

KINDRED HEALTHCARE INC
Form 8-K
March 09, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): March 8, 2004

KINDRED HEALTHCARE, INC.

(Exact name of registrant as specified in its charter)

| | | |
|--|---|---|
| Delaware (State or other jurisdiction of incorporation or organization) | 001-14057 (Commission File Number) | 61-1323993 (IRS Employer Identification No.) |
|--|---|---|

680 South Fourth Street

Louisville, Kentucky

(Address of principal executive offices)

40202-2412

(Zip Code)

Registrant's telephone number, including area code: (502) 596-7300

Not Applicable

(Former name or former address, if changed since last report)

Item 12. Results of Operations and Financial Condition.

On March 8, 2004, the Company issued a press release announcing its financial results for the fourth quarter and year ended December 31, 2003. The press release, dated March 8, 2004, is attached as Annex A to this Form 8-K. On March 8, 2004, the Company also included the press release on its website at www.kindredhealthcare.com.

Annex A is incorporated herein by reference and has been furnished, not filed.

SIGNATURES

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

Date: March 8, 2004

By: /s/ Richard A. Lechleiter

Richard A. Lechleiter
Senior Vice President and Chief Financial Officer

[Kindred Logo appears here]

Contact: Richard A. Lechleiter
Senior Vice President and
Chief Financial Officer
(502) 596-7734

KINDRED HEALTHCARE ANNOUNCES FOURTH QUARTER RESULTS

Fourth Quarter Net Income from Continuing Operations \$15.5 million or \$0.76 per Diluted Share

Fiscal Year Net Income from Continuing Operations \$49.5 million or \$2.82 per Diluted Share

Peoplefirst Rehabilitation to Operate as New Division in 2004

LOUISVILLE, Ky. (March 8, 2004) Kindred Healthcare, Inc. (the Company) (NASDAQ:KIND) today announced its operating results for the fourth quarter and year ended December 31, 2003. All financial and statistical information in this press release reflects the continuing operations of the Company's businesses for all periods presented unless otherwise indicated.

Fourth Quarter Results

Continuing Operations

Consolidated revenues for the fourth quarter ended December 31, 2003 increased 5% to \$831 million from \$792 million for the same period last year. Net income from continuing operations totaled \$15.5 million or \$0.76 per diluted share compared to \$20.9 million or \$1.21 per diluted share in the fourth quarter last year. Fourth quarter 2003 pretax operating results included a favorable adjustment of approximately \$4 million for professional liability costs, a charge of approximately \$3 million related to special incentive compensation awards and a credit of approximately \$1 million to adjust accrued reorganization costs. Fourth quarter 2002 pretax operating results included additional professional liability costs of \$8 million, a reduction in incentive compensation costs of approximately \$9 million, a credit of approximately \$4 million related to adjustments of certain information systems accruals and a \$2 million gain from the sale of property.

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Fourth quarter 2003 operating results also were impacted by certain changes in nursing center Medicare reimbursement. Beginning October 1, 2003, nursing center operating results were favorably impacted by a 3.26% correction to the market basket adjustment to Medicare payment rates. In addition, the annual 3% market basket increase also became effective on October 1, 2003. These adjustments together increased nursing center Medicare revenues by approximately \$19 per patient day or \$8 million for the fourth quarter of 2003.

Discontinued Operations

As previously disclosed, the Company acquired for resale ten unprofitable facilities from Ventas, Inc. (Ventas) (NYSE:VTR) in December 2003. The Company intends to dispose of these properties as soon as practicable. In addition, during the fourth quarter of 2003, the Company allowed two nursing center operating leases to expire, disposed of an ancillary services business in its hospital division, cancelled two hospital pulmonary management agreements and terminated two pharmacy infusion therapy partnerships. For accounting purposes, the operating results of these businesses and losses associated with these transactions have been classified as discontinued operations in the consolidated statement of operations for all historical periods.

Net operating losses for the previously discussed fourth quarter divestitures, along with the Florida and Texas nursing centers that were divested in the second quarter of 2003 (collectively, the Divested Operations), aggregated \$3.4 million or \$0.17 per diluted share in the fourth quarter of 2003 compared to \$17.8 million or \$1.03 per diluted share in the fourth quarter of 2002.

The fourth quarter 2003 net operating loss aggregating \$3.4 million was comprised of a \$2.2 million operating loss related primarily to external professional liability insurance costs for the Florida and Texas nursing centers sold in the second quarter of 2003, a \$2.2 million operating loss related to the ten unprofitable facilities purchased from Ventas in December 2003, and income of \$1.0 million from the other operations divested in the fourth quarter of 2003. The Company did not record any adjustments in the fourth quarter of 2003 to the professional liability reserves for the Florida and Texas nursing centers established at June 30, 2003.

In the fourth quarter of 2003, the Company reduced the carrying values of the Divested Operations to their estimated fair value less costs of disposal. The net loss on the divestitures in the fourth quarter of 2003, substantially all of which related to the ten unprofitable facilities purchased from Ventas in December 2003, aggregated \$42.6 million or \$2.09 per diluted share.

Based upon the status of the Company's negotiations to dispose of the ten unprofitable facilities purchased from Ventas in December 2003, the Company expects sales proceeds from these divestitures to approximate \$27 million. The Company expects to complete these divestitures by June 30, 2004.

Assets not sold at December 31, 2003 have been measured at the lower of carrying value or estimated fair value less costs of disposal and have been classified as held for sale in the Company's consolidated balance sheet.

