

Encompass Health Corp
Form 10-Q
May 02, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q
 QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2018
OR
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File Number 001-10315

Encompass Health Corporation
(Exact name of Registrant as specified in its Charter)
Delaware 63-0860407
(State or Other Jurisdiction of Incorporation or Organization) (I.R.S. Employer Identification No.)

9001 Liberty Parkway 35242
Birmingham, Alabama
(Address of Principal Executive Offices) (Zip Code)

(205) 967-7116
(Registrant's telephone number)

3660 Grandview Parkway, Suite 200
Birmingham, Alabama 35243
(Former name or former address, if changed since last report)

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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Smaller reporting company
Non-Accelerated filer (Do not check if a smaller reporting company) Emerging growth company
If an emerging growth company, indicate by checkmark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2).
Yes No

The registrant had 98,819,848 shares of common stock outstanding, net of treasury shares, as of April 25, 2018.

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NOTE TO READERS

As used in this report, the terms “Encompass Health,” “we,” “us,” “our,” and the “Company” refer to Encompass Health Corporation and its consolidated subsidiaries, unless otherwise stated or indicated by context. This drafting style is suggested by the Securities and Exchange Commission and is not meant to imply that Encompass Health Corporation, the publicly traded parent company, owns or operates any specific asset, business, or property. The hospitals, operations, and businesses described in this filing are primarily owned and operated by subsidiaries of the parent company. In addition, we use the term “Encompass Health Corporation” to refer to Encompass Health Corporation alone wherever a distinction between Encompass Health Corporation and its subsidiaries is required or aids in the understanding of this filing.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report contains historical information, as well as forward-looking statements that involve known and unknown risks and relate to, among other things, future events, changes to Medicare reimbursement and other healthcare laws and regulations from time to time, our business strategy, our dividend and stock repurchase strategies, our financial plans, our growth plans, our future financial performance, our projected business results, or our projected capital expenditures. In some cases, the reader can identify forward-looking statements by terminology such as “may,” “will,” “should,” “could,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “targets,” “potential,” or “contingent,” or the negative of these terms or other comparable terminology. Such forward-looking statements are necessarily estimates based upon current information and involve a number of risks and uncertainties, many of which are beyond our control. Any forward-looking statement is based on information current as of the date of this report and speaks only as of the date on which such statement is made. Actual events or results may differ materially from the results anticipated in these forward-looking statements as a result of a variety of factors. While it is impossible to identify all such factors, factors that could cause actual results to differ, such as decreases in revenues or increases in costs or charges, materially from those estimated by us include, but are not limited to, the following:

each of the factors discussed in Item 1A, Risk Factors, of our Annual Report on Form 10-K for the year ended December 31, 2017, as well as uncertainties and factors, if any, discussed elsewhere in this Form 10-Q, including in the “Executive Overview—Key Challenges” section of Part I, Item 2, Management’s Discussion and Analysis of Financial Condition and Results of Operations, in our other filings from time to time with the SEC, or in materials incorporated therein by reference;

changes in the rules and regulations of the healthcare industry at either or both of the federal and state levels, including those contemplated now and in the future as part of national healthcare reform and deficit reduction (such as the re-basing of payment systems, the introduction of site neutral payments or case-mix weightings across post-acute settings, or the home health groupings model, and other payment system reforms), affecting revenues and related increases in the costs of complying with such changes;

reductions or delays in, or suspension of, reimbursement for our services by governmental or private payors, including our ability to obtain and retain favorable arrangements with third-party payors;

restrictive interpretations of the regulations governing the claims that are reimbursable by Medicare;

delays in the administrative appeals process associated with denied Medicare reimbursement claims, including from various Medicare audit programs, and our exposure to the related delay or reduction in the receipt of the reimbursement amounts for services previously provided;

the ongoing evolution of the healthcare delivery system, including alternative payment models and value-based purchasing initiatives, which may decrease our reimbursement rate or increase costs associated with our operations; our ability to comply with extensive and changing healthcare regulations as well as the increased costs of regulatory compliance and compliance monitoring in the healthcare industry, including the costs of investigating and defending asserted claims, whether meritorious or not;

our ability to attract and retain nurses, therapists, and other healthcare professionals in a highly competitive environment with often severe staffing shortages and the impact on our labor expenses from potential union activity and staffing recruitment and retention;

competitive pressures in the healthcare industry, including from other providers that may be participating in integrated delivery payment arrangements in which we do not participate, and our response to those pressures;

changes in our payor mix or the acuity of our patients affecting reimbursement rates;

our ability to successfully complete and integrate de novo developments, acquisitions, investments, and joint ventures consistent with our growth strategy, including realization of anticipated revenues, cost savings, productivity improvements arising from the related operations and avoidance of unanticipated difficulties, costs or liabilities that could arise from acquisitions or integrations;

any adverse outcome of various lawsuits, claims, and legal or regulatory proceedings, including the ongoing investigations initiated by the U.S. Departments of Justice and of Health and Human Services, Office of the Inspector General;

