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Securities and Exchange Commission

Washington, D.C. 20549

Form 10-K

MANUALLY SIGNED

WITH EXHIBITS

Annual Report Pursuant to Section 13 or 15(d)

of the Securities Exchange Act of 1934

For the fiscal year ended May 31, 1985 C-567825 Commission file no. 0-5751

PROCESSED BY DISCLOSURE INCORPORATED

RECEIVED AUG 19 1985

SECURITIES AND EXCHANGE COMMISSION FEE RECEIVED AUG 15 1985 OFFICE OF REPORTS & INFORMATION SERVICES

Comprehensive Care Corporation

(Exact name of Registrant as specified in its charter)

Delaware	95-2594724
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
660 Newport Center Drive, 4th Floor Newport Beach, California (Address of principal executive offices)	92660 (Zip code)

442
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Registrant's telephone number, including area code (714) 640-8950

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, Par Value $.10 per share
(Title of Class)

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 ___

The aggregate market value of voting stock held by non-affiliates of Registrant at July 17, 1985, was $350,768,787.

At July 17, 1985, Registrant had 15,168,380 shares of Common Stock outstanding.

Part III incorporates information by reference from the Proxy Statement for Registrant's Annual Meeting of Stockholders to be held on September 26, 1985.

Item 1. Business.

The Registrant, Comprehensive Care Corporation, is a Delaware corporation which was organized in January 1969. Registrant is primarily engaged in the development, marketing and management of programs for the treatment of chemical dependency, including alcohol and drugs, and psychiatric disorders (the "Programs"). The Programs are provided under contractual agreements ("Contracts") with independent general hospitals or at freestanding facilities owned and/or operated by Registrant. It is the largest private provider of hospital-based alcoholism treatment Programs in the United States. During fiscal 1985 chemical dependency and psychiatric treatment Programs accounted for approximately 95% of Registrant's total revenues. The following table sets forth for the five years ended May 31, 1985, the contribution to revenues of Registrant's freestanding and Contract operations and its other activities.

	Years Ended May 31,				
	1985	1984	1983	1982	1981
Freestanding Operations	63%	60%	57%	54%	53%
Contract Operations	34	37	38	41	41
Other Activities	3	3	5	5	6
	100%	100%	100%	100%	100%

Freestanding Operations

The Registrant currently operates or participates in the operation of 17 facilities representing 1,609 available beds. Since 1982, Registrant has expanded its freestanding operations through the construction of four freestanding chemical dependency facilities and the acquisition of five chemical dependency or psychiatric facilities, representing approximately 900 beds. Freestanding facilities are either owned or leased by Registrant or by joint ventures in which Registrant and its partners share in the profits or losses. At May 31, 1985, four of the chemical dependency treatment facilities (330 available beds) and one psychiatric hospital (258 available beds) managed by Registrant were owned or leased by such joint ventures, and one psychiatric hospital (100 available beds) was managed by Registrant's partner in a joint venture.

The following table sets forth selected operating data regarding Registrant's freestanding facilities. Facilities are designated either psychiatric or chemical dependency based on the predominant treatment provided. For information concerning the nature of Registrant's interest in the facilities, see Item 2, "Properties".

	Year Acquired[1]	Licensed Beds	Patient Days 1985	1984	1983	1982	1981
Chemical Dependency Facilities							
CareUnit Hosp. of Dallas / Ft. Worth	1971	83	24,278	14,593	12,878	10,917	8,384
Crossroads Hospital (2)	1972	43	14,503	13,266	11,551	11,295	11,135
CareUnit Hosp. of Orange	1976	94	33,677	31,696	30,426	31,098	27,109
CareUnit Hosp. of Los Angeles	1978	104	23,150	20,655	17,112	14,669	1,143(8)
CareUnit Hosp. of Kirkland (3)	1981	83	27,099	25,530	25,818	25,392	26,606
Shenandoah Lodge (4)	1979	24				3,518	4,251
CareUnit of Jacksonville Beach	1982	84	16,539	19,355	12,416	35	
CareUnit Hosp. of Cincinnati	1982	84	29,181	26,880	27,598		
CareUnit Hosp. of St. Louis	1983	144	39,953	31,293	9,784		
Starting Point, Oak Avenue	1983	68	21,136	13,492	1,491		
Starting Point, Orange County (5)	1983	59	15,332	4,515			
Starting Point, Grand Avenue (6)	1983	25	6,158	1,294			
CareUnit of Tampa	1983	120	14,771	3,080			
CareUnit Hosp. of Albuquerque	1984	70	9,597	205			
CareUnit Hospital of Nevada	1984	50	7,640				

Psychiatric Facilities							
Brea Neuropsychiatric Center	1969	142	46,271	44,472	40,100	40,427	33,495
Woodview-Calabasas Hospital	1970	117	25,531	24,375	25,554	23,854	25,612
Golden Valley Health Center	1984	377	64,007	155	—	—	—
Patient days served during period			418,823	274,856	214,728	161,204	137,735
Available beds at end of period (7)			1,609	1,538	1,015	659	560
Average occupancy rate for period			72.0%	67.1%	70.1%	76.0%	81.2%

(1) Calendar year acquired or leased

(2) Registrant contends that this facility is licensed for 43 beds although regulatory agencies contend that it is licensed for only 33 beds.

(3) Managed from 1978 until purchased by Registrant in April 1981

(4) Closed in February 1982.

(5) Opened in September 1983. Prior to this date, Registrant operated a 59-bed skilled nursing facility and a 72-bed residential care facility on these premises.

(6) Acquired in March 1983. Registrant refurbished the facility and opened it as an adolescent treatment facility in November 1983

(7) A facility may have appropriate licensure for more beds than are in use for a number of reasons, including lack of demand, anticipation of future need, seasonality and pr[illegible]al limitations in assigning patients to multiple-bed rooms. Available beds is defined as the number of beds which are available for use at any given time.

(8) Does not include patient days (13,900) prior to May 1, 1981 when Registrant operated this facility primarily as a medical/surgical hospital.

Contract Operations

The Registrant also develops, markets and manages behavioral medicine programs under Contracts with independent general hospitals. Under these Contracts, the hospitals furnish patients with all hospital facilities and services necessary for their generalized medical care, including nursing, dietary and housekeeping services. The Registrant provides support in the areas of Program implementation and management, staff recruiting, continuing education, nurse and hospital employee training, community education, advertising, public relations and ongoing Program quality assurance. Patients are admitted to the Programs under the hospital's standard admission policies and procedures. The hospital submits to the patient or the patient's insurance company a bill which covers the services of the hospital. The hospital pays Registrant a fixed monthly management fee plus a fee for each patient day of service provided. Fees paid to Registrant are subject to annual adjustments to reflect increases in the Consumer Price Index. Registrant and the hospital share the risk of non-payment by patients based on a predetermined percentage participation by Registrant in bad debts. To date, Registrant's share of such bad debts has not exceeded six percent of Contract revenues in any one year. Contracts are generally entered into for a two-year period; thereafter, either party may terminate the Contract by giving 90 days notice. A significant number of Registant's existing Contracts are terminable on 90 days notice.

The following table sets forth selected operating data regarding Programs the Registrant manages on a Contract basis:

	Years Ended May 31,				
	1985	1984	1983	1982	1981
Number of Contracts at end of period (1):					
Adult CareUnits (2)	84	31	73	72	60
Adolescent CareUnits (2)	20	16	11	12	2
Adult CarePsychCenters (2)	17	12	9	8	4
Adolescent CarePsychCenters (2)	5	3	1	—	—
Eating Disorders Units	7	4	—	—	—
RehabCare Units	8	1	—	—	—
Total	141(3)	117	94	92	66
Available beds at end of period	3,346	2,668	2,168	2,1[illegible]3	1,543
Patient days served during period	703,189	580,356	494,740	474,964	396,714
Average occupied beds per Contract	15.3	15.4	14.5	16.8	17.8
Average occupancy rate for period (4)	66.0%	66.9%	64.6%	72.5%	74.2%

(1) Excludes Contracts which have been executed but are not operational as of the end of the period.

(2) CareUnit is the service mark under which Registrant markets chemical dependency treatment programs. CarePsychCenter is the service mark under which Registrant markets mental health treatment programs.

(3) During the twelve-month period ended May 31, 1985, Registrant opened 37 new Contracts and closed 13 Contracts. Fourteen of these new Contracts were added by Behavioral Medical Care ("BMC"), a 70% owned joint venture. Of the 13 closed Contracts, four were terminated by Registrant and nine were terminated by the contracting hospitals. Seven of these hospitals have continued treatment programs.

(4) Average occupancy rate is calculated by dividing total patient days by the number of available bed-days during the relevant period.

Program Descriptions

CHEMICAL DEPENDENCY. The Registrant developed and first introduced chemical dependency treatment Programs in 1973. Originally, these Programs, delivered under the name CareUnit, were directed toward the adult alcoholic but have been adapted and expanded to treat both adults and adolescents suffering from substance abuse.

The chemical dependency Program is hospital based. Each patient admitted to the hospital is subject to a full medical and social history as well as a physical examination which includes those diagnostic studies ordered by the patient's attending physician. Patients are detoxified under close medical supervision for a period averaging four days prior to entry to the rehabilitation phase of treatment.

The rehabilitation phase of treatment begins as soon as detoxification is completed. This phase of treatment includes lectures and individual, family and group counseling sessions administered by an interdisciplinary team of professionals. The average length of hospital stay for an adult patient is 18 days, which includes detoxification. The average length of stay for an adolescent patient is approximately 33 days. After discharge from the hospital, the patient's recovery is monitored for a 10-week period during which the patient and family members return to the hospital once a week for outpatient counseling sessions.

For individuals who do not require the structure and intensity of inpatient hospital services, Registrant has developed outpatient programs which operate in conjunction with existing inpatient Programs. At May 31, 1985, 27 such programs were in operation.

MENTAL HEALTH. The Registrant has, since 1969, managed mental health treatment Programs for individuals suffering from acute emotional problems. Until recently, these Programs were delivered under the name StressCenter. During fiscal 1985, Registrant changed the name of the Programs to CarePsychCenters. Registrant believes this name better reflects the Program provided. These Programs, which are hospital-based, offer diagnostic and therapeutic treatment services conducted by an interdisciplinary team of professionals experienced in the treatment of mental health problems. Admission to the Program is typically voluntary and treatment is tailored to the specific needs of the patient, under the supervision of a psychiatrist.

The length of stay varies in accordance with the severity of the patient's condition but rarely exceeds 90 days. A comprehensive discharge plan is prepared for each patient which may include outpatient psychiatric or psychological treatment, or referral to an alternate treatment facility.

EATING DISORDERS. The Registrant offers a hospital-based, comprehensive eating disorders Program ("EDU"). Registrant began operation of this Program in fiscal 1983. The Program treats those suffering from anorexia nervosa, bulimia and gross obesity. Each patient entering the Program is subject to a physical examination and nutritional assessment. Additional diagnostic and psychiatric evaluations are undertaken when necessary. Each patient's treatment is directed by a physician experienced in the treatment of eating disorders.

The eating disorders Program includes: individual and group therapy, nutritional guidance and management of attendant medical or psychological problems.

Other Activities

REHABILITATION. Registrant and Basic American Medical, Inc. each own 50% of RehabCare Corporation ("RehabCare"). RehabCare is engaged in the development, marketing and management of programs for patients with spinal cord injuries, strokes, closed head injuries and other dysfunctions of neurological or motor systems. The medically supervised treatment provided includes: nursing care; physical, occupational and speech therapy; and such other hospital services necessary to treat the individual patient's disorder.