Fiscal Year Results

Continuing Operations

Consolidated revenues for the year ended December 31, 2003 increased 5% to \$3.3 billion from \$3.1 billion for fiscal 2002. Net income from continuing operations totaled \$49.5 million or \$2.82 per diluted share compared to \$85.5 million or \$4.75 per diluted share in 2002. Despite significant increases in both hospital and pharmacy operating income, operating results in 2003 were adversely impacted by the expiration of certain nursing center Medicare reimbursements on October 1, 2002 that reduced nursing center pretax income by approximately \$42 million for the first nine months of 2003. In addition, increases in professional liability costs in 2003, most of which were incurred by the Company's nursing center business, reduced pretax income by approximately \$27 million.

Operating results for fiscal 2003 included income of \$14 million related to the resolution of certain prior year hospital Medicare cost reports and other hospital reimbursement issues in the third quarter. Operating results for fiscal 2002 included a \$12 million favorable hospital accounts receivable settlement with a private insurance company in the third quarter.

In addition to the fourth quarter items discussed previously, operating results for fiscal 2002 included a \$0.5 million pretax lease termination charge for an unprofitable hospital and a \$5.5 million pretax credit to adjust accrued restructuring costs.

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Interest expense for both the third quarter of 2003 and 2002 included approximately \$2 million of gains realized in connection with the prepayment of long-term debt.

Discontinued Operations

Net operating losses of the Divested Operations aggregated \$45.4 million or \$2.59 per diluted share in 2003 compared to \$50.7 million or \$2.82 per diluted share in 2002. The net loss on the disposal of the Divested Operations aggregated \$79.4 million or \$4.53 per diluted share in 2003.

Other Information

Professional Liability Costs

As previously discussed, the Company recorded a \$4 million pretax reduction in professional liability costs in the fourth quarter of 2003 based on the results of the regular quarterly independent actuarial valuation. Approximately \$3 million of this favorable adjustment was reflected in the Company's nursing center business and the remainder was credited to the Company's hospital division. For the quarter ended December 31, 2003, the Company's professional liability costs aggregated \$17 million, of which approximately \$12 million was charged to the nursing center business. Third quarter 2003 professional liability costs aggregated \$21 million, of which approximately \$15 million was charged to the nursing center business.

For the year ended December 31, 2003, the Company's professional liability costs aggregated \$90 million, of which approximately \$67 million was charged to the nursing center business. While the Company expects that professional liability costs for 2004 may be higher than the costs recorded in 2003, management believes that the annual growth rates for professional liability costs appear to be moderating.

As a result of the regular quarterly independent actuarial valuation, the Company will fund approximately \$15 million into its wholly owned limited purpose insurance subsidiary in 2004. The required additional funding for fiscal 2002 totaling \$63 million was funded in March 2003.

New Operating Division Announced for 2004

The Company also announced that it has reorganized its rehabilitation services business effective January 1, 2004 by transferring its internal rehabilitation personnel from its nursing centers and consolidating them with its external rehabilitation business. This new operating division will operate under the name *Peoplefirst* Rehabilitation. For accounting purposes, the Company expects to present the operating results of *Peoplefirst* Rehabilitation as a separate operating division when it reports its first quarter 2004 operating results. The Company expects that the historical presentation of its nursing center and external rehabilitation services segment operating results will not be restated to conform with the new business alignment in 2004.

Paul J. Diaz, President and Chief Executive Officer of the Company, described the operational benefits of the new division. The primary mission of *Peoplefirst* Rehabilitation is to support our quality initiatives, clinical program development efforts and growing Medicare business in our nursing centers. This new division will also provide the necessary infrastructure to improve our recruitment and retention of qualified therapists and establish a platform from which we can continue to build our external contract business.

Management Commentary

Fiscal 2003 was a year of remarkable achievement for Kindred, Mr. Diaz remarked. The successful completion of the Florida and Texas nursing center divestitures in the second quarter provided clarity to our continuing operations, while the fourth quarter purchase of ten other unprofitable facilities for resale provides us with an additional opportunity to focus on our core nursing centers and expand our hospital, pharmacy and rehabilitation businesses. On the operational front, our hospitals reported an outstanding year, reflecting continued improvements in our clinical, customer service and other quality measures and the successful transition to the new Medicare prospective payment system in September. Likewise, our pharmacy business reported another solid year of growth, expanding our external customer base by almost 15% for the year. We also are excited about the prospects in our nursing center business, which reported a strong fourth quarter that included positive news related to professional liability costs and growing Medicare patient mix. Finally, we successfully contained our overhead costs in 2003.

Commenting on the Company's growth outlook, Mr. Diaz remarked, "Our strong fourth quarter results support our outlook for continuing operational improvement in 2004. While we focused heavily on some key strategic and operational initiatives in 2003 to reposition the Company going forward, we also continued to execute our development strategy. In our hospital business, we opened a new free-standing hospital in Nashville, Tennessee (60 beds), two new hospitals-in-hospitals in Albuquerque, New Mexico (31 beds) and Dallas, Texas (30 beds) and added capacity to our existing hospitals in St. Petersburg, Florida (22 beds) and Boston, Massachusetts (23 beds). In 2004, we have opened or have agreements to open four new hospitals-in-hospitals in Oceanside, California (38 beds), Dover, New Jersey (45 beds), Louisville, Kentucky (30 beds) and St. Louis, Missouri (38 beds), and two free-standing hospitals in Corpus Christi, Texas (74 beds) and Dayton, Ohio (68 beds). In KPS, our institutional pharmacy business, we continue to gain market share by expanding our existing customer base and now have approximately 54% of our pharmacy business with non-affiliated customers. We also plan to open four new pharmacies in 2004 to expand into new markets and provide further growth opportunities in this business. Our new rehabilitation services division, *Peoplefirst*, should provide more opportunities to improve patient care in our nursing centers and the necessary infrastructure to expand our external customer base without deploying significant amounts of capital.

