HEALTHCARE SERVICES GROUP INC
Form 10-Q
April 25, 2011

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-Q

(MARK ONE)

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

For the quarterly period ended March 31, 2011

OR

o **TRANSISTION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from __________ to __________

Commission File Number 0-12015

HEALTHCARE SERVICES GROUP, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania	23-2018365
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification number)
3220 Tillman Drive-Suite 300, Bensalem, Pennsylvania	19020
(Address of principal executive office)	(Zip code)

Registrant s telephone number, including area code: 215-639-4274

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 þ NO o

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES þ NO o

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 definitions of large accelerated filer , accelerated filer and smaller reporting company as defined in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES o NO þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date. Common Stock, $.01 Par Value: 66,375,000 shares outstanding as of April 22, 2011.

INDEX

Table of Contents

Consolidated Balance Sheets

	(Unaudited) March 31, 2011	December 31, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	$ 36,692,000	$ 39,692,000
Marketable securities, at fair value	41,199,000	43,437,000
Accounts and notes receivable, less allowance for doubtful accounts of $4,008,000 in 2011 and $4,069,000 in 2010	111,364,000	108,426,000
Inventories and supplies	20,844,000	20,614,000
Prepaid income taxes		3,978,000
Prepaid expenses and other	6,525,000	5,628,000
Total current assets	216,624,000	221,775,000
Property and equipment:		
Laundry and linen equipment installations	1,935,000	1,886,000
Housekeeping equipment and office furniture	21,227,000	20,111,000
Autos and trucks	299,000	284,000
	23,461,000	22,281,000
Less accumulated depreciation	15,869,000	15,625,000
	7,592,000	6,656,000
GOODWILL	16,955,000	16,955,000
OTHER INTANGIBLE ASSETS, less accumulated amortization of $6,406,000 in 2011 and $5,938,000 in 2010	6,794,000	7,262,000
NOTES RECEIVABLE long term portion, net of discount	4,931,000	5,055,000
DEFERRED COMPENSATION FUNDING, at fair value	12,948,000	12,080,000
DEFERRED INCOME TAXES long term portion	8,425,000	8,109,000
OTHER NONCURRENT ASSETS	42,000	42,000
TOTAL ASSETS	$ 274,311,000	$ 277,934,000
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 12,029,000	$ 11,434,000
Accrued payroll, accrued and withheld payroll taxes	14,122,000	21,429,000
Other accrued expenses	1,487,000	1,988,000
Income taxes payable	680,000	
Deferred income taxes	501,000	604,000
Accrued insurance claims	5,634,000	5,076,000
Total current liabilities	34,453,000	40,531,000
ACCRUED INSURANCE CLAIMS long term portion	13,147,000	11,845,000
DEFERRED COMPENSATION LIABILITY	13,094,000	12,479,000
COMMITMENTS AND CONTINGENCIES		

STOCKHOLDERS EQUITY:				
Common stock, $.01 par value; 100,000,000 shares authorized; 69,369,000 shares issued in 2011 and 69,315,000 shares in 2010		694,000		693,000
Additional paid-in capital		102,416,000		100,138,000
Retained earnings		128,358,000		130,993,000
Accumulated other comprehensive income (loss), net of taxes		12,000		(78,000)
Common stock in treasury, at cost, 3,003,000 shares in 2011 and 3,139,000 shares in 2010		(17,863,000)		(18,667,000)
Total stockholders equity		213,617,000		213,079,000
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$	274,311,000	$	277,934,000

See accompanying notes

Table of Contents

Consolidated Statements of Income
(Unaudited)

	For the Three Months Ended March 31,	
	2011	2010
Revenues	$ 208,390,000	$ 183,801,000
Operating costs and expenses:		
Costs of services provided	179,985,000	158,573,000
Selling, general and administrative	16,780,000	13,901,000
Other income:		
Investment and interest	714,000	750,000
Income before income taxes	12,339,000	12,077,000
Income taxes	4,572,000	4,649,000
Net income	$ 7,767,000	$ 7,428,000
Basic earnings per common share	$ 0.12	$ 0.11
Diluted earnings per common share	$ 0.12	$ 0.11
Cash dividends per common share	$ 0.16	$ 0.14
Weighted average number of common shares outstanding		
Basic	66,401,000	65,849,000
Diluted	67,454,000	66,989,000

