LIFELINE SYSTEMS INC
Form 10-Q
May 11, 2001

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the quarter ended March 31, 2001 Commission File Number 0-13617

LIFELINE SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

MASSACHUSETTS	04-2537528
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

111 Lawrence Street Framingham, Massachusetts	01702-8156
(Address of principal executive offices)	(Zip Code)

(508) 988-1000
(Registrant's telephone number, including area code)

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

Securities registered pursuant to Section 12(g) of the Act:

Common stock $0.02 par value

(Title of Class)

Indicate by check mark whether the registrant (i) 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 (ii) has been subject to such filing requirements for the past 90 days. Yes X No_________

Number of shares outstanding of the issuer's class of common stock as of April 30, 2001: 6,101,233

LIFELINE SYSTEMS, INC.
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LIFELINE SYSTEMS, INC.
CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)

	March 200 --- (Unaud
ASSETS	
Current assets:	
Cash and cash equivalents	$ 1,
Accounts receivable, net	9,
Inventories	1,
Net investment in sales-type leases	2,

Prepaid expenses and other current assets	
Prepaid income taxes	
Deferred income taxes	1,
Total current assets	19,
Property and equipment, net	27,
Goodwill and other intangible assets, net	10,
Net investment in sales-type leases	4,
Other assets	
Total assets	$ 62,
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 1,
Accrued expenses	2,
Accrued payroll and payroll taxes	1,
Deferred revenues	
Current portion of capital lease obligation	
Current portion of long term debt	
Product warranty and other current liabilities	
Accrued restructuring and other non-recurring charges	1,
Total current liabilities	9,
Deferred income taxes	4,
Deferred compensation and other non-current liabilities	
Long term portion of capital lease obligation	1,
Long term debt, net of current portion	1,
Accrued restructuring and other non-recurring charges, long term	1,
Total liabilities	18,
Commitments and contingencies	
Stockholders' equity:	
Common stock, $.02 par value, 20,000,000 shares authorized, 6,673,187 shares issued at March 31, 2001 and 6,641,554 shares issued at December 31, 2000	
Additional paid-in capital	19,
Retained earnings	30,
Less: Treasury stock at cost, 621,089 shares at March 31, 2001 and December 31, 2000	(4,
Notes receivable - officer	(
Accumulated other comprehensive loss/cumulative translation adjustment	(
Total stockholders' equity	44,
Total liabilities and stockholders' equity	$ 62,

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

LIFELINE SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF INCOME
AND COMPREHENSIVE INCOME
(In thousands except for per share data)

(Unaudited)

	Three months en March 31,	
	2001	2
Revenues		
Services	$ 15,806	$
Net product sales	5,385	
Finance and rental income	373	
Total revenues	21,564	
Costs and expenses		
Cost of services	9,510	
Cost of sales	1,858	
Selling, general, and administrative	7,851	
Research and development	391	
Total costs and expenses	19,610	
Income from operations	1,954	
Other income (expense)		
Interest income	57	
Interest expense	(71)	
Other income (expense)	(44)	
Total other income (expense), net	(58)	
Income before income taxes	1,896	
Provision for income taxes	778	
Net income	1,118	
Other comprehensive income, net of tax		
Foreign currency translation adjustments	(102)	
Comprehensive Income	$ 1,016	$
Net income per weighted average share:		
Basic	$ 0.18	$
Diluted	$ 0.18	$

Weighted average shares:		
Basic	6,047	
	==========	====
Diluted	6,307	
	==========	====

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

LIFELINE SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)
(Unaudited)

	Thr
	2001
Cash flows from operating activities:	
Net income	$ 1,11
Adjustments to reconcile net income to net cash provided by operating activities:	
Write off of fixed assets	
Depreciation and amortization	2,16
Deferred income taxes	
Deferred compensation	(3
Changes in operating assets and liabilities:	
Accounts receivable	(33
Inventories	(13
Net investment in sales-type leases	25
Prepaid expenses, other current assets and other assets	(27
Accrued payroll and payroll taxes	(1,85
Accounts payable, accrued expenses and other liabilities	(30
Income taxes payable	(21
Accrued restructuring charge	(26
Net cash provided by operating activities	11
Cash flows from investing activities:	
Additions to property and equipment	(2,27
Business purchases and other	(52
Net cash used in investing activities	(2,79
Cash flows from financing activities:	
Principal payments under long term obligations	(25
Proceeds from issuance of long term debt	