Board of Directors Change

The Company announced that Mr. James Bolin has resigned from the Board of Directors effective March 5, 2004. Mr. Edward L. Kuntz, Executive Chairman of the Board, commented, "We are thankful to Jim for his service on the Board. He played an important role in advising the Company since its reorganization.

Forward Looking Statements

This press release includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements regarding the Company's expected future financial position, results of operations, cash flows, financing plans, business strategy, budgets, capital expenditures, competitive positions, growth opportunities, plans and objectives of management and statements containing the words such as anticipate, approximate, believe, plan, estimate, expect, project, could, should, will, intend, may and other similar expressions, are forward-looking statements.

Such forward-looking statements are inherently uncertain, and stockholders and other potential investors must recognize that actual results may differ materially from the Company's expectations as a result of a variety of factors, including, without limitation, those discussed below. Such forward-looking statements are based on management's current expectations and include known and unknown risks, uncertainties and other factors, many of which the Company is unable to predict or control, that may

cause the Company's actual results or performance to differ materially from any future results or performance expressed or implied by such forward-looking statements. These statements involve risks, uncertainties and other factors discussed below and detailed from time to time in the Company's filings with the Securities and Exchange Commission.

Factors that may affect the Company's plans or results include, without limitation, (a) the Company's ability to operate pursuant to the terms of its debt obligations and its master lease agreements with Ventas; (b) the Company's ability to meet its rental and debt service obligations; (c) adverse developments with respect to the Company's results of operations or liquidity; (d) the Company's ability to attract and retain key executives and other healthcare personnel; (e) increased operating costs due to shortages in qualified nurses and other healthcare personnel; (f) the effects of healthcare reform and government regulations, interpretation of regulations and changes in the nature and enforcement of regulations governing the healthcare industry; (g) changes in the reimbursement rates or methods of payment from third party payors, including the Medicare and Medicaid programs, and changes arising from the Medicare prospective payment system for long-term acute care hospitals and the recently enacted Medicare Prescription Drug, Improvement, and Modernization Act of 2003; (h) national and regional economic conditions, including their effect on the availability and cost of labor, materials and other services; (i) the Company's ability to control costs, including labor and employee benefit costs; (j) the Company's ability to comply with the terms of its Corporate Integrity Agreement; (k) the Company's ability to integrate operations of acquired facilities; (l) the increase in the costs of defending and insuring against alleged professional liability claims and the Company's ability to predict the estimated costs related to such claims; (m) the Company's ability to successfully reduce (by divestiture of operations or otherwise) its exposure to professional liability claims; and (n) the Company's ability to successfully dispose of the ten unprofitable facilities acquired from Ventas. Many of these factors are beyond the Company's control. The Company cautions investors that any forward-looking statements made by the Company are not guarantees of future performance. The Company disclaims any obligation to update any such factors or to announce publicly the results of any revisions to any of the forward-looking statements to reflect future events or developments.

Kindred Healthcare, Inc. is a national healthcare services company operating hospitals, nursing centers, institutional pharmacies and a contract rehabilitation services business.

KINDRED HEALTHCARE, INC.

Financial Summary

(In thousands, except per share amounts)

| | Three months ended | | Year ended | |
|--|--------------------|------------|--------------|--------------|
| | December 31, | | December 31, | |
| | 2003 | 2002 | 2003 | 2002 |
| Revenues | \$ 830,978 | \$ 792,290 | \$ 3,284,019 | \$ 3,120,770 |
| Income from continuing operations | \$ 15,485 | \$ 20,921 | \$ 49,454 | \$ 85,521 |
| Discontinued operations, net of income taxes: | | | | |
| Loss from operations | (3,407) | (17,852) | (45,377) | (50,768) |
| Loss on divestiture of operations | (42,567) | | (79,413) | |
| Net income (loss) | \$ (30,489) | \$ 3,069 | \$ (75,336) | \$ 34,753 |
| Earnings (loss) per common share: | | | | |
| Basic: | | | | |
| Income from continuing operations | \$ 0.88 | \$ 1.21 | \$ 2.83 | \$ 4.93 |
| Discontinued operations: | | | | |
| Loss from operations | (0.19) | (1.03) | (2.60) | (2.93) |
| Loss on divestiture of operations | (2.43) | | (4.55) | |
| Net income (loss) | \$ (1.74) | \$ 0.18 | \$ (4.32) | \$ 2.00 |
| Diluted: | | | | |
| Income from continuing operations | \$ 0.76 | \$ 1.21 | \$ 2.82 | \$ 4.75 |
| Discontinued operations: | | | | |
| Loss from operations | (0.17) | (1.03) | (2.59) | (2.82) |
| Loss on divestiture of operations | (2.09) | | (4.53) | |
| Net income (loss) | \$ (1.50) | \$ 0.18 | \$ (4.30) | \$ 1.93 |
| Shares used in computing earnings (loss) per common share: | | | | |
| Basic | 17,531 | 17,377 | 17,440 | 17,361 |
| Diluted | 20,342 | 17,384 | 17,524 | 18,001 |

KINDRED HEALTHCARE, INC.