See accompanying notes

Table of Contents

Consolidated Statements of Cash Flows

	(Unaudited) For the Three Months Ended March 31, 2011	2010
Cash flows from operating activities:		
Net income	$ 7,767,000	$ 7,428,000
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,004,000	923,000
Bad debt provision	1,160,000	600,000
Deferred income tax benefits	(419,000)	(850,000)
Share-based compensation expense	560,000	264,000
Amortization of premium on marketable securities	232,000	230,000
Unrealized gain on marketable securities	145,000	597,000
Unrealized (gain) on deferred compensation fund investments	(429,000)	(394,000)
Changes in operating assets and liabilities:		
Accounts and notes receivable	(4,099,000)	(1,310,000)
Prepaid income taxes	4,659,000	
Inventories and supplies	(230,000)	(481,000)
Notes receivable long term portion	124,000	(457,000)
Deferred compensation funding	(439,000)	(375,000)
Accounts payable and other accrued expenses	319,000	(1,169,000)
Accrued payroll, accrued and withheld payroll taxes	(6,391,000)	(10,619,000)
Accrued insurance claims	1,860,000	1,057,000
Deferred compensation liability	1,016,000	898,000
Income taxes payable		689,000
Prepaid expenses and other assets	(897,000)	708,000
Net cash provided by (used in) operating activities	5,942,000	(2,261,000)
Cash flows from investing activities:		
Disposals of fixed assets	15,000	6,000
Additions to property and equipment	(1,488,000)	(614,000)
Purchases of marketable securities, net	(4,708,000)	(14,623,000)
Sales of marketable securities, net	6,658,000	22,481,000
Net cash provided by investing activities	477,000	7,250,000
Cash flows from financing activities:		
Dividends paid	(10,402,000)	(9,225,000)
Reissuance of treasury stock pursuant to Dividend Reinvestment Plan	35,000	27,000
Tax benefits transactions in equity compensation plans	27,000	708,000
Proceeds from the exercise of stock options	921,000	848,000
Net cash used in financing activities	(9,419,000)	(7,642,000)

Net decrease in cash and cash equivalents	(3,000,000)	(2,653,000)
Cash and cash equivalents at beginning of the period	39,692,000	31,301,000
Cash and cash equivalents at end of the period	$ 36,692,000	$ 28,648,000
Supplementary Cash Flow Information:		
Income taxes cash payments, net of refunds	$ 311,000	$ 4,103,000
Issuance of 76,000 and 73,000 shares in 2011 and 2010, respectively, of Common Stock pursuant to Employee Stock Plans	$ 1,233,000	$ 1,047,000

See accompanying notes

Table of Contents

Consolidated Statements of Stockholders Equity and Comprehensive Income (Unaudited)

For the Three Months Ended March 31, 2011

	Common Stock Shares	Amount	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Total Retained Earnings	Treasury Stock	Stockholders Equity
Balance, December 31, 2010	**69,315,000**	**$ 693,000**	**$ 100,138,000**	**$ (78,000)**	**$ 130,993,000**	**$ (18,667,000)**	**$ 213,079,000**
Comprehensive income:							
Net income for the period					7,767,000		7,767,000
Unrealized gain on available for sale marketable securities, net of taxes				90,000			90,000
Comprehensive income							7,857,000
Exercise of stock options and other share-based compensation, net of 7,000 shares tendered for payment	54,000	1,000	598,000			322,000	921,000
Tax benefit arising from stock option transactions			27,000				27,000
Share-based compensation expense stock options			467,000				467,000
			381,000			19,000	400,000

Treasury shares issued for Deferred Compensation Plan funding and redemptions (3,000 shares)							
Shares issued pursuant to Employee Stock Plans (76,000 shares)			782,000			451,000	1,233,000
Cash dividends $.16 per common share					(10,402,000)		(10,402,000)
Shares issued pursuant to Dividend Reinvestment Plan (2,000 shares)			23,000			12,000	35,000
Balance, March 31, 2011	**69,369,000**	**$ 694,000**	**$ 102,416,000**	**$ 12,000**	**$ 128,358,000**	**$ (17,863,000)**	**$ 213,617,000**

See accompanying notes.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1 Basis of Reporting

The accompanying financial statements are unaudited and do not include certain information and note disclosures required by accounting principles generally accepted in the United States for complete financial statements. However, in our opinion, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The balance sheet shown in this report as of December 31, 2010 has been derived from, and does not include, all the disclosures contained in the financial statements for the year ended December 31, 2010. The financial statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2010. The results of operations for the three month period ended March 31, 2011 are not necessarily indicative of the results that may be expected for the full fiscal year.

As of March 31, 2011, we operate one wholly-owned subsidiary, Huntingdon Holdings, Inc. (Huntingdon). Huntingdon invests our cash and cash equivalents, and manages our portfolio of marketable securities.

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP), we make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates are used for, but not limited to, our allowance for doubtful accounts, accrued insurance claims, asset valuations and review for potential impairment, share-based compensation, and deferred income taxes. The estimates are based upon various factors including current and historical trends, as well as other pertinent industry and regulatory authority information. We regularly evaluate this information to determine if it is necessary to update the basis for our estimates and to compensate for known changes.

Inventories and supplies include housekeeping and, linen and laundry supplies, as well as dietary provisions and supplies. Inventories and supplies are stated at cost to approximate a first-in, first-out (FIFO) basis. Linen supplies are amortized over a 24 month period.

Revenues are recorded net of sales taxes.

Note 2 Goodwill and Other Intangible Assets

Goodwill represents the excess of the purchase price over the fair value of net assets acquired of businesses and is not amortized. Goodwill is evaluated for impairment on an annual basis, or more frequently if impairment indicators arise, using a fair-value-based test that compares the fair value of the asset to its carrying value. The goodwill associated with the 2009 acquisition of Contract Environmental Services, Inc. (CES) is deductible for tax purposes over a fifteen year period.

Goodwill by reportable operating segment, as described in Note 5 herein, was approximately $14,894,000 and $2,061,000 for Housekeeping and Dietary as of March 31, 2011 and December 31, 2010, respectively.

