AMERICAN PHYSICIANS SERVICE GROUP INC
Form 10QSB
November 14, 2002

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON D.C. 20549

FORM 10-QSB

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF
THE SECURITIES EXCHANGE ACT OF 1934
FOR THE PERIOD ENDED SEPTEMBER 30, 2002

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 0-11453

AMERICAN PHYSICIANS SERVICE GROUP, INC.
(Exact name of registrant as specified in its charter)

TEXAS	75-1458323
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer identification No.)

1301 CAPITAL OF TEXAS HIGHWAY AUSTIN, TEXAS 78746
(Address of principal executive offices) (Zip Code)

(512) 328-0888
(Registrant's telephone number, including area code)

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

YES X NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

TITLE OF EACH CLASS	NUMBER OF SHARES OUTSTANDING AT November 4, 2002
Common Stock, $.10 par value	2,199,143

PART I

FINANCIAL INFORMATION

Item 1 - Financial Statements

AMERICAN PHYSICIANS SERVICE GROUP, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(In thousands)

	Three Months Ended September 30, 2002	Three Months Ended September 30, 2001
Revenues:		
Financial services	$3,429	$3,212
Insurance services	2,854	2,230
Consulting	899	821
Investments and other	59	5
Total revenue	7,241	6,268
Expenses:		
Financial services	3,078	2,869
Insurance services	2,291	1,864
Consulting	760	991
General and administrative	710	235
Gain on sale of assets	(126)	--
Total expenses	6,713	5,959
Operating income	528	309
Gain on sale of investments (Note 4)	64	--
Equity in earnings (loss) of unconsolidated affiliates (Note 5)	--	34
Earnings from continuing operations before interest, income taxes and minority interests	592	343
Interest expense	4	124
Income tax expense	222	95
Minority interests	(70)	(42)

Earnings from continuing operations	296	82
Discontinued operations:		
Earnings from discontinued operations, net of income tax expense of $18 and $56 for the three and nine months in 2001	--	35
Net earnings	$296	$117

See accompanying notes to consolidated financial statements.

AMERICAN PHYSICIANS SERVICE GROUP, INC.
CONSOLIDATED STATEMENT OF EARNINGS PER SHARE (UNAUDITED)

(In thousands, except per share amounts)

	Three Months Ended September 30,	
	2002	2001
Earnings (loss) per common share		
Basic:		
Earnings from continuing operations	$0.13	$0.04
Discontinued operations	--	0.01
Net earnings	$0.13	$0.05
Diluted:		
Earnings from continuing operations	$0.13	$0.04
Discontinued operations	--	0.01
Net earnings	$0.13	$0.05
Basic weighted average shares outstanding	2,223	2,343
Diluted weighted average shares outstanding	2,357	2,608

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See accompanying notes to consolidated financial statements.

AMERICAN PHYSICIANS SERVICE GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

	September 30, 2002	December 31, 2001
ASSETS	(Unaudited)	
Current Assets:		
Cash and cash equivalents	$9,543	$3,851
Trading account securities	106	149
Trade receivables, net	709	603
Notes receivable - current	602	573
Management fees and other receivables	496	484
Deposit with clearing organization	499	499
Receivable from clearing organization	70	69
Net deferred income tax asset	--	282
Income tax receivable	--	167
Prepaid expenses and other	539	1,147
Total current assets	12,564	7,824
Notes receivable, less current portion	566	999
Property and equipment	396	415
Investment in available for sale equity securities (Note 5)	6,953	--
Investment in available for sale fixed income securities	1,394	--
Investment in affiliate (Note 5)	--	10,700
Other investments	10	68
Net deferred income tax asset - non-current	3,127	1,453
Other assets	200	201
Total Assets	$25,210	$21,660

See accompanying notes to consolidated financial statements.

AMERICAN PHYSICIANS SERVICE GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS, continued

(In thousands, except share data)

	September 30, 2002
LIABILITIES AND SHAREHOLDERS' EQUITY	(Unaudited)
Current liabilities:	
Accounts payable - trade	$1,096
Payable to clearing broker	156
Accrued incentive compensation	1,401
Accrued expenses and other liabilities (Note 6)	458
Income tax payable	980
Deferred gain - current	488
Deferred tax liability - current	748
Total current liabilities	5,327
Payable under loan participation agreements	259
Deferred gain - non-current	1,983
Notes payable - long term	--
Total liabilities	7,569
Minority interests	309
Shareholders' Equity:	
Preferred stock, $1.00 par value, 1,000,000 shares authorized, none issued or outstanding	--
Common stock, $0.10 par value, shares authorized 20,000,000; 2,206,543 issued at 9/30/02 and 2,745,231 at 12/31/01 2,206,543 outstanding at 9/30/02 and 2,359,231 at 12/31/01	215
Additional paid-in capital	5,590
Retained earnings	9,395
Accumulated other comprehensive income (loss), net of taxes	2,132
Treasury stock, at cost, zero shares at 9/30/02 and 386,000 shares at 12/31/01	--
Total shareholders' equity	17,332
Total Liabilities and Shareholders' Equity	$25,210

See accompanying notes to consolidated financial statements.

