SECURITY CAPITAL CORP/DE/
Form 10-Q
August 11, 2006

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark one)

x	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	for the quarterly period ended June 30, 2006.
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

for the transition period from to .

1-7921

(Commission file number)

Security Capital Corporation

(Exact name of registrant as specified in its charter)

Delaware	**13-3003070**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Eight Greenwich Office Park, Third Floor, Greenwich, CT 06831

(Address of principal executive offices, including zip code)

(203) 625-0770

(Registrant s telephone number, including area code)

N.A.

(Former address, if changed since last report)

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer o Accelerated Filer o Non-accelerated Filer x

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

As of August 10, 2006, there were 7,358,082 outstanding shares of Class A Common Stock, par value $ 0.01, and 380 outstanding shares of Common Stock, par value $ 0.01, of the Registrant.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

Security Capital Corporation and Subsidiaries

Condensed Consolidated Balance Sheets

(unaudited)

(in thousands, except share and per share amounts)	**June 30, 2006**	**December 31, 2005**
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,553	$ 8,940
Accounts receivable, net	18,380	21,124
Deferred income taxes.	1,339	1,244
Other current assets	2,689	1,580
Current assets of discontinued operations		7,425
Total current assets	23,961	40,313
Property and equipment, net	8,141	8,282
Goodwill, net	55,727	55,727
Identified intangible assets, net	11,180	12,358
Deferred income taxes	475	668
Other assets	1,523	1,055
Non-current assets of discontinued operations		23,371
Total assets	$ 101,007	$ 141,774
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Notes payable	$ 1,236	$
Accounts payable	562	2,171
Accrued expenses and other liabilities	10,591	12,013
Income taxes payable	5,435	6,784
Unearned revenue	21,010	25,239
Current portion of long-term debt	8,100	9,674
Current liabilities of discontinued operations		4,303
Total current liabilities	46,934	60,184
Long-term debt	20,701	24,751
Other long-term obligations	2,317	2,465
Long-term liabilities of discontinued operations		3,182
Minority interests	4,403	3,637
Commitments and contingencies (Note 12)		
Stockholders equity:		
Common stock, $0.01 par value, 7,500 shares authorized; 380 shares issued and outstanding		
Class A common stock, $0.01 par value, 10,000,000 shares authorized; 7,365,804 shares issued, 7,358,082 shares outstanding	74	68
Additional paid-in capital	74,070	67,010
Accumulated deficit	(47,665)	(19,632)
Accumulated other comprehensive income	258	194
Less: treasury stock, at cost, 7,722 shares	(85)	(85)
Total stockholders equity	26,652	47,555
Total liabilities and stockholders equity	$ 101,007	$ 141,774

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

Security Capital Corporation and Subsidiaries

Condensed Consolidated Statements of Income

(unaudited)

(in thousands, except per share amounts)	Three Months Ended June 30, 2006	2005	Six Months Ended June 30, 2006	2005
Revenues	$ 38,610	$ 36,478	$ 75,922	$ 68,063
Selling, general and administrative expenses	33,928	32,006	66,249	60,880
Depreciation and amortization	1,231	1,161	2,459	2,054
Operating income	3,451	3,311	7,214	5,129
Interest expense	(611)	(684)	(1,235)	(1,114)
Other income, net	977	186	1,078	325
Income from continuing operations before income taxes, minority interest and gain on sale of discontinued operations	3,817	2,813	7,057	4,340
Income tax (expense) benefit	(169)	448	(1,386)	(232)
Minority interest in income of consolidated subsidiaries	(432)	(451)	(766)	(711)
Income from continuing operations	3,216	2,810	4,905	3,399
Income from discontinued operations (net of tax of $233 for the six months ended June 30, 2006 and $585 and $1,173 for the three and six months ended June 30, 2005, respectively)		1,005	448	2,018
Gain on sale of discontinued operations (net of tax of $21,044 for the six months ended June 30, 2006)	(3,431)		33,135	
Net (loss) income	$ (215)	$ 3,815	$ 38,488	$ 5,415
Net (loss) income	$ (215)	$ 3,815	$ 38,488	$ 5,415
Unrealized gain (loss) on interest rate swap (net of tax and minority interest of $24 and $(83) for the three months ended June 30, 2006 and 2005, respectively, and tax and minority interest of $66 and $32 for the six months ended June 30, 2006 and 2005, respectively)	25	(74)	65	28
Comprehensive (loss) income	$ (190)	$ 3,741	$ 38,553	$ 5,443
Basic (loss) earnings per common share:				
Earnings from continuing operations	$ 0.44	$ 0.41	$ 0.70	$ 0.51
(Loss) earnings from discontinued operations	(0.47)	0.15	4.76	0.30
Basic (loss) earnings per common share	$ (0.03)	$ 0.56	$ 5.46	$ 0.81
Diluted (loss) earnings per common share:				
Earnings from continuing operations	$ 0.44	$ 0.41	$ 0.69	$ 0.48
(Loss) earnings from discontinued operations	(0.47)	0.14	4.74	0.30
Diluted (loss) earnings per common share	$ (0.03)	$ 0.55	$ 5.43	$ 0.78
Basic weighted average shares used in computation	7,263	6,771	7,049	6,677
Diluted weighted average shares used in computation	7,263	6,861	7,080	6,757

