company is involved in various legal and regulatory actions occurring in the normal course of business. Based on current information including consultation with outside counsel, management believes any ultimate liability that may arise from the above-mentioned and all other legal and regulatory actions would not materially affect the Company's consolidated financial position or results of operations. However, management's evaluation of the likely impact of these actions could change in the future and an unfavorable outcome could have a material adverse effect on the Company's consolidated financial position, results of operations or cash flow of a future period.

9. Shareholders' Equity

Statutory Financial Information

State insurance laws and regulations prescribe accounting practices for determining statutory net income and equity for insurance companies. These regulations require, among other matters, the filing of financial statements prepared in accordance with statutory accounting practices prescribed or permitted for insurance companies. The combined statutory capital and surplus of the Company's insurance subsidiaries, United Wisconsin Life Insurance Company and American Medical Security Insurance Company of Georgia, at December 31, 2001 and 2000, was $161,789,000 and $153,912,000, respectively. The combined statutory net income of the Company's insurance subsidiaries was $18,052,000 and $7,808,000 for the years ended December 31, 2001 and 2000, respectively, and the combined statutory net loss was $20,782,000 for the year ended December 31, 1999.

State insurance regulations also require the maintenance of a minimum compulsory surplus based on a percentage of premiums written. At December 31, 2001, the Company's insurance subsidiaries were in compliance with these compulsory regulatory requirements.

Effective January 1, 2001, the National Association of Insurance Commissioners revised the Accounting Practices and Procedures Manual in a process referred to as Codification. Codification has changed certain prescribed statutory accounting practices resulting in changes to the accounting practices that the insurance subsidiaries of the Company use to prepare their statutory-basis financial statements. The impact of Codification to the Company's insurance subsidiaries' statutory-basis capital and surplus was not material.

Restrictions on Dividends From Subsidiaries

Dividends paid by the insurance subsidiaries to the parent Company are limited by state insurance regulations. The insurance regulator in the insurer's state of domicile may disapprove any dividend which, together with other dividends paid by an insurance company in the prior 12 months, exceeds the regulatory maximum, computed as the lesser of 10% of statutory surplus or total statutory net gain from operations as of the end of the preceding calendar year. Based upon the financial statements of the Company's insurance subsidiaries as of December 31, 2001, as filed with the insurance regulators,

dividends are limited to $6,963,000 without prior regulatory approval until September 2002, at which time the aggregate amount available without regulatory approval is $14,963,000. In February 2002, a $5,000,000 dividend was paid to the parent Company by an insurance subsidiary.

Shareholders' Rights Agreement

In August 2001, the Board of Directors of the Company adopted a shareholders' rights agreement (the "rights agreement") and declared a dividend of one preferred share purchase right for each outstanding share of common stock of the Company. When exercisable, each right entitles the registered holder to purchase from the Company a unit consisting of one ten-thousandth of a share of Series B Junior Cumulative Preferred Stock of the Company at a price of $30.00. The rights agreement, as amended, is designed to deter takeover initiatives not considered to be in the best interests of the Company's shareholders. In the event that a person or a group has become the beneficial owner of 12% or more of the common shares then outstanding, in certain circumstances the rights become exercisable, and each holder of a right will have the right to receive, upon exercise, common shares having a value equal to two times the exercise price of the right. The rights are redeemable by action of the Company's Board of Directors at any time prior to their becoming exercisable. The rights expire on August 20, 2011.

10. Employee Benefit Plans

Retirement Savings Plan

The Company's employees are included in a qualified defined contribution plan (the "Retirement Savings Plan") with profit sharing and discretionary savings provisions covering all eligible salaried and hourly employees. Participant contributions up to 6% of the participant's compensation are matched 60% by the Company. Effective January 1, 2002, participant contributions up to 6% of the participant's compensation are matched 70% by the Company. Profit sharing contributions to the Retirement Savings Plan are determined annually by the Company. Participants vest in Company contributions in three years. The Company recognized expense associated with the Retirement Savings Plan of $1,881,000, $1,944,000 and $1,610,000 in 2001, 2000 and 1999, respectively.

Nonqualified Executive Retirement Plan

During 2000, the Company adopted a nonqualified executive retirement plan (the "Nonqualified Plan") to provide key management with the opportunity to accumulate deferred compensation which cannot be accumulated under the Retirement Savings Plan due to compensation limitations imposed by the Internal Revenue Service. The Nonqualified Plan is funded through a rabbi trust and has contribution and investment options similar to those of the Retirement Savings Plan. The Company recognized expense associated with the Nonqualified Plan of $53,000 and $77,000 during 2001 and 2000, respectively.

Stock Based Compensation Plans

The Company has a stock-based compensation plan, the Equity Incentive Plan (the "Plan"), for the benefit of eligible employees and directors of the Company. The Plan permits the grant of nonqualified

stock options ("NQSO"), incentive stock options, stock appreciation rights, restricted stock awards and performance awards. Persons eligible to participate in the Plan include all full-time active employees and outside directors of the board of directors. The Plan allows for the granting of up to 4,000,000 shares of which 472,297 shares are available for grant as of December 31, 2001. The Company's 1995 Director Stock Option Plan also permits the grant of NQSOs. The plan allows for the granting of up to 75,000 shares of which 14,000 shares are available for grant, as of December 31, 2001.