AMERICAN PHYSICIANS SERVICE GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(In thousands)

	Nine Months Ended September 30,	
	2002	2001
Cash flows from operating activities:		
Cash received from customers	$19,195	$17,678
Cash paid to suppliers and employees	(17,332)	(16,719)
Change in trading account securities	43	37
Change in receivable from clearing organization	(99)	(73)
Interest paid	(24)	(397)
Income tax paid	(2,406)	(45)
Interest, dividends and other investment proceeds	103	91
Net cash (used in) provided by operating activities	(520)	572
Cash flows from investing activities:		
Capital expenditures	(133)	(176)
Proceeds from the sale of an investment	10,719	--
Purchase of bonds	(1,394)	--
Investments in and advances to affiliate	(230)	--
Funds loaned to others	(150)	(2,373)
Collection of notes receivable	558	1,736
Other	--	66
Net cash provided by (used in) investing activities	9,370	(747)
Cash flows from financing activities:		
Proceeds from borrowings	--	1,715
Payment of long term debt	(2,275)	(1,208)
Purchase of treasury stock	(1,058)	--
Exercise of stock options	175	--
Distribution to minority interest	--	(80)
Net cash provided by (used in) financing activities	(3,158)	427
Net change in cash and cash equivalents	$5,692	$252
Cash and cash equivalents at beginning of period	3,851	2,988
Cash and cash equivalents at end of period	$9,543	$3,240

See accompanying notes to consolidated financial statements.

AMERICAN PHYSICIANS SERVICE GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED), continued

(In thousands)

	Nine Months Ended September 30, 2002	Nine Months Ended September 30, 2001
Reconciliation of net earnings to net cash provided by operating activities:		
Net earnings	$3,347	$527
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	152	214
Forgiveness of debt and other	151	164
Minority interest in consolidated earnings	185	105
Undistributed loss of affiliates	44	62
Gain on sale of assets	(881)	--
Gain on sale of investment	(2,797)	--
Change in income tax receivable	1,147	468
Provision for deferred taxes	(1,631)	(146)
Provision for bad debt	117	15
Change in trading account securities	43	37
Change in receivable from clearing organization	(99)	(73)
Change in management fees & other receivables	(12)	(603)
Change in trade receivables	(223)	(42)
Change in prepaid expenses & other assets	609	(1)
Change in trade accounts payable	52	(88)
Change in accrued expenses & other liabilities	(724)	(67)
Net cash (used in) provided by operating activities	($520)	$572

See accompanying notes to consolidated financial statements.

AMERICAN PHYSICIANS SERVICE GROUP, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)
For the Nine Months Ended September 30, 2001 and 2002
(In thousands)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Comprehensive Income (loss)	Accum Ot Compr Incom

Balance December 31, 2000 (audited)	$ 275	$ 5,539	$ 8,888		$
Comprehensive income:					
Net income	--	--	527	527	
Other comprehensive loss:					
Unrealized loss on securities, net of tax of $2	--	--	--	(26)	
Comprehensive income	--	--	--	501	
Balance Sept 30, 2001 (unaudited)	$ 275	$ 5,539	$ 9,415	$ --	$
Balance December 31, 2001(audited)	$ 275	$ 5,539	$ 8,310		$
Comprehensive income:					
Net income	--	--	3,347	$ 3,347	
Other comprehensive income:					
Unrealized gain on securities, net of taxes of $1,118	--	--	--	2,171	2,
Comprehensive income	--	--	--	$ 5,518	
Treasury stock purchases	--	--	--		
Cancelled treasury stock	(61)	--	(2,415)		
Stock options exercised	1	21	154		
Stock Options expensed	--	30	--		
Balance Sept 30, 2002 (unaudited)	$215	$5,590	$9,395	$ --	$ 2,

See accompanying notes to consolidated financial statements.

AMERICAN PHYSICIANS SERVICE GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2002
(Unaudited)

1. GENERAL

The accompanying unaudited consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States of America have been condensed or omitted pursuant to such rules and regulations. The consolidated financial statements for the three and nine months ended September 30, 2002 and 2001 reflect all adjustments which are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows for the periods presented. Such adjustments consist of only items of a normal recurring nature. These consolidated financial statements have not been audited by our independent certified public accountants. The operating results for the interim periods are not necessarily indicative of results for the full fiscal year.

The notes to consolidated financial statements appearing in our Annual Report on Form 10-KSB for the year ended December 31, 2001 filed with the Securities Exchange Commission should be read in conjunction with this Quarterly Report on Form 10-QSB. There have been no significant changes in the information reported in those notes other than from normal business activities.

Certain reclassifications have been made to amounts in prior periods to be consistent with the 2002 presentation.

2. MANAGEMENT'S ESTIMATES

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

3 CONTINGENCIES

Under agreements with former doctor shareholders of Syntera, our practice management company that was merged with FemPartners in 1999, we agreed to exchange their shares in Syntera for the common stock of American Physicians Service Group, Inc., or cash, if the Syntera shares did not become publicly traded. Through March 31, 2002 we paid approximately

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3 CONTINGENCIES, continued

$2,956,000 in cash related to these agreements, thus satisfying all liabilities related to these agreements.