- increased costs of defending and insuring against alleged professional liability and other claims and the ability to predict the costs related to claims;
- potential incidents affecting the proper operation, availability, or security of our information systems, including the patient information stored there;
- our ongoing rebranding and name change initiative and the impact on our existing operations, including our ability to attract patient referrals to our hospitals as well as the associated costs of rebranding;
- new or changing quality reporting requirements impacting operational costs or our Medicare reimbursement;
- the price of our common stock as it affects our willingness and ability to repurchase shares and the financial and accounting effects of any repurchases;
- our ability and willingness to continue to declare and pay dividends on our common stock;
- our ability to maintain proper local, state and federal licensing, including compliance with the Medicare conditions of participation, which is required to participate in the Medicare program;
- our ability to attract and retain key management personnel; and
- general conditions in the economy and capital markets, including any instability or uncertainty related to armed conflict or an act of terrorism, governmental impasse over approval of the United States federal budget, an increase to the debt ceiling, or an international sovereign debt crisis.

The cautionary statements referred to in this section also should be considered in connection with any subsequent written or oral forward-looking statements that may be issued by us or persons acting on our behalf. We undertake no duty to update these forward-looking statements, even though our situation may change in the future. Furthermore, we cannot guarantee future results, events, levels of activity, performance, or achievements.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

Encompass Health Corporation and Subsidiaries
Condensed Consolidated Statements of Operations
(Unaudited)

	Three Months Ended March 31, 2018 2017 (In Millions, Except Per Share Data)	
Net operating revenues	\$1,046.0	\$957.1
Operating expenses:		
Salaries and benefits	570.2	530.1
Other operating expenses	141.2	127.8
Occupancy costs	18.6	17.9
Supplies	39.9	37.0
General and administrative expenses	61.1	36.5
Depreciation and amortization	45.9	45.2
Total operating expenses	876.9	794.5
Interest expense and amortization of debt discounts and fees	35.6	41.3
Other loss (income)	0.1	(1.0)
Equity in net income of nonconsolidated affiliates	(2.3)	(2.1)
Income from continuing operations before income tax expense	135.7	124.4
Provision for income tax expense	30.0	39.7
Income from continuing operations	105.7	84.7
Loss from discontinued operations, net of tax	(0.5)	(0.3)
Net income	105.2	84.4
Less: Net income attributable to noncontrolling interests	(21.4)	(17.6)
Net income attributable to Encompass Health	\$83.8	\$66.8
Weighted average common shares outstanding:		
Basic	97.8	88.8
Diluted	99.4	99.0
Earnings per common share:		
Basic earnings per share attributable to Encompass Health common shareholders:		
Continuing operations	\$0.86	\$0.75
Discontinued operations	(0.01)	—
Net income	\$0.85	\$0.75
Diluted earnings per share attributable to Encompass Health common shareholders:		
Continuing operations	\$0.85	\$0.70
Discontinued operations	(0.01)	—
Net income	\$0.84	\$0.70
Cash dividends per common share	\$0.25	\$0.24
Amounts attributable to Encompass Health common shareholders:		
Income from continuing operations	\$84.3	\$67.1

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Loss from discontinued operations, net of tax	(0.5)	(0.3)
Net income attributable to Encompass Health	\$83.8	\$66.8

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

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Encompass Health Corporation and Subsidiaries
 Condensed Consolidated Statements of Comprehensive Income
 (Unaudited)

	Three Months Ended March 31, 2018 2017 (In Millions)	
COMPREHENSIVE INCOME		
Net income	\$105.2	\$84.4
Other comprehensive income, net of tax:		
Net change in unrealized gain on available-for-sale securities:		
Unrealized net holding gain arising during the period	—	0.4
Other comprehensive income before income taxes	—	0.4
Provision for income tax expense related to other comprehensive income items	—	(0.1)
Other comprehensive income, net of tax	—	0.3
Comprehensive income	105.2	84.7
Comprehensive income attributable to noncontrolling interests	(21.4)	(17.6