Consolidated Statement of Operations

(In thousands, except per share amounts)

| | Three months ended | | Year ended | |
|--|--------------------|-----------------|--------------------|------------------|
| | December 31, | | December 31, | |
| | 2003 | 2002 | 2003 | 2002 |
| Revenues | \$ 830,978 | \$ 792,290 | \$ 3,284,019 | \$ 3,120,770 |
| Salaries, wages and benefits | 473,263 | 450,139 | 1,865,447 | 1,770,654 |
| Supplies | 113,293 | 103,298 | 429,616 | 401,348 |
| Rent | 64,230 | 63,431 | 256,306 | 249,195 |
| Other operating expenses | 131,524 | 121,442 | 563,507 | 487,855 |
| Depreciation | 21,328 | 18,164 | 80,857 | 68,251 |
| Interest expense | 3,388 | 3,135 | 10,322 | 12,040 |
| Investment income | (1,491) | (2,029) | (6,135) | (9,638) |
| | <u>805,535</u> | <u>757,580</u> | <u>3,199,920</u> | <u>2,979,705</u> |
| Income from continuing operations before reorganization items and income taxes | 25,443 | 34,710 | 84,099 | 141,065 |
| Reorganization items | (1,010) | | (1,010) | (5,520) |
| Income from continuing operations before income taxes | 26,453 | 34,710 | 85,109 | 146,585 |
| Provision for income taxes | 10,968 | 13,789 | 35,655 | 61,064 |
| Income from continuing operations | 15,485 | 20,921 | 49,454 | 85,521 |
| Discontinued operations, net of income taxes: | | | | |
| Loss from operations | (3,407) | (17,852) | (45,377) | (50,768) |
| Loss on divestiture of operations | (42,567) | | (79,413) | |
| Net income (loss) | <u>\$ (30,489)</u> | <u>\$ 3,069</u> | <u>\$ (75,336)</u> | <u>\$ 34,753</u> |
| Earnings (loss) per common share: | | | | |
| Basic: | | | | |
| Income from continuing operations | \$ 0.88 | \$ 1.21 | \$ 2.83 | \$ 4.93 |
| Discontinued operations: | | | | |
| Loss from operations | (0.19) | (1.03) | (2.60) | (2.93) |
| Loss on divestiture of operations | (2.43) | | (4.55) | |
| Net income (loss) | <u>\$ (1.74)</u> | <u>\$ 0.18</u> | <u>\$ (4.32)</u> | <u>\$ 2.00</u> |
| Diluted: | | | | |
| Income from continuing operations | \$ 0.76 | \$ 1.21 | \$ 2.82 | \$ 4.75 |
| Discontinued operations: | | | | |
| Loss from operations | (0.17) | (1.03) | (2.59) | (2.82) |
| Loss on divestiture of operations | (2.09) | | (4.53) | |

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| | | | | |
|--|------------------|----------------|------------------|----------------|
| Net income (loss) | <u>\$ (1.50)</u> | <u>\$ 0.18</u> | <u>\$ (4.30)</u> | <u>\$ 1.93</u> |
| Shares used in computing earnings (loss) per common share: | | | | |
| Basic | 17,531 | 17,377 | 17,440 | 17,361 |
| Diluted | 20,342 | 17,384 | 17,524 | 18,001 |

KINDRED HEALTHCARE, INC.**Condensed Consolidated Balance Sheet**

(In thousands, except per share amounts)

| | December 31, 2003 | December 31, 2002 |
|---|----------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 66,524 | \$ 244,070 |
| Cash restricted | 7,339 | 7,908 |
| Insurance subsidiary investments | 146,325 | 130,415 |
| Accounts receivable less allowance for loss | 429,304 | 420,611 |
| Inventories | 29,984 | 30,460 |
| Deferred tax assets | 89,836 | 32,123 |
| Assets held for sale | 27,400 | |
| Other | 46,375 | 54,729 |
| | <u>843,087</u> | <u>920,316</u> |
| Property and equipment | 671,850 | 611,944 |
| Accumulated depreciation | (193,310) | (115,373) |
| | <u>478,540</u> | <u>496,571</u> |
| Goodwill | 31,417 | 88,259 |
| Insurance subsidiary investments | 74,618 | 18,171 |
| Deferred tax assets | 92,093 | 43,338 |
| Other | 65,659 | 77,523 |
| | <u>\$ 1,585,414</u> | <u>\$ 1,644,178</u> |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 119,087 | \$ 124,466 |
| Salaries, wages and other compensation | 214,113 | 220,124 |
| Due to third party payors | 31,406 | 25,177 |
| Professional liability risks | 83,725 | 45,346 |
| Other accrued liabilities | 88,333 | 104,674 |
| Income taxes | 36,684 | 62,111 |
| Long-term debt due within one year | 4,532 | 258 |
| | <u>577,880</u> | <u>582,156</u> |
| Long-term debt | 139,397 | 162,008 |
| Professional liability risks | 212,013 | 211,771 |
| Deferred credits and other liabilities | 58,559 | 56,615 |
| Commitments and contingencies | | |
| Stockholders equity: | | |
| Common stock, \$0.25 par value; authorized 175,000 shares; issued 18,170 shares December 31, 2003 and 17,649 shares December 31, 2002 | 4,543 | 4,412 |
| Capital in excess of par value | 589,936 | 547,609 |
| Deferred compensation | (8,040) | (6,967) |
| Accumulated other comprehensive income | 348 | 460 |

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| | | |
|-------------------|---------------------|--------------|
| Retained earnings | 10,778 | 86,114 |
| | 597,565 | 631,628 |
| | \$ 1,585,414 | \$ 1,644,178 |

KINDRED HEALTHCARE, INC.