We have extended various lines of credit to Uncommon Care totaling $4.69 million with interest rates between 10% and 12%. During 2001 we agreed to modify the terms of the foregoing notes. For the period July 1, 2001 through September 30, 2002 the interest rate was 4% and payments were paid in-kind (PIK) in the form of Uncommon Care common stock at $0.57 per share. Additionally, the PIK stock may be repurchased by Uncommon Care through June 30, 2004 at a price of $.64 per share. We agreed to these modified terms to improve Uncommon Care's liquidity and to assist it in complying with the terms of its bank covenants. PIK payments during 2002 increased our ownership in Uncommon Care preferred and common stock from 38% to 42% as of September 30, 2002 on a fully converted basis.

During the year we guaranteed a loan in the maximum amount of $110,000 for a director, William Searles. The guarantee was collateralized by Mr. Searles' options to purchase American Physicians and Prime Medical shares as well as Mr. Searles' common stock interest in Uncommon Care. As a result of recent regulatory restrictions, we informed all of our officers and directors that we could no longer make or guarantee loans. The loan had a zero balance as of the date of this filing.

We are involved in various claims and legal actions that have arisen in the ordinary course of business. Management believes that any liabilities arising from these actions will not have a significant adverse effect on our financial condition or results of operations.

During the third quarter of 2002 we entered into discussions with senior management of our environmental consulting subsidiary, Eco Systems, Inc. ("Eco"), regarding a management buyout of Eco. We expect to complete the transaction following the date of this report. Terms of the transaction call for us to recover, on an accelerated basis, certain loans made to Eco and for Eco to continue our management services agreement. We do not expect the transaction to have a material impact on our financial condition or results of operations.Eco had been acquired in a foreclosure proceeding related to loans which we had made in 1996 and does not fit into our long-term business plan.

4. GAIN RECOGNITION

During the three and nine months ended September 30, 2002, we sold 11,200 and 1,591,200 shares of the common stock of Prime Medical reducing our interest to less than 5%. In connection with these sales we received proceeds of approximately $119,000 and $10,719,000 and recognized a gain of $64,000 and $2,855,000, respectively.

4. GAIN RECOGNITION, continued

Additionally, we recognized $512,000 of deferred gain related to the sale of real estate to Prime in November 2001. At the time of the real estate sale, we deferred a portion of the total gain to reflect our interest in the purchaser. During the first nine months of 2002, we have recognized these deferred gains proportionately to our reduction of our interest in Prime.

5. EQUITY IN EARNINGS OF UNCONSOLIDATED AFFILIATES

At September 30, 2002 we owned less than 5% (752,603 shares) of the outstanding common stock of Prime Medical. As a result of our reduced ownership interest and as a result of Board of Directors changes mentioned in our Form 10-KSB for the year ended December 31, 2001, we ceased accounting for our investment in Prime Medical using the equity method effective March 19, 2002 and began accounting for our investment in Prime as an available for sale security in accordance with SFAS 115. Accordingly, our investment in Prime Medical is reported at fair value in our balance sheet. We recognized $186,000 of equity earnings during the first quarter of 2002 prior to converting to the cost method. This change in accounting also resulted in a balance sheet reclassification for our investment in Prime Medical from "Investment in Affiliate" to "Investment in Available for Sale Equtiy Securities".

The common stock of Prime Medical is traded in the over-the-counter market under the symbol "PMSI". Prime Medical is a Delaware corporation which is required to file with the Securities and Exchange Commission annually, quarterly and other reports and documents containing financial and other information regarding Prime Medical. Such reports and documents may be examined and copies may be obtained from the offices of the Securities and Exchange Commission. A table detailing our investment in Prime Medical follows:

Fair Value September 30, 2002			Book Value at Date of Conversion *	
No. of Shares Owned	MV per Share	Fair Value	BV per Share	Book Value

752,603	$9.24	$6,953,000	$5.02	$3,837,000

* Book Value at March 19, 2002, the date of conversion from accounting for our investment in Prime Medical common stock using the equity method to accounting for it as a marketable security.

The difference between the September 30, 2002 fair value and book value at date of conversion is classified on the consolidated balance sheet in accumulated other comprehensive income.

5. EQUITY IN EARNINGS OF UNCONSOLIDATED AFFILIATES, continued

The condensed statements of operations for Prime Medical follows (unaudited, in thousands):

Condensed statements of operations for the nine months ended September 30, 2002 and 2001

	2002	2001
Total revenue	$126,305	$114,092
Gross profit	25,151	50,122
Income from continuing operations	19,851	39,465
Net income (loss)	(2,970)	6,313

At September 30, 2002 the Company owned convertible preferred and common stock of Uncommon Care, a developer and operator of dedicated Alzheimer's care facilities. We have applied the guidance of EITF 99-10, specifically the percentage of ownership method, in applying the equity method to our investment in Uncommon Care. Uncommon Care's common stock equity had been eliminated by losses prior to our investment and, accordingly, we recognized 100% of the losses of Uncommon Care based on our ownership of 100% of its preferred stock equity and subordinated debt. During 2001 our total basis in our investment and advances to Uncommon Care was reduced to zero. Until such time as Uncommon Care becomes profitable and our future equity in these profits fully offsets our prior period combined equity losses, future advances to Uncommon Care will result in a loss when advanced. Advances to Uncommon Care have totaled $230,000 through September 30, 2002.