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

Security Capital Corporation and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(unaudited)

(in thousands)	**For the Six Months Ended June 30, 2006**	**2005**
Cash flows from operating activities:		
Net income	$ 38,488	$ 5,415
Adjustments to reconcile net income to net cash provided by operating activities:		
Income from discontinued operations	(448)	(2,018)
Gain on sale of discontinued operations	(33,135)	
Benefit from reversal of certain reserves	(1,431)	(1,684)
Stock-based compensation	389	
Depreciation	1,280	1,105
Amortization	1,179	949
Minority interest in income of consolidated subsidiary	766	711
Amortization of deferred financing costs	96	91
Allowances for doubtful accounts	63	238
Unrealized gain on derivative		(153)
Changes in operating assets and liabilities, net of effects of acquisition:		
Decrease in accounts receivable	2,681	3,180
Increase in other assets	(1,578)	(295)
Decrease in unearned revenue	(4,229)	(9,725)
Decrease in accounts payable, accrued expenses and other liabilities	(4,797)	(3,567)
Cash flow from discontinued operations	853	425
Net cash provided by (used in) operating activities	177	(5,328)
Cash flows from investing activities:		
Net proceeds from sale of subsidiary (net of tax See Note 4)	57,807	
Capital expenditures	(1,139)	(1,042)
Acquisition (net of acquired cash of $2,611 in 2005)		(13,730)
Net cash provided by (used in) investing activities	56,668	(14,772)
Cash flows from financing activities:		
Proceeds from long-term borrowings (net of deferred financing costs of $141)		40,359
Repayments of long-term borrowings	(5,624)	(26,954)
Proceeds from notes payable borrowings	15,408	2,465
Repayments of notes payable	(14,172)	(450)
Dividends paid	(66,521)	
Proceeds from employee stock option exercises	5,329	1,960
Tax benefit of stock option exercises	1,348	201
Net cash (used in) provided by financing activities	(64,232)	17,581
Decrease in cash and cash equivalents	(7,387)	(2,519)
Cash and cash equivalents, beginning of period	8,940	10,400
Cash and cash equivalents, end of period	$ 1,553	$ 7,881
Supplemental cash flow information:		
Non-cash investing activities		
Accrued transaction costs related to acquisition	$	$ 479

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

Security Capital Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements *(unaudited)*

(in thousands, except share and per share amounts, unless otherwise noted)

(1) Basis of Presentation

The unaudited interim financial statements of Security Capital Corporation and its subsidiaries (the Company, we, us and our) have been prepared in accordance with United States generally accepted accounting principles (GAAP) and the instructions to Form 10-Q and Article 10 of Regulation S-X and should be read in conjunction with the financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2005. In the opinion of management, all adjustments (which consist only of normal recurring adjustments) necessary to present fairly the financial position and results of operations for the interim periods presented have been made. The consolidated balance sheet at December 31, 2005 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements. The consolidated financial statements include 100% of the assets and liabilities of the Company s subsidiaries, and the ownership interests of the minority investors in the subsidiaries are recorded as minority interests.