Net proceeds (payments) under short-term borrowings	4
Proceeds from issuance of common stock	24
Net cash provided by financing activities	3
Effect of foreign exchange on cash	(5
Net increase (decrease) in cash and cash equivalents	(2,69
Cash and cash equivalents at beginning of period	4,41
Cash and cash equivalents at end of period	$ 1,71
Non-cash activity:	
Capital leases	$ 19
Deferred compensation	7

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

LIFELINE SYSTEMS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. The information furnished has been prepared from the accounts without audit. In the opinion of the Company, the accompanying consolidated financial statements contain all adjustments necessary, consisting only of those of a normal recurring nature, to present fairly its consolidated financial position as of March 31, 2001 and the consolidated statements of income and cash flows for the three months ended March 31, 2001 and 2000.

   While the Company believes that the disclosures presented are adequate to make the information not misleading, these statements should be read in conjunction with the consolidated financial statements and the related notes included in the Company's Annual Report on Form 10-K, as filed with the Securities and Exchange Commission on March 30, 2001, for the year ended December 31, 2000.

   Certain amounts in the prior year have been reclassified from cost of sales to revenue to conform to the current year presentation.

   The results of operations for the three-month period ended March 31, 2001 are not necessarily indicative of the results expected for the full year.

2. Details of certain balance sheet captions are as follows (in thousands):

	March 31, 2001	December 31, 2000
Inventories:		
Purchased parts and assemblies	$ 87	$ -
Work-in-process	-	-
Finished goods	1,688	1,641
	$ 1,775	$ 1,641

Property and equipment:		
Equipment	$ 22,952	$ 22,608
Furniture and fixtures	613	613
Equipment leased to others	12,618	11,707
Equipment under capital leases	3,727	3,535
Leasehold improvements	5,186	4,984
Capital in progress	1,896	1,230
	46,992	44,677
Less: accumulated depreciation and amortization	(19,661)	(18,271)
Total property and equipment, net	$ 27,331	$ 26,406

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

3. The calculation of per share earnings is as follows:

(In thousands except per share figures)

	Three months ended March 31,	
	2001	2000
Basic:		
Net income	$ 1,118	$ 923
Weighted average common shares outstanding	6,047	5,952
Net income per share, basic	$ 0.18	$ 0.16
Diluted:		
Net income for calculating diluted earnings per share	$ 1,118	$ 923
Weighted average common shares outstanding	6,047	5,952
Common stock equivalents	260	208
Total weighted average shares	6,307	6,160
Net income per share, diluted	$ 0.18	$ 0.15

For the three months ended March 31, 2001 and 2000, options to purchase 345,087 and 558,464 shares, respectively at an average exercise price of $19.81 and $17.64, respectively have not been included in the computation of diluted net income per share as their effect would have been anti-dilutive.

4. SEGMENT INFORMATION

The Company is active in one business segment: designing, marketing, monitoring and supporting its personal response units. The Company maintains sales, marketing and monitoring operations in both the United States and Canada.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. SEGMENT INFORMATION (continued)

Geographic Segment Data

Net sales from external customers are based on the location of the customer. Geographic information related to the results of operations for the periods ended March 31, 2001 and 2000 and the financial position as of March 31, 2001 and December 31, 2000 is presented as follows:

	March 31, 2001	March 31, 2000
Net Sales:		
United States	$ 19,816	$ 17,301
Canada	1,748	1,486
	$ 21,564	$ 18,787
Net Income:		
United States	$ 982	$ 797
Canada	136	126
	$ 1,118	$ 923

	March 31, 2001	December 31, 2000
Total Assets:		
United States	$ 56,686	$ 58,725
Canada	6,024	5,803
	$ 62,710	$ 64,528

5. RESTRUCTURING AND NON RECURRING CHARGES

In September 2000, the Company recorded a pre-tax non-recurring charge of approximately $2.7 million for costs it expects to incur to address erroneous low-battery signals in some of its personal help buttons. Included in the non-recurring charge are anticipated material and mailing costs for exchanging buttons, providing hospital programs with higher inventory levels for the planned swap, and the cost of installer visits to subscriber homes to replace the buttons.