As of May 31, 1985, RehabCare programs were offered solely in independent general hospitals under contract. However, RehabCare is exploring opportunities to establish regional freestanding facilities. RehabCare opened its first contract program in February 1984.

LONG TERM CARE. Registrant leases and operates a 99-bed intermediate care facility. This facility provides nursing, rehabilitative and sustaining care over extended periods of time to persons who do not require the extensive care provided in a general hospital. For the fiscal year ended May 31, 1985, the intermediate care facility accounted for less than one percent of Registrant's total revenues. Registrant does not intend to expand its long-term care operations and desires to dispose of its existing facility.

PUBLISHING ACTIVITIES. Since 1976, Registrant (under the name CompCare Publications) has been engaged in the publication, distribution and sale of books, pamphlets and brochures relating to Registrant's health care activities and to other life-style management subjects. The primary purpose of these activities is to support Registrant's treatment, training and marketing programs. Literature distributed by Registrant is sold to patients participating in its programs. Such literature is also sold to the general public and educational institutions. Registrant does not own or operate the printing facilities used in the publication of its literature. Publishing activities accounted for less than two percent of Registrant's total revenues in fiscal 1985.

SMOKING CESSATION. Registrant operates smoking cessation seminars under an eight-year license agreement with SmokEnders, Inc. Smoking cessation programs accounted for less than one percent of Registrant's total revenues in fiscal 1985.

Competition

Registrant competes first for the development and implementation of freestanding or Contract Programs and subsequently for patients who utilize these Programs. With respect to both of these areas of competition, Registrant's primary competitors are hospitals and hospital management companies (both not-for-profit and investor owned) which offer programs similar to that of Registrant. An increasing number of such hospitals and management companies have begun offering such programs in the last few years.

Factors to be considered in the development of successful programs include population base and demographic characteristics, community pricing standards, state licensure and rate control issues and Certificate of Need ("CON") requirements (See "Governmental Regulation"). Registrant either markets Contract Programs or develops freestanding Programs accordingly. Registrant has a 13 person marketing staff which identifies potential sites and develops Programs.

With respect to contract programs, Registrant believes that experience, reputation for quality programs, the availability of program support services and price are the principal factors in a hospital's decision to implement a contract program. While a number of competing companies are offering contract programs at prices lower than those of Registrant, Registrant believes that its experience, reputation and program support are superior to that of its competitors. Registrant's experience with CON issues and program implementation often result in a reduced start-up period. Risk to the hospital is also reduced because Registrant's compensation is based primarily on bed occupancy.

The primary competitive factors in attracting referral sources, patients and physicians are marketing, reputation, success record, quality of care and location and scope of services offered. The Registrant has an active marketing program, described below, and is competitive in reputation and other factors necessary for patient attraction. Some of the hospitals which compete with Registrant are either owned or supported by governmental agencies or are owned by nonprofit corporations supported by endowments and charitable contributions which enable some of these hospitals to provide a wider range of services regardless of cost-effectiveness.

Marketing

Registrant has an active public relations program designed to increase public awareness of the Programs offered by Registrant. During fiscal 1985, Registrant spent $10,075,000 for all forms of advertising. Media advertising (television, radio and print) was $8,951,000 (six percent of operating revenues). Registrant's media activities include a series of television commercials advertising Registrant's Programs. The forms of media used are specifically geared to the geographic area in which the marketing efforts are directed. Accordingly, the focal point in Registrant's public relations program is the Program manager whose role in the local community is to identify referral sources and to carry out all marketing activities, including promotional campaigns, media coverage, conferences and distribution of literature, necessary to make the local community aware of the Program. Each Program manager is assisted on an ongoing basis by Registrant's various support services.

Other aspects of Registrant's public awareness program include a nationwide telephone hot line which is staffed by counselors who provide referral advice and help on a 24-hour basis; a Crisis Intervention Program which assists relatives of chemically dependent or emotionally disturbed individuals in motivating a potential patient to seek professional help through an appropriate Program; and CareInstitute conferences which are educational programs designed for health professionals. Registrant also offers an occupational program service which is designed to encourage and assist businesses in developing Employee Assistance Programs. The Employee Assistance Programs are aimed at employees who exhibit deteriorating job performance related to chemical dependency, mental illness or other personal problems.

Joint Ventures
The Registrant places a major emphasis on the development of joint venture partnerships for the management of behavioral medicine programs. In 1972, Registrant entered into its first joint venture to operate two hospitals in California. Subsequently, Registrant formed additional joint ventures to operate chemical dependency facilities in Florida and Ohio. The Registrant owns a 50% interest in each of these joint ventures. Except for one hospital in California, Registrant manages all of these facilities.

In June 1983, Registrant entered into a joint venture with a subsidiary of Voluntary Hospitals of America, Inc. ("VHA"), one of the largest associations of not-for-profit hospitals in the United States. The VHA network encompasses more than 400 community hospitals and major teaching institutions. Registrant has a 70% interest in the joint venture which is called Behavioral Medical Care ("BMC"). BMC markets Registrant's Programs to the VHA network of hospitals. As of May 31, 1985, BMC was operating 28 Contracts consisting of 699 beds.

In May 1984, Registrant entered into a joint venture with a subsidiary of The Health Central System, a non-profit, multi-hospital management and service organization headquartered in Minneapolis, Minnesota. Registrant manages the joint venture and has a 50% interest in it. As of May 31, 1985 the joint venture owned and operated a 258-bed behavioral medicine hospital and two contract units.

Source of Revenues
During fiscal 1985, approximately 96% of Registrant's operating revenue was received from private sources (private health insurers or directly from patients or hospitals in which the Registrant has Contracts) and the balance from the Medicare and Medicaid programs.

Private health insurers offer plans which typically include coverage for chemical dependency or psychiatric treatment. In some instances, the level of coverage for chemical dependency or psychiatric benefits is less than that provided for medical-surgical services. Lower coverage levels result in higher co-payments by the patient who is often unable to meet his or her commitment in its entirety or is unable to pay as rapidly as the insurance company. These factors tend to increase bad debts and days outstanding in receivables at Registrant's freestanding facilities.

Private insurance plans vary significantly in their methods of payment, including: cost, cost plus, prospective rate, negotiated rate, percentage of charges, and billed charges. Blue Cross and other commercial insurance plans have adopted a number of payment mechanisms for the primary purpose of decreasing the amounts paid to hospitals (including Registrant's) for services rendered. These mechanisms include various forms of utilization review, preferred provider arrangements where use of participating hospitals is encouraged in exchange for a discount, and payment limitations which are based on community norms. To date, Registrant believes that these mechanisms have had no material adverse effect on it. Registrant is unable to predict the impact of changing payment mechanisms in future years.

The Medicare program provides hospitalization, physicians, diagnostic and certain other services to eligible persons 65 years of age and over and others considered disabled. Providers of service are paid by the federal government in accordance with regulations promulgated by the United States Department of Health and Human Services ("HHS") and accept said payment, with nominal co-insurance amounts required of the service recipient, as payment in full. Payments under the Medicare program are generally less than billed charges. Regulations governing the Medicare program are subject to change due to modifications in the enabling statutes, changes in administrative policy and interpretation, and certain court actions. These changes may increase or decrease payment by the Medicare program to Registrant's facilities.

The Medicare program had previously paid hospitals the lesser of reasonable cost, as defined by regulation, or the hospital's billed charges. The Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") required the Secretary of HHS ("Secretary") to promulgate regulations substantially limiting payments and increases in payments for hospital operating costs. Regulations established under TEFRA limit annual increases in payment from historical costs to a "target rate." The target rate is calculated from regional and national wage and price indices. Current proposals by the Health Care Financing Administration and pending bills in Congress would freeze the current target rate for the next fiscal year. Registrant is unable to predict whether any of these proposals will be adopted. Hospitals with operating costs less than the target rate may under certain circumstances be entitled to a bonus, hospitals that exceed the limit are penalized. TEFRA also required the Secretary to propose a prospective payment system to

Congress by December 31, 1982. Under a prospective payment system a hospital is paid a predetermined fee without regard to the direct costs of providing the service. In response to the Secretary's proposal, Congress passed and the President signed P.L. 98-21 into law in April 1983. This law requires prospective payment for hospitals effective October 1, 1983 but provides temporary exclusion for certain psychiatric and alcoholism treatment facilities.

The Secretary intends to implement prospective payment for psychiatric services at an unspecified date. The exclusion from prospective payment for qualified providers of alcohol and drug services is afforded on a temporary basis until October 1, 1985. Regulations proposed on June 10, 1985, to be effective October 1, 1985 ("Proposed Regulations"), extend the exclusion from October 1, 1985 to the end of any cost reporting period of an excluded hospital or subunit that began prior to October 1, 1985. This extension will obviate the need for excluded providers to disrupt normal cost reporting procedures in order to file special reports. If the Proposed Regulations are implemented in their current form, Registrant believes they will have the effect of reducing Medicare reimbursement for alcohol and drug services.

Nine of Registrant's facilities participate in the Medicare program. Of these, six are currently excluded from prospective payment (TEFRA target rate limits are applicable to these facilities). Medicare utilization at those facilities participating in the program averaged approximately three percent in fiscal 1985. Registrant does not believe that the imposition of TEFRA limits or prospective payment have had a material adverse impact on its business at freestanding facilities. Loss of exclusion would also not materially impact Registrant's business. Substantially all of the hospitals contracting with Registrant for Programs participate in the Medicare program. Registrant believes that these changes will not have a material adverse impact on its Contract operations, however, until the exclusions for alcoholism and psychiatric services are eliminated Registrant is unable to predict their impact.

Hospitals participating in the Medicare program are required to retain the services of a Peer Review Organization ("PRO"). The PRO is responsible for determining the medical necessity, appropriateness and quality of care given program patients. In instances where the medical necessity of an admission or procedure is challenged by the PRO, payment may be delayed, reduced or denied in its entirety. Amounts denied because of medical review may not be charged to the service recipient, they are absorbed by the hospital. In non-emergency admissions (which encompasses most of Registrant's admissions), review is performed prior to the patient's arrival at the hospital. In the event that the PRO does not approve the admission, the patient is referred to an alternative treatment provider such as an outpatient program or sent home. Registrant believes that the existence of PRO's has had a negative impact on census growth in certain owned and Contract units, but is unable to measure the magnitude because the primary impact is in lost admissions.

The Medicaid program is a combined federal and state program providing coverage for low income persons. The specific services offered and reimbursement methods vary from state to state. In the majority of states Medicaid reimbursement is patterned after the Medicare program. Less than three percent of Registrant's operating revenues are derived from the Medicaid program. Accordingly, changes in reimbursement are not expected to have a material adverse impact on Registrant.

Governmental Regulation

The development and operation of health care facilities is subject to compliance with various federal, state and local statutes and regulations. Hospitals and other health care facilities operated by Registrant as well as hospitals under contract for Programs must comply with the licensing requirements of federal, state and local health agencies, with state mandated rate control initiatives and with the requirements of municipal building codes and local fire departments. State licensing of facilities is a prerequisite to participation in the Medicare and Medicaid programs.