The terms of incentive stock options and nonqualified stock options granted under the Plan cannot exceed more than 10 and 12 years, respectively, and the option exercise price generally cannot be less than the fair market value of the Company's common stock on the date of grant. Incentive stock options and NQSOs are not exercisable in any event prior to six months following the grant date.

Stock appreciation rights generally have a grant price at least equal to 100% of the fair market value of the Company's common stock. The term of the stock appreciation rights cannot exceed 12 years. Stock appreciation rights are not exercisable prior to six months following the grant date.

Restricted stock generally may not be sold or otherwise transferred for certain periods based on the passage of time, the achievement of performance goals or the occurrence of other events. However, participants may exercise full voting rights and are entitled to receive all dividends and other distributions with respect to restricted stock. Restricted stock does not vest prior to six months following the date of grant.

During 1998, the Company and a key executive entered into a deferred stock agreement. Under the agreement the Company has an obligation to issue 73,506 shares of the Company's common stock provided the executive remains continuously employed with the Company through November 17, 2002. The Company incurred expense of $225,000 in each of the three years ended 2001, 2000 and 1999 related to this agreement.

On July 9, 2001, the Company and a key executive entered into a restricted stock agreement. Under the agreement, the Company granted the executive 25,000 shares of common stock, subject to certain rights and restrictions, in exchange for the surrender for cancellation of 443,857 shares of the executive's nonqualified stock options. The 25,000 shares of restricted stock vested in December 2001 upon the occurrence of certain triggering events, as specified under the restricted stock agreement. The Company incurred expense of $139,000 during 2001 related to this agreement.

Effective January 1, 2000, the Company adopted a deferred compensation plan for the benefit of certain outside directors of the Company who wish to defer the receipt of eligible compensation which they may otherwise be entitled to receive from the Company. Directors who choose to participate in the plan may elect to have their deferred compensation credited to, in whole or in part, either an interest account or a Company stock unit account.

Stock option activity for all plans is as follows:

	December 31,		
	2001	**2000**	**1999**
Total number of NQSOs			
Outstanding at beginning of year	3,460,130	2,809,143	2,918,893
Granted	426,000	715,000	999,000
Exercised	(26,756)		
Forfeited	(615,607)	(64,013)	(1,108,750)
Outstanding at end of year	3,243,767	3,460,130	2,809,143
Exercisable at end of year	1,826,017	1,807,963	1,504,976
Available for grant at end of year	486,297	296,690	947,677
Weighted average exercise price of NQSOs			
Outstanding at beginning of year	$ 9.86	$ 11.10	$ 15.18
Granted Exercise price equals market price on grant date	9.97	5.28	7.33
Granted Exercise price is less than market price on grant date			
Granted Exercise price exceeds market price on grant date			
Exercised	5.15		
Forfeited	14.09	13.14	18.45
Outstanding at end of year	9.11	9.86	11.10
Exercisable at end of year	10.33	12.60	13.68

NQSOs by exercise price range			
Range of exercise prices	$ 3.01 - $8.88	$ 3.01 - $8.88	$ 3.01 - $8.88
Weighted average exercise price	$ 5.75	$ 5.71	$ 6.07
Weighted average remaining contractual life (years)	10.08	11.03	11.34
Exercisable at end of year	605,954	260,877	47,960
Outstanding at end of year	1,471,454	1,571,960	856,960
	$ 5.77	$ 5.64	$ 3.01

Weighted average exercise price of options exercisable at end of year						
Range of exercise prices	$	10.20 - $14.38	$	10.25 - $14.38	$	10.25 - $14.38
Weighted average exercise price	$	11.07	$	11.54	$	11.53
Weighted average remaining contractual life (years)		8.78		8.75		9.79
Exercisable at end of year		964,984		848,151		734,848
Outstanding at end of year		1,517,234		1,189,234		1,230,015
Weighted average exercise price of options exercisable at end of year	$	11.48	$	11.66	$	11.76
Range of exercise prices	$	15.76 - $22.74	$	15.76 - $22.74	$	15.76 - $22.74
Weighted average exercise price	$	16.83	$	16.33	$	16.33
Weighted average remaining contractual life (years)		6.45		7.48		8.50
Exercisable at end of year		255,079		698,936		722,168
Outstanding at end of year		255,079		698,936		722,168
Weighted average exercise price of options exercisable at end of year	$	16.83	$	16.33	$	16.33

The Black-Scholes option valuation model is commonly used in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Since the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimates, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The Company follows Accounting Principles Board Opinion No. 25 under which no compensation expense is recorded when the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant. The Company's pro forma information regarding net income and net income per share has been determined as if these options had been accounted for since January 1, 1995, in accordance with the fair value method of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation".

