

SELECTED CONSOLIDATED FINANCIAL DATA

The following selected financial data for the five years ended March 31, 2001, have been derived from the Company's audited consolidated financial statements. The following data should be read in conjunction with the Company's Consolidated Financial Statements, the related notes thereto, and "Management's Discussion and Analysis of Financial Condition and Results of Operations." The following amounts are in thousands, except per share data.

Year Ended March 31,

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>
Statement of Income Data:					
Revenues	\$121,704	\$141,709	\$165,457	\$186,765	\$209,554
Costs and Expenses:					
Cost of revenues	99,323	115,553	136,082	152,710	172,010
General and administrative	8,645	11,029	12,596	14,752	16,389
	<u>107,968</u>	<u>126,582</u>	<u>148,678</u>	<u>167,462</u>	<u>188,399</u>
Income before income taxes	13,736	15,127	16,779	19,303	21,155
Income tax provision	5,220	5,670	6,376	7,336	7,933
Net income	<u>\$ 8,516</u>	<u>\$ 9,457</u>	<u>\$ 10,403</u>	<u>\$ 11,967</u>	<u>\$ 13,222</u>
Net income per share:					
Basic	<u>\$ 0.93</u>	<u>\$ 1.13</u>	<u>\$ 1.28</u>	<u>\$ 1.49</u>	<u>\$ 1.74</u>
Diluted	<u>\$ 0.91</u>	<u>\$ 1.10</u>	<u>\$ 1.26</u>	<u>\$ 1.47</u>	<u>\$ 1.70</u>
Shares used in computing net income per share:					
Basic	9,170	8,386	8,155	8,021	7,599
Diluted	9,370	8,572	8,261	8,151	7,781
Return on beginning of year equity	18.8%	20.5%	22.7%	22.5%	23.9%
Return on beginning of year assets	15.8%	16.1%	17.2%	17.4%	18.6%
Balance Sheet Data as of March 31,					
	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>
Cash and cash equivalents	\$15,665	\$ 8,430	\$ 9,052	\$ 5,643	\$ 9,457
Accounts receivable, net	22,294	25,633	31,562	35,874	34,316
Working capital	28,596	24,726	31,700	34,396	35,130
Total assets	58,824	60,491	68,737	71,187	77,565
Retained earnings	27,426	36,883	47,286	59,253	72,475
Treasury stock	9,461	21,727	26,990	39,956	53,903
Total stockholders' equity	46,087	45,771	53,214	55,293	58,718

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

This Management's Discussion and Analysis of Financial Condition and Results of Operations may include certain forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including (without limitation) statements with respect to anticipated future operating and financial performance, growth and acquisition opportunities and other similar forecasts and statements of expectation. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates" and "should" and variations of these words and similar expressions, are intended to identify these forward-looking statements. Forward-looking statements made by the Company and its management are based on estimates, projections, beliefs and assumptions of management at the time of such statements and are not guarantees of future performance.

The Company disclaims any obligations to update or revise any forward-looking statement based on the occurrence of future events, the receipt of new information or otherwise. Actual future performance, outcomes and results may differ materially from those expressed in forward-looking statements made by the Company and its management as a result of a number of risks, uncertainties and assumptions. Representative examples of these factors include (without limitation) general industry and economic conditions; cost of capital and capital requirements; competition from other managed care companies; the ability to expand certain areas of the Company's business; shifts in customer demands; the ability of the Company to produce market-competitive software; changes in operating expenses including employee wages, benefits and medical inflation; governmental and public policy changes; dependence on key personnel; possible litigation and legal liability in the course of operations; and the continued availability of financing in the amounts and at the terms necessary to support the Company's future business.