Pursuant to the requirements of federal law, most states have enacted CON laws, the purpose of which is to curtail the proliferation of unnecessary health care services. Thus, prior to the introduction of new facilities, the expansion of old facilities or the introduction of major new services (such as Registrant's Contract Programs) in existing facilities, Registrant (in the case of its facilities), or the contracting hospital for a Contract Program, must demonstrate to either state or local authorities, or both, that it is in compliance with the plan adopted by such agencies. Registrant, because of its experience in the processing of the CON documentation required for such Programs, usually prepares such documentation on behalf of the contracting hospital, with the assistance of the hospital. The CON application process ordinarily takes from six to 18 months, and may in some instances take two years or more, depending upon the state involved and whether the application is contested by a competitor or the health agency. As of

May 31, 1985, Registrant had entered into, but not yet opened 16 CareUnit Contracts, three CarePsych-Center Contracts, two EDU Contracts and five RehabCare Contracts with general hospitals, 10 of which are awaiting governmental approval. Some states have enacted or have under legislative consideration "sunset" provisions which require the review, modification or deletion of statutes when no longer needed. CON legislation is under review in a number of states under these provisions. Registrant is unable to predict the outcome of these deliberations but believes that the elimination of CON requirements would positively impact its business.

The Joint Commission on the Accreditation of Hospitals ("JCAH"), at a facility's request, will participate in the periodic surveys which are conducted by state and local health agencies to insure continuous compliance with all licensing requirements by health care facilities. JCAH accreditation satisfies certain of the certification requirements for participation in the Medicare and Medicaid programs. A facility found to substantially comply with JCAH standards receives accreditation. A patient's choice of a treatment facility may be affected by JCAH accreditation considerations because most major third-party payors limit coverage to services provided by an accredited facility. Registrant believes that all of the facilities operated by it and hospitals under Contract have received or, in the case of new facilities, applied for, such accreditation.

The laws of various states in which Registrant operates generally prevent corporations from engaging in the practice of medicine or other professions. Although Registrant believes that its operations do not violate these prohibitions, recent legal precedents in this area are unclear and there can be no assurance that state authorities or courts will not determine that Registrant is engaged in unauthorized professional practice. In the event of an unfavorable determination, Registrant could be required to modify its method of operation or could be restrained from the continuation of certain of its operations, the result of which could be materially adverse to Registrant.

Both the Medicare and Medicaid programs contain specific physical plant, safety, patient care and other requirements which must be satisfied by health care facilities in order to qualify under said programs. Registrant believes that the facilities it owns or leases are in substantial compliance with the various Medicare and Medicaid regulatory requirements applicable to them.

Administration and Employees

Registrant's executive and administrative offices are located in Newport Beach, California, where management controls operations, marketing, accounting, medical insurance claims, governmental and statistical reporting, advertising and public relations, research and treatment program evaluation. Registrant has purchased a 75,000 square foot office building in Irvine, California, where it intends to relocate its headquarters in fiscal 1986. In addition to housing Registrant's administrative staff, this facility will be the site of its primary training center.

At May 31, 1985, Registrant employed approximately 220 persons in its corporate and administrative offices, 2,700 persons in the hospital and long-term care facilities operated by it, and 740 persons assigned to its Contract units. The physicians and psychiatrists who are the medical directors of Registrant's Contract units, the psychologists serving on treatment teams, and the doctors utilizing the facilities operated by Registrant are not employed by Registrant.

Registrant has not encountered any work stoppages due to labor disputes with its employees. Although Registrant has expanded rapidly in the last five years, it has not experienced any significant difficulty in attracting competent employees.

Item 2. Properties.

The following table sets forth certain information regarding the properties owned or leased by Registrant at May 31, 1985:

Name and Location	Owned or Leased	Lease Expires (1)	Monthly Rental (2)
Chemical Dependency Treatment Facilities			
CareUnit Hospital (3) Fort Worth, Texas	Owned (4)	—	—
Crossroads Hospital (5) Van Nuys, California	Leased	1997	$ 5,577
CareUnit Hospital (6) Orange, California	Owned (4)	—	—
CareUnit Hospital Los Angeles, California	Owned (4)	—	—
CareUnit Hospital (7) Kirkland, Washington	Leased	2035	12,000(8)
CareUnit Facility (9) Jacksonville Beach, Florida	Owned (4)	—	—
CareUnit Hospital (9) Cincinnati, Ohio	Owned (4)	—	—
CareUnit Hospital St. Louis, Missouri	Owned (4)	—	—
Starting Point, Oak Avenue Orangevale, California	Owned	—	—
Starting Point, Orange County (10) Costa Mesa, California	Owned (4)	—	—
Starting Point, Grand Avenue Sacramento, California	Owned (4)	—	—
CareUnit Facility (9) Tampa, Florida	Owned	—	—
CareUnit Hospital (11) Albuquerque, New Mexico	Leased	2012	4,049
CareUnit Hospital Las Vegas, Nevada	Owned	—	—
Psychiatric Treatment Facilities			
Brea Neuropsychiatric Center (12) Brea, California	Owned	—	—
Woodview-Calabasas Hospital (13) Calabasas, California	Leased	1996	19,227(14)(17)
Golden Valley Health Center (9) Golden Valley, Minnesota	Owned	—	—
Other Operating Facilities			
Tustin Manor Tustin, California (Intermediate Care Facility)	Leased	1995	7,754(14)
CompCare Publications Minneapolis, Minnesota	Leased	1986	4,879
Administrative Facilities			
Corporate Headquarters (15) Newport Beach, California	Leased	1996	27,496
Corporate Headquarters (16) Irvine, California	Owned	—	—
Regional Headquarters Tampa, Florida	Leased	1989	8,623

(1) Assumes all options to renew will be exercised.

(2) All leases, other than those relating to Registrant's administrative facilities, are triple net leases under which Registrant bears all costs of operations, including insurance, taxes and utilities. Registrant is responsible for specified percentages of increases in taxes, assessments and operating costs relating to its administrative facilities.

(3) Leased by Registrant from 1971 to 1981.

(4) Subject to encumbrances. For information concerning Registrant's long-term debt see Note 3 to Consolidated Financial Statements appearing elsewhere in this report.

(5) Leased by a joint venture and managed by Registrant.

(6) Leased by Registrant from 1976 to 1981.

(7) Managed by Registrant from 1978 to 1981.

(8) Subject to increase every three years based upon increases in the Consumer Price Index, not to exceed 10%.

(9) Owned by a joint venture and managed by Registrant.

(10) In September 1983, two of Registrant's long-term care facilities were converted to a single chemical dependency treatment facility.

(11) The Registrant has a 30-year land lease for the facility in Albuquerque which includes 182,200 square feet of land.

(12) Leased by Registrant from 1969 to 1982.

(13) Leased by Registrant and managed by the Registrant's partner in a joint venture.

(14) Subject to increase every five years based upon the Consumer Price Index.

(15) Lease expires in November 1986. Registrant intends to sublease this space after relocating to its new corporate headquarters.

(16) Purchased by Registrant in May 1985. Registrant anticipates occupying in Fall of 1985.

(17) Subject to legal action commenced in December 1979 in Superior Court, State of California, by the lessor. The lessor contends that a 1971 amendment to the lease, which reduced the amount of basic rent subject to five-year increases based upon the Consumer Price Index from $177,600 to $47,600, is void for lack of consideration. The amount of rent in dispute was approximately $4,000 per month from June 1976 to May 1981 and increased to approximately $13,000 per month in June 1981. In April 1985 the case was dismissed for failure to commence trial within the five-year statute of limitations. The lessor is appealing this dismissal.

Item 3. Legal Proceedings.

Registrant is routinely engaged in the defense of lawsuits arising out of the ordinary course and conduct of its business and has insurance policies covering such potential insurable losses where such coverage is cost effective. During the period March 1, 1977 through February 28, 1983, Registrant's Contract operations were covered by liability insurance policies underwritten by Glacier General Assurance Company of Missoula, Montana ("Glacier"). In March 1985, courts in California and Montana appointed a receiver and a rehabilitator, respectively, for Glacier's assets in those states and entered moratoria on the payment of policy claims. At present Registrant is unable to determine whether Glacier would be able to fulfill its obligations under the liability policies issued to Registrant or whether the proceeds, if any, from Glacier's reinsurance policies would be available to Registrant. However, Registrant does not believe that Glacier's potential failure would be likely to result in a material adverse effect on its financial condition. In March 1983, Registrant replaced Glacier with other liability insurance carriers.

On June 1, 1984, the State Department of Health Services and Office of Statewide Health Planning and Development ("OSHPD") filed an action against Registrant in Superior Court, State of California for the County of Orange. The action seeks an injunction prohibiting the operation of chemical dependency recovery services at Starting Point, Orange County, a licensed skilled nursing facility. The primary issue is whether such services can be offered in a skilled nursing facility or whether a change of license category is required. The action also seeks civil penalties for allegedly violating the Certificate of Need law and for advertising its services for which it is not properly licensed. A hearing has been held and the Court refused to issue a preliminary injunction, thus permitting the facility to continue in operation. The OSHPD then unsuccessfully sought a writ of mandate in the Court of Appeal. At present the OSHPD is pursuing the appeal of the denial of the preliminary injunction in the Court of Appeal. Registrant considers this action to be without merit.

Item 4. Submission of Matters to a Vote of Security Holders.

Inapplicable.

Item 5. Market for Registrant's Common Stock and Related Stockholder Matters.

(a) Registrant's Common Stock is traded on the national over-the-counter market and is quoted on the NASDAQ National Market System under the symbol CMPH. The following table sets forth the range of high and low bid prices for the Common Stock for the fiscal quarters indicated. All quotations have been adjusted to give effect to a 33-1/3% stock dividend (which had the effect of a four-for-three stock split) effected July 16, 1985 and are rounded to the nearest one-eighth. Such prices represent interdealer prices without adjustment for retail markup, markdown or commission and do not necessarily represent actual transactions.

Fiscal Year		Bid Price High	Bid Price Low
1985	First quarter	18	12-7/8
	Second quarter	18-1/2	15-5/8
	Third quarter	22-5/8	16
	Fourth quarter	22-7/8	19-5/8
1984:	First quarter	29-3/4	17-3/4
	Second quarter	18-7/8	13-3/8
	Third quarter	19	14
	Fourth quarter	16-5/8	13-5/8

(b) As of June 30, 1985, Registrant had 2,913 stockholders of record.

(c) Registrant paid $.06 and $.075 per share cash dividends on a quarterly basis during the fiscal years ended May 31, 1984 and May 31, 1985, respectively, or an aggregate of $.24 and $.30 per share for those years. Registrant intends to continue to pay regular cash dividends in the future, although the payment of such dividends will be dependent upon the earnings, financial position, cash requirements of Registrant and other relevant factors existing at the time. On June 26, 1985, Registrant's Board of Directors declared a quarterly dividend of $.08 per share payable August 15, 1985, to stockholders of record July 31, 1985.

Item 6. Selected Financial Data.

The following tables summarize selected consolidated financial data and should be read in conjunction with the more detailed consolidated financial statements and notes thereto appearing at page 15 of this report.