The cost of intangible assets is based on fair values at the date of acquisition. Intangible assets with determinable lives are amortized on a straight-line basis over their estimated useful life (between 7 and 8 years). The following table sets forth the amounts of our identifiable intangible assets subject to amortization, which were acquired in acquisitions.

	March 31, 2011	December 31, 2010
Customer relationships	$ 12,400,000	$ 12,400,000
Non-compete agreements	800,000	800,000
Total other intangibles, gross	$ 13,200,000	$ 13,200,000
Less accumulated amortization	(6,406,000)	(5,938,000)
Other intangibles, net	$ 6,794,000	$ 7,262,000

Table of Contents

The customer relationships have a weighted-average amortization period of seven years and the non-compete agreements have a weighted-average amortization period of eight years. The following table sets forth the estimated amortization expense for intangibles subject to amortization for the balance of 2011 and the subsequent five fiscal years:

Period/Year	Customer Relationships	Non-Compete Agreements	Total
April 1 to December 31, 2011	$ 1,329,000	$ 75,000	$ 1,404,000
2012	1,771,000	100,000	1,871,000
2013	1,452,000	100,000	1,552,000
2014	814,000	67,000	881,000
2015	814,000		814,000
2016	271,000		271,000

Amortization expense for the three month periods ended March 31, 2011 and 2010 were $468,000 and $497,000, respectively.

Note 3 Fair Value Measurements and Marketable Securities

We, in accordance with U.S. GAAP, define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). Effective January 1, 2008, we elected the fair value option for certain of our marketable securities purchased since such adoption. Management initially elected the fair value option for certain of our marketable securities because it views such investment securities as highly liquid and available to be drawn upon for working capital purposes making them similar to its cash and cash equivalents. Accordingly, we record net unrealized gain or loss in the other income investment and interest caption in our consolidated income statements for such investments. We have not elected the fair value option for marketable securities acquired after December 31, 2009. Although these assets continue to be highly liquid and available, we do not believe these assets are representative of our operating activities. These assets are representative of our investing activities, and they will be available for future needs of the Company to support its current and projected growth.

Table of Contents

Certain of our assets and liabilities are reported at fair value in the accompanying balance sheets. Such assets and liabilities include cash and cash equivalents, marketable securities, accounts and notes receivable, accounts payable, income taxes payable and other accrued expenses. The following tables provide fair value measurement information for our marketable securities and deferred compensation fund investment assets as of March 31, 2011 and December 31, 2010.

	As of March 31, 2011				
			Fair Value Measurement Using:		
	Carrying Amount	Total Fair Value	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets					
Marketable securities					
Municipal bonds	$ 41,199,000	$ 41,199,000	$	$ 41,199,000	$
Equity securities Deferred comp fund					
Money Market	$ 2,943,000	$ 2,943,000	$	$ 2,943,000	$
Large Cap Value	2,624,000	2,624,000	2,624,000		
Large Cap Growth	2,256,000	2,256,000	2,256,000		
Small Cap Value	1,258,000	1,258,000	1,258,000		
Fixed Income	968,000	968,000	968,000		
Specialty	791,000	791,000	791,000		
Balanced and Lifestyle	622,000	622,000	622,000		
International	609,000	609,000	609,000		
Large Cap Blend	468,000	468,000	468,000		
Mid Cap Growth	409,000	409,000	409,000		
Equity securities Deferred comp fund	$ 12,948,000	$ 12,948,000	$ 10,005,000	$ 2,943,000	$

	As of December 31, 2010				
			Fair Value Measurement Using:		
	Carrying Amount	Total Fair Value	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets					
Marketable securities					
Municipal bonds	$ 43,437,000	$ 43,437,000	$	$ 43,437,000	$
Equity securities Deferred comp fund					
Money Market	$ 2,737,000	$ 2,737,000	$	$ 2,737,000	$
Large Cap Value	2,433,000	2,433,000	2,433,000		

Large Cap Growth	2,106,000	2,106,000	2,106,000		
Small Cap Value	1,152,000	1,152,000	1,152,000		
Fixed Income	987,000	987,000	987,000		
Specialty	712,000	712,000	712,000		
Balanced and Lifestyle	566,000	566,000	566,000		
International	572,000	572,000	572,000		
Large Cap Blend	444,000	444,000	444,000		
Mid Cap Growth	371,000	371,000	371,000		
Equity securities Deferred comp fund	$ 12,080,000	$ 12,080,000	$ 9,343,000	$ 2,737,000	$

Table of Contents

The fair value of the municipal bonds is measured using pricing service data from an external provider. The fair value of equity investments in the funded deferred compensation plan are valued (Level 1) based on quoted market prices. The money market fund in the funded deferred compensation plan is valued (Level 2) at the net asset value (NAV) of the shares held by the plan at the end of the period. As a practical expedient, fair value of our money market fund is valued at the NAV as determined by the custodian of the fund. The money market fund includes short-term United States dollar denominated money-market instruments. The money market fund can be redeemed at its NAV at its measurement date as there are no significant restrictions on the ability of participants to sell this investment.
For the three month periods ended March 31, 2011 and 2010, the other income investment and interest caption on our consolidated statements of income includes an unrealized loss from marketable securities of $145,000 and $597,000, respectively, for investments recorded under the fair value option. For the three month periods ended March 31, 2011 and 2010, the accumulated other comprehensive income on our consolidated balance sheet and stockholders equity includes unrealized gains from marketable securities of $90,000 and unrealized losses of $60,000, respectively, related to marketable securities that are not recognized under the fair value option in accordance with U.S. GAAP.