(2) Organization and Description of Business

The Company operates as a holding company that actively participates in the management of its subsidiaries. Until March 31, 2006, we conducted business through our two majority-owned operating subsidiaries, WC Holdings, Inc. (WC) and Primrose Holdings, Inc. (Primrose).

WC, through its wholly owned subsidiary, CompManagement, Inc. (CMI), is a leading independent provider of comprehensive claims management, cost containment and consulting services designed to control the cost to employers of workers compensation, medical malpractice, automobile, general liability, unemployment and short- and long-term disability insurance benefits. WC s activities are primarily centered in Ohio, California, Virginia, Maryland, Texas, Michigan, Florida, Washington, Minnesota and New York. The operations of WC are reported in our Employer Cost Containment and Health Services segment. See Note 11 for further details regarding this operating segment.

Primrose, through its wholly owned subsidiary, Primrose School Franchising Company, Inc., is the exclusive franchisor of Primrose Schools, an industry leader in early childhood education and high-quality childcare services, with related activities in real estate consulting and site selection services. Due to the sale of Primrose on March 31, 2006, the results of operations and cash flows of Primrose for the six months ended June 30, 2006 are reported as discontinued operations (see Note 4). The operations of Primrose and its wholly owned subsidiaries had comprised our Educational Services segment.

The Company has an Advisory Services Agreement (the Agreement) with Capital Partners, Inc. (Capital Partners), the representative of the Company s controlling stockholder, whereby Capital Partners provides certain advisory services related to investments, general administration, corporate development, strategic planning, stockholder relations, financial matters and general business policy (see Note 10). Mr. Brian Fitzgerald controls Capital Partners and serves as our Chairman of the Board of Directors, President and Chief Executive Officer.

(3) Significant Accounting Policies

For additional disclosures with respect to our significant accounting policies, see our Annual Report on Form 10-K for the year ended December 31, 2005.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results could differ from those estimates. Significant estimates include an allowance for doubtful accounts, incurred but not reported employee health care costs, reserves for potential loss contingencies, the utilization of future tax benefits, the estimates and assumptions inherent in our goodwill impairment testing procedures, the allocation of the purchase price to the fair value of assets acquired and liabilities assumed, the determination of the economic lives of intangible assets, and the estimates inherent in the determination of the fair value of stock-based awards.

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Revenue Recognition

Revenues for the Employer Cost Containment and Health Services segment are derived from third-party administrator services, self-insured plan administrator services, consulting services, group rating services, and managed care administration services. Revenues are recorded based on the terms and duration of the related contracts. Revenues from managed care administration services with the Ohio Bureau of Workers Compensation (the OBWC) are recognized on a monthly basis based on the contracted administrative fee. Certain contracts also provide for an incentive or bonus award based on the attainment of certain criteria stipulated in the contracts. Revenues from incentive or bonus awards are recognized when they are earned and collectibility is reasonably assured. Cash received in advance of the services being provided is initially deferred and recognized as revenue on a pro rata basis over the related contract period, which typically ranges between three and 12 months.

Allowance for Doubtful Accounts

Receivables are comprised primarily of amounts due for contract services provided by WC. We establish an allowance for doubtful accounts based on a review of the current status of the receivable, customer credit evaluations, collection history and other pertinent information. Receivables are generally not collateralized.

Goodwill and Intangible Assets

Acquisitions are accounted for under the purchase method, whereby acquired tangible and intangible assets and assumed liabilities are recorded at fair value. Identified intangible assets are amortized over their estimated useful lives. The determination of fair value of tangible and intangible assets and their respective useful lives requires management to make certain estimates, judgments and assumptions.

Goodwill represents the excess of the purchase price of acquisitions over the estimated fair value of the tangible and identified intangible assets acquired and liabilities assumed. Goodwill is not amortized; however, it is subject to annual impairment testing. We conduct our annual impairment test at December 31. During the six months ended June 30, 2006, nothing came to our attention that would indicate that the carrying value of goodwill may be impaired.