	Years Ended May 31,				
	1985	1984	1983	1982	1981
Income Statement Data	(Amounts in thousands, except per share data)				
Revenues:					
Operating	$153,035	$107,913	$86,126	$68,709	$51,351
Interest	4,637	5,416	2,845	4,610	1,232
Other	864	353	412	166	173
	158,536	113,682	89,383	73,485	52,756
Costs and Expenses:					
Operating	84,912	58,817	46,619	39,349	29,546
General, administrative and marketing	32,926	22,742	18,574	16,930	12,227
Depreciation and amortization	4,240	2,781	1,952	1,448	977
Interest	1,577	783	660	603	617
	123,655	85,123	67,805	58,330	43,367
Earnings before taxes on income and extraordinary item	34,881	28,559	21,578	15,155	9,389
Net earnings (1)	17,226	14,058	10,767	7,586	4,627
Earnings per common and common equivalent share (1)					
Primary	1.13	.93	.81	.63	49
Fully diluted	1.13	.93	.81	62	.45
Cash dividends per share	.30	24	.19	.12	.08
Weighted average common and common equivalent shares outstanding	15,315	15,160	13,367	12,680	10,370

(1) Excludes extraordinary gain of $231,000 ($.02 per share) recorded in fiscal 1982. Earnings per share have been adjusted to effect a four-for-three stock split issued July 16, 1985

	At May 31,				
	1985	1984	1983	1982	1981
Balance Sheet Data	(Dollars in thousands)				
Working capital	$ 92,852	$ 55,481	$ 59,691	$30,934	$16,828
Total assets	216,397	144,290	119,491	69,073	41,116
Long-term liabilities	64,5[illegible]2	15,493	6,446	5,291	7,686
Stockholders' equity	1[illegible],745	110,910	100,489	53,561	23,188

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following table sets forth for the periods indicated (i) percentages which certain items reflected in the financial data bear to total revenues and (ii) the percentage increase of such items as compared to the indicated prior period:

	Relationship to Total Revenues			Period-to-Period Increase	
	Years Ended May 31,			Years Ended	
	1985	1984	1983	1984-85	1983-84
Revenues:					
Operating	96.6%	94.9%	96.3%	41.8%	25.3%
Interest	2.9	4.8	3.2	(14.4)	90.4
Other	[illegible]	.3	.5	144.8	(14.3)
	100.0	100.0	100.0	39.5	27.2
Costs and Expenses:					
Operating	53.5	51.8	52.2	44.4	26.2
General, administrative and marketing	20.8	20.0	20.8	44.8	22.4
Depreciation and amortization	2.7	2.4	2.2	52.5	42.5
Interest	1.0	.7	.7	101.4	18.6
Earnings before taxes on income	22.0	25.1	24.1	22.1	32.4
Taxes on income	11.1	12.7	12.1	21.7	34.1
Net earnings	10.9	12.4	12.0	22.5	30.6

Results of Operations

Registrant's revenues have increased from approximately $89,000,000 in fiscal 1983 to $159,000,000 in fiscal 1985. Revenue increases have been generated by increases in the utilization of Registrant's existing facilities, the addition of new facilities and by price increases. Facility utilization varies as to its impact on revenues depending on the type of services provided and the method of delivery employed. Increased utilization of Registrant's freestanding chemical dependency and psychiatric facilities has a greater effect on revenues than does increased utilization of Contract operations. This difference is attributable to higher prices charged for each day of service rendered in freestanding facilities where a broader range of patient care services are provided. From the beginning of fiscal 1983 through fiscal 1985 Registrant opened 10 such freestanding facilities. Reflecting these facts, the contribution to operating revenues of Registrant's freestanding facilities increased from approximately 58% in fiscal 1983, to 60% in fiscal 1984 and to 63% in fiscal 1985. Contract operations represented approximately 37% in fiscal 1983, 37% in fiscal 1984 and 34% in fiscal 1985.

Operating revenues for fiscal 1985 and 1984 increased by 42% and 25% respectively, over the previous periods. Of the increase for fiscal 1985, approximately (i) 45% was derived from the improved utilization of existing freestanding facilities and Contract programs, (ii) 15% was due to price increases, (iii) 30% from new freestanding facilities (principally Golden Valley Health Center), and (iv) 10% from new Contracts net of closures. Of the increase for fiscal 1984, approximately (i) 35% was due to increased utilization of existing Contracts and freestanding facilities, (ii) 25% was due to price increases, (iii) 30% was from the two freestanding facilities opened in fiscal 1983, (iv) 5% was from other new freestanding facilities, and (v) 5% was from revenues of new Contracts, net of Contracts closed.

Costs and expenses increased approximately 45% when comparing fiscal 1985 to 1984, and 25% when comparing fiscal 1984 to 1983. A major factor contributing to this increase is the addition of new facilities during these periods. The increases in depreciation expense in fiscal 1985 and 1984 are primarily due to new freestanding facilities and the remodeling and expansion of existing facilities. Interest expense increased $794,000 in fiscal 1985. This increase resulted from the issuance of $46,000,000 in convertible subordinated debentures in the fourth quarter of fiscal 1985, the financing of CareUnit Hospital of St. Louis during the second quarter of fiscal 1984 and the reduction in capitalized interest that decreased interest expense in fiscal 1984. Interest incurred in fiscal 1984 increased by approximately $453,000 and was offset by the capitalization of interest relating to the construction of new facilities. Media advertising was approximately 6% of operating revenues in fiscal 1985 and 7% in fiscal 1984. For fiscal 1985, Registrant's charge to earnings for its executive bonus plan was approximately $1,200,000 ($.04 per share) while Registrant accrued no charge to earnings during fiscal 1984 as it did not meet its internal operating goals upon which the bonus is determined.

Operating margins (operating and other revenues less costs and expenses) declined from approximately 21% to 20% when comparing fiscal 1985 to 1984. In addition to the factors discussed above, start-up losses or lower than average margins in newer freestanding facilities inhibited improved margin performance. Margins were also negatively impacted by the increase in start-up losses associated with Registrant's Canadian operations and its RehabCare subsidiary (combined $.02 per share). As a result of the decline in operating margin and the decrease in interest income, Registrant's total margin declined from 25% in fiscal 1984 to 22% in fiscal 1985. Operating margins remained at approximately 21% when comparing fiscal 1984 to fiscal 1983. Although margins were positively impacted because no executive bonus was accrued in fiscal 1984 (while approximately $1,600,000 was charged to earnings in fiscal 1983) this was offset by the increase in media advertising from 6% to 7% of revenues, the lower-than-average margin at its CareUnit Hospital of St. Louis, start-up costs associated with and the losses incurred during the conversion of Registrant's two long-term care facilities to a Starting Point facility and the start-up costs associated with its BMC, RehabCare and Canadian operations.

Liquidity and Capital Commitments

Registrant's current ratio increased to approximately 4.3:1 at May 31, 1985 as compared to 4.1:1 at May 31, 1984. Accounts receivable days outstanding increased from 79 days at May 31, 1984 to 85 days at May 31, 1985. This increase in days is primarily due to slower payments by third-party payors and the increased proportion of receivables in freestanding facilities in which days outstanding are generally higher than Contract receivables.

The Registrant has committed approximately $17,600,000 for construction of new freestanding facilities in Coral Springs, Florida and Chicago, Illinois, refurbishment of existing freestanding facilities and completion of the interior of its new corporate headquarters. At May 31, 1985, approximately $4,800,000 had been expended on the Coral Springs project. Registrant has committed approximately $6,800,000 to finance the construction of an 84-bed psychiatric hospital to be located in the City of Manchester, New Hampshire. The loan is for a period of approximately two years and bears interest at the rate of prime plus two percent. At May 31, 1985, approximately $3,162,000 was outstanding on the loan.

Registrant has a $10,000,000 bank line of credit, unused at May 31, 1985, which expires September 30, 1985. During the line period Registrant must maintain a compensating balance equal to 5% of the commitment. Because of its present cash on hand, expected cash flow from earnings, bank line of credit and the possibility of obtaining secured financing for a portion of its major planned expenditures, Registrant believes it will have no difficulty in meeting its obligations during the coming fiscal year.

Impact of Inflation

Although inflation has become less of a significant factor in the nation's economy, to cope with its effect of increasing expenses, Registrant regularly raises prices charged at its leased and owned facilities. Registrant's Contracts provide for annual price increases to reflect increases in the Consumer Price Index. To date, these price increases have been adequate to offset Registrant's increase in costs.

Item 8. Financial Statements and Supplementary Data.

Comprehensive Care Corporation
Index to Consolidated Financial Statements
Years Ended May 31, 1985, 1984 and 1983

Report of Independent Certified Public Accountants

To the Stockholders and Board of Directors
Comprehensive Care Corporation

We have examined the consolidated balance sheet of Comprehensive Care Corporation and subsidiaries as of May 31, 1985 and the related consolidated statements of earnings, stockholders' equity and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. The financial statements for the years ended May 31, 1984 and 1983 were examined by other accountants whose report dated July 20, 1984 expressed an unqualified opinion on those statements.

In our opinion, the accompanying 1985 consolidated financial statements present fairly the financial position of Comprehensive Care Corporation and subsidiaries at May 31, 1985 and the results of their operations and the changes in their financial position for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Peat, Marwick, Mitchell & Co.

Newport Beach, California
July 18, 1985

Report of Independent Certified Public Accountants

To the Stockholders and Board of Directors
Comprehensive Care Corporation

We have examined the consolidated balance sheet of Comprehensive Care Corporation and subsidiaries as of May 31, 1984 and the related consolidated statements of earnings, stockholders' equity and changes in financial position for each of the two years in the period ended May 31, 1984. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of Comprehensive Care Corporation and subsidiaries at May 31, 1984 and the results of their operations and the changes in their financial position for each of the two years in the period ended May 31, 1984, in conformity with generally accepted accounting principles applied on a consistent basis.

Newport Beach, California
July 20, 1984

Lesley, Thomas, Schwarz & Postma

Consolidated Balance Sheets

Comprehensive Care Corporation and Subsidiaries

	May 31, 1985	May 31, 1984
Assets	(Dollars in thousands)	
Current assets:		
Cash and cash items, including time deposits of $58,197 and $37,263	$ 62,228	$ 41,761
Accounts and notes receivable, less allowance for doubtful accounts of $6,674 and $3,513 (Note 13)	47,903	27,270
Prepaid taxes	4,531	—
Other current assets	6,320	4,337
Total current assets	120,982	73,368
Property and equipment, at cost (Notes 3, 5 and 8)	84,216	63,432
Less accumulated depreciation and amortization	11,711	7,946
Total property and equipment	72,505	55,486
Other assets:		
Costs in excess of net assets of businesses purchased	4,774	4,915
Notes receivable (Note 2)	1,158	4,592
Investments	4,548	3,760
Deferred contract costs	3,218	845
Other (Note 6)	9,212	1,324
Total other assets	22,910	15,436
	$216,397	$144,290

	1985	1984
Liabilities and Stockholders' Equity		
Current liabilities:		
Note payable, accounts payable and accrued liabilities (Note 10)	$ 19,611	$ 12,325
Long-term debt payable within one year (Note 3)	1,183	1,163
Deferred income taxes (Note 7)	7,001	3,300
Income taxes payable	335	1,099
Total current liabilities	28,130	17,887
Long-term debt due after one year (Note 3)	59,233	14,658
Other liabilities	2,076	—
Deferred income taxes (Note 7)	3,213	835
Commitments and contingent liabilities (Notes 5 and 14)		
Stockholders' equity (Note 4):		
Common stock, $.10 par value; authorized 30,000,000 shares; issued and outstanding 15,169,483 and 15,160,283 shares	1,138	1,137
Additional paid-in capital	76,021	75,862
Retained earnings	46,586	33,911
Total stockholders' equity	123,745	110,910
	$216,397	$144,290

See notes to consolidated financial statements.