The common and preferred shares owned by the Company, together with common stock to be paid-in-kind, are convertible into approximately a 42% interest in the common equity in Uncommon Care. We continue to record our investment in and advances to Uncommon Care on the equity method.

The condensed statements of operations for Uncommon Care follows (unaudited, in thousands):

Condensed statements of operations for the nine months ended September 30, 2002 and 2001

	2002	2001
Total revenue	$5,691	$4,756
Gross profit	980	376

Loss from continuing operations	(440)	(1,393)
Net loss	(631)	(1,322)

6. ACCRUED EXPENSES AND OTHER LIABILITIES

Accrued expenses and other liabilities consists of the following:

	September 30 2002 (Unaudited)	December 31 2001
Taxes	$ 79,000	$ 61,000
Contractual/legal fees and claims	13,000	1,031,000
Vacation	140,000	140,000
Other	226,000	105,000
	$458,000	$1,337,000

7. Earnings Per Share

Basic earnings per share is based on the weighted average shares outstanding without any dilutive effects considered. Diluted earnings per share reflect dilution from all contingently issuable shares, such as options and convertible debt. A reconciliation of earnings and average shares outstanding used in the calculation of basic and diluted earnings per share from continuing and discontinued operations follows:

7. EARNINGS PER SHARE, continued

	For the Three Months Ended September 30, 2002		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Earnings from continuing operations	$ 296,000		
Basic EPS			
Earnings available to common stockholders	296,000	2,223,000	$0.13
Effect of dilutive securities	--	134,000	
Diluted EPS			
Earnings available to common stockholders and assumed conversions	$ 296,000	2,357,000	$0.13

	For the Three Months Ended September 30, 2001		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Earnings from continuing operations	$ 82,000		
Discontinued operations, net of tax	35,000		
Basic EPS			
Earnings available to Common stockholders	117,000	2,343,000	$ 0.05
Effect of dilutive securities	--	265,000	
Diluted EPS			
Earnings available to common stockholders and assumed conversions	$ 117,000	2,608,000	$ 0.05

7. EARNINGS PER SHARE, continued

	For the Nine Months Ended September 30, 2002		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Earnings from continuing operations	$ 3,347,000		
Basic EPS			
Earnings available to common stockholders	3,347,000	2,266,000	$1.48
Effect of dilutive securities	--	127,000	
Diluted EPS			
Earnings available to common stockholders and assumed conversions	$ 3,347,000	2,393,000	$1.40

	For the Nine Months Ended September 30, 2001		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Earnings from continuing operations	$ 417,000		

Discontinued operations, net of tax	110,000		
Basic EPS			
Earnings available to common stockholders	527,000	2,343,000	$0.22
Effect of dilutive securities	--	258,000	
Diluted EPS			
Earnings available to common stockholders and assumed conversions	$ 527,000	2,601,000	$0.20

Unexercised employee stock options to purchase 116,500 and 515,500 shares of the Company's common stock for the three months ended September 30, 2002 and 2001, respectively, and to purchase 266,500 and 515,500 for the nine months ended September 30, 2002 and 2001, respectively, were not included in the computations of diluted EPS because the effect would be antidilutive as their exercise price exceeded the average stock price during the period.

8. SEGMENT INFORMATION

The Company's segments are distinct by type of service provided. Comparative financial data for the three and nine month periods ended September 30, 2002 and 2001 are shown as follows:

	Three months ended September 30,	
	2002	2001
Operating Revenue:		
Financial services	$3,429,000	$3,212,000
Insurance services	2,854,000	2,230,000
Consulting	899,000	821,000
Corporate	69,000	517,000
	$7,251,000	$6,780,000
Reconciliation to Consolidated Statement of Operations:		
Total segment revenues	$7,251,000	$6,780,000
Less: Intercompany dividends	--	(450,000)
Intercompany interest	(10,000)	(62,000)
Total Revenues	$7,241,000	$6,268,000
Operating Income (Loss)		
Financial services	$ 351,000	$ 343,000
Insurance services	563,000	366,000
Consulting	139,000	(170,000)
Corporate	(525,000)	(230,000)
Total segments operating profits	528,000	309,000
Gain on sale of investments	64,000	--
Equity in earnings of unconsolidated		

affiliates	--	34,000
Earnings from continuing operations before income taxes and minority interests	592,000	343,000
Interest expense	4,000	124,000
Income tax expense	222,000	95,000
Minority interests	(70,000)	(42,000)
Net earnings from discontinued operations, net of income tax	--	35,000
Net earnings	$ 296,000	$117,000

8. SEGMENT INFORMATION, continued

	Nine months ended September 30, 2002	2001
Operating Revenue:		
Financial services	$ 9,727,000	$10,269,000
Insurance services	7,204,000	5,384,000
Consulting	2,499,000	2,107,000
Corporate	387,000	1,569,000
	$19,817,000	$19,329,000
Reconciliation to Consolidated Statement of Operations:		
Total segment revenues	$19,817,000	$19,329,000
Less: Intercompany dividends	(245,000)	(1,300,000)
Intercompany interest	(39,000)	(178,000)
Total Revenues	$19,533,000	$17,851,000
Operating Income (Loss)		
Financial services	$ 1,178,000	$ 1,293,000
Insurance services	1,523,000	936,000
Consulting	379,000	(85,000)
Corporate	(435,000)	(803,000)
Total segments operating profits	2,645,000	1,341,000
Gain on sale of investments	2,855,000	--
Equity in loss of unconsolidated affiliates	(44,000)	(62,000)
Earnings from continuing operations before income taxes and minority interests	5,456,000	1,279,000
Interest expense	25,000	393,000
Income tax expense	1,899,000	364,000
Minority interests	(185,000)	(105,000)

Earnings from continuing operations	$ 3,347,000	$417,000
Net earnings from discontinued operations, net of income tax	--	110,000
Net earnings	$ 3,347,000	$527,000
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Item 2.