Impairment of Long-lived Assets, Other Than Goodwill

We review long-lived assets, including intangible assets, for impairment in accordance with the provisions of Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144). SFAS 144 requires companies to test long-lived assets when events or circumstances lead management to believe that the carrying value of an asset may not be recoverable. During the six months ended June 30, 2006, nothing came to our attention that would indicate that the carrying value of a long-lived asset may not be recoverable.

Income Tax Expense and Accruals

Income taxes are accounted for in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*, whereby deferred taxes are recognized based on the temporary differences between the financial reporting basis and the tax basis of the assets and liabilities, using presently enacted rates. Certain judgment is required in determining our annual effective tax rate and in evaluating our tax positions. While we believe that our tax return positions are fully supportable, we expect that certain positions could be challenged, and we may not be able to successfully defend our positions. Accordingly, we establish certain reserves, including interest, for these items. We adjust these reserves as facts and circumstances change or as we become aware of additional information. In the second quarters of 2006 and 2005, we reversed $1,431 and $1,684, respectively, of previously recorded tax reserves due to the passage of time and management s belief that these reserves were no longer necessary. The reversal of these reserves reduced our reported income tax provision.

Certain items are included in our tax return at different times than they are reflected in our financial statements. As a result, our effective tax rate reflected in our financial statements is different than that reported in our tax return. Some of the differences are permanent, such as expenses that are not tax deductible, and some of the differences are temporary, and will reverse over time, such as depreciation expense. These temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that can be used as a tax deduction in our tax return in future years for which we have already recorded the benefit in our statements of income. We establish valuation allowances when we believe expected future taxable income will not be sufficient to realize the deferred tax asset.

In February 2006, we received notification that our federal tax return for 2004 was selected for examination. The examination is in process, and we cannot at this time assess what the outcome of the examination will be.

Stock Options

We have granted stock options to certain key employees and directors of the Company to purchase shares of Class A Common Stock of the Company. We have also granted stock options to certain key employees of WC to purchase shares of WC. We account for these stock options in accordance with the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R). We adopted the provisions of SFAS 123R effective July 1, 2005 (the Effective Date), using the modified prospective transition method allowed under SFAS 123R. Under this method, the provisions of SFAS 123R are applied to new awards and awards modified, repurchased or cancelled after the Effective Date.

Compensation cost for the unvested portion of awards outstanding as of the Effective Date is recognized as the requisite service is rendered after the Effective Date. During the second quarter of 2006, in connection with the declaration of a special cash dividend (see Note 9), the Board of Directors accelerated the vesting of 104,008 unvested stock options to purchase shares of Class A Common Stock of the Company. As a result of the accelerated vesting of these stock options, the remaining unrecognized compensation cost relating to these options of $236 was recognized in the quarter. Consolidated stock-based compensation expense for the three and six months ended June 30, 2006 was $312 and $389, respectively.

Prior to adopting SFAS 123R, we applied the disclosure only provisions of Statement of Financial Accounting Standards No. 148, *Accounting for Stock-Based Compensation - Transitions and Disclosure, an amendment to FASB Statement No. 123* (SFAS 148). The following table is presented in accordance with SFAS 148 and illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS 123R for the three and six months ended June 30, 2005:

	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005
Net income, as reported	$ 3,815	$ 5,415
Deduct: Stock-based compensation expense determined under the fair value method, net of related tax effects and minority interest	(156)	(307)
Pro forma net income	$ 3,659	$ 5,108
Basic earnings per common share:		
As reported	$ 0.56	$ 0.81
Pro forma	$ 0.54	$ 0.77
Diluted earnings per common share:		
As reported	$ 0.55	$ 0.78
Pro forma	$ 0.53	$ 0.74

(4) Sale of Primrose

On March 31, 2006, we completed the sale of Primrose for a net aggregate sale price of $82,800, after giving effect to certain adjustments set forth in the definitive stock purchase agreement. We received net pre-tax proceeds of $76,753 for our 91.52% (on a fully diluted basis) interest and incurred a net tax liability of $18,946. The net tax liability is composed of a $21,044 tax liability arising out of the sale of Primrose less a $2,098 estimated tax benefit from certain compensation deductions that will arise in connection with the consummation of the merger. Our net after-tax proceeds from the sale of Primrose were $57,807.