Consolidated Statements of Earnings
Comprehensive Care Corporation and Subsidiaries

	Years Ended May 31,		
	1985	1984	1983
	(Dollars in thousands, except per share amounts)		
Revenues:			
Operating	$153,035	$107,913	$86,126
Interest	4,637	5,416	2,845
Other	864	353	412
	158,536	113,682	89,383
Costs and Expenses:			
Operating	84,912	58,817	46,619
General, administrative and marketing	32,926	22,742	18,574
Depreciation and amortization (Note 8)	4,240	2,781	1,952
Interest	1,577	783	660
	123,655	85,123	67,805
Earnings before taxes on income	34,881	28,559	21,578
Taxes on income (Note 7)	17,655	14,501	10,811
Net earnings	$ 17,226	$ 14,058	$10,767
Earnings per common and common equivalent share (Note 1):			
Primary and fully diluted	$1.13	$.93	$.81
Dividends per common share	$ .30	$.24	$.18

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' Equity
Comprehensive Care Corporation and Subsidiaries

	Common Stock		Additional Paid-In	Retained
	Shares	Amount	Capital	Earnings
	(Amounts in thousands)			
Balances, May 31, 1982	13,208	$ 991	$37,379	$15,191
Net earnings	—	—	—	10,767
Additional shares issued in public offering concluded April 21, 1983, net of expenses	1,907	143	38,142	—
Dividends	—	—	—	(2,468)
Exercise of stock options	45	3	341	—
Balances, May 31, 1983	15,160	1,137	75,862	23,490
Net earnings	—	—	—	14,058
Dividends	—	—	—	(3,637)
Balances, May 31, 1984	15,160	1,137	75,862	33,911
Net earnings	—	—	—	17,226
Exercise of stock options	9	1	159	—
Dividends	—	—	—	(4,551)
Balances, May 31, 1985	15,169	$1,138	$76,021	$46,586

See notes to consolidated financial statements.

Consolidated Statements of Changes in Financial Position
Comprehensive Care Corporation and Subsidiaries

	Years Ended May 31, 1985	1984	1983
	(Dollars in thousands)		
Financial resources provided by:			
Operations:			
Net earnings	$17,226	$14,058	$10,767
Items not requiring outlay of working capital:			
Depreciation and amortization of property and equipment	3,878	2,614	1,906
Deferred income taxes	2,378	451	151
Annuity income	(347)	(362)	(86)
Amortization of goodwill and other intangible assets	362	167	44
Working capital provided by operations	23,497	16,928	12,784
Disposal of property and equipment	299	4,109	179
Additional long-term debt	48,076	10,129	1,434
Decrease in notes receivable	3,518	882	1,433
Issuance of common stock	160	—	38,629
Other sources	—	183	220
	75,550	32,231	54,679
Financial resources used for:			
Acquisition of property and equipment	21,196	25,179	14,892
Reduction of long-term debt	1,425	1,533	457
Increase in notes receivable	84	3,570	1,418
Dividends	4,551	3,637	2,468
Deferred contract costs	2,599	845	—
Increase in costs in excess of net assets of businesses purchased	—	68	4,187
Investments	1,250	817	2,500
Other applications	7,074	792	—
	38,179	36,441	25,922
Increase (decrease) in working capital	$37,371	$(4,210)	$28,757
Summary of changes in components of working capital:			
Increase (decrease) in current assets:			
Cash and cash items	$20,467	$(6,987)	$24,505
Accounts and notes receivable	20,633	6,389	5,985
Prepaid taxes	4,531	—	—
Other current assets	1,983	1,719	629
	47,614	1,121	31,119
Increase (decrease) in current liabilities:			
Note payable, accounts payable and accrued liabilities	7,286	2,590	2,283
Long-term debt payable within one year	20	684	76
Deferred income taxes	3,701	1,731	1,569
Income taxes payable	(764)	326	(1,566)
	10,243	5,331	2,362
Increase (decrease) in working capital	$37,371	$(4,210)	$28,757

See notes to consolidated financial statements.

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Note 1-Summary of Significant Accounting Policies
The consolidated financial statements include the accounts of the Company, its subsidiaries and the Company's interest in the accounts of joint venture partnerships (see Note 2). All intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications of prior year amounts have been made to conform with current year classifications.

Revenue Recognition
Approximately 96% of the Company's operating revenues are received from private sources; the remainder from Medicare and Medicaid. The latter are governmental programs which provide for payments at rates generally less than the established billing rates. Payments are subject to audit by intermediaries administering these programs. Revenues from these programs are recorded under reimbursement principles applicable under the circumstances. Although management believes estimated provisions currently recorded properly reflect these revenues, any differences between final settlement and these estimated provisions are reflected in operating revenues in the year finalized.

Intangible Assets
Costs in excess of net assets of businesses purchased (goodwill) are being amortized over 25 to 40 years. The amounts included in the consolidated balance sheets are net of accumulated amortization of $384,000 and $244,000 at May 31, 1985 and 1984, respectively. The costs of purchased licenses, copyrights and similar rights are amortized over the period of benefit.

Capitalized Interest
Interest incurred during the construction of freestanding facilities is capitalized and subsequently charged to depreciation expense over the life of the related asset. The interest rate utilized is either the rate of the specific borrowing associated with the project or the Company's average interest rate on borrowings where there is no specific borrowing associated with the project. The amount of interest capitalized was $161,000 and $330,000 in fiscal 1985 and 1984, respectively.

Deferred Contract Costs
The Company has entered into a limited number of contracts with independent general hospitals whereby it will provide services over a period in excess of the standard two year agreement. In recognition of the hospital's long-term commitment, the Company has paid certain amounts to them. These amounts may be used by the hospital for capital improvements or as otherwise determined by the hospital. The Company is entitled to a pro rata refund in the event that the hospital terminates the contract before its scheduled termination date; accordingly, these amounts are charged to expense over the life of the contract.

Investment Tax Credits
Investment tax credits are accounted for under the "flow through" method

Earnings Per Share
Primary and fully diluted earnings per common and common equivalent share have been computed by dividing net earnings, after giving effect to the elimination of interest expense applicable to the convertible debentures (less income tax effect), by the weighted average number of shares of common stock and common stock equivalents outstanding during the period. The convertible debentures issued in April 1985 are considered to be common stock equivalents from the time of issuance. The weighted average of the number of shares issuable on conversion of the debentures was added to the number of common shares outstanding.

The weighted average number of shares outstanding used to compute primary and fully diluted earnings per share has been adjusted to reflect a four-for-three stock split effected July 16, 1985.

Stock options granted are common stock equivalents but do not have a significant dilutive effect and have not been included in the computation of earnings per share for the periods presented.

The weighted average number of shares is as follows:

	Years Ended May 31,		
	1985	1984	1983
	(Shares in thousands)		
Primary and fully diluted	15,315	15,160	13,367

Note 2-Accounting for Interests in Joint Venture Partnerships

In 1972, the Company entered into a joint venture partnership, named Neuro Affiliates Company, with another corporation for the purpose of operating two hospitals. Under the terms of the joint venture agreement, the Company manages one of the hospitals and its partner manages the other. Each of the partners in the joint venture receives a management fee for the hospital it manages, and they share equally in the profits or losses.

In May 1981, the Company entered into two joint venture partnerships in Florida organized for the purpose of owning and operating 84-bed and 120-bed chemical dependency treatment facilities in Jacksonville Beach and Tampa on properties owned by the joint venturers. The Company has a 50% interest in each joint venture and manages each facility for a management fee based on gross revenues. The Company and its partners share the joint ventures' profits and losses in proportion to their respective joint venture interests. The Company agreed to loan the Tampa joint venture up to $4,000,000 for the purpose of constructing and furnishing the facility. The loan bears interest at the prime rate plus 2% and is secured by a first mortgage against the facility. Construction of the Tampa facility was completed in December 1983. At May 31, 1985, the amount outstanding under the construction loan agreement was $3,506,000. In July 1983, the Company purchased land in Coral Springs, Florida for approximately $850,000. A joint venture, in which the Company has a 50% interest, has been formed and purchased the land from the Company to build a 100-bed chemical dependency treatment facility on it. The Company will serve as facility and joint venture manager. In December 1983, long-term financing was secured for the project in the form of Industrial Development Bonds.

In July 1981, the Company entered into a joint venture partnership in Ohio for the purpose of owning and operating an 84-bed chemical dependency hospital. The Company's partner loaned the joint venture $4,000,000 (at 10% interest) which was used to purchase the building and equipment necessary for operation of the hospital. The Company has a 50% interest in the partnership and manages it for a fee based on gross revenues.

In May 1984, the Company entered into a joint venture agreement with a subsidiary of The Health Central System ("HCS"). The joint venture owns and operates Golden Valley Health Center, a 258-bed behavioral medicine hospital located in a suburb of Minneapolis. The joint venture is marketing the Company's behavioral medicine services to HCS affiliate hospitals. The Company serves as managing partner of the joint venture for which it earns a fee based on profitability. The Company has a 50% interest in the joint venture.

The Company consolidates its interest in the assets, liabilities, income and expenses of the joint ventures. The assets and liabilities of the joint ventures included in the consolidated balance sheets are as follows:

	May 31,	
	1985	1984
Assets	(Dollars in thousands)	
Current assets	$ 8,144	$ 6,870
Property and equipment (net)	18,367	16,312
Other assets	233	1,433
	$26,744	$24,615
Liabilities and partners' equity		
Current liabilities	$ 1,991	$ 1,802
Note payable (1)	1,753	2,024
Long-term liabilities	5,365	5,054
Partners' equity	17,635	15,735
	$26,744	$24,615

(1) This amount was offset against the Company's notes receivable of $3,506,000 and $4,048,000 at May 31, 1985 and 1984, respectively, in the consolidated financial statements.

The Company's proportionate share of the operating results of the joint ventures included in the consolidated statements of earnings is as follows:

	Years Ended May 31,		
	1985	1984	1983
	(Dollars in thousands)		
Revenues	$25,354	$14,557	$10,668
Costs and expenses			
Operating, general, administrative and marketing	18,135	10,924	7,787
Depreciation and amortization	841	317	146
Interest	608	451	147
	19,584	11,692	8,080
Earnings before taxes on income	$ 5,770	$ 2,865	$ 2,588

Note 3-Long-Term Debt

Long-term debt consists of the following:

	May 31,	
	1985	1984
	(Dollars in thousands)	
7% to 10% notes, payable in monthly installments with maturity dates through 2002. Collateralized by real and personal property having a net book value of $6,993.	$ 2,360	$ 2,644
Note payable bearing interest at 72% of prime through 1988, and at 74% of prime for years 1989 through maturity, payable quarterly maturing in December 1995. Collateralized by real and personal property having a net book value of $3,195.	2,625	2,939
Note payable bearing interest at 70% of prime through June 1986, and at 74% of prime from July 1986 through 1995, payable quarterly maturing in 1995. Collateralized by real and personal property having a net book value of $7,827	4,315	4,734
Note payable bearing interest at 10%, payable quarterly with level payments of principal and interest based upon a twenty year amortization schedule, with unpaid principal and interest due in 1975. Collateralized by real and personal property having a net book value of $2,463	1,881	1,923
Note payable bearing interest at 65% of prime, payable monthly maturing in 1994. Collateralized by real property having a net book value of $1,487.	859	913
7-1/2% convertible subordinated debentures due 2010	46,000	—
Capital lease obligations (Note 5)	1,980	2,070
Other	396	598
	60,416	15,821
Less amounts due within one year	1,183	1,163
	$59,233	$14,658

As of May 31, 1985, the annual maturities of long-term debt for the next five years amounted to $1,183,000 in 1986 $1,199,000 in 1987, $1,222,000 in 1988, $1,247,000 in 1989, and $1,624,000 in 1990.