The Company derives the majority of its revenues from providing patient management and provider program services to payors of workers' compensation benefits and health insurance benefits. Patient management services include early intervention, utilization review, medical case management, vocational rehabilitation, and independent medical examinations. Provider program revenues include fee schedule auditing, hospital bill auditing, and preferred provider referral services. The percentages of revenues attributable to patient management and provider program services for the fiscal years ended March 31, 1999, 2000, and 2001 are as follows:

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Patient management services	58.5%	59.9%	59.3%
Provider program services	41.5%	40.1%	40.7%
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

Results of Operations

The following table sets forth, for the periods indicated, the percentage of revenues represented by certain items reflected in the Company's consolidated statements of income. The Company's past operating results are not necessarily indicative of future operating results.

	<u>Year Ended March 31,</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>
Revenues	100.0%	100.0%	100.0%
Cost of revenues	82.3	81.8	82.1
Gross profit	17.7	18.2	17.9
General and administrative	7.6	7.9	7.8
Income before income taxes	10.1	10.3	10.1
Net income	6.3	6.4	6.3

Years Ended March 31, 1999, 2000 and 2001

Revenues for fiscal 2000 increased by 13% to \$187 million from \$165 million in fiscal 1999, an increase of \$22 million. The majority of this growth came from patient management services, which grew 15% from \$97 million in fiscal year 1999 to \$112 million in fiscal 2000, primarily due to new national contracts to provide patient management services along with an increase in referrals from existing customers. Provider program services increased by \$6 million from \$69 million in fiscal 1999 to \$75 million in fiscal 2000, an increase of 9%.

Revenues for fiscal 2001 increased by 12% to \$210 million from \$187 million in fiscal 2000, an increase of \$23 million. The majority of this growth came from patient management services, which grew 11% from \$112 million in fiscal year 2000 to \$124 million in fiscal 2001, primarily due to an increase in referrals from existing customers. Provider program services increased by \$10 million from \$75 million in fiscal 2000 to \$85 million in fiscal 2001, an increase of 13%. This increase is primarily due to the increased volume of bills processed along with continued growth in the Company's provider network.

The Company's cost of revenues consists primarily of salaries, salary related taxes and benefits, rent, telephone, and costs related to the Company's computer operations, including depreciation and amortization. Costs of revenues increased from \$136 million in fiscal 1999 and \$153 million in fiscal 2000, to \$172 million in fiscal 2001, primarily due to the increases in revenues as noted above.

Cost of services as a percentage of revenues was 82.3% during fiscal 1999 and 81.8% in fiscal 2000, and increased to 82.1% in fiscal 2001. During fiscal 2001, the cost of revenue percentage increased due to improved margins in the provider programs business offset by declining margins in the patient management business due to the percentage increase in costs exceeding the percentage increase in prices. Patient management services have a higher cost of services percentage than that of provider programs. There is no guarantee the cost of service percentage will remain constant or decrease, should the Company pursue a strategy of reducing price in order to obtain greater market share or if competition causes pricing pressure in the industry.

General and administrative expense increased from \$13 million in fiscal 1999 and \$15 million in fiscal 2000 to \$16 million in fiscal 2001. This increase was primarily due to increased MIS staff to support the Company's implementation of Care^{MC} and further electronic data interface capabilities as required by customer needs. General and administrative expenses were 7.6%, 7.9%, and 7.8% for the years ended March 31, 1999, 2000 and 2001, respectively.

Liquidity and Capital Resources

The Company has funded its operations and capital expenditures primarily from cash flow from operations. During fiscal 2000, net working capital increased by \$1 million from \$34 million at March 31, 2000 to \$35 million at March 31, 2001. This increase is primarily due to the \$13 million of net income earned by the Company during fiscal 2001 offset by repurchase of the Company's common stock. As of March 31, 2001, the Company had \$9 million in cash and cash equivalents, invested primarily in short-term, highly liquid investments with maturities of 90 days or less. The Company has no interest-bearing short-term debt.

The Company has historically required substantial capital to fund the growth of its operations, particularly working capital to fund the growth in accounts receivable and capital expenditures. The Company believes, however, that the cash balance at March 31, 2001 along with anticipated internally generated funds will be sufficient to meet the Company's expected cash requirements for at least the next twelve months.