Condensed Consolidated Statement of Cash Flows

(In thousands)

| | Year ended December 31, | |
|--|-------------------------|-----------|
| | 2003 | 2002 |
| Cash flows from operating activities: | | |
| Net income (loss) | \$ (75,336) | \$ 34,753 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | |
| Depreciation | 83,301 | 71,356 |
| Amortization of deferred compensation costs | 5,828 | 6,778 |
| Provision for doubtful accounts | 29,575 | 13,551 |
| Deferred income taxes | (8,500) | (17,608) |
| Loss on divestiture of discontinued operations | 79,413 | |
| Unusual transactions | | (1,795) |
| Reorganization items | (1,010) | (5,520) |
| Other | 1,278 | 1,224 |
| Change in operating assets and liabilities: | | |
| Accounts receivable | (52,977) | (3,063) |
| Inventories and other assets | 19,403 | (11,303) |
| Accounts payable | (3,624) | 11,887 |
| Income taxes | 11,585 | 45,519 |
| Due to third party payors | 6,229 | (12,108) |
| Other accrued liabilities | 25,508 | 119,995 |
| Net cash provided by operating activities before reorganization items | 120,673 | 253,666 |
| Payment of reorganization items | (1,378) | (4,987) |
| Net cash provided by operating activities | 119,295 | 248,679 |
| Cash flows from investing activities: | | |
| Purchase of property and equipment | (84,096) | (84,071) |
| Acquisition of healthcare facilities | (149,266) | (45,931) |
| Sale of assets | 66,741 | 752 |
| Surety bond deposits | 1,766 | 9,676 |
| Purchase of insurance subsidiary investments | (156,774) | (4,494) |
| Sale of insurance subsidiary investments | 61,940 | 3,703 |
| Net change in insurance subsidiary cash and cash equivalents | 22,477 | (31,718) |
| Net change in other investments | 1,059 | 6,166 |
| Other | (353) | 64 |
| Net cash used in investing activities | (236,506) | (145,853) |
| Cash flows from financing activities: | | |
| Repayment of long-term debt | (62,219) | (50,570) |
| Payment of deferred financing costs | (3,677) | (1,375) |
| Issuance of common stock | 7,881 | 159 |
| Repurchase of common stock | | (1,046) |
| Other | (2,320) | 3,277 |

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| | | |
|--|------------------|------------|
| Net cash used in financing activities | (60,335) | (49,555) |
| Change in cash and cash equivalents | (177,546) | 53,271 |
| Cash and cash equivalents at beginning of period | 244,070 | 190,799 |
| Cash and cash equivalents at end of period | \$ 66,524 | \$ 244,070 |

KINDRED HEALTHCARE, INC.

Business Segment Data

(In thousands)

| | 2002 Quarters | | | | | 2003 Quarters | | | | |
|--|---------------|------------|------------|------------|--------------|---------------|------------|------------|------------|--------------|
| | First | Second | Third | Fourth | Year | First | Second | Third | Fourth | Year |
| Revenues: | | | | | | | | | | |
| Hospital division | \$ 285,626 | \$ 313,856 | \$ 321,951 | \$ 319,904 | \$ 1,241,337 | \$ 331,862 | \$ 338,360 | \$ 341,368 | \$ 325,619 | \$ 1,337,209 |
| Health services division: | | | | | | | | | | |
| Nursing centers | 411,273 | 412,253 | 422,392 | 412,741 | 1,658,659 | 410,832 | 416,768 | 431,978 | 433,532 | 1,693,110 |
| Rehabilitation services | 7,830 | 8,566 | 8,697 | 9,203 | 34,296 | 8,502 | 8,795 | 12,065 | 14,121 | 43,483 |
| | 419,103 | 420,819 | 431,089 | 421,944 | 1,692,955 | 419,334 | 425,563 | 444,043 | 447,653 | 1,736,593 |
| Pharmacy division | 57,049 | 57,915 | 62,076 | 64,699 | 241,739 | 66,126 | 64,850 | 67,075 | 74,382 | 272,433 |
| | 761,778 | 792,590 | 815,116 | 806,547 | 3,176,031 | 817,322 | 828,773 | 852,486 | 847,654 | 3,346,235 |
| Elimination of pharmacy charges to Company nursing centers | (13,353) | (13,637) | (14,014) | (14,257) | (55,261) | (15,164) | (14,925) | (15,451) | (16,676) | (62,216) |
| | \$ 748,425 | \$ 778,953 | \$ 801,102 | \$ 792,290 | \$ 3,120,770 | \$ 802,158 | \$ 813,848 | \$ 837,035 | \$ 830,978 | \$ 3,284,019 |
| Income from continuing operations: | | | | | | | | | | |
| Operating income (loss): | | | | | | | | | | |
| Hospital division | \$ 57,701 | \$ 62,499 | \$ 70,828 | \$ 70,191 | \$ 261,219 | \$ 70,538 | \$ 75,455 | \$ 87,171 | \$ 73,702 | \$ 306,866 |
| Health services division: | | | | | | | | | | |
| Nursing centers | 82,507 | 85,564 | 62,431 | 62,182 | 292,684 | 43,424 | 57,235 | 54,944 | 64,436 | 220,039 |
| Rehabilitation services | (66) | 288 | 1,155 | (1,639) | (262) | (959) | (750) | 261 | (315) | (1,763) |
| | 82,441 | 85,852 | 63,586 | 60,543 | 292,422 | 42,465 | 56,485 | 55,205 | 64,121 | 218,276 |
| Pharmacy division | 5,492 | 5,633 | 5,630 | 5,926 | 22,681 | 6,702 | 6,133 | 6,150 | 7,508 | 26,493 |
| Corporate: | | | | | | | | | | |
| Overhead | (31,674) | (29,200) | (30,812) | (19,469) | (111,155) | (26,713) | (28,354) | (28,670) | (28,898) | (112,635) |
| Insurance subsidiary | (1,001) | (1,203) | (1,745) | (2,100) | (6,049) | (2,607) | (3,407) | (4,002) | (3,535) | (13,551) |
| | (32,675) | (30,403) | (32,557) | (21,569) | (117,204) | (29,320) | (31,761) | (32,672) | (32,433) | (126,186) |
| | 112,959 | 123,581 | 107,487 | 115,091 | 459,118 | 90,385 | 106,312 | 115,854 | 112,898 | 425,449 |
| Unusual transactions | | (525) | | 2,320 | 1,795 | | | | | |
| Reorganization items | | 5,520 | | | 5,520 | | | | 1,010 | 1,010 |
| Operating income | 112,959 | 128,576 | 107,487 | 117,411 | 466,433 | 90,385 | 106,312 | 115,854 | 113,908 | 426,459 |
| Rent | (60,323) | (62,483) | (62,958) | (63,431) | (249,195) | (63,078) | (64,215) | (64,783) | (64,230) | (256,306) |
| Depreciation | (16,022) | (16,664) | (17,401) | (18,164) | (68,251) | (19,195) | (19,927) | (20,407) | (21,328) | (80,857) |
| Interest, net | (1,856) | (413) | 973 | (1,106) | (2,402) | (1,253) | (1,316) | 279 | (1,897) | (4,187) |
| Income from continuing operations before income taxes | 34,758 | 49,016 | 28,101 | 34,710 | 146,585 | 6,859 | 20,854 | 30,943 | 26,453 | 85,109 |
| Provision for income taxes | 14,314 | 20,085 | 12,876 | 13,789 | 61,064 | 4,348 | 7,710 | 12,629 | 10,968 | 35,655 |