At May 31, 1985, the Company had a $10,000,000 bank line of credit. During the line period, the Company must maintain compensating balances equal to 5% of the commitment plus 5% of the average outstanding balance. No amounts were outstanding under this line of credit at May 31, 1985.

On April 25, 1985, the Company issued $46,000,000 in convertible subordinated debentures. These debentures require that the Company make semi-annual interest payments in April and October at an interest rate of 7-1/2%. The debentures are due in 2010 but may be converted to common stock of the Company at the option of the holder at a conversion price of $25.97 per share, subject to adjustment in certain events. The debentures are also redeemable, at the option of the Company, in certain circumstances. Mandatory annual sinking fund payments sufficient to retire 5% of the aggregate principal amount of the debentures are required to be made on each April 15 commencing in April 1996 to and including April 15, 2009.

Note 4-Stockholders' Equity

The Company effected a four-for-three stock split on July 16, 1985. All share and per share information has been restated to reflect the stock split. The par value of the additional shares of common stock issued in connection with the stock split will be credited to common stock and a like amount charged to additional paid-in-capital in fiscal 1986.

In November 1973, the Company adopted a non-qualified stock option plan which expired May 31, 1983. Options outstanding at May 31, 1985 must be exercised by October 1986.

		Option Price		Market Price When Granted	
	Number of Shares	Per Share	Aggregate	Per Share	Aggregate
		(Dollars in thousands, except share amounts)			
Options granted in March 1980	186,667	$3.75-4.41	$760	$4.41	$823
Options granted in October 1981	27,600	10.88	300	10.88	300
Options exercised in fiscal 1982	(150,667)	3.75-4.41	(610)	4.41	(664)
Options exercised in fiscal 1983	(45,200)	3.75-10.88	(250)	4.41-10.88	(259)
Options exercised in fiscal 1984	(9,200)	10.88	(100)	10.88	(100)
Options outstanding at May 31, 1985	9,200	$10.88	$100	$10.88	$100

On June 24, 1983, the Company adopted a stock option plan which was approved at the stockholders annual meeting held in September, 1983. The total number of shares of common stock which may be granted under this plan cannot exceed 333,333 shares. The Plan is intended to qualify as an Incentive Stock Option Plan. At the time of granting an option under the plan, "stock appreciation rights" and "cash appreciation rights" may be concurrently granted. The Plan provides that 25% of the options become exercisable in each of the four years following the date of grant. The options must be exercised within 10 years of the date of grant and no options may be granted under the Plan subsequent to May 31, 1993.

The following table sets forth the options granted under this plan:

		Option Price		Market Price When Granted	
	Number of Shares	Per Share	Aggregate	Per Share	Aggregate
		(Dollars in thousands, except share amounts)			
Options granted in fiscal 1985	140,345	$13.78-18.38	$1,959	$13.78-18.38	$1,959
Options forfeited	(5,802)	13.78	(80)	13.78	(80)
Options outstanding at May 31, 1985	134,543	$13.78-18.38	$1,879	$13.78-18.38	$1,879

During fiscal 1984 the Company authorized the issuance of the following non-statutory options outstanding at May 31, 1985:

		Option Price		Market Price When Granted	
	Number of Shares	Per Share	Aggregate	Per Share	Aggregate
		(Dollars in thousands, except share amounts)			
Options granted in fiscal 1984	33,333	$15.56-16.88	$526	$15.56-16.88	$526
Options outstanding at May 31, 1985	33,333	$15.56-16.88	$526	$15.56-16.88	$526

The non-statutory options become exercisable at the rate of 25% per year following the date of grant and must be exercised within five years after the date of grant. At May 31, 1985, options for 8,333 shares are exercisable.

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Note 5-Lease Commitments

The Company and the Neuro Affiliates joint venture partnership lease facilities, furniture and equipment. The facility leases contain escalation clauses based on the Consumer Price Index and provisions for payment of real estate taxes, insurance, maintenance and repair expenses.

Total rental expenses for all operating leases were as follows:

	Years Ended May 31, 1985	1984	1983
	(Dollars in thousands)		
Minimum rentals	$603	$637	$482
Contingent rentals	71	78	9
Total rentals	$674	$715	$491

Assets under capital leases are capitalized using interest rates appropriate at the inception of each lease; contingent rents associated with capital leases in fiscal 1985, 1984 and 1983 were $123,000, $122,000 and $122,000, respectively. The net book value of capital leases at May 31, 1985 and 1984 was $1,416,000 and $1,531,000, respectively.

Future minimum payments, by year and in the aggregate, under capital leases and non-cancellable operating leases with initial or remaining terms of one year or more consisted of the following at May 31, 1985:

	Capital Leases: Company	Joint Venture	Total	Operating Leases
	(Dollars in thousands)			
1986	$ 204	$ 122	$ 326	$ 589
1987	204	122	326	522
1988	204	100	304	324
1989	204	89	293	146
1990	204	89	293	49
Later years	2,480	533	3,013	1,097
Total minimum lease payments	$3,500	$1,055	4,555	$2,727
Less amounts representing interest			2,575	
Present value of net minimum lease payments			$1,980	

Note 6-Deferred Compensation Plans

The Company has a deferred compensation plan for its Chairman. The vested unfunded benefits at May 31, 1985 and 1984 ($901,000 and $765,000), have been accrued by the Company. The Company utilized an 8% discount rate in determining the present value of vested unfunded past service cost. The total charges to earnings for fiscal years 1985, 1984 and 1983 amounted to $136,000, $143,000 and $142,000, respectively. During the fiscal year ended May 1983, the Company purchased a $500,000 annuity from which it intends to meet future obligations of this plan.

In fiscal 1983, the Company also adopted deferred compensation plans for its key executives and Medical Directors. Under provisions of these plans, participants may elect to defer a portion of their current compensation to future periods. In 1985, the plan for key executives was modified to provide payout of termination benefits over a five-year period. Insurance contracts were purchased in 1985 to meet anticipated obligations under these plans.

The cash surrender value of the insurance contracts is included in other assets on the consolidated balance sheets.

Note 7-Taxes on Income

Taxes on income consist of the following:

	Years Ended May 31,		
	1985	1984	1983
	(Dollars in thousands)		
Currently payable:			
Federal income taxes	$10,264	$10,336	$ 7,247
State income taxes	1,974	1,984	1,473
	12,238	12,320	8,720
Deferred federal income taxes	4,518	1,824	1,788
Deferred state income taxes	899	357	303
	5,417	2,181	2,091
	$17,655	$14,501	$10,811

A reconciliation between taxes on income and the amount computed by applying the statutory federal income tax rate (46%) to earnings before taxes on income is as follows:

	Years Ended May 31,		
	1985	1984	1983
	(Dollars in thousands)		
Income taxes at the statutory tax rate	$16,045	$13,137	$ 9,926
State income taxes net of federal tax benefit	1,540	1,279	981
Investment tax credit	(303)	(270)	(237)
Loss from unconsolidated subsidiary	312	118	—
Amortization of goodwill	65	77	21
Other	(4)	160	120
	$17,655	$14,501	$10,811

Total taxes on income differs from taxes currently payable as a result of differences in the recognition of revenue and expense for tax and financial statement purposes. The sources of these differences and the tax effect of each are as follows:

	Years Ended May 31,		
	1985	1984	1983
	(Dollars in thousands)		
Excess tax over book depreciation	$ 572	$ 406	$ 238
Cash basis accounting and different reporting period for tax purposes by joint ventures	2,312	481	928
State income taxes not currently deductible	(462)	(197)	(194)
Deferred compensation expense not currently deductible	(351)	(403)	(77)
Cash basis accounting by subsidiaries	1,363	1,378	573
Employee benefit expenses not currently recorded for book purposes	2,405	407	589
Other	(422)	109	34
	$5,417	$ 2,181	$ 2,091

Note 8-Property and Equipment

Depreciation and amortization of property and equipment are computed on the straight-line method over the estimated useful lives of the related assets, principally: buildings and improvements — 5 to 40 years; furniture and equipment — 3 to 12 years; leasehold improvements — life of lease or life of asset, whichever is less.

Cost	Balance Beginning of Period	Additions at Cost	Retirements	Reclassifications	Balance End of Period
			(Dollars in thousands)		
Year ended May 31, 1985:					
Land and improvements	$ 7,476	$ 6,957	$ 147	$ (19)	$14,267
Buildings and improvements	42,607	11,359	18	(129)	53,819
Furniture and equipment	10,144	2,850	237	155	12,912
Leasehold improvements	501	30	10	(7)	514
Capitalized building leases	2,704	--	—	—	2,704
	$63,432	$21,196	$ 412	$ —	$84,216
Year ended May 31, 1984:					
Land and improvements	$ 7,253	$ 1,725	$ 1,008	$ (494)	$ 7,476
Buildings and improvements	25,315	20,121	3,146	317	42,607
Furniture and equipment	7,071	3,220	324	177	10,144
Leasehold improvements	891	113	503	—	501
Capitalized building leases	2,704	—	—	—	2,704
	$43,234	$25,179	$ 4,981	$ —	$63,432
Year ended May 31, 1983:					
Land and improvements	$ 4,000	$ 3,253	$ —	$ —	$ 7,253
Buildings and improvements	16,464	8,851	57	57	25,315
Furniture and equipment	4,643	2,783	298	(57)	7,071
Leasehold improvements	886	5	—	—	891
Capitalized building leases	2,704	—	—	—	2,704
	$28,697	$14,892	$ 355	$ —	$43,234

Accumulated Depreciation and Amortization	Balance Beginning of Period	Additions Charged to Expense	Retirements	Reclassifications	Balance End of Period
			(Dollars in thousands)		
Year ended May 31, 1985:					
Buildings and improvements	$ 3,147	$ 1,882	$ 2	$ —	$ 5,027
Furniture and equipment	3,345	1,703	111	22	4,959
Leasehold improvements	281	177	—	(22)	436
Capitalized building leases	1,173	116	—	—	1,289
	$ 7,946	$ 3,878	$ 113	$ —	$11,711
Year ended May 31, 1984:					
Buildings and improvements	$ 2,255	$ 1,154	$ 277	$ 15	$ 3,147
Furniture and equipment	2,503	1,095	238	(15)	3,345
Leasehold improvements	389	249	357	—	281
Capitalized building leases	1,057	116	—	—	1,173
	$ 6,204	$ 2,614	$ 872	$ —	$ 7,946
Year ended May 31, 1983:					
Buildings and improvements	$ 1,382	$ 917	$ 43	$ (1)	$ 2,255
Furniture and equipment	1,862	774	133	—	2,503
Leasehold improvements	287	101	—	1	389
Capitalized building leases	941	116	—	—	1,057
	$ 4,472	$ 1,908	$ 176	$ —	$ 6,204

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Note 9-Acquisitions

In June 1984, the Company opened CareUnit Hospital of Nevada. The hospital, located in Las Vegas, has a capacity of 50 beds and specializes in the treatment of adolescents.