Due to the sale of Primrose, the results of operations and cash flows of Primrose for the six months ended June 30, 2006 are reported as discontinued operations. The sale of Primrose was effective March 31, 2006; accordingly, the results of operations and cash flows of Primrose for the three months ended June 30, 2006 are not included in our consolidated financial statements. The financial statements at December 31, 2005 and for the three and six months ended June 30, 2005 have been restated to present the financial condition, results of operations and cash flows of Primrose as discontinued operations consistent with the 2006 presentation. Revenues and income from discontinued operations for the

three and six months ended June 30, 2006 and 2005 were as follows:

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	Three Months Ended June 30, 2006	2005	Six Months Ended June 30, 2006	2005
Revenues	$	$ 3,389	$ 4,010	$ 6,691
Net income	$	$ 1,005	$ 448	$ 2,018
Gain on sale of discontinued operations	(3,431)		33,135	
Total income from discontinued operations	$ (3,431)	$ 1,005	$ 33,583	$ 2,018

During the second quarter of 2006, the determination of the amount of taxes owed from the sale of Primrose was finalized and resulted in a downward adjustment of $3,431 to our previously reported gain.

At December 31, 2005, the assets and liabilities of Primrose consisted of the following:

Cash and cash equivalents	$ 3,400
Restricted cash	175
Accounts receivable, net	1,400
Recoverable costs, net	817
Deferred tax assets	1,348
Other assets	285
Current assets of discontinued operations	$ 7,425
Property, plant and equipment, net	$ 308
Goodwill, net	16,830
Intangible assets, net	6,179
Other	54
Non-current assets of discontinued operations	$ 23,371
Accounts payable	$ 254
Accrued expenses and other liabilities	749
Unearned revenue	3,300
Current liabilities of discontinued operations	$ 4,303
Deferred taxes	$ 2,863
Minority interests	319
Long-term liabilities of discontinued operations	$ 3,182

(5) Sale of the Company

On June 12, 2006, we entered into a merger agreement to be acquired by Sedgwick CMS Holdings, Inc. (Sedgwick CMS). The merger contemplated by the merger agreement is subject to a vote of the stockholders of Security Capital at a special meeting of stockholders scheduled to be held on September 8, 2006 (the Special Meeting). Under the terms of the merger agreement, Security Capital stockholders will receive $16.46 per share in cash for their Company shares.

Concurrent with the execution of the merger agreement, the holders of approximately 80% of the Company s outstanding Class A Common Stock and Common Stock (including Brian D. Fitzgerald and CP Acquisition, L.P. No. 1) entered into a voting agreement with Sedgwick CMS pursuant to which these stockholders have agreed, among other things, to vote all of their shares in favor of the merger. The voting agreement will terminate if the merger agreement is terminated.

In order to enable Sedgwick CMS to acquire 100% of the principal subsidiaries of Security Capital, the Company has also entered into a stock purchase agreement to acquire all of the outstanding WC shares and options not currently owned by the Company. It is expected that the Company will acquire such shares and options immediately prior to consummating the merger.

Additionally, concurrent with the execution of the merger agreement and the WC stock purchase agreement, certain of the Company s stockholders (including Brian D. Fitzgerald, CP Acquisition, L.P. No. 1 and each of the Company s directors) and the minority holders of WC shares and options have entered into an indemnification agreement pursuant to which such parties have agreed to provide Sedgwick CMS with indemnification with respect to certain matters. As security for such indemnification, a portion of the consideration otherwise payable to such stockholders under the merger agreement and the WC stock purchase agreement will be placed into escrow at the time such transactions are consummated. The Company s public stockholders will not be subject to such indemnification agreement, and none of the merger consideration payable to the public stockholders will be placed into escrow.

The consummation of the merger is subject to customary closing conditions, including the approval of Security Capital stockholders and the Company s acquisition of all of the shares and options of WC not currently owned by the Company. The merger is expected to close shortly after receiving stockholder approval at the Special Meeting. Upon such closing, shares of the Company s Class A Common Stock will no longer be listed on the American Stock Exchange and will be deregistered under the Securities Exchange Act of 1934, as amended.