REPORT OF INDEPENDENT AUDITORS

*Stockholders and Board of Directors
CorVel Corporation*

We have audited the accompanying consolidated balance sheet of CorVel Corporation as of March 31, 2001, and the related consolidated statements of income, stockholders' equity, and cash flows for the year then ended. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audit.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of CorVel Corporation at March 31, 2001, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

We have also audited Schedule II of CorVel Corporation for the year ended March 31, 2001. In our opinion, this schedule presents fairly, in all material respects, the information required to be set forth therein.

/s/ Grant Thornton LLP

Portland, Oregon
May 11, 2001

REPORT OF INDEPENDENT AUDITORS

*Stockholders and Board of Directors
CorVel Corporation*

We have audited the accompanying consolidated balance sheet of CorVel Corporation as of March 31, 2000, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the two years in the period ended March 31, 2000. Our audits also included the financial statement schedule listed in the Index at Item 14(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of CorVel Corporation at March 31, 2000, and the consolidated results of its operations and its cash flows for each of the two years in the period ended March 31, 2000, in conformity with generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ ERNST & YOUNG LLP

Orange County, California
May 9, 2000

CORVEL CORPORATION
CONSOLIDATED STATEMENTS OF INCOME

	<u>Years Ended March 31,</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>
REVENUES	\$165,457,000	\$186,765,000	\$209,554,000
COSTS AND EXPENSES			
Cost of revenues	136,082,000	152,710,000	172,010,000
General and administrative	12,596,000	14,752,000	16,389,000
	<u>148,678,000</u>	<u>167,462,000</u>	<u>188,399,000</u>
Income before income taxes	16,779,000	19,303,000	21,155,000
Income tax provision	6,376,000	7,336,000	7,933,000
NET INCOME	<u>\$ 10,403,000</u>	<u>\$ 11,967,000</u>	<u>\$ 13,222,000</u>
Net income per share:			
Basic	<u>\$ 1.28</u>	<u>\$ 1.49</u>	<u>\$ 1.74</u>
Diluted	<u>\$ 1.26</u>	<u>\$ 1.47</u>	<u>\$ 1.70</u>
Shares used in computing net income per share:			
Basic	8,155,000	8,021,000	7,599,000
Diluted	8,261,000	8,151,000	7,781,000

See accompanying notes to consolidated financial statements

**CORVEL CORPORATION
CONSOLIDATED BALANCE SHEETS**

	March 31,	
	<u>2000</u>	<u>2001</u>
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 5,643,000	\$ 9,457,000
Accounts receivable (less allowance for doubtful accounts of \$3,395,000 in 2000 and \$3,387,000 in 2001)	35,874,000	34,316,000
Prepaid expenses and taxes	1,931,000	2,465,000
Deferred income taxes	3,833,000	4,130,000
Total current assets	<u>47,281,000</u>	<u>50,368,000</u>
Property and equipment, net	16,631,000	20,071,000
Other assets	7,275,000	7,126,000
	<u>\$ 71,187,000</u>	<u>\$ 77,565,000</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts and taxes payable	\$ 5,310,000	\$ 3,006,000
Accrued liabilities	7,575,000	12,232,000
Total current liabilities	<u>12,885,000</u>	<u>15,238,000</u>
Deferred income taxes	3,009,000	3,609,000
Commitments and Contingencies		
Stockholders' Equity		
Common Stock, \$.0001 par value: 20,000,000 shares authorized; 10,079,001 and 10,296,469 shares issued and outstanding in 2000 and 2001, respectively	1,000	1,000
Paid-in Capital	35,995,000	40,145,000
Treasury Stock, at cost (2,333,340 shares in 2000, 2,807,940 shares in 2001)	(39,956,000)	(53,903,000)
Retained Earnings	59,253,000	72,475,000
Total stockholders' equity	<u>55,293,000</u>	<u>58,718,000</u>
	<u>\$ 71,187,000</u>	<u>\$ 77,565,000</u>

See accompanying notes to consolidated financial statements.