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. The Company's pro forma information is as follows:

	Year ended December 31,					
	2001		2000		1999	
	(In thousands, except per share data)					
Net income (loss)	$	4,175	$	2,669	$	(25,946)
Compensation expense in accordance with SFAS No. 123		(1,119)		(933)		(483)
Pro forma net income (loss)	$	3,056	$	1,736	$	(26,429)
Earnings (loss) per common share:						
Basic	$	0.30	$	0.18	$	(1.58)
Diluted	$	0.29	$	0.18	$	(1.58)
Pro forma earnings (loss) per common share:						
Basic	$	0.22	$	0.12	$	(1.60)
Diluted	$	0.21	$	0.12	$	(1.60)

The pro forma disclosures only include the effect of options granted subsequent to January 1, 1995. Accordingly, the effects of applying the SFAS No. 123 pro forma disclosures to future periods may not be indicative of future effects.

In determining compensation expense in accordance with SFAS No. 123, the fair value for these options was estimated at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	Year ended December 31,		
	2001	2000	1999
Expected life of options	6.00 years	6.00 years	6.00 years
Risk-free interest rate	4.67%	5.73%	6.13%
Expected dividend yield	0.00%	0.00%	0.00%
Expected volatility factor	53%	56%	45%
Grant date fair value of options:			
Exercise price equals market price	$ 5.51	$ 3.09	$ 3.84
Exercise price is less than market price	$	$	$
Exercise price exceeds market price	$	$	$

11. Quarterly Financial Information (Unaudited)

Selected quarterly financial data for the years ended December 31, 2001 and 2000 are as follows:

	Quarter				
	First	Second	Third	Fourth	Total
	(In thousands, except per share data)				
2001					
Total revenues	$ 232,258	$ 223,306	$ 213,388	$ 207,669	$ 876,621
Net income (loss)	(5,140)	1,466	3,504	4,345	4,175
Earnings (loss) per common share:					
Basic	(0.36)	0.10	0.25	0.31	0.30
Diluted	(0.36)	0.10	0.25	0.30	0.29
2000					
Total revenues	$ 257,677	$ 250,326	$ 241,756	$ 240,106	$ 989,865
Net income (loss)	1,659	2,260	(1,376)	126	2,669
Earnings (loss) per common share:					
Basic	0.11	0.15	(0.09)	0.01	0.18
Diluted	0.11	0.15	(0.09)	0.01	0.18

12. Segments of the Business

The Company has two reportable segments: 1) health insurance products; and 2) life insurance products. The Company's health insurance products consist of the following coverages related to small group PPO products: MedOne^{SM} and small group medical, self-funded medical, dental and short-term disability. Life products consist primarily of group term life insurance. The "All Other" category includes operations not directly related to the business segments and unallocated corporate items (i.e., corporate investment income, interest expense on corporate debt, amortization of goodwill and intangibles and unallocated overhead expenses). The reportable segments are managed separately because they differ in the nature of the products offered and in profit margins.

The Company evaluates segment performance based on income or loss before income taxes, excluding gains and losses on the Company's investment portfolio. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies. Significant intercompany transactions have been eliminated prior to reporting reportable segment information.

Selected financial data for the Company by segment is as follows:

Three months ended March 31, 2002:	Health Insurance	Life Insurance	All Other	Total Consolidated
(Unaudited)		(In thousands)		
Revenues:				
Insurance premiums	$ 190,720	$ 3,678	$ 3	$ 194,401
Net investment income	1,934	150	1,840	3,924
Net realized investment gain			14	14
Other revenue	4,460	32	913	5,405
Total revenues	197,114	3,860	2,770	203,744
Expenses:				
Medical and other benefits	130,564	1,218	18	131,800
Selling, general and administrative	58,208	1,219	2,597	62,024
Interest			494	494
Amortization of other intangibles			183	183
Total expenses	188,772	2,437	3,292	194,501
Income (loss) before income taxes	$ 8,342	$ 1,423	$ (522)	$ 9,243
As of March 31, 2002:				
Segment assets	$ 143,720	$ 4,024	$ 300,602	$ 448,346

Three months ended March 31, 2001:	Health Insurance	Life Insurance	All Other	Total Consolidated
(Unaudited)		(In thousands)		
Revenues:				
Insurance premiums	$ 216,974	$ 4,963	$ 533	$ 222,470
Net investment income	2,450	174	1,890	4,514
Net realized investment losses			(27)	(27)
Other revenue	4,230	42	1,029	5,301
Total revenues	223,654	5,179	3,425	232,258
Expenses:				
Medical and other benefits	164,197	1,992	391	166,580
Selling, general and administrative	67,963	1,437	2,011	71,411
Interest			876	876
Amortization of goodwill and other intangibles			907	907
Total expenses	232,160	3,429	4,185	239,774
Income (loss) before income taxes(a)	$ (8,506)	$ 1,750	$ (760)	$ (7,516)

As of March 31, 2001:

Three months ended March 31, 2001:	Health Insurance	Life Insurance	All Other	Total Consolidated
Segment assets	$ 154,217	$ 3,808	$ 306,492	$ 464,517

(a) Excluding the first quarter 2001 litigation charge, pre-tax income for the health segment would have been $494,000 and consolidated pre-tax income would have been $1,484,000.