In February 1985, the Company consummated a new agreement with SmokEnders, Inc. Under terms of the new agreement the Company has been granted an eight year license to operate smoking cessation seminars using the name and materials of SmokEnders. As consideration, the Company agreed to forego repayment of amounts due from SmokEnders under the prior agreement, paid certain obligations of SmokEnders, and agreed to pay a royalty based on future revenues derived from the operation of the seminars. The amount included in other assets for the license consideration is approximately $1,460,000 at May 31, 1985. The Company is amortizing the license fee ratably over its eight year life.

Note 10-Note payable, accounts payable and accrued liabilities

Note payable, accounts payable and accrued liabilities consist of the following:

	At May 31, 1985	At May 31, 1984
	(Dollars in thousands)	
Note payable	$ 1,410	$ 554
Accounts payable and accrued liabilities	10,690	7,059
Accrued salaries and wages	5,930	3,850
Payable to third-party intermediaries	1,581	862
	$19,611	$12,325

Note 11-Quarterly Results (unaudited): Years Ended May 31, 1985 and 1984

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(Dollars in thousands, except per share amounts)			
1985				
Revenues	$32,547	$37,208	$39,736	$49,045
Earnings before taxes on income	$ 8,214	$ 8,797	$ 8,020	$ 9,850
Taxes on income	4,132	4,492	4,242	4,789
Net earnings	$ 4,082	$ 4,305	$ 3,778	$ 5,061
Earnings per share—primary and fully diluted	$.27	$.28	$.25	$.33
1984				
Revenues	$25,763	$26,945	$28,150	$32,824
Earnings before taxes on income	$ 6,521	$ 7,065	$ 5,962	$ 9,011
Taxes on income	3,261	3,532	2,981	4,727
Net earnings	$ 3,260	$ 3,533	$ 2,981	$ 4,284
Earnings per share—primary and fully diluted	$.21	$.23	$.20	$.29

29.

Note 12-Supplementary Statement of Earnings Information

Advertising costs for fiscal years 1985, 1984 and 1983 amounted to $10,075,000, $8,797,000 and $6,217,000 respectively. No other reporting categories are required for Form 10-K.

Note 13-Valuation and Qualifying Accounts

Description	Balance Beginning of Period	Additions: Charged to Revenue	Additions: Charged to Other Accounts	Deductions: Write-off of Accounts	Balance End of Period
		(Dollars in thousands)			
Allowance for doubtful accounts:					
Year ended May 31, 1985	$3,513	$12,398	$1,930(a)	$11,167	$6,674
Year ended May 31, 1984	$3,252	$5,935	$1,275(a)	$6,949	$3,513

(a) Amounts are recoveries on accounts previously charged to this allowance.

Note 14-Contingencies

The Company is routinely engaged in the defense of lawsuits arising out of the ordinary course and conduct of its business and has insurance policies covering such potential insurable losses where such coverage is cost effective. During the period March 1, 1977 through February 28, 1983, the Company's contract operations were covered by liability insurance policies underwritten by Glacier General Assurance Company of Missoula, Montana ("Glacier"). In March 1985, courts in California and Montana appointed a receiver and a rehabilitator, respectively, for Glacier's assets in those states and entered moratoria on the payment of policy claims. At present the Company is unable to determine whether Glacier would be able to fulfill its obligations under the liability policies issued to the Company or whether the proceeds, if any, from Glacier's reinsurance policies would be available to the Company. However, the Company does not believe that Glacier's potential failure would be likely to result in a material adverse effect on its financial condition. In March 1983, the Company replaced Glacier with other liability insurance carriers.

On June 1, 1984, the State Department of Health Services and Office of Statewide Planning and Development ("OSHPD") filed an action against the Company in the Superior Court, State of California, for the County of Orange. The action seeks an injunction prohibiting the operation of chemical dependency recovery services at Starting Point, Orange County, a licensed skilled nursing facility. The primary issue is whether such services can be offered in a skilled nursing facility or whether a change of license category is required. The action also seeks civil penalties for allegedly violating the Certificate of Need law and for advertising its services for which it is not properly licensed. A hearing has been held and the Court refused to issue a preliminary injunction, thus permitting the facility to continue in operation. The OSHPD then unsuccessfully sought a writ of mandate in the Court of Appeal. At present the OSHPD is pursuing the appeal of the denial of the preliminary injunction in the Court of Appeal. The Company believes this action to be without merit.

Item 9. Disagreements on Accounting and Financial Disclosure.

None.

Item 10. Directors and Executive Officers of the Registrant.
There is hereby incorporated by reference the information which will appear under the caption "Election of Directors" in a Proxy Statement to be filed with the Securities and Exchange Commission relating to Registrant's Annual Meeting of Stockholders to be held on September 26, 1985.

Item 11. Executive Compensation.
There is hereby incorporated by reference the information which will appear under the caption "Executive Compensation" in a Proxy Statement to be filed with the Securities and Exchange Commission relating to Registrant's Annual Meeting of Stockholders to be held on September 26, 1985.

Item 12. Security Ownership of Certain Beneficial Owners and Management.
There is hereby incorporated by reference the information which will appear under the caption "Principal Stockholders" and "Election of Directors" in a Proxy Statement to be filed with the Securities and Exchange Commission relating to Registrant's Annual Meeting of Stockholders to be held on September 26, 1985.

Item 13. Certain Relationships and Related Transactions.
There is hereby incorporated by reference the information which will appear under the caption "Executive Compensation" in a Proxy Statement to be filed with the Securities and Exchange Commission relating to Registrant's Annual Meeting of Stockholders to be held on September 26, 1985.

Part IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K.

(a) 1. Financial Statements
  Included in Part II of this report:
    Reports of Independent Certified Public Accountants
    May 31, 1985 and 1984
      Consolidated balance sheets
    Years Ended May 31, 1985, 1984 and 1983
      Consolidated statements of earnings
      Consolidated statements of changes in stockholders' equity
      Consolidated statements of changes in financial position
      Notes to consolidated financial statements
  2. Financial Statement Schedules
  Information required to be filed as Financial Statement Schedules has been included in Notes to Consolidated Financial Statements. Other schedules are omitted because the conditions requiring their filing do not exist.
  3. Exhibits
  The exhibits listed on the accompanying index to exhibits are filed as part of this annual report.

(b) Reports on Form 8-K
  None filed during the 4th quarter of fiscal year 1985

Signatures

Pursuant to the requirements of Sections 13 or 15(d) 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, August 12, 1985.

COMPREHENSIVE CARE CORPORATION

By________________________

B. Lee Karns
Chairman

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates so indicated.

Signature	Title	Date
B. Lee Karns	Chairman (Chief Executive Officer)	August 12, 1985
Stephen R. Munroe	Senior Vice President (Chief Financial Officer)	August 12, 1985
Mark A. Edwards	Vice President (Chief Accounting Officer)	August 12, 1985
Walter W. Heller, Ph.D.	Director	August 12, 1985
Stewart B. Hoover, M.D.	Director	August 12, 1985
Robert B. Hunter, M.D.	Director	August 12, 1985
George J. Lyon	Director	August 12, 1985
Jack A. McLeod	Director	August 12, 1985
William J. Nicol	Director	August 12, 1985
Joseph A. Pursch, M.D.	Director	August 12, 1985
Richard A. Santoni, Ph.D.	Director	August 12, 1985

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William J. Nicol	Director	August 12, 1985
Joseph A. Pursch, M.D.	Director	August 12, 1985
Richard A. Santoni, Ph.D.	Director	August 12, 1985

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Robert B. Hunter, M.D.	Director	August 12, 1985
George J. Lyon George J. Lyon	Director	August 12, 1985
Jack A. McLeod	Director	August 12, 1985
William J. Nicol	Director	August 12, 1985
Joseph A. Purich, M.D.	Director	August 12, 1985
Richard A. Santoni, Ph.D.	Director	August 12, 1985

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George J. Lyon	Director	August 12, 1985
Jack A. McLeod	Director	August 12, 1985
William J. Nicol	Director	August 12, 1985
Joseph A. Pursch, M.D.	Director	August 12, 1985
Richard A. Santoni, Ph.D.	Director	August 12, 1985

Index to Exhibits Item 14(a)3

		Sequentially Numbered Page
3.1	Restated Articles of Incorporation(1)	
3.2	Amendment to Articles of Incorporation(9)	
3.3	By-Laws of Registrant as presently in effect(5)	
4.1	Indenture dated April 25, 1985, between Registrant and Bank of America, NT&SA relating to Convertible Subordinated Debentures(10)	
10.1	Regular form of CareUnit Contract(1)	
10.2	Regular form of CarePsychCenter Contract(1)	
10.3	Stock Bonus Plan of Registrant, including pamphlet describing such Plan(2)	
10.4	Deferred Compensation Agreement dated April 6, 1982, between Registrant and B. Lee Karns(6)	
10.5	Amendment No. 1 to Deferred Compensation Agreement between Registrant and B. Lee Karns(9)	
10.6	Registrant's Amended and restated 1983 Stock Option Plan(filed herewith)	38
10.7	Form of Individual Benefit Agreement(9)	
10.8	Deferred Compensation Plan for executive management (filed herewith)	53
10.9	Form of Non-Statutory Stock Option Agreement (filed herewith)	84
10.10	Description of Executive Bonus Plan (filed herewith)	89
10.11	Lease dated January 15, 1970, between SoCal Projects, Inc., as Lessor and Registrant as Lessee(3); Amendments to such Lease dated November 25, 1970, April 20, 1971, and March 10, 1972, (re Woodview-Calabasas Hospital)(1)	
10.12	Woodview Lease dated November 1, 1972, between American Psychiatric Hospitals of California, Inc., as Lessor and Neuro Affiliates Company as Lessee (re Crossroads Hospital)(filed herewith)	90
10.13	Lease Dated September 23, 1975, between Bernard Hambleton and Marion Hambleton as Lessors and Alcoholism Center Associates, Inc., as Lessee (re CareUnit Hospital of Kirkland)(1)	
10.14	Standard Lease dated April 28, 1976, amended June 28, 1976, between The Irvine Company as Lessor and Registrant as Lessee (re Executive Offices at Newport Beach, California)(filed herewith)	118
10.15	Joint Venture Agreement November 1, 1972 (re Neuro Affiliates Company)(filed herewith)	249
10.16	Amendment to Joint Venture Agreement dated March 1, 1973, between American Psychiatric Hospitals of California, Inc., and NPHS, Inc., a wholly-owned subsidiary of Registrant (re Neuro Affiliates Company)(1)	
10.17	Joint Venture Agreement dated May 29, 1981, among Registrant, Womlar, Inc., and Carter La Prade and James C. Gibbons as Co-Trustees for the Trust for the Benefit of Children and Grandchildren of Burch Williams (re Caremanor of Northeast Florida)(4)	
10.18	Joint Venture Agreement dated May 29, 1981 among Registrant, Allow, Inc., and Carter La Prade and James C. Gibbons as Co-Trustees of the Trust for the Benefit of Children and Grandchildren of Burch Williams (re Caremanor of Tampa)(5)	
10.19	Guarantee Agreement dated March 30, 1981, between Registrant, Caremanor Hospital of Washington, Inc., Alcoholism Center Associates, Inc., James K. Milam and Doris M. Hutchinson (re purchase of business and assets of CareUnit Hospital of Kirkland)(5)	
10.20	Stock Purchase Agreement dated March 18, 1983, between Registrant and the shareholders of Starting Point, Inc. (re purchase of all of the capital stock of Starting Point, Inc.)(7)	
10.21	Joint Venture Agreement dated July 29, 1981, between Registrant and FLA Realty Corp., and FKLA Realty Corp. and First Amendment to Joint Venture Agreement dated September 30, 1981 (re CareUnit Hospital of Cincinnati)(7)	
10.22	Jacksonville Port Authority Alcoholic Treatment and Rehabilitation Facility Revenue Bond (Caremanor of Northeast Florida Project) dated June 30, 1982, in the amount of $2,000,000(7)	
10.23	Guaranty Agreement dated June 1, 1982, from Caremanor of Northeast Florida, Registrant, Womlar, Inc., Burch Williams, Arthur Lucas, Fred Ahern, Sr., and Algie Outlaw to Southeast Bank, N.A.(7)	
10.24	Construction Loan Agreement dated November 12, 1982, between Registrant and Caremanor of Tampa (re CareUnit of Tampa)(7)	
10.25	Contractor's Agreement dated August 30, 1982, between CareUnit of Tampa and Metric Constructors, Inc. (re construction of CareUnit of Tampa alcoholism facility)(7)	
10.26	Lease Agreement dated January 27, 1982, between St Joseph Development Corporation and Registrant and Addendum to Base Lease dated March 4, 1983 (re Albuquerque alcoholism facility)(7)	
10.27	Loan Agreement between Registrant and Union Bank (re $10,000,000 Bank Line of Credit)(9)	
10.28	Group Annuity Contract between Registrant and Manufacturers Life Insurance Company dated April 18, 1983(8)	