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Other-than-temporary Impairments
March 31, 2011					
Type of security:					
Municipal bonds	$ 13,353,000	$ 423,000	$	$ 13,776,000	$
Municipal bonds available for sale	27,411,000	12,000		27,423,000	
Total debt securities	$ 40,764,000	$ 435,000	$	$ 41,199,000	$
December 31, 2010					
Type of security:					
Municipal bonds	$ 18,029,000	$ 568,000	$	$ 18,597,000	$
Municipal bonds available for sale	24,918,000		(78,000)	24,840,000	
Total debt securities	$ 42,947,000	$ 568,000	$ (78,000)	$ 43,437,000	$

The contractual maturities of available for sale investments held at March 31, 2011 and December 31, 2010 are as follows.

	March 31, 2011	December 31, 2010
Maturing in one year or less	$ 1,024,000	$ 313,000
Maturing after one year through three years	17,339,000	22,325,000
Maturing after three years	9,060,000	2,202,000
Total debt securities available for sale	$ 27,423,000	$ 24,840,000

Note 4 Other Contingencies

We have a $42,000,000 bank line of credit on which we may draw to meet short-term liquidity requirements in excess of internally generated cash flow. Amounts drawn under the line of credit are payable upon demand. At March 31, 2011, there were no borrowings under the line of credit. However, at such date, we had outstanding a $40,420,000 irrevocable standby letter of credit which relates to payment obligations under our insurance programs. As a result of the letters of credit issued, the amount available under the line of credit was reduced by $40,420,000 at March 31, 2011. The line of credit requires us to satisfy two financial covenants. We are in compliance with the financial covenants at March 31, 2011 and expect to continue to remain in compliance with such financial covenants. This line of credit expires on June 30, 2012. We believe the line of credit will be renewed at that time.

Table of Contents

We provide our services in 47 states and we are subject to numerous local taxing jurisdictions within those states. Consequently, the taxability of our services is subject to various interpretations within these jurisdictions. In the ordinary course of business, a jurisdiction may contest our reporting positions with respect to the application of its tax code to our services, which may result in additional tax liabilities.

We have tax matters with various taxing authorities. Because of the uncertainties related to both the probable outcomes and amount of probable assessments due, we are unable to make a reasonable estimate of liability. We do not expect the resolution of any of these matters, taken individually or in the aggregate, to have a material adverse effect on our consolidated financial position or results of operations based on our best estimate of the outcomes of such matters.

We are also subject to various claims and legal actions in the ordinary course of business. Some of these matters include payroll and employee-related matters and examinations by governmental agencies. As we become aware of such claims and legal actions, we provide accruals if the exposures are probable and estimable. If an adverse outcome of such claims and legal actions is reasonably possible, we assess materiality and provide such financial disclosure, as appropriate. We believe that these matters, taken individually or in the aggregate, would not have a material adverse effect on our financial position or results of operations.

As a result of the current economic crisis, many states have significant budget deficits. State Medicaid programs are experiencing increased demand, and with lower revenues than projected, they have fewer resources to support their Medicaid programs. In addition, comprehensive health care legislation under the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (together, the Act) was signed into law in March 2010. The Act will significantly impact the governmental healthcare programs which our clients participate, and reimbursements received thereunder from governmental or third-party payors. Furthermore, in the coming year, new proposals or additional changes in existing regulations could be made to the Act which could directly impact the governmental reimbursement programs in which our clients participate. As a result, some state Medicaid programs are reconsidering previously approved increases in nursing home reimbursement or are considering delaying or foregoing those increases. A few states have indicated it is possible they will run out of cash to pay Medicaid providers, including nursing homes. Any negative changes in our clients reimbursements may negatively impact our results of operations. Although we are currently evaluating the Act s effect on our client base, we may not know the full effect until such a time as these laws are fully implemented and the Centers for Medicare and Medicaid Services and other agencies issue applicable regulations or guidance.

Note 5 Segment Information

Reportable Operating Segments

We manage and evaluate our operations in two reportable segments. The two reportable segments are Housekeeping (housekeeping, laundry, linen and other services), and Dietary (dietary department services). Although both segments serve the same client base and share many operational similarities, they are managed separately due to distinct differences in the type of service provided, as well as the specialized expertise required of the professional management personnel responsible for delivering the respective segment s services. We consider the various services provided within each reportable segment to comprise an identifiable reportable operating segment since such services are rendered pursuant to a single service agreement, specific to that reportable segment, as well as the fact that the delivery of the respective reportable segment s services are managed by the same management personnel of the particular reportable segment.