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

FORWARD LOOKING STATEMENTS

All statements past and future, written or oral, made by the us or our officers, directors, shareholders, agents, representatives or employees, including without limitation, those statements contained in this Report on Form 10-QSB, that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements regarding our expectations, hopes, intentions or strategies regarding the future. Forward-looking statements may appear in this document or other documents, reports, press releases, and written or oral presentations made by our officers to shareholders, analysts, news organizations or others. Readers should not place undue reliance on forward-looking statements. All forward-looking statements are based on information available to us and the declarant at the time the forward-looking statement is made, and we assume no obligation to update any such forward-looking statements. It is important to note that our actual results could differ materially from those described in such forward-looking statements. In addition to any risks and uncertainties specifically identified in connection with such forward-looking statements, the reader should consult our reports on previous filings under the Securities Act of 1933 and the Securities Exchange Act of 1934, for factors that could cause actual results to differ materially from those presented.

Forward-looking statements are necessarily based on various assumptions and estimates and are inherently subject to various risks and uncertainties, including risks and uncertainties relating to the possible invalidity of the underlying assumptions and estimates and possible changes or developments in social, economic, business, industry, market, legal and regulatory circumstances and conditions and actions taken or omitted to be taken by third parties, including customers, suppliers, business partners and competitors and legislative, judicial and other governmental authorities and officials. Assumptions relating to the foregoing involve judgements with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond control. Any such assumptions could be inaccurate and, therefore, there can be no assurance that any forward-looking statements by us or our officers, directors, shareholders, agents, representatives or employees, including those forward-looking statements contained in this Report on Form 10-QSB, will prove to be accurate.

CRITICAL ACCOUNTING POLICIES

The preparation of our consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an on-going basis, we evaluate our estimates, including those related to, impairment of assets; bad debts; income taxes; and contingencies and litigation. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which 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.

We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements. We periodically review the carrying value of our assets to determine if events and circumstances exist indicating that assets might be impaired. If facts and circumstances support this possibility of impairment, our management will prepare undiscounted and discounted cash flow projections which require judgments that are both subjective and complex. Management may also obtain independent valuations. See Note 21 to the consolidated financial statements in our annual report for the year ended December 31, 2001 on Form 10-KSB.

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

We record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. While we have considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, in the event we were to determine that we would be able to realize our deferred tax assets in the future in excess of its net recorded amount, an adjustment to the deferred tax asset would increase income in the period the determination was made. Likewise, should we determine that we would not be able to realize all or part of our net deferred tax asset in the future, an adjustment to the deferred tax asset would be charged to income in the period the determination was made.

We are a defendant in lawsuits that arise out of, and are incidental to, the conduct of our business. Our management uses its judgment, with the aid of legal counsel, to determine if accruals are necessary as a result of any pending actions against us.

At September 30, 2002 we owned less than 5% of the outstanding common stock of Prime Medical. As a result of our reduced ownership interest and as a result of Board of Directors changes mentioned in our Form 10-KSB for the year ended December 31, 2001, we ceased accounting for our investment in Prime Medical using the equity method effective March 19, 2002 and began accounting for our investment in Prime as an available for sale security in accordance with SFAS 115. Accordingly, our investment in Prime Medical is reported at fair value in our balance sheet. We recognized $186,000 of equity earnings during the first quarter of 2002 prior to converting to the cost method. This change in accounting also resulted in a balance sheet reclassification for our investment in Prime Medical from "Investment in Affiliate" to "Investment in Available for Sale Equtiy Securities".

At September 30, 2002 the Company owned convertible preferred and common stock of Uncommon Care, a developer and operator of dedicated Alzheimer's care facilities. We have applied the guidance of EITF 99-10, specifically the percentage of ownership method, in applying the equity method to our investment in Uncommon Care. Uncommon Care's common stock equity had been eliminated by losses prior to our investment and, accordingly, we recognized 100% of the losses of Uncommon Care based on our ownership of 100% of its preferred stock equity and subordinated debt. During 2001 our total basis in our investment and advances to Uncommon Care was reduced to zero. Until such time as Uncommon Care becomes profitable and our future equity

in these profits fully offsets our prior period combined equity losses, future advances to Uncommon Care will result in a loss when advanced. Advances to Uncommon Care have totaled $230,000 through September 30, 2002.

RESULTS OF OPERATIONS

REVENUES

Revenues from operations increased $973,000 (16%) and $1,682,000 (9%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. Revenues increased in the current three month period at all segments compared to the same period in 2001. For the current year nine month period, revenues increased at our insurance services, consulting and corporate segments and decreased at our financial services segment compared to the same period in 2001.