Year ended December 31, 2001:	Health Insurance	Life Insurance	All Other	Total Consolidated
		(In thousands)		
Revenues:				
Insurance premiums	$ 820,658	$ 17,424	$ 590	$ 838,672
Net investment income	9,197	656	7,590	17,443
Net realized investment losses			(779)	(779)
Other revenue	17,272	154	3,859	21,285
Total revenues	847,127	18,234	11,260	876,621
Expenses:				
Medical and other benefits	595,811	6,334	(203)	601,942
Selling, general and administrative	244,453	5,446	7,843	257,742
Interest			2,877	2,877
Amortization of goodwill and other intangibles			3,628	3,628
Total expenses	840,264	11,780	14,145	866,189
Income (loss) before income taxes(a)	$ 6,863	$ 6,454	$ (2,885)	$ 10,432
As of December 31, 2001:				
Segment assets	$ 147,889	$ 3,958	$ 321,168	$ 473,015

(a) Excluding the first quarter 2001 litigation charge, pre-tax income for the health segment would have been $15,863,000 and consolidated pre-tax income would have been $19,432,000.

Year ended December 31, 2000:	Health Insurance	Life Insurance	All Other	Total Consolidated
		(In thousands)		
Revenues:				
Insurance premiums	$ 907,722	$ 22,578	$ 20,771	$ 951,071

Year ended December 31, 2000:	Health Insurance	Life Insurance	All Other	Total Consolidated
Net investment income	9,513	638	8,856	19,007
Net realized investment losses			(325)	(325)
Other revenue	16,115	217	3,780	20,112
Total revenues	933,350	23,433	33,082	989,865
Expenses:				
Medical and other benefits	700,511	7,781	16,321	724,613
Selling, general and administrative	235,649	6,581	9,537	251,767
Interest			3,584	3,584
Amortization of goodwill and other intangibles			3,785	3,785
Total expenses	936,160	14,362	33,227	983,749
Income (loss) before income taxes	$ (2,810)	$ 9,071	$ (145)	$ 6,116
As of December 31, 2000:				
Segment assets	$ 180,683	$ 4,292	$ 286,948	$ 471,923

Year ended December 31, 1999:	Health Insurance	Life Insurance	All Other	Total Consolidated
		(In thousands)		
Revenues:				
Insurance premiums	$ 985,322	$ 26,183	$ 44,602	$ 1,056,107
Net investment income	9,254	202	10,310	19,766
Net realized investment losses			(854)	(854)
Other revenue	17,857	258	4,246	22,361
Total revenues	1,012,433	26,643	58,304	1,097,380
Expenses:				
Medical and other benefits	805,768	10,270	44,435	860,473
Selling, general and administrative	245,676	7,640	14,743	268,059
Interest			3,564	3,564
Amortization of goodwill and other intangibles			4,273	4,273
Total expenses	1,051,444	17,910	67,015	1,136,369
Income (loss) before income taxes(a)	$ (39,011)	$ 8,733	$ (8,711)	$ (38,989)
As of December 31, 1999:				
Segment assets	$ 186,611	$ 4,229	$ 312,254	$ 503,094

(a)
Excluding the third quarter 1999 premium deficiency charge, pre-tax loss for the health segment would have been $23,926,000 and consolidated pre-tax loss would have been $17,904,000.

13. Stock Purchase Agreement (unaudited)

On March 19, 2002, the Company entered into a stock purchase agreement with Cobalt Corporation ("Cobalt") and its wholly owned subsidiary, Blue Cross & Blue Shield United of Wisconsin, the Company's largest shareholder, to purchase 1.4 million shares of the Company's common stock owned by BCBSUW at a total cost of $19.5 million, including related transaction costs. In conjunction with the stock purchase, the Company received a $20.0 million dividend from UWLIC with regulatory approval. The Company's revolving bank line of credit agreement was amended in March 2002 to allow for the stock purchase. Also in conjunction with the stock purchase, which was completed on March 22, 2002, the Company, Cobalt and BCBSUW agreed to an underwritten secondary offering of at least 3.0 million shares of the remaining shares of the Company's common stock owned by BCBSUW.

Schedule II

American Medical Security Group, Inc.
(Parent Company Only)

Condensed Financial Information of Registrant

Condensed Balance Sheets

	December 31,	
	2001	2000
	(In thousands)	
Assets:		
Cash and cash equivalents	$ 3,137	$ 1,671
Other assets:		
Investment in consolidated subsidiaries	250,794	240,784
Goodwill and other intangibles, net	19,666	20,229
Due from affiliates		1,761
Other assets	239	309
Total other assets	270,699	263,083
Total assets	$ 273,836	$ 264,754

Liabilities and Shareholders' Equity:

	December 31,	
Liabilities:		
Notes payable	$ 35,158	$ 35,158
Taxes payable	7,821	7,019
Payables and accrued expenses	5	50
Due to affiliates	634	
Other liabilities	818	1,350
Total liabilities	44,436	43,577
Shareholders' equity:		
Common stock	16,654	16,654
Paid-in capital	187,927	187,956
Retained earnings	40,470	36,295
Accumulated other comprehensive gain (loss)	1,903	(3,948)
Treasury stock	(17,554)	(15,780)
Total shareholders' equity	229,400	221,177
Total liabilities and shareholders' equity	$ 273,836	$ 264,754