Differences between the reportable segments operating results and other disclosed data and our consolidated financial statements relate primarily to corporate level transactions and recording of transactions at the reportable segment level which use methods other than generally accepted accounting principles. Additionally, included in the differences between the reportable segments operating results and other disclosed data are amounts attributable to Huntingdon, our investment holding company subsidiary. Huntingdon does not transact any business with the reportable segments. Segment amounts disclosed are prior to any elimination entries made in consolidation.

Table of Contents

Housekeeping provides services in Canada, although essentially all of its revenues and net income, 99% in both categories, are earned in one geographic area, the United States. Dietary provides services solely in the United States.

	Housekeeping Services	Dietary Services	Corporate and Eliminations	Total
Quarter Ended March 31, 2011				
Revenues	$ 156,462,000	$ 51,657,000	$ 271,000(1)	$ 208,390,000
Income before income taxes	17,195,000	3,469,000	(8,325,000)(1)	12,339,000
Quarter Ended March 31, 2010				
Revenues	$ 140,896,000	$ 42,954,000	$ (49,000)(1)	$ 183,801,000
Income before income taxes	14,858,000	2,190,000	(4,971,000)(1)	12,077,000

(1) Represents primarily corporate office cost and related overhead, recording of transactions at the reportable segment level which use methods other than U.S. GAAP and consolidated subsidiaries operating expenses that are not allocated to the reportable segments, net of investment and interest income.

Total Consolidated Revenues from Clients

The following revenues earned from clients represent their reporting in accordance with U.S. GAAP and differ from segment revenues reported above due to the inclusion of adjustments used for segment reporting purposes by management. We earned total revenues from clients in the following service categories:

	Quarter Ended March 31, 2011	2010
Housekeeping services	$ 105,645,000	$ 94,655,000
Laundry and linen services	50,174,000	45,535,000
Dietary services	51,953,000	43,087,000
Maintenance services and other	618,000	524,000
	$ 208,390,000	$ 183,801,000

Major Client

We have one client, a nursing home chain (Major Client), which accounted for the respective percentages of our revenues as detailed below:

	Quarter Ended March 31, 2011	2010
Total revenues	10%	11%
Housekeeping services	11%	12%
Dietary services	6%	10%

Additionally, at both March 31, 2011 and December 31, 2010, amounts due from such client represented less than 1% of our accounts receivable balance. The loss of such client, or a significant reduction in revenues from such client, would have a material adverse effect on the results of operations of our two operating segments. In addition, if such client changes its payment terms it would increase our accounts receivable balance and have a material adverse effect on our cash flows and cash and cash equivalents.

Table of Contents

Note 6 Earnings Per Common Share

A reconciliation of the numerator and denominator of basic and diluted earnings per common share is as follows:

	Quarter ended March 31, 2011		
	Income (Numerator)	Shares (Denominator)	Per-share Amount
Net income	$ 7,767,000		
Basic earnings per common share	$ 7,767,000	66,401,000	$ .12
Effect of dilutive securities Options		1,053,000	
Diluted earnings per common share	$ 7,767,000	67,454,000	$ .12

	Quarter ended March 31, 2010		
	Income (Numerator)	Shares (Denominator)	Per-share Amount
Net income	$ 7,428,000		
Basic earnings per common share	$ 7,428,000	65,849,000	$ .11
Effect of dilutive securities Options		1,140,000	
Diluted earnings per common share	$ 7,428,000	66,989,000	$ .11

Options to purchase 480,000 shares of common stock having an average exercise price of $16.11 per common share were outstanding during the three month period ended March 31, 2011 but not included in the computation of diluted earnings per common share because the options exercise price were greater than the average market price of the common shares, and therefore, would be antidilutive.

No outstanding options were excluded from the computations of diluted earnings per common share for the three month period ended March 31, 2010 as no outstanding options have an exercise price in excess of the average market value of our common stock at March 31, 2010.

Note 7 Dividends

On March 4, 2011 we paid, to shareholders of record on February 11, 2011, a regular quarterly cash dividend of $.15625 per common share. Such regular quarterly cash dividend payment in the aggregate was $10,402,000. Additionally, on April 12, 2011, our Board of Directors declared a regular cash dividend of $.1575 per common share to be paid on May 13, 2011 to shareholders of record as of April 22, 2011.

Table of Contents

Note 8 Share-Based Compensation

Stock Options

During the three months ended March 31, 2011, the stock option activity under our 2002 Stock Option Plan, 1995 Incentive and Non-Qualified Stock Option Plan for key employees, and 1996 Non-Employee Director s Stock Option Plan (collectively the Stock Option Plans), was as follows:

	Weighted Average Price	Number of Shares	Weighted Average Remaining Contractual Life (In Years)	Aggregate Intrinsic Value
Outstanding, January 1, 2011	$ 9.13	3,002,000		
Granted	16.11	508,000		
Cancelled	11.95	(60,000)		
Exercised	9.00	(116,000)		
Outstanding, March 31, 2011	$ 10.16	3,334,000	6.22	$ 24,710,000
Options exercisable as of March 31, 2011		1,772,000	4.09	$ 19,144,000

The weighted average fair value of options granted during the 2011 and 2010 first quarters was $3.26 and $3.98, respectively. The following table summarizes information about stock options outstanding at March 31, 2011.