(6) Acquisition

On March 31, 2005, we acquired, through our indirect, majority-owned subsidiary, Octagon Risk Services, Inc., 100% of the outstanding capital stock of Managed Care Holdings Corporation (MCHC) and its wholly owned subsidiary, Caronia Corporation (Caronia). Upon the consummation of the transaction, MCHC and Caronia became part of our Employer Cost Containment and Health Services operating segment.

The results of Caronia are reflected in our condensed consolidated statements of income from the acquisition date. Accordingly, the condensed consolidated statement of income for the six months ended June 30, 2005 includes the operating results of Caronia from April 1, 2005.

The following unaudited pro forma statement of income presents the combined results of the Company and Caronia for the six months ended June 30, 2005 as if the acquisition of Caronia had taken place on January 1, 2005. The pro forma amounts give effect to the amortization of intangibles, increased interest expense and the related income tax and minority interest effects. This pro forma information does not necessarily reflect the results of operations if the business had been managed by the Company during this period and is not indicative of results that may be obtained in the future.

Revenues	$ 71,781
Selling, general and administrative expenses	63,769
Depreciation and amortization	2,259
Operating income	5,753
Interest expense	(1,385)
Other income, net	325
Income from continuing operations before income taxes and minority interest	4,693
Income tax expense	(550)
Minority interest in income of consolidated subsidiaries	(718)
Income from continuing operations	3,425
Income from discontinued operations	2,018
Net income	$ 5,443
Basic earnings per common share:	
Continuing operations	$ 0.52
Discontinued operations	0.30
Total	$ 0.82
Diluted earnings per common share:	
Continuing operations	$ 0.48
Discontinued operations	0.30
Total	$ 0.78

(7) Earnings (Loss) Per Share

Basic earnings (loss) per common share (EPS) are derived by dividing net income (loss) by the weighted average shares outstanding. The denominator for diluted EPS includes the weighted average shares outstanding plus the additional shares issued from the assumed exercise of stock options in Company stock and in stock of subsidiary companies (diluted shares). The assumed exercise of stock options of subsidiary companies has the effect of reducing our earnings (diluted earnings) since our overall ownership interest in the subsidiary companies, and thus our share of the net income of the subsidiaries, would be reduced. Diluted EPS are derived by dividing diluted earnings by the weighted average diluted shares outstanding. The calculation of basic and diluted EPS for the three and six months ended June 30, 2006 and 2005 is shown below. Share amounts are in thousands.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Basic weighted average shares outstanding denominator for basic EPS	7,263	6,771	7,049	6,677
Dilutive effect of stock options		90	31	80
Diluted weighted average shares outstanding denominator for diluted EPS	7,263	6,861	7,080	6,757
Income from continuing operations numerator for basic EPS from continuing operations	$ 3,216	$ 2,810	$ 4,905	$ 3,339
(Loss) income from discontinued operations numerator for basic EPS from discontinued operations	(3,431)	1,005	33,583	2,018
Net (loss) income numerator for basic EPS	(215)	3,815	38,488	5,415
Effect of subsidiary stock options on income	(13)	(52)	(44)	(129)
Diluted earnings numerator for diluted EPS	$ (228)	$ 3,763	$ 38,444	$ 5,286
Basic (loss) earnings per common share:				
Earnings from continuing operations	$ 0.44	$ 0.41	$ 0.70	$ 0.51
(Loss) earnings from discontinued operations	(0.47)	0.15	4.76	0.30
Basic EPS	$ (0.03)	$ 0.56	$ 5.46	$ 0.81
Diluted (loss) earnings per common share:				
Earnings from continuing operations	$ 0.44	$ 0.41	$ 0.69	$ 0.48
(Loss) earnings from discontinued operations	(0.47)	0.14	4.74	0.30
Diluted EPS	$ (0.03)	$ 0.55	$ 5.43	$ 0.78

(8) Long-Term Debt and Notes Payable

Our debt at June 30, 2006 consisted of amounts outstanding under a five-year, fully-amortizing term loan and borrowings under a revolving line of credit. The term loan was issued on March 31, 2005 by WC and had an initial principal amount of $40,500 (the Term Loan). The Term Loan bears interest at LIBOR plus 2.5% or Prime, at the Company s option and matures March 31, 2010. Principal payments of $675 are due monthly, and an additional principal payment is due on April 30 of each year, based on the earnings of WC, as defined, for the preceding fiscal year. The additional principal payment based on 2005 earnings of WC was $1,574 and was paid during the second quarter of 2006. The outstanding balance of the Term Loan at June 30, 2006 was $28,801, including the current portion of $8,100.