F-32

Schedule II

American Medical Security Group, Inc.
(Parent Company Only)

Condensed Financial Information of Registrant

Condensed Statements of Operations

	Year ended December 31,		
	2001	2000	1999
		(In thousands)	
Revenues:			
Fees from consolidated subsidiaries	$ 4,427	$ 4,139	$ 3,199
Other revenue	103	140	92
Total revenues	4,530	4,279	3,291
Expenses:			
General and administrative	563	430	1,071

	Year ended December 31,		
Interest	2,377	2,972	2,802
Amortization of goodwill and other intangibles	563	563	563
Total expenses	3,503	3,965	4,436
Income (loss) before income tax expense (benefit) and equity in net income (loss) of subsidiaries	1,027	314	(1,145)
Income tax expense (benefit)	874	154	(347)
Income (loss) before equity in net income (loss) of subsidiaries	153	160	(798)
Equity in net income (loss) of subsidiaries	4,022	2,509	(25,148)
Net income (loss)	$ 4,175	$ 2,669	$ (25,946)

Schedule II

American Medical Security Group, Inc.
(Parent Company Only)

Condensed Financial Information of Registrant

Condensed Statements of Cash Flows

	Year ended December 31,		
	2001	2000	1999
		(In thousands)	
Operating Activities:			
Net income (loss)	$ 4,175	$ 2,669	$ (25,946)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Equity in net (income) loss of subsidiaries	(4,022)	(2,509)	25,148
Dividends received from subsidiaries		16,400	15,250
Amortization of intangibles	563	563	563
Deferred income tax expense (benefit)	72	186	(399)
Changes in operating accounts:			
Net other assets and liabilities	2,481	(7,622)	3,011
Net cash provided by operating activities	3,269	7,018	17,627

	Year ended December 31,		
Investing Activities:			
Net cash used in investing activities			
Financing Activities:			
Issuance of common stock	413	4	5
Purchase of treasury stock	(2,216)	(8,292)	(7,488)
Proceeds from notes payable borrowings		39,158	5,000
Repayment of notes payable		(39,158)	(15,000)
Net cash used in financing activities	(1,803)	(8,288)	(17,483)
Cash and cash equivalents:			
Net increase during year	1,466	1,399	144
Balance at beginning of year	1,671	272	128
Balance at end of year	$ 3,137	$ 1,671	$ 272

Schedule III

American Medical Security Group, Inc.

Supplementary Insurance Information

Segment	Deferred Policy Acquisition Costs	Medical and Other Benefits Payable	Advance Premiums	Other Policyholder Funds
		(In thousands)		
December 31, 2001:				
Health	$	$ 125,834	$ 15,472	$
Life		9,480	816	
All Other		190	449	
Total	$	$ 135,504	$ 16,737	$
December 31, 2000:				
Health	$	$ 133,001	$ 16,367	$
Life		9,924	745	
All Other		2,385	456	
Total	$	$ 145,310	$ 17,568	$

Segment	Deferred Policy Acquisition Costs	Medical and Other Benefits Payable	Advance Premiums	Other Policyholder Funds
December 31, 1999:				
Health	$	$ 150,201	$ 16,171	$
Life		9,328	530	
All Other		9,588	576	
Total	$	$ 169,117	$ 17,277	$

Segment	Premium Revenue	Net Investment Income	Medical and Other Benefit Expenses	Amortization of Deferred Policy Acquisition Costs	Other Operating Expenses	Premiums Written
			(In thousands)			
December 31, 2001:						
Health	$ 820,658	$ 9,197	$ 595,811	$	$ 244,453	$ 819,763
Life	17,424	656	6,334		5,446	
All Other	590	6,811	(203)		7,843	583
Total	$ 838,672	$ 16,664	$ 601,942	$	$ 257,742	
December 31, 2000:						
Health	$ 907,722	$ 9,513	$ 700,511	$	$ 235,649	$ 907,918
Life	22,578	638	7,781		6,581	
All Other	20,771	8,531	16,321		9,537	20,651
Total	$ 951,071	$ 18,682	$ 724,613	$	$ 251,767	
December 31, 1999:						
Health	$ 985,322	$ 9,254	$ 805,768	$	$ 245,676	$ 984,715
Life	26,183	202	10,270		7,640	
All Other	44,602	9,456	44,435		14,743	44,726
Total	$ 1,056,107	$ 18,912	$ 860,473	$	$ 268,059	

Schedule IV

American Medical Security Group, Inc.