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| | | | | | | | | | |
|-----------|-----------|-----------|-----------|-----------|----------|-----------|-----------|-----------|-----------|
| \$ 20,444 | \$ 28,931 | \$ 15,225 | \$ 20,921 | \$ 85,521 | \$ 2,511 | \$ 13,144 | \$ 18,314 | \$ 15,485 | \$ 49,454 |
|-----------|-----------|-----------|-----------|-----------|----------|-----------|-----------|-----------|-----------|

KINDRED HEALTHCARE, INC.

Business Segment Data (Continued)

(In thousands)

| | 2002 Quarters | | | | | 2003 Quarters | | | | |
|--|------------------|------------------|------------------|------------------|-------------------|------------------|------------------|------------------|------------------|-------------------|
| | First | Second | Third | Fourth | Year | First | Second | Third | Fourth | Year |
| Rent: | | | | | | | | | | |
| Hospital division | \$ 22,309 | \$ 23,702 | \$ 23,515 | \$ 23,393 | \$ 92,919 | \$ 23,284 | \$ 23,706 | \$ 23,441 | \$ 22,753 | \$ 93,184 |
| Health services division: | | | | | | | | | | |
| Nursing centers | 37,323 | 38,048 | 38,684 | 39,016 | 153,071 | 39,031 | 39,808 | \$ 40,459 | 40,530 | 159,828 |
| Rehabilitation services | 24 | 24 | 37 | 43 | 128 | 69 | 95 | 123 | 185 | 472 |
| | <u>37,347</u> | <u>38,072</u> | <u>38,721</u> | <u>39,059</u> | <u>153,199</u> | <u>39,100</u> | <u>39,903</u> | <u>40,582</u> | <u>40,715</u> | <u>160,300</u> |
| Pharmacy division | 634 | 646 | 670 | 913 | 2,863 | 630 | 547 | 698 | 703 | 2,578 |
| Corporate | 33 | 63 | 52 | 66 | 214 | 64 | 59 | 62 | 59 | 244 |
| | <u>\$ 60,323</u> | <u>\$ 62,483</u> | <u>\$ 62,958</u> | <u>\$ 63,431</u> | <u>\$ 249,195</u> | <u>\$ 63,078</u> | <u>\$ 64,215</u> | <u>\$ 64,783</u> | <u>\$ 64,230</u> | <u>\$ 256,306</u> |
| Depreciation: | | | | | | | | | | |
| Hospital division | \$ 6,196 | \$ 6,468 | \$ 6,820 | \$ 6,897 | \$ 26,381 | \$ 7,054 | \$ 7,450 | \$ 7,684 | \$ 8,257 | \$ 30,445 |
| Health services division: | | | | | | | | | | |
| Nursing centers | 5,730 | 5,788 | 6,035 | 6,129 | 23,682 | 6,373 | 6,569 | 6,688 | 6,740 | 26,370 |
| Rehabilitation services | 9 | 6 | 13 | 15 | 43 | 16 | 20 | 22 | 25 | 83 |
| | <u>5,739</u> | <u>5,794</u> | <u>6,048</u> | <u>6,144</u> | <u>23,725</u> | <u>6,389</u> | <u>6,589</u> | <u>6,710</u> | <u>6,765</u> | <u>26,453</u> |
| Pharmacy division | 380 | 410 | 451 | 498 | 1,739 | 517 | 539 | 561 | 560 | 2,177 |
| Corporate | 3,707 | 3,992 | 4,082 | 4,625 | 16,406 | 5,235 | 5,349 | 5,452 | 5,746 | 21,782 |
| | <u>\$ 16,022</u> | <u>\$ 16,664</u> | <u>\$ 17,401</u> | <u>\$ 18,164</u> | <u>\$ 68,251</u> | <u>\$ 19,195</u> | <u>\$ 19,927</u> | <u>\$ 20,407</u> | <u>\$ 21,328</u> | <u>\$ 80,857</u> |
| Capital expenditures, excluding acquisitions (including discontinued operations): | | | | | | | | | | |
| Hospital division | \$ 3,316 | \$ 6,430 | \$ 6,056 | \$ 10,831 | \$ 26,633 | \$ 2,822 | \$ 4,133 | \$ 5,773 | \$ 13,388 | \$ 26,116 |
| Health services division | 2,116 | 4,728 | 6,498 | 10,785 | 24,127 | 3,273 | 6,422 | 9,803 | 9,815 | 29,313 |
| Pharmacy division | 396 | 782 | 882 | 1,431 | 3,491 | 616 | 522 | 815 | 2,254 | 4,207 |
| Corporate: | | | | | | | | | | |
| Information systems | 3,330 | 6,632 | 6,474 | 9,140 | 25,576 | 3,207 | 5,992 | 4,071 | 8,223 | 21,493 |
| Other | 710 | 787 | 1,056 | 1,691 | 4,244 | 647 | 408 | 361 | 1,551 | 2,967 |
| | <u>\$ 9,868</u> | <u>\$ 19,359</u> | <u>\$ 20,966</u> | <u>\$ 33,878</u> | <u>\$ 84,071</u> | <u>\$ 10,565</u> | <u>\$ 17,477</u> | <u>\$ 20,823</u> | <u>\$ 35,231</u> | <u>\$ 84,096</u> |