CORVEL CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years Ended March 31, 1999, 2000, and 2001

	<u>Common stock – shares</u>	<u>Common stock – amount</u>	<u>Common stock and paid in capital</u>	<u>Treasury shares</u>
Balance – March 31, 1998	9,706,944	\$1,000	\$ 30,614,000	(1,461,200)
Stock issued under employee stock purchase plan	34,428	—	541,000	—
Stock issued and income tax benefits under stock option plan, net of shares repurchased	144,204	—	1,762,000	—
Purchase of common stock	—	—	—	(286,080)
Net income				
Balance – March 31, 1999	<u>9,885,576</u>	<u>1,000</u>	<u>32,917,000</u>	<u>(1,747,280)</u>
Stock issued under employee stock purchase plan	34,800	—	588,000	—
Stock issued and income tax benefits under stock option plan, net of shares repurchased	158,625	—	2,490,000	—
Purchase of common stock	—	—	—	(586,060)
Net income				
Balance – March 31, 2000	<u>10,079,001</u>	<u>1,000</u>	<u>35,995,000</u>	<u>(2,333,340)</u>
Stock issued under employee stock purchase plan	30,072	—	687,000	—
Stock issued and income tax benefits under stock option plan, net of shares repurchased	187,396	—	3,463,000	—
Purchase of common stock	—	—	—	(474,600)
Net income				
Balance – March 31, 2001	<u>10,296,469</u>	<u>\$1,000</u>	<u>\$40,145,000</u>	<u>(2,807,940)</u>

See accompanying notes to consolidated financial statements.

CORVEL CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years Ended March 31, 1999, 2000, and 2001

	Treasury shares – cost	Retained earnings	Total shareholders' equity
Balance – March 31, 1998	\$ (21,727,000)	\$ 36,883,000	\$45,771,000
Stock issued under employee stock purchase plan	–	–	541,000
Stock issued and income tax benefits under stock option plan, net of shares repurchased	–	–	1,762,000
Purchase of common stock	(12,266,000)	–	(5,263,000)
Net income	–	10,403,000	10,403,000
Balance – March 31, 1999	(26,990,000)	47,286,000	53,214,000
Stock issued under employee stock purchase plan	–	–	588,000
Stock issued and income tax benefits under stock option plan	–	–	2,490,000
Purchase of common stock	(12,966,000)	–	(12,966,000)
Net income	–	11,967,000	11,967,000
Balance – March 31, 2000	(39,956,000)	59,253,000	55,293,000
Stock issued under employee stock purchase plan	–	–	687,000
Stock issued and income tax benefits under stock option plan, net of shares repurchased	–	–	3,463,000
Purchase of common stock	(13,947,000)	–	(13,947,000)
Net income	–	11,967,000	11,967,000
Balance – March 31, 2001	\$(53,903,000)	\$72,475,000	\$58,718,000

See accompanying notes to consolidated financial statements.

CORVEL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS

	<u>Years Ended March 31,</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	\$ 10,403,000	\$ 11,967,000	\$ 13,222,000
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	6,344,000	6,965,000	6,759,000
Deferred income taxes	(588,000)	(131,000)	303,000
Loss on write down and disposal of property and equipment	37,000	192,000	(45,000)
Changes in operating assets and liabilities:			
Accounts receivable	(5,929,000)	(4,312,000)	1,558,000
Prepaid taxes and expenses	(120,000)	(1,075,000)	(534,000)
Accounts and taxes payable	390,000	(1,158,000)	(2,304,000)
Accrued liabilities	154,000	1,050,000	4,657,000
Other assets	(482,000)	(779,000)	149,000
Net cash provided by operating activities	<u>10,209,000</u>	<u>12,719,000</u>	<u>23,765,000</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of property and equipment	<u>(6,627,000)</u>	<u>(6,240,000)</u>	<u>(10,154,000)</u>
Net cash used in investing activities	<u>6,627,000</u>	<u>(6,240,000)</u>	<u>(10,154,000)</u>
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds and tax benefits from exercise of stock options	2,303,000	3,078,000	4,150,000
Purchase of common stock	<u>(5,263,000)</u>	<u>(12,966,000)</u>	<u>(13,947,000)</u>
Net cash used in financing activities	<u>(2,960,000)</u>	<u>(9,888,000)</u>	<u>(9,797,000)</u>
Net increase (decrease) in cash and cash equivalents	622,000	(3,409,000)	3,814,000
Cash and cash equivalents at beginning of year	<u>8,430,000</u>	<u>9,052,000</u>	<u>5,643,000</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 9,052,000</u>	<u>\$ 5,643,000</u>	<u>\$ 9,457,000</u>

See accompanying notes to consolidated financial statements.