At March 31, 2001, accrued restructuring and other non-recurring charges of approximately $2.3 million included nearly $73,000 of total remaining severance costs, previously disclosed, and $2.2 million of costs associated with the anticipated cost of addressing erroneous low-battery signals in personal help buttons.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

5. RESTRUCTURING AND NON RECURRING CHARGES (continued)

The following is a roll-forward of accrued restructuring and non-recurring charges for the three months ended March 31, 2001:

	December 31, 2000	Amounts Utilized	March 31, 2001
Reduction of workforce and other cash flows	$85	($12)	$73
Erroneous low battery signals	2,493	(250)	2,243
Total	$2,578	($262)	$2,316

6. LONG TERM DEBT

In June 1999, the Company entered into an amended $10.0 million line of credit which was originally obtained in April 1998. The agreement contains several covenants, including the Company maintaining certain levels of financial performance and capital structure. These financial covenants include a requirement for a current ratio of at least 1.5 to 1.0 and a leverage ratio of no more than 1.0 to 1.0. In addition, there are certain negative covenants that include limitations on the Company's capital and other expenditures, restrictions on the Company's capacity to obtain additional debt financing, restrictions on the disposition of the Company's assets, and restrictions on its investment portfolio. The line of credit matures on June 30, 2002, and as of March 31, 2001 the Company had $1.5 million outstanding under this line.

7. GOODWILL AND INTANGIBLES

During the first three months of 2001, the Company paid approximately $0.5 million to local community hospitals for conversion to services provided by the Company. The intangible assets related to these agreements consist of the cost of purchasing the rights to service and/or manage the personal response systems program located in various stand-alone facilities. These agreements allow the Company to monitor and provide other related services to existing and future subscribers over the term of the agreements. The Company amortizes the acquisitions costs over the life of the agreements, which is typically five years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

8. SUBSEQUENT EVENT

In April 2001, the Company acquired certain assets formerly owned by SOS Industries, Inc. a personal response service provider based in New Smyrna Beach, Florida with more than 10,000 subscribers located in 37 states. The purchase price was $3.8 million plus $250 for every subscriber in excess of 10,000 who signs an agreement to be monitored by the Company. Approximately $2.5 million was paid at the closing with the remainder to be paid within 90 days after the closing. The acquisition will be accounted for as a purchase transaction, and any resulting goodwill will be amortized over an estimated life of 10 years.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

This and other reports, proxy statements, and other communications to stockholders, as well as oral statements by the Company's officers or its agents, may contain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, with respect to, among other things, the Company's future revenues, operating income, or earnings per share. Without limiting the foregoing, the words "believes," "anticipates," "plans," "expects," and similar expressions are intended to identify forward-looking statements. There are a number of factors of which the Company is aware that may cause the Company's actual results to vary materially from those forecast or projected in any such forward-looking statement. These factors include, without limitation, those set forth below under the caption "Certain Factors That May Affect Future Results." The Company's failure to successfully address any of these factors could have a material adverse effect on the Company's future results of operations.

RESULTS OF OPERATIONS

Total revenues for the quarter ended March 31, 2001 increased nearly 15% to $21.6 million as compared to total revenues of $18.8 million for the quarter ended March 31, 2000.

Service revenues, at $15.8 million for the first quarter of 2001, represented approximately 73% of the Company's first quarter total revenues. This increase, up from $13.1 million or 70% of total revenues for the first quarter of 2000, is a result of the Company's continued service offering strategy and reflects a 12% increase in the Company's monitored subscriber base to approximately 319,000 subscribers as of March 31, 2001 from the 285,000 subscribers monitored at the end of the first quarter of 2000 as well as a price increase for its monitoring services which resulted in a higher average revenue per subscriber in the first quarter of 2001 as compared to the same period in 2000. The Company's ability to sustain the current level of service revenue growth depends on its ability to continue to make improvements in service delivery, expand the market for its personal response services, convert community hospital programs to services provided by the Company and increase its focus on referral development and innovative partner relationships in new channels of distribution. The Company believes that the high quality of its services and its commitment to providing caring and rapid response to the at-risk elderly and the physically challenged will be factors in meeting this challenge.

Net product revenues for the first quarter of 2001 increased slightly to $5.4 million from $5.3 million for the same period in 2000. The Company sold more of its units during the first quarter of 2001 versus the first quarter of 2000. However, large volume discounts during the quarter and a slight shift in the mix of product sold to lower priced products substantially offset any potential favorable increase in product revenue. The Company still expects declining product sales in future periods as it continues packaging products and services into a single service offering.