KINDRED HEALTHCARE, INC.

Business Segment Data (Continued)

(Unaudited)

| | 2002 Quarters | | | | | 2003 Quarters | | | | |
|-------------------------------|---------------|-----------|-----------|-----------|-----------|---------------|-----------|-----------|-----------|-----------|
| | First | Second | Third | Fourth | Year | First | Second | Third | Fourth | Year |
| Hospital data: | | | | | | | | | | |
| End of period data: | | | | | | | | | | |
| Number of hospitals | 55 | 61 | 62 | 63 | | 63 | 63 | 64 | 66 | |
| Number of licensed beds | 4,629 | 4,944 | 5,012 | 5,053 | | 5,076 | 5,098 | 5,129 | 5,219 | |
| Revenue mix % (a): | | | | | | | | | | |
| Medicare | 58 | 60 | 58 | 61 | 59 | 60 | 59 | 62 | 63 | 61 |
| Medicaid | 10 | 9 | 8 | 9 | 9 | 8 | 8 | 7 | 8 | 8 |
| Private and other | 32 | 31 | 34 | 30 | 32 | 32 | 33 | 31 | 29 | 31 |
| Admissions: | | | | | | | | | | |
| Medicare | 5,295 | 6,259 | 5,770 | 6,193 | 23,517 | 6,612 | 6,346 | 6,053 | 6,681 | 25,692 |
| Medicaid | 579 | 567 | 606 | 620 | 2,372 | 648 | 604 | 670 | 661 | 2,583 |
| Private and other | 1,117 | 1,569 | 1,217 | 1,181 | 5,084 | 1,281 | 1,322 | 1,333 | 1,359 | 5,295 |
| | 6,991 | 8,395 | 7,593 | 7,994 | 30,973 | 8,541 | 8,272 | 8,056 | 8,701 | 33,570 |
| Patients days: | | | | | | | | | | |
| Medicare | 188,530 | 211,684 | 203,199 | 205,735 | 809,148 | 216,266 | 214,116 | 193,069 | 191,904 | 815,355 |
| Medicaid | 32,680 | 31,948 | 32,410 | 34,206 | 131,244 | 31,764 | 32,470 | 31,362 | 29,488 | 125,084 |
| Private and other | 56,018 | 54,901 | 54,847 | 55,225 | 220,991 | 56,225 | 59,339 | 54,080 | 52,725 | 222,369 |
| | 277,228 | 298,533 | 290,456 | 295,166 | 1,161,383 | 304,255 | 305,925 | 278,511 | 274,117 | 1,162,808 |
| Average length of stay: | | | | | | | | | | |
| Medicare | 35.6 | 33.8 | 35.2 | 33.2 | 34.4 | 32.7 | 33.7 | 31.9 | 28.7 | 31.7 |
| Medicaid | 56.4 | 56.3 | 53.5 | 55.2 | 55.3 | 49.0 | 53.8 | 46.8 | 44.6 | 48.4 |
| Private and other | 50.2 | 35.0 | 45.1 | 46.8 | 43.5 | 43.9 | 44.9 | 40.6 | 38.8 | 42.0 |
| Weighted average | 39.7 | 35.6 | 38.3 | 36.9 | 37.5 | 35.6 | 37.0 | 34.6 | 31.5 | 34.6 |
| Revenues per admission (a): | | | | | | | | | | |
| Medicare | \$ 31,397 | \$ 30,208 | \$ 32,062 | \$ 31,386 | \$ 31,241 | \$ 30,050 | \$ 31,594 | \$ 35,157 | \$ 30,987 | \$ 31,878 |
| Medicaid | 49,561 | 46,462 | 44,113 | 46,755 | 46,695 | 40,547 | 44,766 | 36,974 | 37,825 | 39,910 |
| Private and other | 81,187 | 62,740 | 90,567 | 81,747 | 77,869 | 83,449 | 83,830 | 77,860 | 68,870 | 78,395 |
| Weighted average | 40,856 | 37,386 | 42,401 | 40,018 | 40,078 | 38,855 | 40,904 | 42,374 | 37,423 | 39,833 |
| Revenues per patient day (a): | | | | | | | | | | |
| Medicare | \$ 882 | \$ 893 | \$ 910 | \$ 945 | \$ 908 | \$ 919 | \$ 936 | \$ 1,102 | \$ 1,079 | \$ 1,004 |
| Medicaid | 878 | 825 | 825 | 847 | 844 | 827 | 833 | 790 | 848 | 824 |
| Private and other | 1,619 | 1,793 | 2,010 | 1,748 | 1,791 | 1,901 | 1,868 | 1,919 | 1,775 | 1,867 |
| Weighted average | 1,030 | 1,051 | 1,108 | 1,084 | 1,069 | 1,091 | 1,106 | 1,226 | 1,188 | 1,150 |
| Average daily census | 3,080 | 3,281 | 3,157 | 3,208 | 3,182 | 3,381 | 3,362 | 3,027 | 2,980 | 3,186 |
| Occupancy % | 69.8 | 68.3 | 66.0 | 66.7 | 67.6 | 69.8 | 69.0 | 61.9 | 59.9 | 65.1 |