Financial services revenues increased $217,000 (7%) but decreased $542,000 (5%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. The increase in the current year three month period was due to strong September 2002 commission revenues at APS Financial, our broker dealer division of APS Investment Services, Inc., compared to those of last year following the significant negative effects in the stock market resulting from the tragic events of September 11, 2001. For the nine month period, revenues were down, continuing to reflect the general industry slowdown in the volume of securities transactions. With treasury rates at historic lows, market participants have been reluctant to invest in longer-term fixed income securities. And, investor demand for corporate debt continues to be limited due to weak economic and revenue forecasts.

Our insurance services revenues from our premium-based insurance management segment, APS Insurance Services, increased $624,000 (28%) and $1,820,000 (34%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. The increase in both periods is due to greater management fees and commissions, resulting from higher insurance premiums. Premiums have increased due to rate increases at the managed insurance company.

Our consulting segment revenues increased $78,000 (9%) and $392,000 (19%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. Billable hours have increased 14% in 2002 resulting from an increased workload performed for our largest client and new business involving wetlands mitigation construction and remedial investigation projects.

During the third quarter of 2002 we entered into discussions with senior management of our environmental consulting subsidiary, Eco Systems, Inc. ("Eco"), regarding a management buyout of Eco. We expect to complete the transaction following the date of this report. Terms of the transaction call for us to recover, on an accelerated basis, certain loans made to Eco and for Eco to continue our management services agreement. We do not expect the transaction to have a material impact on our financial condition or results of operations.

Eco had been acquired in a foreclosure proceeding related to loans which we had made in 1996 and does not fit into our long-term business plan.

EXPENSES

Total operating expenses increased $754,000 (13%) and $378,000 (2%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. For the current year three month period, expenses increased at our financial services, insurance services and corporate segments and decreased at our consulting segment. For the current year nine month period, expenses at our insurance services and corporate segments increased while expenses at our financial services and consulting segments decreased.

Financial services expense increased $209,000 (7%) but decreased $427,000 (5%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. The primary reason for the current year variances in both periods is the variances in commission expense resulting from the changes in commission revenue at APS Financial mentioned earlier. For the current year three month period, commission expenses increased $216,000 (12%) compared to the same three months in 2001 due to increased commission revenues during the current quarter. For the current year nine month period, commission expenses were down $279,000 (5%) compared to the same nine months in 2001 due to lower commission revenues earned in the current year. Profits at APS Financial are down 4% and 18% for the three and nine month period ended September 30, 2002, respectively, compared to the same periods in 2001. This decrease in profits was responsible for a current year nine month decrease of $273,000 (31%) in accrued management incentive compensation as this accrual is calculated solely on net profits. Also, legal and professional fees decreased 39% in the first nine months of 2002 compared to the same period in 2001 as there were no legal fees associated with investment banking activities this year that were incurred last year.

Insurance services expenses at the insurance management subsidiary increased $427,000 (23%) and $1,233,000 (28%) for the three and nine month periods September 30, 2002, respectively, compared to the same periods in 2001. The current three and nine month period increase is due primarily to a $222,000 (23%) and $698,000 (38%) increase, respectively, in commission expense paid to third party agents arising because of the aforementioned increase in commission income. Also higher this year is payroll related expenses which rose $126,000 (18%) and $327,000 (16%) in the current year three and nine month periods, respectively, as a result of creating two new vice-presidential positions and normal annual merit raises.

Consulting expenses decreased $231,000 (23%) and $72,000 (3%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. The primary reason for the decrease in the current quarter is a reduction in legal fees. During 2001, we were involved in a lawsuit that was eventually lost in the fourth quarter of 2001.

General and administrative expenses increased $475,000 (202%) and $525,000 (59%) for the three and nine month periods September 30, 2002, respectively, compared to the same periods in 2001. The increase in both current year periods is due primarily to a $366,000 and $364,000 increase in the three and nine month current periods, respectively, to accrued management incentive expense. Management incentive, a formula driven expense, has increased this year as a result of the increase in consolidated profit brought about in large part by the profits on the sales of Prime Medical common stock mentioned below.

Gain on sale of assets for the three months ended September 30, 2002, in the amount of $126,000, primarily represents the amortization of deferred gain attributable to the November, 2001 sale of real estate and subsequent leaseback of office space. We had deferred $2,400,000 of the $5,000,000 gain and will recognize income monthly over the life of the five year lease. For the nine month period ended September 30, 2002, amortization of deferred gains equaled $365,000. In addition, since the sale of the real estate was to our then 15% owned affiliate, Prime Medical, we had deferred an additional $760,000 of the $5,000,000 gain, as required by the equity method of accounting. During 2002 we reduced our investment in Prime Medical and subsequently recognized a proportionate percentage of the deferred gain, or about $516,000.

Interest expense decreased $120,000 (97%) and $368,000 (94%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001. The primary cause of the current period decrease is the payoff of the Company's note payable from a balance of $5,150,000 at September 30, 2001 to zero at September 30, 2002.

GAIN ON SALE OF INVESTMENTS

The three and nine month gains represent gains on the sale of 11,200 and 1,591,200 shares of Prime Medical common stock. As a result of these sales, as of September 30, 2002, we own approximately 753,000 shares of Prime Medical amounting to an ownership percentage of slightly less than 5%.