Finance and rental income, representing income earned from the Company's portfolio of sales-type leases, increased 3% to $373,000 for the three months ended March 31, 2001 from $361,000 recorded for the same period in the previous year. With the Company's focus on its service business segment it expects finance income to decline in future periods because leasing is directly related to its product business.

Total recurring revenues, consisting of service revenues and finance and rental income, rose to $16.2 million for the three months ended March 31, 2001 and represented 75% of total revenue as compared to $13.5 million and 72% of total revenue for the three months ended March 31, 2000. This 20% increase in recurring revenue and the increase as a percentage of total revenue reflect the Company's continued focus on its service business segment. The Company expects its recurring revenues to continue to increase in future periods.

Cost of services increased to $9.5 million from $8.8 million from the comparable prior period as a result of a variety of factors. The Company incurred higher amortization of goodwill along with associated operational costs in the first quarter of 2001 as a result of the purchase of Argus Emergency Medical Division in the third quarter of 2000. The Company also had higher amortization of continued intangible acquisition costs for agreements entered into with community hospitals for conversion to services provided by the Company. Information technology consultants and information technology professionals hired for the CareSystem platform also impacted cost of services for the first quarter of 2001 as compared to the same period last year. However, cost of services, as a percentage of service revenues, was 60% for the first quarter of 2001, a significant improvement from the 67% in the first quarter of 2000 and is aligned with the Company's goal of making its service offerings more profitable. The Company expects gradual improvement in its service margins in 2001.

Cost of sales was 35% of net product sales for the three months ended March 31, 2001 as compared to 32% for the three months ended March 31, 2000. Cost of sales was higher as a percentage of net product sales than the comparable prior period due to large product volume discounts which resulted in a lower average selling price and therefore lower margins. Also, with the significant improvements in the Company's service delivery, its customers are having renewed interest in marketing and growing their Lifeline service. As a result, the Company also experienced an increase in sales of its lower margin marketing accessories as compared to the same period in 2000. The Company expects to maintain cost of sales at a relatively consistent percentage of net product sales for the remainder of 2001.

Selling, general and administrative ("SG&A") expenses as a percentage of total revenues was 36% for the first quarter of 2001 as compared to 34% for the first quarter of 2000. Actual first quarter SG&A expenditures increased $1.4 million to $7.9 million for the first quarter of 2001 from $6.5 million for the same period in 2000. The Company's increased expenditures are primarily attributable to sales and marketing initiatives in the first quarter of 2001 that the Company did not incur during the first quarter of 2000. Increased information technology personnel and consultants in the first quarter of 2001 as compared to the same period in 2000 also contributed to the increased SG&A expenses. The Company expects an increase in SG&A expenses during 2001 as it continues with its sales, marketing and business initiatives, but believes that these expenses will be lower as a percentage of total revenues than in 2000.

Research and development expenses were nearly 2% of total revenues for the quarters ended March 31, 2001 and 2000. Research and development efforts are focused on ongoing product improvements and developments. The Company expects to maintain or slightly increase these expenses as percentage of total revenues for the remainder of 2001.

The Company's effective tax rate was 41.0% for the three months ended March 31, 2001 and 2000.

LIQUIDITY AND CAPITAL RESOURCES

During the three months ended March 31, 2001, the Company's portfolio of cash and cash equivalents decreased $2.7 million to $1.7 million at March 31, 2001 from $4.4 million at December 31, 2000. The decrease was mainly attributable to payments of approximately $2.3 million in employee bonuses and purchases of property and equipment amounting to $2.3 million. The Company also paid approximately $0.5 million to local community hospitals for conversions to services provided by the Company. This represented the cost of purchasing the rights to service and/or manage the personal response systems program previously operated by the local community hospitals. Profitable operations of $3.2 million helped to offset these expenditures.

The Company is party to Master Lease Agreements for up to $5.6 million for furniture, computers, security systems and other related equipment purchases. For financial reporting purposes, these leases are recorded as capital leases and accordingly the associated assets are being depreciated over their estimated useful life. As of March 31, 2001 the Company had made purchases of approximately $3.1 million under these agreements.