WC also maintains an $8,000 revolving line of credit (the Revolver). Borrowings under the Revolver bear interest at LIBOR plus 2.0% or Prime minus 0.5%, at the Company s option. At June 30, 2006, there was $1,236 outstanding under the Revolver. WC had outstanding letters of credit aggregating $1,250 at June 30, 2006, which reduce the amount of available borrowing capacity under the Revolver on a dollar-for-dollar basis. At June 30, 2006, WC could borrow up to an additional $5,514 under the Revolver.

The Term Loan and Revolver contain restrictive covenants that prohibit or limit certain actions, including specified levels of capital expenditures, investments and incurrence of additional debt, and require the maintenance of a minimum fixed charge ratio. Borrowings are secured by a pledge of substantially all assets at the subsidiary level, as well as a pledge of the Company s ownership in the subsidiary. Management believes that the Company is currently in compliance with all of these requirements.

(9) Stock Options and Stockholders Equity

For the three months ended June 30, 2006, options to purchase 209,510 shares of Class A Common Stock were exercised at a weighted average exercise price of $9.56, and the Company issued 209,510 shares of Class A Common Stock to satisfy these option exercises. At June 30, 2006, there were no remaining outstanding options. No options were exercised in the three months ended June 30, 2005.

For the six months ended June 30, 2006, options to purchase 587,510 shares of Class A Common Stock were exercised at a weighted average exercise price of $9.06, and the Company issued 587,510 shares of Class A Common Stock to satisfy these option exercises. For the six months ended June 30, 2005, options to purchase 320,000 shares of Class A Common Stock were exercised at a weighted average exercise price of $6.13, and the Company issued 320,000 shares of Class A Common Stock to satisfy these option exercises.

On June 28, 2006, we paid a special cash dividend of $66,521, or $9.04 per share, to our stockholders. The cash to fund the dividend was obtained principally from the net after-tax proceeds from the Primrose sale.

(10) Related-Party Transactions

We pay Capital Partners an annual fee of $1,550 under the terms of the Agreement. The fee is payable quarterly at the beginning of each quarter. The Agreement is effective for the calendar year and terminable by either Capital Partners or the Company as of any December 31 upon not less than 60 days prior written notice to the other. Fees paid to Capital Partners for advisory services provided under the Agreement were $388 and $775 for the three and six months ended June 30, 2006 and 2005.

The Agreement also provides for the payment of investment banking fees to Capital Partners for acquisition opportunities presented to the Company at usual and customary rates for transactions of similar size and complexity. Capital Partners is under no obligation to present to the Company any or all acquisition candidates of which it becomes aware. Furthermore, the Company is under no obligation to utilize Capital Partners for investment banking services. The payment of an investment banking fee to Capital Partners requires the approval of the Audit Committee, the Compensation Committee and the full Board of Directors. We paid Capital Partners an investment banking fee of $240 in May 2005 in connection with the Caronia acquisition.

In December 2005, the Company and Primrose entered into the Second Amended and Restated Advisory Services Agreement (the Amended Agreement) with Capital Partners effective January 1, 2006. The Amended Agreement with Capital Partners is similar to the Agreement with respect to fees and scope of services; however, under the terms of the Amended Agreement, if the Company and/or Primrose were sold prior to June 30, 2006, Capital Partners would continue to provide services to the Company and/or Primrose under the Amended Agreement for a period of six months following the effective date of sale.