EQUITY IN EARNINGS (LOSS) OF UNCONSOLIDATED AFFILIATES

Our equity in the earnings of Prime Medical decreased $346,000 (100%) and $765,000 (80%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001 as we no longer account for our investment in Prime Medical using the equity method of accounting, as was the case in 2001. As of March 19, 2002, we ceased accounting for our investment in Prime Medical using the equity method of accounting because (1) on January 1, 2002, Kenneth S. Shifrin, the Company's Chairman and CEO, stepped down from day-to-day operations as Executive Chairman of the Board of Prime Medical, but will continue to serve as non-executive Chairman; (2) in December 2001, Prime Medical's CEO, Brad Hummel, resigned from our board of directors; and (3) from January to March 19, 2002, we sold 1,570,000 shares of Prime Medical reducing our ownership percentage to slightly less than 5%.

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Our equity in losses of Uncommon Care decreased $312,000 (100%) and $782,000 (77%) for the three and nine month periods ended September 30, 2002, respectively, compared to the same periods in 2001 primarily as a result of our limiting our losses in Uncommon Care to our total investment and advances to Uncommon Care, which was reduced to zero during 2001. Once we reduced our total investment to zero, as required under the equity method, we ceased recording equity losses. Until such time as Uncommon Care becomes profitable and future equity in these profits fully offsets our prior period combined equity losses, future advances to Uncommon Care will result in a loss when advanced. Advances to Uncommon Care totaling $230,000 in February 2002 account for the loss recorded during the first quarter 2002. Repayments by Uncommon Care totaling $125,000 received in the third quarter of 2002 were recorded as deferred income. Future advances will not affect net income until such time as they exceed the amount repaid.

MINORITY INTERESTS

Minority interests represents the combination of two outside interests in subsidiaries of the Company: a twenty percent interest of Insurance Services owned by FPIC Insurance Group, Inc. and a three percent interest of APS Asset Management, a subsidiary of the financial services subsidiary of the Company (APS Investment Services), owned by key individuals within APS Asset Management. Minority interests increased in the current year primarily as a result of increased profitability of our insurance services segment.

SHAREHOLDERS' EQUITY

For the three months ended September 30, 2002, we purchased 71,000 and cancelled 73,000 shares of treasury stock. The net effect of these purchases and cancellations was to decrease treasury stock $8,000, representing the cost of the cancelled shares, to decrease common stock by $7,000, determined by multiplying the number of shares cancelled by $0.10 par value, and to decrease retained earnings $302,000. For the nine months ended September 30, 2002, we purchased 226,000 and cancelled 612,000 shares of treasury stock. The net effect of these purchases and cancellations was to decrease the treasury stock $1,418,000, to decrease common stock by $60,000, and to decrease retained earnings $2,158,000.

Through September 30, 2002, we recorded other comprehensive income of $2,132,000 which represents unrealized holding gains on securities held for sale, primarily in Prime Medical common stock, net of tax. Changes in fair value for securities categorized as "available for sale" are excluded from earnings and reported net of deferred income taxes in shareholders' equity until realized.

LIQUIDITY AND CAPITAL RESOURCES

Current assets exceeded current liabilities by $7,237,000 at September 30, 2002 and $3,444,000 at December 31, 2001. Working capital rose in 2002 due to the sale of 1,591,200 shares of Prime Medical common stock which added approximately $10,719,000 in cash. Partially offsetting this was $2,275,000 in cash used to pay off a note payable and the purchase of $1,395,000 in available for sale bonds.

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Capital expenditures through the nine month period ended September 30, 2002 were approximately $133,000. Total capital expenditures are expected to be approximately $150,000 in 2002.

Historically, the Company has maintained a positive working capital position and has been able to satisfy its operational and capital expenditure requirements with cash generated from its operating and investing activities.

These same sources of funds have also allowed the Company to pursue investment and expansion opportunities consistent with its growth plans. Although it is uncertain if our operating activities will continue to provide positive cash flow in 2002, we believe that our current strong working capital position will enable us to meet our working capital requirements for the foreseeable future.

ADOPTION OF ACCOUNTING PRONOUNCEMENTS

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141, Business Combinations, and Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets. Statement 141 requires that we use the purchase method of accounting for all business combinations initiated after June 30, 2001 as well as all purchase method business combinations completed after June 30, 2001. Statement 141 also specifies criteria that intangible assets acquired in a purchase method business combination must meet to be recognized and reported apart from goodwill. We adopted the provisions of Statement 141 in 2001. Our adoption of Statement 141 did not have any impact on our consolidated financial statements. As of September 30, 2002, we had no goodwill or other intangible assets.

In June 2001, the Financial and Accounting Standards Board issued Statement of Financial Accounting Standards No. 142. Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), which applies to all acquired intangible assets whether acquired singularly, as part of a group, or in a business combination. SFAS 142 supersedes APB Opinion No. 17, "Intangible Assets," and carries forward provisions in Opinion 17 related to internally developed intangible assets. SFAS 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Goodwill should no longer beamortized, but instead tested for impairment at least annually at the reporting unit level. The accounting provisions are effective for fiscal years beginning after December 15, 2001. Our adoption of Statement 142 effective January 1, 2002 did not have a material effect on our financial position or results of operations.