	Options Outstanding				Options Exercisable
Exercise Price Range	Number Outstanding	Average Remaining Contractual Life	Weighted Average Exercise price	Number Exercisable	Weighted Average Exercise Price
$1.83 2.50	458,000	1.09	$ 2.11	458,000	$ 2.11
3.68 3.68	388,000	2.74	3.68	388,000	3.68
6.07 6.07	338,000	3.74	6.07	338,000	6.07
10.39 10.39	530,000	7.76	10.39	196,000	10.39
$13.93 16.11	1,620,000	8.51	14.77	392,000	14.05
	3,334,000	6.22	$ 10.16	1,772,000	$ 6.77

Other information pertaining to option activity during the three month periods ended March 31, 2011 and 2010 was as follows:

	March 31, 2011	**March 31, 2010**
Weighted average grant-date fair value of stock options granted:	$ 1,477,000	$ 2,176,000

Total fair value of stock options vested:	$	1,015,000	$	681,000
Total intrinsic value of stock options exercised:	$	918,000	$	2,048,000
Total pre-tax stock-based compensation expense charged against income:	$	467,000	$	190,000
Total unrecognized compensation expense related to non-vested options:	$	4,950,000	$	4,181,000

Under our Stock Option Plans at March 31, 2011, in addition to the 3,334,000 shares issuable pursuant to outstanding option grants, an additional 5,873,000 shares of our Common Stock are available for future grants. Options outstanding and exercisable were granted at stock option prices which were not less than the fair market value of our Common Stock on the date the options were granted and no option has a term in excess of ten years. Additionally, with the exception of the options granted in years 2008 through 2011, options became vested and exercisable either on the date of grant or commencing six months after the option grant date. The options granted in 2008 through 2011 become vested and exercisable ratably over a five year period on each anniversary date of the option grant.

At March 31, 2011, the total unrecognized compensation expense related to non-vested options, as reported above, was expected to be recognized through the fourth quarter of 2015 for the options granted in 2011 and the fourth quarter of 2014 for the options granted in 2010. The fair value of options granted in 2011 and 2010 was estimated on the date of grant using the Black-Scholes valuation model with the following weighted average assumptions:

	2011	2010
Risk-free interest rate	2.6%	2.5%
Expected volatility	27.4%	42.1%
Weighted average expected life in years	7.4	4.5
Dividend yield	3.7%	3.5%

Employee Stock Purchase Plan

Total pre-tax share-based compensation expense charged against income for the three month periods ended March 31, 2011 and 2010 for options granted under our Employee Stock Purchase Plan (ESPP) was $93,000 and $74,000, respectively. It is estimated, at this time, that the expense attributable to such share-based payments in each of the subsequent quarters of 2011 will approximate the amount recorded in the 2011 first quarter. However, such future expense related to our ESPP will be impacted by, and be dependent on the change in our stock price over the remaining period up to the December 31, 2011 measurement date.

Such expense was estimated on the date of grant using the Black-Scholes valuation model with the following weighted average assumptions:

	2011	2010
Risk-free interest rate	0.04%	0.2%
Expected volatility	25.0%	34.0%
Weighted average expected life in years	1.0	1.0
Dividend yield	3.7%	3.5%

We may issue new common stock or re-issue common stock from treasury to satisfy our obligations under any of our share-based compensation plans.

Note 9 Related Party Transactions

The brother of a director (Related Party) has ownership interests in several different facilities which had entered into service agreements with us. In the three month period ended March 31, 2011, we did not have any active services agreements with these facilities. For the three month period ended March 31, 2010, the service agreements with these facilities in which the Related Party had ownership interests resulted in revenues of approximately $1,096,000. At December 31, 2010, accounts receivable from these Related Party facilities of $750,000 are included in the accompanying consolidated balance sheet; during the three month period ended March 31, 2011, we wrote off such accounts receivable due from the Related Party due to the completion of these facilities bankruptcy proceedings and, accordingly, do not have any outstanding receivables from the Related Party as of March 31, 2011.

Another of our directors is a member of a law firm which was retained by us. In each of the three month periods ended March 31, 2011 and 2010, fees received from us by such firm did not exceed $100,000. Additionally, such fees did not exceed, in either three month period, 5% of such firm s revenues.

Table of Contents

Note 10 Income Taxes

For the three month period ended March 31, 2011, our effective tax rate was 37.0%, a decrease from the 38.5% effective tax rate for the comparable 2010 period. Such differences between the effective tax rates and the applicable U.S. federal statutory rate arise primarily from the effect of state and local income taxes and tax credits available to the Company. The decrease in the effective tax rate is primarily due to an increase in expected tax credits realized for 2011 compared to previous fiscal periods. The Company may realize a significant tax credit during 2011 from the New Hire Retention Credit, a one-time general business credit at the Federal level that was authorized by the Hiring Incentives to Restore Employment Act of 2010. The new hire retention credit allows an employer a credit of up to $1,000 for each eligible worker that was retained for at least 52 consecutive weeks of qualified employment. The Company has earned an immaterial amount for the three month period ended March 31, 2011, but due to the eligibility requirements, cannot reasonably estimate the expected amount of the credit to be realized for the remainder of the year. If a significant amount of the credit is earned in 2011, our effective tax rate could be reduced below 37.0%.