Reinsurance

		Direct Business		Ceded to Other Companies		Assumed From Other Companies		Net Amount	Percentage Of Amount Assumed to Net
						(In thousands)			
Year Ended December 31, 2001:									
Life insurance in force	$	9,351,321	$	6,913,662	$		$	2,437,659	0.0%
Premiums:									
Accident and Health		821,994		2,259		1,513		821,248	0.2%
Life		17,695		273		2		17,424	0.0%
Total Premiums		839,689		2,532		1,515		838,672	0.2%
Year Ended December 31, 2000:									
Life insurance in force	$	14,839,256	$	11,412,772	$	1,942	$	3,428,426	0.1%
Premiums:									
Accident and Health		922,087		2,236		8,642		928,493	0.9%
Life		22,782		287		83		22,578	0.4%
Total Premiums		944,869		2,523		8,725		951,071	0.9%
Year Ended December 31, 1999:									
Life insurance in force	$	14,355,089	$	12,731,969	$	9,455	$	1,632,575	0.6%
Premiums:									
Accident and Health		976,457		4,309		57,776		1,029,924	5.6%
Life		25,642		607		1,148		26,183	4.4%
Total Premiums		1,002,099		4,916		58,924		1,056,107	5.6%

Schedule V

American Medical Security Group, Inc.

Valuation and Qualifying Accounts

		Balance at Beginning of Period		Additions Charged to Costs and Expenses		Deductions		Balance at End of Period
				(In thousands)				
Year ended December 31, 2001:								
Allowance for bad debts	$	344	$	1,250	$	302	$	1,292

	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions	Balance at End of Period
Valuation allowance for deferred taxes	3,861	1,810	277	5,394
Total	$ 4,205	$ 3,060	$ 579	$ 6,686
Year ended December 31, 2000:				
Allowance for bad debts	$ 651	$ 7	$ 314	$ 344
Valuation allowance for deferred taxes	3,549	398	86	3,861
Total	$ 4,200	$ 405	$ 400	$ 4,205
Year ended December 31, 1999:				
Allowance for bad debts	$ 1,118	$ 14	$ 481	$ 651
Valuation allowance for deferred taxes	2,654	1,029	134	3,549
Total	$ 3,772	$ 1,043	$ 615	$ 4,200

3,500,000 Shares

Common Stock

PROSPECTUS

, 2002

CIBC World Markets

Robert W. Baird & Co.

Stifel, Nicolaus & Company
Incorporated

You should rely only on the information contained in this prospectus. No dealer, salesperson or other person is authorized to give information that is not contained in this prospectus. This prospectus is not an offer to sell nor is it seeking an offer to buy these securities in any jurisdiction where the offer or sale is not permitted. The information contained in this prospectus is correct only as of the date of this prospectus, regardless of the time of the delivery of this prospectus or any sale of these securities.

PART II

INFORMATION NOT REQUIRED IN PROSPECTUS

Item 14. Other Expenses of Issuance and Distribution.

SEC registration fee	$	6,647
NASD filing fee		7,725
Printing and engraving expenses		100,000
Legal fees and expenses		275,000
Accounting fees and expenses		90,000
Transfer agent fees and other miscellaneous expenses		75,628
Total	$	555,000

All of the above fees and expenses up to an aggregate of $650,000 will be paid by American Medical Security Group, Inc. (the "registrant"). Any expenses in excess of such amount will be borne equally by the registrant and the selling shareholder. Other than the SEC registration fee and the NASD filing fee, all fees and expenses are estimated.

Item 15. Indemnification of Directors and Officers.

The registrant is incorporated under the Wisconsin Business Corporation Law ("WBCL"). Under Section 180.0851(1) of the WBCL, the registrant is required to indemnify a director or officer, to the extent such person is successful on the merits or otherwise in the defense of a proceeding, for all reasonable expenses incurred in the proceeding if such person was a party because he or she was a director or officer of the registrant. In all other cases, the registrant is required by Section 180.0851(2) of the WBCL to indemnify a director or officer against liability incurred in a proceeding to which such person was a party because he or she was an officer or director of the registrant, unless it is determined that he or she breached or failed to perform a duty owed to the registrant and the breach or failure to perform constitutes: (i) a willful failure to deal fairly with the registrant or its shareholders in connection with a matter in which the director or officer has a material conflict of interest; (ii) a violation of criminal law, unless the director or officer had reasonable cause to believe his or her conduct was lawful or no reasonable cause to believe his or her conduct was unlawful; (iii) a transaction from which the director or officer derived an improper personal profit; or (iv) willful misconduct. Section 180.0858(1) of the WBCL provides that, subject to certain limitations, the mandatory indemnification provisions do not preclude any additional right to indemnification or allowance of expenses that a director or officer may have under the registrant's articles of incorporation, bylaws, a written agreement or a resolution of the board of directors or shareholders.

Section 180.0859 of the WBCL provides that it is the public policy of the State of Wisconsin to require or permit indemnification, allowance of expenses and insurance to the extent required or permitted under Sections 180.0850 to 180.0858 of the WBCL for any liability incurred in connection with a proceeding involving a federal or state statute, rule or regulation regulating the offer, sale or purchase of securities.

Section 180.0828 of the WBCL provides that, with certain exceptions, a director is not liable to a corporation, its shareholders, or any person asserting rights on behalf of the corporation or its shareholders, for damages, settlements, fees, fines, penalties or other monetary liabilities arising from a breach of, or failure to perform, any duty resulting solely from his or her status as a director, unless the person asserting liability proves that the breach or failure to perform constitutes any of the four exceptions to mandatory indemnification under Section 180.0851(2) referred to above.