In addition, under the Amended Agreement, Capital Partners provides advisory services to the Company in connection with managing the formal sale process, including in the areas of planning such sale process, selecting and evaluating potential buyers, negotiating directly or indirectly with potential buyers and consummating a sale of the Company. In exchange for such services, if the sale of the Company were consummated on or before June 30, 2006, the Company would pay Capital Partners a sale bonus of $2,000 (the Incentive Sale Bonus), plus or minus an amount (the Adjustment Amount) based on the aggregate sale proceeds obtained from the sale of the Company.

In connection with the closing of the sale of Primrose, on March 31, 2006 the Amended Agreement was amended to remove Primrose as a party to the Amended Agreement, and to require Primrose to pay Capital Partners at the closing Primrose s $194 share of the advisory fee owed by the Company to Capital Partners. On May 11, 2006, the Amended Agreement was further amended to extend the date by which Capital Partners could earn the Incentive Sale Bonus and Adjustment Amount from June 30, 2006 to September 30, 2006. Concurrently with the execution of the merger agreement with Sedgwick CMS, on June 12, 2006 the Amended Agreement was again amended to provide that the Amended Agreement would automatically terminate on the closing of the merger, and that Capital Partners right to receive any remaining portion of the advisory fee, the Incentive

Sale Bonus and Adjustment Amount survives the termination of the Agreement. The amendment also clarifies that, for purposes of calculating the Incentive Sale Bonus, the Per Share Consideration (as defined in the Amended Agreement) includes the aggregate dollar value per share to be received by the Company s stockholders in connection with the merger, without regard to any amount placed in escrow or used to satisfy indemnification claims, and the aggregate dollar value per share of the special cash dividend. Each of the Amended Agreement, the March 31, 2006 amendment, the May 11, 2006 amendment and the June 12, 2006 amendment was unanimously approved by the Audit Committee, the Compensation Committee and the full Board of Directors.

In connection with the execution of the merger agreement, the Company and Capital Partners also entered into an Assignment and Assumption of Lease, dated as of June 12, 2006 (the Lease Assignment), with respect to the lease covering certain premises in Greenwich, Connecticut that serve as the Company s corporate headquarters (the Lease). Pursuant to the Lease Assignment, the Company will assign to Capital Partners all of its right, title, interest, obligations and liabilities in, to and under the Lease and pay Capital Partners the sum of $125 to assume the Lease on the closing of the merger. In connection with the Lease Assignment, the Company also assigned to Capital Partners a sublease covering a portion of the premises and transferred to Capital Partners certain furnishings and leasehold improvements at the premises. The terms of the Lease Assignment and the related agreements were established through arms -length negotiations between Capital Partners and the Audit Committee and unanimously approved by the Audit Committee, the Compensation Committee and the full Board of Directors.

(11) Segment Disclosure

After the sale of Primrose, we have one operating segment, the Employer Cost Containment and Health Services segment. Management evaluates the performance of this segment based upon segment income, defined as earnings before interest, taxes, depreciation, amortization, minority interests, corporate expenses and management fee, other income and discontinued operations. Segment income is used to evaluate performance because management believes this is the best financial indicator of value, our ability to incur and service debt, and to generate operating cash flows. It is also one method by which management evaluates and values potential acquisition opportunities. Segment income is not a substitute for operating income or cash flows from operating activities determined in accordance with GAAP. Segment income was $6,734 and $5,624 for the three months ended June 30, 2006 and 2005, respectively, and $12,506 and $9,180 for the six months ended June 30, 2006 and 2005, respectively. A reconciliation of segment income to its most comparable GAAP measure, net income, is provided below:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2006	**2005**	**2006**	**2005**
Segment income	$ 6,734	$ 5,624	$ 12,506	$ 9,180
Depreciation and amortization	(1,231)	(1,161)	(2,459)	(2,054)
Interest expense	(611)	(684)	(1,235)	(1,114)
Income tax (expense) benefit	(169)	448	(1,386)	(232)
Minority interest	(432)	(451)	(766)	(711)
Corporate expenses and management fee	(2,052)	(1,152)	(2,833)	(1,997)
Other income	977	186	1,078	325
Income from discontinued operations		1,005	448	2,018
Gain on sale of discontinued operations	(3,431)		33,135	
Net (loss) income				