CorVel Corporation
Notes to Consolidated Financial Statements
March 31, 2001

Note A – Summary of Significant Accounting Policies

Organization: CorVel Corporation (CorVel or the Company) provides services and programs nationwide that are designed to enable insurance carriers, third party administrators and employers with self-insured programs to administer, manage and control the cost of workers' compensation and other healthcare benefits.

Basis of Presentation: The consolidated financial statements include the accounts of CorVel and its subsidiaries. Significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the accompanying financial statements. Actual results could differ from those estimates.

Cash and Cash Equivalents: Cash and cash equivalents consists of short-term highly-liquid investments with maturities of 90 days or less when purchased. The carrying amounts of the Company's financial instruments approximate their relative fair values at March 31, 2000 and 2001.

Revenue Recognition: The Company's revenues are recognized primarily as services are rendered based on time and expenses incurred. A certain portion of the Company's revenues are derived from fee schedule auditing which is based on the number of provider charges audited and, to a limited extent, on a percentage of savings achieved for the Company's clients. Accounts receivable includes \$2,486,000 and \$3,749,000 of unbilled receivables at March 31, 2000 and 2001, respectively. No one customer accounted for more than 10% of consolidated revenues during the years ended March 31, 1999, 2000 and 2001.

Property and Equipment: Additions to property and equipment are recorded at cost. Depreciation and amortization are provided using the straight-line and accelerated methods over the estimated useful lives of the related assets which range from three to seven years.

Long-Lived Assets: The carrying amount of all long-lived assets is evaluated periodically to determine if adjustment to the depreciation and amortization period or to the unamortized balance is warranted. Such evaluation is based principally on the expected utilization of the long-lived assets and the projected, undiscounted cash flows of the operations in which the long-lived assets are deployed.

CorVel Corporation
Notes to Consolidated Financial Statements
March 31, 2001

Note A – Summary of Significant Accounting Policies (continued)

Other Assets: Other assets consists primarily of the excess of the purchase price over the estimated fair value of the net assets of businesses acquired (goodwill) and is being amortized using the straight-line method over periods not exceeding 40 years. Goodwill amounted to \$6,013,000 (net of accumulated amortization of \$1,736,000) at March 31, 2000 and \$5,978,000 (net of accumulated amortization of \$1,672,000) at March 31, 2001.

Concentrations of Credit Risk: The Company performs periodic credit evaluations of its customers' financial condition and does not require collateral. No other single customer accounted for 10% of accounts receivable in 2000 or 2001. Receivables are generally due within 60 days. Credit losses relating to customers in the workers' compensation insurance industry consistently have been within management's expectations.

Income Taxes: The Company provides for income taxes under the liability method. Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities as measured by the enacted tax rates which are expected to be in effect when these differences reverse. Income tax expense is the tax payable for the period and the change during the period in net deferred tax assets and liabilities.

Earnings Per Share: Earnings per common share-basic is based on the weighted average number of common shares outstanding during the period. Earnings per common shares-diluted is based on the weighted average number of common shares and common share equivalents outstanding during the period. In calculating earnings per share, earnings are the same for the basic and diluted calculations. Weighted average shares outstanding increased for diluted earnings due to the effect of stock options

Stock Option Plans: The Company applies the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123) and accordingly, is continuing to account for its stock-based compensation plans under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations.