Under Section 180.0833 of the WBCL, directors of the registrant against whom claims are asserted with respect to the declaration of an improper dividend or other distribution to shareholders to which they assented are entitled to contribution from other directors who assented to such distribution and from shareholders who knowingly accepted the improper distribution, as provided therein.

Article VII of the registrant's bylaws contains provisions that generally parallel the indemnification provisions of the WBCL. Directors and officers of the registrant are also covered by directors' and officers' liability insurance under which they are insured (subject to certain exceptions and limitations specified in the policy) against expenses and liabilities arising out of proceedings to which they are parties by reason of being or having been directors or officers.

The underwriting agreement provides that the underwriters will indemnify the directors, certain officers of the registrant, the selling shareholder, and the selling shareholder's parent, Cobalt Corporation, against certain liabilities, including liabilities under the Securities Act of 1933, or will contribute to payments which may be made in respect thereof.

Section 8.01 of the stock purchase agreement by and among the selling shareholder, its parent and the registrant, dated as of March 19, 2002, provides that the registrant agrees to indemnify the selling shareholder, its parent and the underwriters, and their respective officers, directors and controlling persons, against certain liabilities, including liabilities under the Securities Act of 1933, or to contribute to payments which may be made in respect thereof, and provides that the selling shareholder and its parent agree to indemnify the registrant, its directors and officers and each controlling person of the registrant against certain liabilities, including liabilities under the Securities Act of 1933, or to contribute to payments which may be made in respect thereof.

Section 4.01 of the distribution and indemnity agreement between Newco/UWS, Inc. and United Wisconsin Services, Inc. dated as of September 11, 1998 provides that Cobalt Corporation (formerly Newco/UWS) shall indemnify the registrant's directors and officers from certain liabilities, including those arising from any breach of the distribution agreement by Cobalt Corporation.

Item 16. Exhibits.

The exhibits listed in the accompanying exhibit index are filed or incorporated by reference as exhibits to this registration statement.

Item 17. Undertakings.

The undersigned registrant hereby undertakes (in accordance with the corresponding lettered undertaking in Item 512 of Regulation S-K):

(b) That, for purposes of determining any liability under the Securities Act of 1933, each filing of the registrant's annual report pursuant to Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 that is incorporated by reference in the registration statement shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(h) Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers and controlling persons of the registrant pursuant to the indemnification provisions described in Item 15 of this registration statement, or otherwise, the registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against

public policy as expressed in the Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the registrant of expenses incurred or paid by a director, officer or controlling person of the registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Act and will be governed by the final adjudication of such issue.

(i) (1) For purposes of determining any liability under the Securities Act of 1933, the information omitted from the form of prospectus filed as part of this registration statement in reliance upon Rule 430A and contained in a form of prospectus filed by the registrant pursuant to Rule 424(b)(1) or (4) or 497(h) under the Securities Act shall be deemed to be part of this registration statement as of the time it was declared effective.

(2) For the purpose of determining any liability under the Securities Act of 1933, each post-effective amendment that contains a form of prospectus shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial *bona fide* offering thereof.

SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, the registrant certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-3 and has duly caused this amendment to the registration statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Green Bay, State of Wisconsin, on May 8, 2002.

AMERICAN MEDICAL SECURITY GROUP, INC.

By: /s/ SAMUEL V. MILLER

Samuel V. Miller, *Chairman of the Board, President and Chief Executive Officer*

Pursuant to the requirements of the Securities Act of 1933, this amendment to the registration statement has been signed by the following persons in the capacities indicated as of the 8th day of May, 2002.

Signature	Title
/s/ SAMUEL V. MILLER Samuel V. Miller	Chairman of the Board, President and Chief Executive Officer; Director (Principal Executive Officer)
/s/ GARY D. GUENGERICH Gary D. Guengerich	Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)
/s/ ROGER H. BALLOU* Roger H. Ballou	Director
/s/ W. FRANCIS BRENNAN* W. Francis Brennan	Director
/s/ MARK A. BRODHAGEN* Mark A. Brodhagen	Director
/s/ KENNETH L. EVASON* Kenneth L. Evason	Director
/s/ THOMAS R. HEFTY*	Director

Signature	Title
Thomas R. Hefty	
/s/ JAMES C. HICKMAN*	Director
James C. Hickman	

/s/ WILLIAM R. JOHNSON*	Director
William R. Johnson	
/s/ EUGENE A. MENDEN*	Director
Eugene A. Menden	
/s/ EDWARD L. MEYER, JR.*	Director
Edward L. Meyer, Jr.	
/s/ MICHAEL T. RIORDAN*	Director
Michael T. Riordan	
/s/ H.T. RICHARD SCHREYER*	Director
H.T. Richard Schreyer	
/s/ FRANK L. SKILLERN*	Director
Frank L. Skillern	
/s/ J. GUS SWOBODA*	Director
J. Gus Swoboda	

* By: /s/ TIMOTHY J. MOORE

Timothy J. Moore
Attorney-in-Fact

AMERICAN MEDICAL SECURITY GROUP, INC.
(the "Registrant")
(Commission File No. 1-13154)