In June 1999, the Company entered into an amended $10.0 million line of credit which was originally obtained in April 1998. The agreement has two components, the first of which is a working capital line of credit, the other, the ability to convert up to five million dollars into a five-year fixed loan. The working capital line of credit's interest rate is based on the London Interbank Offered Rate (LIBOR), while the fixed loan is at the bank's prime interest rate. The agreement contains several covenants, including the Company maintaining certain levels of financial performance and capital structure. These financial covenants include a requirement for a current ratio of at least 1.5 to 1.0 and a leverage ratio of no more than 1.0 to 1.0. In addition, there are certain negative covenants that include limitations on the Company's capital and other expenditures, restrictions on the Company's capacity to obtain additional debt financing, restrictions on the disposition of the Company's assets, and restrictions on its investment portfolio. This line of credit matures on June 30, 2002, and as of March 31, 2001 the Company had $1.5 million outstanding under this line.

The Company expects that funding requirements for operations and in support of future growth are expected to be met primarily from operating cash flow, existing cash and marketable securities and its $10.0 million line of credit. The Company expects these sources will be sufficient to finance the cash needs of the Company through the next twelve months. This includes the continued investment in its response center platform, the requirements of its internally funded lease financing program, the second quarter acquisition of certain assets formerly owned by SOS Industries, Inc., any future potential acquisitions and other investments in support of its current business.

CERTAIN FACTORS THAT MAY AFFECT FUTURE RESULTS

The following important factors, among others, could cause actual results to differ materially from those indicated by forward-looking statements made in this Quarterly Report on Form 10-Q and presented elsewhere by management from time to time.

The Company completed the transition of its United States subscribers to its new CareSystem call center platform during 1999 and experienced certain software design deficiencies in connection with

the transition, which it has worked to resolve. The Company may continue to experience problems associated with this new information technology. There can be no assurance that the Company will realize the intended benefits from the new system.

The Company is currently experiencing a battery-related issue with some of its personal help buttons worn by subscribers. Certain personal help buttons are erroneously transmitting low battery signals. While the buttons that exhibit this erroneous low battery condition still contain sufficient power to activate the communicator when the button is pressed and do not place the Company's subscribers at risk, the Company believes it is prudent to replace those buttons exhibiting this condition. The Company recorded a non-recurring charge of approximately $2.7 million in the third quarter of 2000 for costs it expects to incur to address this issue, including anticipated material and mailing costs for exchanging buttons, providing hospital programs with higher inventory levels for the planned swap, and support for the cost of installer visits to subscriber homes to replace the button. The Company cannot be certain that the charge it recorded to address this issue will be sufficient to cover all of its associated expenses, or that its reputation, business, financial condition or results of operations will not be otherwise affected. In addition, the Company has changed its battery vendor. The Company cannot be certain that it will not experience disruption related to such change.

During the third quarter of 1999, the Company completed the outsourcing of the manufacturing of its personal response equipment to the Ademco Group, a division of Honeywell International, Inc. This decision represented a change in the Company's manufacturing strategy, as it no longer supports a manufacturing site at its corporate location. There can be no assurance that the Company will realize the intended cost savings it anticipates, or that it will not experience delays in obtaining products from Ademco as a result of process difficulties, component shortages or for other reasons. Any such delay could have a material adverse effect on the Company's business, financial condition, or results of operations.

The Company's results are partially dependent on its ability to develop services and products that keep pace with continuing technological changes, evolving industry standards, changing subscriber preferences and new service and product introductions by the Company's competitors. Lifeline's future success will depend on its ability to enhance its existing services and products (including accessories), to introduce new service and product offerings to meet and adapt to changing customer requirements and emerging technologies on a timely basis and to offer such products and services at competitive prices. There can be no assurance that Lifeline will be successful in identifying, developing, manufacturing or marketing new services and products or enhancing its existing services and products on a timely basis or that Lifeline will be able to offer such services and products at competitive prices. Also, there can be no assurance that services, products or technologies developed by others will not render Lifeline's services or products noncompetitive or obsolete.

The Company's growth is dependent on its ability to increase the number of subscribers served by its monitoring centers. The Company's ability to continue to increase service revenue is a key factor in its long-term growth, and there can be no assurance that the Company will be able to do so. The Company's failure to increase service revenue could have a material adverse effect on the Company's business, financial condition, or results of operations.

The Company's monitoring operations are concentrated principally in its corporate headquarters facility. Although the Company believes that it has constructed safeguards to protect against system failures, the disruption of service at its monitoring facility, whether due to telephone or electrical

failures, earthquakes, fire, weather or other similar events or for any other reason, could have a material adverse effect on the Company's business, financial condition, or results of operations.