CorVel Corporation
Notes to Consolidated Financial Statements
March 31, 2001

Note A – Summary of Significant Accounting Policies (continued)

In 1998, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 133 (“SFAS 133”), Accounting for Derivative Instruments and Hedging Activities, which is effective for 2000. SFAS 133 will require the Company to record all derivatives on the balance sheet at fair value. For derivatives that are hedges, changes in the fair value of derivatives will be offset by the changes in the fair value of the hedged assets, liabilities or firm commitments. The new standard, as amended by SFAS 137 and SFAS 138, is effective for fiscal years beginning after June 15, 2000. The Company believes the impact of adopting this standard will not be material to results of operations or equity.

Note B – Property and Equipment

Property and equipment consists of the following at March 31:

	2000	2001
Office equipment and computers	\$ 30,851,000	\$ 27,560,000
Computer software	13,735,000	14,201,000
Leasehold improvements	1,460,000	1,731,000
	<hr/>	<hr/>
Less: accumulated depreciation and amortization	46,046,000	43,492,000
	29,415,000	23,421,000
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	\$ 16,631,000	\$ 20,071,000

Note C – Accrued Liabilities

Accrued liabilities consist of the following at March 31:

	2000	2001
Payroll and related benefits	\$ 4,495,000	\$ 9,401,000
Self-insurance reserves	829,000	1,610,000
Other	2,251,000	1,221,000
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	\$ 7,575,000	\$ 12,232,000

CorVel Corporation
Notes to Consolidated Financial Statement
March 31, 2001

Note D – Income Taxes

The income tax provision consists of the following for the three years ended March 31:

	1999	2000	2001
Current – Federal	\$ 6,337,000	\$ 6,745,000	\$ 7,010,000
Current – State	627,000	722,000	620,000
Subtotal	6,964,000	7,467,000	7,630,000
Deferred – Federal	(537,000)	(118,000)	277,000
Deferred – State	(51,000)	(13,000)	26,000
Subtotal	(588,000)	(131,000)	303,000
	<u>\$ 6,376,000</u>	<u>\$ 7,336,000</u>	<u>\$ 7,933,000</u>

Income tax benefits associated with the exercise of stock options were \$289,000, \$577,000 and \$673,000 for fiscal 1999, 2000, and 2001, respectively.

The following is a reconciliation of the income tax provision from the statutory federal income tax rate to the effective rate for the three years ended March 31:

	1999	2000	2001
Income taxes at federal statutory rate	\$ 5,873,000	\$ 6,756,000	\$ 7,404,000
State income taxes, net of federal benefit	471,000	465,000	646,000
Permanent differences	45,000	115,000	47,000
Other	(13,000)	—	(164,000)
	<u>\$ 6,376,000</u>	<u>\$ 7,336,000</u>	<u>\$ 7,933,000</u>

Income taxes paid totaled \$4,787,000, \$9,307,000 and \$7,570,000 for the years ended March 31, 1999, 2000, and 2001, respectively

CorVel Corporation
Notes to Consolidated Financial Statements
March 31, 2001

Note D – Income Taxes (continued)

Deferred taxes at March 31, 1999 and 2000 are:

	<u>2000</u>	<u>2001</u>
Deferred tax assets:		
Accrued liabilities not currently deductible	\$ 2,432,000	\$ 2,806,000
Allowance for doubtful accounts	1,207,000	1,321,000
Other	194,000	3,000
Deferred assets	<u>3,833,000</u>	<u>4,130,000</u>
Deferred tax liabilities:		
Excess of tax under book basis of fixed assets	(2,619,000)	(3,067,000)
Other	(390,000)	(542,000)
Deferred liability	<u>(3,009,000)</u>	<u>(3,606,000)</u>
Net deferred tax asset	<u>\$ 824,000</u>	<u>\$ 521,000</u>

Note E – Stock Option Plans

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB No. 25) and related interpretations in accounting for its employee stock options because, as discussed below, the alternative fair value accounting provided for under SFAS No. 123 requires use of option valuation models that were not developed for use in valuing employee stock options. Under APB No. 25, because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized.