EXHIBIT INDEX
to
AMENDMENT NO. 1
to

FORM S-3 REGISTRATION STATEMENT

Exhibit Number	Document Description	Incorporated Herein by Reference to	Filed Herewith
1*	Form of Underwriting Agreement		
2.1	Distribution and Indemnity Agreement between United Wisconsin Services, Inc., now known as American Medical Security Group, Inc. ("AMSG f/k/a UWS" or "Registrant") and Newco/UWS, Inc. ("Newco/UWS") dated as of September 11, 1998	Exhibit 2.1 to Newco/UWS' Registration Statement on Form 10, as amended (File No. 1-14177)	
2.2	Employee Benefits Agreement dated as of September 11, 1998, by and between AMSG f/k/a UWS and Newco/UWS	Exhibit 10.1 to Newco/UWS' Registration Statement on Form 10, as amended (File No. 1-14177)	
2.3	Tax Allocation Agreement, entered into as of September 11, 1998, by and between AMSG f/k/a UWS and Newco/UWS	Exhibit 10.2 to Newco/UWS' Registration Statement on Form 10, as amended (File No. 1-14177)	
4.1(a)	Restated Articles of Incorporation of Registrant dated as February 17, 1999	Exhibit 3.1 to the Registrant's Form 10-K for the year ended December 31, 1998 (the "1998 10-K")	
4.1(b)	Articles of Amendment to Restated Articles of Incorporation with Respect to Designation, Preferences, Limitations and Relative Rights of Series B Junior Cumulative Preferred Stock	Exhibit 3 to the Registrant's Form 10-Q for the quarter ended June 30, 2001.	
4.2	Bylaws of Registrant as amended and restated November 17, 1999	Exhibit 3.2 to the Registrant's Form 10-K for the year ended December 31, 1999	
4.3(a)	Credit Agreement dated as of March 24, 2000, (the "Credit Agreement") among the Registrant, LaSalle Bank National Association and other Lenders	Exhibit 4 to the Registrant's Form 10-Q for the quarter ended March 31, 2000	
4.3(b)	First Amendment dated as of July 18, 2000 to Credit Agreement	Exhibit 4 to the Registrant's Form 10-Q for the quarter ended June 30, 2000	

EI-1

4.3(c)	Second Amendment dated as of November 10, 2000 to Credit Agreement	Exhibit 4 to the Registrant's Form 10-Q for the quarter ended September 30, 2000	
4.3(d)	Third Amendment dated as of January 29, 2001 to Credit Agreement	Exhibit 4.4 to the Registrant's Form 10-K for the year ended December 31, 2000	
4.3(e)	Fourth Amendment dated as of April 27, 2001 to Credit Agreement	Exhibit 4 to the Registrant's Form 10-Q for the quarter ended March 31, 2001	
4.3(f)(i)	Fifth Amendment dated as of March 21, 2002 to Credit Agreement	Exhibit 4 to the Registrant's Form 8-K dated March 25, 2002	
4.3(f)(ii)	Revised Fifth Amendment dated as of March 21, 2002 to Credit Agreement (replacing Exhibit 4.3(f)(i))		X**
4.4(a)	Rights Agreement, dated as of August 9, 2001, between the Registrant and Firstar Bank, N.A., as Rights Agent (the	Exhibit 1 to the Registrant's Registration Statement on Form 8-A filed August 14,	

	"Rights Agreement') including the form of Rights Certificate as Exhibit B thereto	2001 and Exhibit 4 to the Registrant's Current Report on Form 8-K dated August 9, 2001, and filed on August 14, 2001	
4.4(b)	Amendment dated as of February 1, 2002 to the Rights Agreement	Exhibit 4.1 to the Registrant's Form 8-K dated February 1, 2002 (the "2/1/02 8-K")	
4.4(c)	Appointment and Assumption Agreement dated December 17, 2001, between the Registrant and Firstar Bank, N.A., appointing LaSalle Bank, N.A. as Rights Agent for the Rights Agreement	Exhibit 4.2 to the 2/1/02 8-K	
5	Opinion of Quarles & Brady LLP		X
23.1	Consent of Ernst & Young LLP		X
23.2	Consent of Quarles & Brady LLP		Contained in Exhibit 5
24	Power of Attorney		Contained in Signatures page to original registration statement

99.1	Registration Rights Agreement between the Registrant and Blue Cross & Blue Shield United of Wisconsin dated as of September 1, 1998	Exhibit 10.19 to 1998 10-K	
99.2	Agreement dated February 1, 2002, among the Registrant, Cobalt Corporation and Blue Cross & Blue Shield United of Wisconsin concerning the Rights Agreement	Exhibit 10.1 to the 2/1/02 8-K	
99.3	Stock Purchase Agreement, dated as of March 19, 2002, among Blue Cross & Blue Shield United of Wisconsin, Cobalt Corporation and the Registrant	Exhibit 10 to the Registrant's Form 8-K dated March 19, 2002	

* To be filed by amendment or as an exhibit to a report on Form 8-K.

** Filed with original registration statement.

QuickLinks