We account for income taxes using the asset and liability method, which results in recognizing income tax expense based on the amount of income taxes payable or refundable for the current year. Additionally, we evaluate regularly the tax positions taken or expected to be taken resulting from financial statement recognition of certain items. Based on our evaluation, we have concluded that there are no significant uncertain tax positions requiring recognition in our financial statements. Our evaluation was performed for the tax years ended December 31, 2007 through 2010 (with regard to U.S. federal income tax returns) and December 31, 2006 through 2010 (with regard to various state and local income tax returns), the tax years which remain subject to examination by major tax jurisdictions as of March 31, 2011.

We may from time to time be assessed interest or penalties by taxing jurisdictions, although any such assessments historically have been minimal and immaterial to our financial results. When we have received an assessment for interest and/or penalties, it has been classified in the financial statements as selling, general and administrative expense.

Note 11 Subsequent Event

We evaluated all subsequent events through the date these financial statements are being filed with the SEC. There were no events or transactions occurring during this subsequent event reporting period which require recognition or disclosure in the financial statements.

Table of Contents

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

Cautionary Statement Regarding Forward Looking Statements

This report and documents incorporated by reference into this report contain 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 (the Exchange Act), as amended, which are not historical facts but rather are based on current expectations, estimates and projections about our business and industry, our beliefs and assumptions. Words such as believes , anticipates , plans , expects , will , goal , and similar expressions are intended to identify forward-looking statemen inclusion of forward-looking statements should not be regarded as a representation by us that any of our plans will be achieved. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Such forward looking information is also subject to various risks and uncertainties. Such risks and uncertainties include, but are not limited to, risks arising from our providing services exclusively to the health care industry, primarily providers of long-term care; proposed and enacted legislation and/or regulations to reform the U.S. healthcare system in an effort to contain healthcare costs; credit and collection risks associated with this industry; one client accounting for approximately 10% of revenues in the three month period ended March 31, 2011 - (see note 5, Segment Information Major Client in the accompanying Notes to Consolidated Financial Statements); our claims experience related to workers compensation and general liability insurance; the effects of changes in, or interpretations of laws and regulations governing the industry, our workforce and services provided, including state and local regulations pertaining to the taxability of our services; and the risk factors described in Part I of our Form 10-K for the year ended December 31, 2010 (the 2010 10-K) under Government Regulation of Clients , Competition , Service Agreements/Collections , and under Item IA of the 2010 10-K, Risl Factors . Many of our clients revenues are highly contingent on Medicare and Medicaid reimbursement funding rates, which Congress has affected through the enactment of a number of major laws during the past decade, most recently the March 2010 enactment of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (together, the Act). Currently, the U.S. Congress is considering further changes in legislation relating to health care in the United States which, among other initiatives, may impose cost containment measures impacting our clients. These enacted and proposed laws have significantly altered, or threaten to alter, overall government reimbursement funding rates and mechanisms. In addition, further adverse economic conditions could adversely affect such funding. The overall effect of these laws and trends in the long-term care industry has affected and could adversely affect the liquidity of our clients, resulting in their inability to make payments to us on agreed-upon payment terms. These factors, in addition to delays in payments from clients, have resulted in, and could continue to result in, significant additional bad debts in the near future. Additionally, our operating results would be adversely affected if unexpected increases in the costs of labor and labor related costs, materials, supplies and equipment used in performing services could not be passed on to our clients.

In addition, we believe that to improve our financial performance we must continue to obtain service agreements with new clients, provide new services to existing clients, achieve modest price increases on current service agreements with existing clients and maintain internal cost reduction strategies at our various operational levels. Furthermore, we believe that our ability to sustain the internal development of managerial personnel is an important factor impacting future operating results and successfully executing projected growth strategies.

RESULTS OF OPERATIONS

The following discussion is intended to provide the reader with information that will be helpful in understanding our financial statements including the changes in certain key items in comparing financial statements period to period. We also intend to provide the primary factors that accounted for those changes, as well as a summary of how certain accounting principles affect our financial statements. In addition, we are providing information about the financial results of our two operating segments to further assist in understanding how these segments and their results affect our consolidated results of operations. This discussion should be read in conjunction with our financial statements as of March 31, 2011 and December 31, 2010 and the periods then ended and the notes accompanying those financial statements.

-16-

Table of Contents

Overview

We provide management, administrative and operating expertise and services to the housekeeping, laundry, linen, facility maintenance and dietary service departments of the health care industry, including nursing homes, retirement complexes, rehabilitation centers and hospitals located throughout the United States. We believe that we are the largest provider of housekeeping and laundry management services to the long-term care industry in the United States, rendering such services to approximately 2,550 facilities in 47 states as of March 31, 2011. Although we do not directly participate in any government reimbursement programs, our clients reimbursements are subject to government regulation. Therefore, clients are directly affected by any legislation relating to Medicare and Medicaid reimbursement programs.

We primarily provide our services pursuant to full service agreements with our clients. In such agreements, we are responsible for the day to day management of the department managers and hourly employees located at our clients facilities. We also provide services on the basis of a management-only agreement for a very limited number of clients. Our agreements with clients typically provide for renewable one year service terms, cancelable by either party upon 30 to 90 days notice after the initial 90-day period.