Under the Company's Restated 1988 Executive Stock Option Plan, ("the Plan") as amended, options for up to 3,470,000 shares of the Company's common stock may be granted to key employees, nonemployee directors and consultants at prices not less than 85% of the fair value of the stock at the date of grant as determined by the Board. Options granted under the Plan may be either incentive stock options or non-statutory stock options and are generally exercisable beginning one year from the date of grant and vest monthly thereafter for three years.

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Note E – Stock Option Plans (continued)

Summarized information for all stock options for the past three fiscal years follows:

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Options outstanding at the Beginning of the year	761,932	796,406	789,343
Options granted	219,100	175,500	193,700
Options exercised	(149,554)	(164,313)	(187,396)
Options cancelled	(35,072)	(18,250)	(58,984)
Options outstanding at the end of the year	<u>796,406</u>	<u>789,343</u>	<u>736,663</u>

During the year, weighted average price of options:

Granted	\$18.09	\$21.13	\$28.54
Exercised	\$10.55	\$12.41	\$15.08
Cancelled	\$15.20	\$17.52	\$19.54

At the end of the year:

Price range of outstanding options	\$ 8.50– \$18.88	\$8.50– \$23.63	\$8.50– \$34.75
Weighted average price per share	\$15.13	\$16.99	\$20.30
Options available for future grants	625,598	468,348	334,579
Exercisable options	333,764	339,889	321,627

CorVel Corporation
Notes to Consolidated Financial Statements
March 31, 2001

Note E – Stock Option Plans (continued)

The following table summarizes the status of stock options outstanding and exercisable at March 31, 2000:

Range of Exercise Prices	Number of Outstanding Options	Weighted Average Remaining Contractual Life	Outstanding Options – Weighted Average Exercise Price	Exercisable Options – Number of Exercisable Options	Exercisable Options – Weighted Average Exercise Price
\$ 8.50 - \$15.50	175,720	2.92 years	\$13.59	127,781	\$13.55
17.44 - 18.00	151,575	2.31 years	17.84	93,998	17.82
18.09 - 23.63	221,721	3.56 years	20.33	99,848	19.77
26.25 - 34.75	186,700	4.78 years	28.59	-	-
Total	735,716	3.39 years	\$20.09	321,627	\$16.73

The Company has adopted the disclosure-only provisions of SFAS No. 123. Had compensation cost for the Company's stock option and stock purchase plans been recorded consistent with the provisions of SFAS No. 123, net income, net income per share-basic and net income per common share-diluted would have been for the three fiscal years ended March 31, 2000:

	1999	2000	2001
Net income – adjusted	\$9,971,000	\$11,406,000	\$12,584,000
Net income per share – basic	\$1.22	\$1.42	\$1.66
Net income per share – diluted	\$1.21	\$1.40	\$1.62

The weighted average fair values at date of grant for options during fiscal 1999, 2000, and 2001, were \$6.28, \$6.56, and \$9.59, respectively.

The fair value of each plan is estimated on the date of grant using the Black-Scholes option-pricing model. The following weighted average assumptions were used for fiscal years ended March 31:

	1999	2000	2001
Expected volatility	.28	.37	.41
Risk free interest rate	5.7%	6.6%	4.8%

The assumptions for all three years reflect no dividend yield and a weighted average option life of 4.7 years.

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Notes to Consolidated Financial Statements
March 31, 2001

Note E – Stock Option Plans (continued)

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

Note F – Employee Stock Purchase Plan

The Company maintains an Employee Stock Purchase Plan which allows employees of the Company and its subsidiaries to purchase shares of common stock on the last day of two six-month purchase periods (i.e. March 31 and September 30) at a purchase price which is 85% of the closing sale price of shares as quoted on NASDAQ on the first or last day of such purchase period, whichever is lower. Employees are allowed to participate up to 20% of their gross pay. A maximum of 500,000 shares has been authorized for issuance under the plan, as amended. As of March 31, 1999, 339,000 shares had been issued pursuant to the plan. Summarized plan information is as follows:

	1999	2000	2001
Employee contributions	\$541,000	\$588,000	\$687,000
Shares acquired	34,428	34,800	30,072
Average purchase price	\$15.71	\$16.90	\$22.85

Note G – Treasury Stock

The Company's Board of Directors has approved a plan to repurchase up to 3,400,000 shares of the Company's outstanding common stock. Purchases may be made from time to time depending on market conditions and other relevant factors. The share repurchases for fiscal years ending March 31, 1999, 2000 and 2001 are as follows:

	1999	2000	2001	Cummulative
Shares repurchased	286,080	586,060	474,600	2,807,940
Cost	\$5,263,000	\$12,966,000	\$13,947,000	\$53,903,000
Average price	\$18.40	\$22.12	\$29.38	\$19.20

The repurchased shares were recorded as treasury stock, at cost, and is available for general corporate purposes. The repurchases were financed from cash generated from operations.

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Notes to Consolidated Financial Statements
March 31, 2001

Note H – Commitments and Contingencies

The Company leases office facilities under noncancelable operating leases. Future minimum rental commitments under operating leases at March 31, 2001 are \$7,202,000 in fiscal 2002, \$5,574,000 in fiscal 2003, \$3,878,000 in fiscal 2004, \$2,757,000 in fiscal 2005, \$1,802,000 in fiscal 2006, and \$827,000 thereafter. Total rental expense of \$6,100,000, \$7,100,000, and \$8,685,000 was charged to operations for the years ended March 31, 1999, 2000, and 2001, respectively.

The Company is involved in litigation arising in the normal course of business. The Company believes that resolution of these matters will not result in any payment that, in the aggregate, would be material to the financial position and results of the operations of the Company.

Note I – Savings Plan

The Company maintains a retirement savings plan for its employees, which is a qualified plan under Section 401(k) of the Internal Revenue Code. Full-time employees that meet certain requirements are eligible to participate in the plan. Contributions are made annually primarily at the discretion of the Company's Board of Directors. Contributions of \$155,000, \$199,000, and \$224,000, were charged to operations for the years ended March 31, 1999, 2000 and 2001, respectively.

Note J – Shareholder Rights Plan

During fiscal 1997, the Company's Board of Directors approved the adoption of a Shareholder Rights Plan. The Rights Plan, which is similar to rights plans adopted by numerous other public companies, provides for a dividend distribution to CorVel stockholders of one preferred stock purchase "Right" for each outstanding share of CorVel's common stock. The Rights are designed to assure that all stockholders receive fair and equal treatment in the event of any proposed takeover of the company and to encourage a potential acquirer to negotiate with the Board of Directors prior to attempting a takeover. The Rights have an exercise price of \$62.50 per Right, as adjusted for the 2-for-1 stock split in the form of a 100% stock dividend, paid on June 14, 1999, and subject to subsequent adjustment. Initially, the Rights will trade with the company's common stock, and will not be exercisable until the occurrence of certain takeover-related events. The issuance of the Rights has no dilutive effect on the Company's earnings per share.

CorVel Corporation
Notes to Consolidated Financial Statements
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Note K – Quarterly Results

The following is a summary of unaudited results of operations for the two years ended March 31, 2000 and 2001:

	Revenues	Gross Margin	Net income	Net income per basic common share	Net income per diluted common share
Fiscal Year Ended March 31, 1999:					
First Quarter	\$ 45,705,000	\$ 8,251,000	\$ 2,877,000	\$.35	\$.35
Second Quarter	45,865,000	8,406,000	2,970,000	.37	.36
Third Quarter	46,269,000	8,487,000	3,013,000	.38	.37
Fourth Quarter	48,926,000	8,911,000	3,107,000	.40	.39
Fiscal Year Ended March 31, 2000:					
First Quarter	\$ 50,557,000	9,328,000	\$ 3,227,000	\$.42	\$.41
Second Quarter	51,658,000	9,347,000	3,272,000	.43	.42
Third Quarter	52,241,000	9,059,000	3,328,000	.44	.43
Fourth Quarter	55,098,000	9,810,000	3,395,000	.45	.44