10.29 Annuity Contract between Registrant and New York Life Insurance and Annuity Corporation dated November 2, 1982(8)

10.30 Joint Venture Agreement dated June 17, 1983, between Registrant and Voluntary Health Enterprises, Inc. (re Behavioral Medical Care)(9)

10.31 Joint Venture Agreement dated May 30, 1984 between Registrant and Brookside Ventures, Inc. (re Golden Valley Health Center)(9)

10.32 Agreements between Registrant and SmokEnders, Inc.(filed herewith) 270

10.33 Agreement for purchase of Headquarters Building(9)

10.34 City of Coral Springs, Florida Industrial Development Revenue Bonds (CareUnit of Coral Springs Project) dated September 19, 1983, in the amount of $6,000,000(9)

10.35 The Industrial Development Authority of the City of St. Louis, Missouri, Industrial Revenue Bond (Comprehensive Care Project) dated September 1, 1983 in the amount of $5,050,000(9)

10.36 Loan Guarantee by Registrant for Comprehensive Care Corporation (Canada) Limited (filed herewith) 370

10.37 Construction loan agreement between Registrant and Lake Shore Hospital, Inc. dated June 1, 1984 (filed herewith) 373

0.38 Option Agreement for Purchase and Sale between Registrant and Western Medical Center dated November 14, 1984 (re proposed Santa Ana, California facility) (filed herewith) 414

11 Computation of Earnings per Share (filed herewith) 432

22 List of Registrant's subsidiaries (filed herewith) 433

24.1 Consent of Peat, Marwick, Mitchell & Co. (filed herewith) 435

24.2 Consent of Lesley, Thomas, Schwarz & Postma (filed herewith) 436

(1) Filed as an exhibit to Registrant's Form S-1 Registration Statement No. 2-69263.
(2) Filed as an exhibit to Registrant's Form S-8 Registration Statement No. 2-62410.
(3) Filed as an exhibit to Registrant's Form S-1 Registration Statement No. 2-35139.
(4) Filed as an exhibit to Registrant's Form 8-K dated July 1, 1981.
(5) Filed as an exhibit to Registrant's Form 10-K for the fiscal year ended May 31, 1981.
(6) Filed as an exhibit to Registrant's Form 10-K for the fiscal year ended May 31, 1982.
(7) Filed as an exhibit to Registrant's Form 10-Q for the quarter ended February 28, 1983.
(8) Filed as an exhibit to Registrant's Form 10-K for the fiscal year ended May 31, 1983.
(9) Filed as an exhibit to Registrant's Form 10-K for the fiscal year ended May 31, 1984.
(10) Filed as an exhibit to Registrant's Form S-3 Registration Statement No. 2-97160.

All such exhibits are incorporated herein by this reference.

COMPREHENSIVE CARE CORPORATION, a Delaware corportion

Date: 11/14/84

By: Edward

Name: ______

Title: ______

By: ______

Name: ______

Title: ______

"Buyer"

COMPREHENSIVE CARE CORPORATION AND SUBSIDIARIES
CALCULATION OF EARNINGS PER SHARE

	YEAR ENDED MAY 31, 1985	1984	1983	1982	1981
PRIMARY					
NET EARNINGS APPLICABLE TO COMMON STOCK(a)	$17,361,000	$14,058,000	$10,767,000	$7,817,000	$4,627,000
AVERAGE NUMBER OF SHARES OF COMMON STOCK AND COMMON STOCK EQUIVALENTS OUTSTANDING(d):					
SHARES OF COMMON STOCK	15,169,483	15,160,283	13,366,797	12,459,786	9,534,323
ADDITIONAL AVERAGE NUMBER OF SHARES OUTSTANDING ASSUMING CONVERSION OF 7.5% CONVERTIBLE DEBENTURES	145,591				
AVERAGE NUMBER OF SHARES OF COMMON STOCK AND COMMON STOCK EQUIVALENTS(c)	15,315,074	15,160,283	13,366,797	12,459,786	9,534,323
EARNINGS PER COMMON SHARE AND COMMON STOCK EQUIVALENTS	$1.13	$0.93	$0.81	$0.63	$0.49

	YEAR ENDED MAY 31, 1985	1984	1983	1982	1981
FULLY DILUTED					
NET EARNINGS APPLICABLE TO COMMON STOCK ON A FULLY DILUTED BASIS(b)	$17,361,000	$14,058,000	$10,767,000	$7,817,000	$4,702,000
AVERAGE NUMBER OF SHARES OF COMMON STOCK AND COMMON STOCK EQUIVALENTS OUTSTANDING(d):					
SHARES USED IN CALCULATING PRIMARY EARNINGS PER SHARE	15,315,074	15,160,283	13,366,797	12,459,786	9,534,323
ADDITIONAL AVERAGE NUMBER OF SHARES OUTSTANDING ASSUMING CONVERSION OF 9% CONVERTIBLE DEBENTURES				220,373	835,256
COMMON STOCK EQUIVALENTS(c)	15,315,074	15,160,283	13,366,797	12,680,159	10,3[illegible]9,579
EARNINGS PER COMMON SHARE-ASSUMING FULL DILUTION	$1.13	$0.93	$0.81	$0.62	$0.45

	YEAR ENDED MAY 31, 1985	1984	1983	1982	1981
NET EARNINGS PER SELECTED FINANCIAL DATA	$17,226,000	$14,058,000	$10,767,000	$7,586,000	$4,627,000
ADD EXTRAORDINARY ITEM, NET OF APPLICABLE INCOME TAXES				231,000	
ADD INTEREST EXPENSE ATTRIBUTABLE TO 7.5% CONVERTIBLE SUBORDINATED DEBENTURES	135,000				
(a) NET EARNINGS APPLICABLE TO COMMON STOCK	17,361,000	14,058,000	10,767,000	7,817,000	4,627,000
ADD INTEREST EXPENSE ATTRIBUTABLE TO 9% CONVERTIBLE SUBORDINATED DEBENTURES					75,000
(b) NET EARNINGS APPLICABLE TO COMMON STOCK ON A FULLY DILUTED BASIS	$17,361,000	$14,058,000	$10,767,000	$7,817,000	$4,702,000

(c) STOCK OPTIONS GRANTED ARE COMMON STOCK EQUIVALENTS BUT DO NOT HAVE A SIGNIFICANT DILUTIVE EFFECT AND HAVE NOT BEEN INCLUDED IN THE COMPUTATION OF EARNINGS PER SHARE FOR THE PERIODS PRESENTED.

(d) THE WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING USED TO COMPUTE PRIMARY AND FULLY DILUTED EARNINGS PER SHARE HAS BEEN ADJUSTED TO REFLECT A FOUR-FOR-THREE STOCK SPLIT EFFECTED JULY 16, 1985.

EXHIBIT 11

COMPREHENSIVE CARE CORPORATION
SCHEDULE OF SUBSIDIARIES

SUBSIDIARY NAME	STATE OF INCORPORATION
COMPREHENSIVE CARE CORPORATION (Parent)	Delaware
N.P.H.S., INC.	California
CAREMANOR HOSPITAL OF WASHINGTON, INC.	Washington
TRINITY OAKS HOSPITAL, INC.	Texas
CAREMANOR HOSPITAL OF VIRGINIA, INC.	California
TERRACINA CONVALESCENT HOSPITAL & HOME, INC.	California
CAREUNIT, INC.	California
CAREUNIT HOSPITAL OF ST. LOUIS, INC.	Missouri
STARTING POINT, INC.	California
CAREUNIT HOSPITAL OF ALBUQUERQUE, INC.	New Mexico
CAREUNIT HOSPITAL OF NEVADA, INC.	Nevada
COMPREHENSIVE CARE CORPORATION (CANADA) LIMITED	Canada
REHABCARE CORPORATION	Delaware
CAREINSTITUTE	California
CAREUNIT CLINIC OF WASHINGTON, INC.	Washington
CAREUNIT REDEVELOPMENT CORP.	Missouri
COMPREHENSIVE CARE CORP.	Nevada

EXHIBIT 22

COMPREHENSIVE CARE CORPORATION
SCHEDULE OF JOINT VENTURES

JOINT VENTURES (COMPREHENSIVE CARE CORPORATION IS THE JOINT VENTURER IN ALL EXCEPT NEUROAFFILIATES)

CAREMANOR OF NORTHEAST FLORIDA

CAREUNIT OF CINCINNATI

CAREUNIT OF TAMPA

BEHAVIORAL MEDICAL CARE

NEUROAFFILIATES
(N.P.H.S., INC. IS JOINT VENTURER)

CAREUNIT OF CORAL SPRINGS

GOLDEN VALLEY HEALTH CENTER

PEAT MARWICK

Peat, Marwick, Mitchell & Co.
Certified Public Accountants
Orange County Office
Center Tower
650 T wr Center Drive
Costa Mesa, California 92626
714-350-4300

To the Stockholders and Board of Directors
Comprehensive Care Corporation

We consent to incorporation by reference in the Registration Statements No. 2-62410 and 2-75129 on Form S-8 of Comprehensive Care Corporation, of our report dated July 18, 1985, relating to the balance sheet of Comprehensive Care Corporation as of May 31, 1985 and the related statements of earnings, stockholders' equity, and changes in financial position for the year ended May 31, 1985 which report appears in the May 31, 1985 annual report on Form 10-K of Comprehensive Care Corporation.

Peat, Marwick, Mitchell & Co.

Newport Beach, California
August 14, 1985

EXHIBIT 24.1

CONSENT OF CERTIFIED PUBLIC ACCOUNTANTS

We hereby consent to the incorporation by reference in the Prospectuses constituting part of the Registration Statements on Form S-8 (Nos. 2-75129 and 2-62410) of Comprehensive Care Corporation of our report dated July 20, 1984 appearing in the Comprehensive Care Corporation Annual Report on Form 10-K for the year ended May 31, 1985.

Lesley, Thomas, Schwarz & Postma

LESLEY, THOMAS, SCHWARZ & POSTMA

Newport Beach, California
August 14, 1985

EXHIBIT 24.2

END

00436