(a) Includes income of \$14 million related to certain Medicare reimbursement issues recorded in the third quarter of 2003 and income of \$12 million related to a favorable accounts receivable settlement with a private insurance company recorded in the third quarter of 2002.

KINDRED HEALTHCARE, INC.

Business Segment Data (Continued)

(Unaudited)

| | 2002 Quarters | | | | | 2003 Quarters | | | | |
|--|------------------|------------------|------------------|------------------|-------------------|------------------|------------------|------------------|------------------|-------------------|
| | First | Second | Third | Fourth | Year | First | Second | Third | Fourth | Year |
| Nursing center data: | | | | | | | | | | |
| End of period data: | | | | | | | | | | |
| Number of nursing centers: | | | | | | | | | | |
| Owned or leased | 250 | 248 | 248 | 248 | | 248 | 248 | 248 | 248 | |
| Managed | 14 | 10 | 10 | 7 | | 7 | 7 | 7 | 7 | |
| | <u>264</u> | <u>258</u> | <u>258</u> | <u>255</u> | | <u>255</u> | <u>255</u> | <u>255</u> | <u>255</u> | |
| Number of licensed beds: | | | | | | | | | | |
| Owned or leased | 32,407 | 32,342 | 32,333 | 32,314 | | 32,293 | 32,124 | 32,118 | 32,124 | |
| Managed | 1,417 | 1,017 | 1,017 | 803 | | 803 | 803 | 803 | 803 | |
| | <u>33,824</u> | <u>33,359</u> | <u>33,350</u> | <u>33,117</u> | | <u>33,096</u> | <u>32,927</u> | <u>32,921</u> | <u>32,927</u> | |
| Revenue mix %: | | | | | | | | | | |
| Medicare | 34 | 34 | 33 | 31 | 33 | 33 | 33 | 32 | 33 | 32 |
| Medicaid | 46 | 47 | 48 | 50 | 48 | 48 | 48 | 50 | 48 | 49 |
| Private and other | 20 | 19 | 19 | 19 | 19 | 19 | 19 | 18 | 19 | 19 |
| Patients days (excludes managed facilities): | | | | | | | | | | |
| Medicare | 388,198 | 392,362 | 383,976 | 377,106 | 1,541,642 | 398,646 | 399,150 | 394,957 | 397,254 | 1,590,007 |
| Medicaid | 1,705,650 | 1,713,448 | 1,757,643 | 1,764,892 | 6,941,633 | 1,699,726 | 1,707,907 | 1,757,580 | 1,737,615 | 6,902,828 |
| Private and other | 446,087 | 446,163 | 446,399 | 437,462 | 1,776,111 | 410,378 | 418,824 | 422,529 | 426,890 | 1,678,621 |
| | <u>2,539,935</u> | <u>2,551,973</u> | <u>2,588,018</u> | <u>2,579,460</u> | <u>10,259,386</u> | <u>2,508,750</u> | <u>2,525,881</u> | <u>2,575,066</u> | <u>2,561,759</u> | <u>10,171,456</u> |
| Revenues per patient day: | | | | | | | | | | |
| Medicare | \$ 359 | \$ 358 | \$ 361 | \$ 335 | \$ 353 | \$ 338 | \$ 342 | \$ 344 | \$ 364 | \$ 347 |
| Medicaid | 112 | 112 | 115 | 117 | 114 | 117 | 118 | 123 | 120 | 119 |
| Private and other | 180 | 180 | 183 | 182 | 181 | 188 | 189 | 188 | 190 | 189 |
| Weighted average | 162 | 162 | 163 | 160 | 162 | 164 | 165 | 168 | 169 | 167 |
| Average daily census | | | | | | | | | | |
| | 28,222 | 28,044 | 28,131 | 28,038 | 28,108 | 27,875 | 27,757 | 27,990 | 27,845 | 27,867 |
| Occupancy % | 86.2 | 86.1 | 86.7 | 86.4 | 86.4 | 86.0 | 85.6 | 86.8 | 86.4 | 86.2 |
| Pharmacy data: | | | | | | | | | | |
| Number of customer licensed beds at end of period: | | | | | | | | | | |
| Company-operated | 30,471 | 30,568 | 30,279 | 29,966 | | 29,804 | 27,566 | 27,886 | 28,280 | |
| Non-affiliated | 25,695 | 27,148 | 28,460 | 28,873 | | 28,365 | 28,848 | 29,507 | 33,127 | |

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| | | | | | | | |
|--------|--------|--------|--------|--------|--------|--------|--------|
| 56,166 | 57,716 | 58,739 | 58,839 | 58,169 | 56,414 | 57,393 | 61,407 |
|--------|--------|--------|--------|--------|--------|--------|--------|