We are organized into two reportable segments; housekeeping, laundry, linen and other services (Housekeeping), and dietary department services (Dietary). At March 31, 2011, Housekeeping is being provided at essentially all of our approximately 2,550 client facilities, generating approximately 75% or $156,437,000 of the total revenues for the three month period ending March 31, 2011. Dietary is being provided to approximately 410 client facilities at March 31, 2011 and contributed approximately 25% or $51,953,000 to the three month period ended March 31, 2011 total revenues.

Housekeeping consists of managing the client s housekeeping department which is principally responsible for the cleaning, disinfecting and sanitizing of patient rooms and common areas of a client s facility, as well as the laundering and processing of the personal clothing belonging to the facility s patients. Also within the scope of this segment s service is the responsibility for laundering and processing of the bed linens, uniforms and other assorted linen items utilized by a client facility.

Dietary consists of managing the client s dietary department which is principally responsible for food purchasing, meal preparation and providing dietician consulting professional services, which includes the development of a menu that meets the patient s dietary needs.

We currently operate one wholly-owned subsidiary, Huntingdon Holdings, Inc. (Huntingdon). Huntingdon invests our cash and cash equivalents, as well as managing our portfolio of available-for-sale marketable securities.

Consolidated Operations

The following table sets forth, for the periods indicated, the percentage which certain items bear to consolidated revenues:

	Relation to Consolidated Revenues For the Quarter Ended March 31,	
	2011	2010
Revenues	100.0%	100.0%
Operating costs and expenses:		
Costs of services provided	86.4%	86.3%
Selling, general and administrative	8.1%	7.6%
Investment and interest	0.3%	0.4%
Income before income taxes	5.8%	6.5%
Income taxes	2.2%	2.5%
Net income	3.6%	4.0%

Subject to the factors noted in the Cautionary Statement Regarding Forward Looking Statements included in this report, we anticipate our financial performance for the remainder of 2011 may be comparable to the percentages presented in the above table as they relate to consolidated revenues.

Housekeeping is our largest and core reportable segment, representing approximately 75% of consolidated revenues for the quarter ended March 31, 2011. Dietary revenues represented approximately 25% of consolidated revenues for such quarter.

Although there can be no assurance thereof, we believe that for the remainder of 2011 each of Housekeeping s and Dietary s revenues, as a percentage of consolidated revenues, will remain approximately the same as their respective percentages noted above. Furthermore, we expect the sources of organic growth for the remainder of 2011 for the respective operating segments will be primarily the same as historically experienced. Accordingly, although there can be no assurance thereof, the growth in Dietary is expected to come from our current Housekeeping client base, while growth in Housekeeping will primarily come from obtaining new clients.

2011 First Quarter Compared with 2010 First Quarter

The following table sets forth 2011 first quarter income statement key components that we use to evaluate our financial performance on a consolidated and reportable segment basis, as well as the percentage increases of each compared to 2010 first quarter amounts. The difference between the reportable segments operating results and other disclosed data and our consolidated financial statements relate primarily to corporate level transactions and recording of transactions at the reportable segment level which use methods other than generally accepted accounting principles.

	Consolidated	% inc./ (dec.)	Corporate and Eliminations	Housekeeping Amount	% inc.	Dietary Amount	% inc.
Revenues	$ 208,390,000	13.4%	$ 271,000	$ 156,462,000	11.0%	$ 51,657,000	20.3%
Cost of services provided	179,985,000	13.5	(7,470,000)	139,267,000	0.1	48,188,000	0.2
Selling, general and administrative	16,780,000	20.7	16,780,000				
Investment and interest income	714,000	(4.8)	714,000				
Income before income taxes	$ 12,339,000	2.2%	(8,325,000)	$ 17,195,000	15.7%	$ 3,469,000	58.4%

Revenues

Consolidated

Consolidated revenues increased 13.4% to $208,390,000 in the 2011 first quarter compared to $183,801,000 in the 2010 first quarter as a result of the factors discussed below under Reportable Segments.

Our Major Client accounted for approximately 10% and 11%, respectively, of consolidated revenues in the three month periods ended March 31, 2011 and 2010, respectively. The loss of such client would have a material adverse effect on the results of operations of our two operating segments. In addition, if such client changes its payment terms it would increase our accounts receivable balance and have a material adverse effect on our cash flows and cash and cash equivalents.

Reportable Segments

Housekeeping s 11.0% net growth in reportable segment revenues resulted primarily from an increase in revenues attributable to service agreements entered into with new clients.

Dietary s 20.3% net growth in reportable segment revenues is primarily a result of providing this service to existing Housekeeping clients.

We derived 11% and 6%, respectively, of Housekeeping and Dietary s 2011 first quarter revenues from our Major Client.

Costs of services provided

Consolidated

Cost of services provided, on a consolidated basis, as a percentage of consolidated revenues for the 2011 first quarter remained essentially unchanged at 86.4% from the 86.3% recognized in the corresponding 2010 quarter. The following table provides a comparison of the primary cost of services provided-key indicators that we manage on a consolidated basis in evaluating our financial performance. In addition, see the discussion below on Reportable Segments which provides additional details to explain the slight increase in consolidated costs of services provided.