In August 2001, the FASB issued Statement of Financial Accounting Standards No. 144 ("Statement 144"), Accounting for the Impairment or Disposal of Long-Lived Assets. Statement 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. Statement 144 requires that one accounting model be used for long-lived assets to be disposed of by sale and broadens presentation of discontinued operations to include more disposals. Our adoption of Statement 144 effective January 1, 2002 did not have a material effect on our financial position or results of operations.

In April 2002, the Financial and Accounting Standards Board issued Statement of Financial Accounting Standards No. 145. Statement of Financial Accounting Standards No. 145, "Rescission of SFAS Statements No. 4, 44, and 64, Amendment of SFAS Statement No. 13, and Technical Corrections" ("SFAS 145"), which updates, clarifies and simplifies existing accounting pronouncements. SFAS 145 rescinds SFAS No. 4, "Reporting Gains and Losses from Extinguishment of Debt." SFAS 145 amends SFAS No. 13, "Accounting for Leases," to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. The provisions of SFAS 145 related to SFAS No. 4 and SFAS No. 13 are effective for fiscal years beginning and transactions occurring after May 15, 2002, respectively. Adoption of this standard will not have any immediate effect on our consolidated financial statements.

In September 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities", which addresses accounting for restructuring and similar costs. SFAS No. 146 supersedes previous accounting guidance, principally Emerging Issues Task Force (EITF) Issue No. 94-3. will adopt the provisions of SFAS No. 146 for restructuring activities initiated after December 31, 2002. SFAS No. 146 requires that the liability for costs associated with an exit or disposal activity be recognized when the liability is incurred. Under EITF No. 94-3, a liability for an exit cost was recognized at the date of a company's commitment to an exit plan. SFAS No. 146 also establishes that the liability should initially be measured and recorded at fair value. Accordingly, SFAS No. 146 may affect the timing of recognizing future restructuring costs as well as the amount recognized. Adoption of this standard will not have any immediate effect on our consolidated financial statements.

Item 3.

CONTROLS AND PROCEDURES

a.) Within the 90-day period prior to the date of this report, we carried out an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-14 of the Securities and Exchange Act of 1934 (the "Exchange Act"). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to our reports (including those of our consolidated subsidiaries) required to be included in our Exchange Act filings.

b) There have been no significant changes in our internal controls or in other factors which could significantly affect internal controls subsequent to the date we carried out our evaluation.

PART II

OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

We are involved in various claims and legal actions that have arisen in the ordinary course of business. We believe that the liability provision in our consolidated financial statements is sufficient to cover any unfavorable outcome related to lawsuits in which we are currently named. Management believes that liabilities, if any, arising from these actions will not have a significant adverse effect on our financial condition or results of operations. However, due to the uncertain nature of legal proceedings, the actual outcome of these lawsuits may differ from the liability provision recorded in our consolidated financial statements.

Item 2. CHANGES IN SECURITIES

For the three months ended September 30, 2002, we purchased 71,000 and cancelled 73,000 shares of treasury stock. The net effect of these purchases and cancellations was to decrease treasury stock $8,000, representing the cost of the cancelled shares, to decrease common stock by $7,000, determined by multiplying the number of shares cancelled by $0.10 par value, and to decrease retained earnings $302,000. For the nine months ended September 30, 2002, we purchased 226,000 and cancelled 612,000 shares of treasury stock. The net effect of these purchases and cancellations was to decrease the treasury stock $1,418,000, to decrease common stock by $60,000, and to decrease retained earnings $2,158,000.

Item 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

99.1 Certification of Chief Executive Officer
99.2 Certification of Chief Financial Officer

(b) Reports on Form 8-K.

Report filed July 25, 2002 concerning the change in certifying accountants from KPMG LLP to BDO Seidman LLP.

SIGNATURES

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

AMERICAN PHYSICIANS SERVICE GROUP, INC.

By: /s/ William H. Hayes

William H. Hayes, Vice President
and Chief Financial Officer

Dated: November 14, 2002

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PUSUANT TO SECTION 302 OF
SARBANES-OXLEY ACT OF 2002

I, Kenneth S. Shifrin, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of American Physicians Service Group, Inc.

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this quarterly report;

4. The issuer's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the issuer and we:

a) designed such disclosure controls and procedures to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the issuer's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The issuer's other certifying officers and I have disclosed, based on our most recent evaluation, to the issuer's auditors and the audit committee of the board of directors:

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the issuer's ability to record, process, summarize and report financial data and have identified for the issuer's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal controls; and

6. The issuer's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

/s/ Kenneth S. Shifrin

Kenneth S. Shifrin
Chairman of the Board

CERTIFICATION OF CHIEF FINANCIAL OFFICER PUSUANT TO SECTION 302 OF SARBANES-OXLEY ACT OF 2002

I, William H. Hayes, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of American Physicians Service Group, Inc.

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this quarterly report;

4. The issuer's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the issuer and we:

a) designed such disclosure controls and procedures to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the issuer's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The issuer's other certifying officers and I have disclosed, based on our most recent evaluation, to the issuer's auditors and the audit committee of the board of directors:

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the issuer's ability to record, process, summarize and report financial data and have identified for the issuer's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal controls; and

6. The issuer's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

/s/ William H. Hayes

William H. Hayes
Senior Vice President-Finance