The Company believes that its future success will depend in large part upon its ability to attract and retain key personnel, especially in its information technology department. Although the Company believes it is making progress in retaining and recruiting well-trained, highly capable people despite a very competitive employment market, there can be no assurance that the Company will continue to be successful in attracting and retaining such personnel.

While the Company has maintained its product revenue during the first quarter of 2001 as compared to the first quarter of 2000, product revenue is anticipated to decline as a result of the Company's strategy of combining service and hardware offerings to support the transition to a service oriented business. As the Company continues growing its service business segment to increase its recurring revenue, there can be no assurance that service revenue will increase at a rate sufficient to offset the expected decrease in higher margin product revenue both on a quarterly and annual basis. Moreover, the Company's product sales are ordinarily made to healthcare providers that establish their own Lifeline programs. These healthcare providers typically rent, rather than sell, the Lifeline products to subscribers and accordingly following such time as a product is no longer used by a subscriber, it is returned to the healthcare provider and becomes available for rent to another subscriber. As a result of this use and reuse of the Company's products, sales of such products are dependent on growth in the number of subscribers and on the ability of the Company to encourage its healthcare provider customers to replace their existing inventory by continuing to enhance its products with new features.

The Company may expand its operations through the acquisition of additional businesses, such as its recent acquisition of certain assets formerly owned by SOS Industries, Inc. in April 2001. There can be no assurance that the Company will be able to identify, acquire or profitably manage additional businesses or successfully integrate any acquired businesses into the Company without substantial expenses, delays or other operational or financial problems. In addition, acquisitions may involve a number of special risks, including diversion of management's attention, failure to retain key acquired personnel, unanticipated events, contingent liabilities and amortization of acquired intangible assets. There can be no assurance that the acquired businesses, if any, will achieve anticipated revenues or earnings.

ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company has considered the provisions of Financial Reporting Release No. 48 "Disclosure of Accounting Policies for Derivative Financial Instruments and Derivative Commodity Instruments, and Disclosure of Quantitative and Qualitative Information about Market Risk Inherent in Derivative Financial Instruments, Other Financial Instruments and Derivative Commodity Instruments." The Company had no holdings of derivative financial or commodity-based instruments or other market risk sensitive instruments entered into for trading purposes at March 31, 2001. As described in the following paragraphs, the Company believes that it currently has no material exposure to interest rate and foreign currency exchange rate risks in its instruments entered into for other than trading purposes.

Interest rates

The Company's balance sheet includes a revolving credit facility and a term loan that are subject to interest rate risk. Both loans are priced at floating rates of interest, with a base of LIBOR or prime rate at the Company's option. As a result of these factors, at any given time, a change in interest rates could result in either an increase or decrease in the Company's interest expense. The Company performed a sensitivity analysis as of March 31, 2001 to assess the potential effect of a 100 basis point increase or decrease in interest rates and concluded that short-term changes in interest rates should not materially affect the Company's consolidated financial position, results of operations or cash flows.

Foreign currency exchange rates

The Company's earnings are affected by fluctuations in the value of the U.S. Dollar as compared to the Canadian Dollar, as a result of the sale of its products and services in Canada and translation adjustments associated with the conversion of the Company's Canadian subsidiary into the reporting currency (U.S. Dollar). As such, the Company's exposure to changes in Canadian exchange rates could impact the Company's consolidated financial position, results of operations or cash flows. The Company performed a sensitivity analysis as of March 31, 2001 to assess the potential effect of a 10% increase or decrease in Canadian foreign exchange rates and concluded that short-term changes in Canadian exchange rates should not materially affect the Company's consolidated financial position, results of operations or cash flows. The Company's sensitivity analysis of the effects of changes in foreign currency exchange rates did not factor in a potential change in sales levels or local prices for its services/products.

PART II. OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Reports on Form 8-K - No reports on Form 8-K were filed for the three months ended March 31, 2001.

LIFELINE SYSTEMS, INC.

SIGNATURES

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

May 11, 2001	LIFELINE SYSTEMS, INC.
Date	Registrant
	/s/ Ronald Feinstein
	Ronald Feinstein Chief Executive Officer

/s/ Dennis M. Hurley

Dennis M. Hurley
Senior Vice President of Finance and
Administration, Principal Financial
and Accounting Officer