ENSIGN GROUP, INC
Form 10-Q
May 04, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2011.

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

For the transition period from to .

Commission file number: 001-33757

THE ENSIGN GROUP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	33-0861263
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

27101 Puerta Real, Suite 450
Mission Viejo, CA 92691
(Address of Principal Executive Offices and Zip Code)
(949) 487-9500
(Registrant's Telephone Number, Including Area Code)
N/A
(Former Name, Former Address and Former Fiscal Year, 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. x Yes o 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 (§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). o Yes o No

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

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

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

As of April 30, 2011, 20,903,105 shares of the registrant's common stock were outstanding.

THE ENSIGN GROUP, INC.
QUARTERLY REPORT ON FORM 10-Q
FOR THE THREE MONTHS ENDED MARCH 31, 2011
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Part I. Financial Information

Item 1. Financial Statements

THE ENSIGN GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par values)
(Unaudited)

	March 31, 2011	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	$50,973	$72,088
Accounts receivable—less allowance for doubtful accounts of $10,856 and $9,793 at March 31, 2011 and December 31, 2010, respectively	76,474	69,437
Prepaid income taxes	—	1,333
Prepaid expenses and other current assets	7,661	7,175
Deferred tax asset—current	8,696	9,975
Total current assets	143,804	160,008
Property and equipment, net	311,372	262,527
Insurance subsidiary deposits and investments	15,751	16,358
Escrow deposits	—	14,422
Deferred tax asset	5,973	4,987
Restricted and other assets	8,665	6,509
Intangible assets, net	4,427	4,070
Goodwill	10,339	10,339
Other indefinite-lived intangibles	672	672
Total assets	$501,003	$479,892
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$20,027	$17,897
Accrued wages and related liabilities	33,191	37,377
Accrued self-insurance liabilities—current	12,742	11,480
Income taxes payable	6,152	—
Other accrued liabilities	13,445	13,557
Current maturities of long-term debt	3,165	3,055
Total current liabilities	88,722	83,366
Long-term debt—less current maturities	138,656	139,451
Accrued self-insurance liabilities—less current portion	29,019	25,920
Deferred rent and other long-term liabilities	2,663	2,952
Commitments and contingencies (Note 14)		
Stockholders' equity:		
Common stock; $0.001 par value; 75,000 shares authorized; 21,462 and 20,898 shares issued and outstanding at March 31, 2011, respectively, and 21,397 and 20,815 shares issued and outstanding at December 31, 2010, respectively	21	21
Additional paid-in capital	72,861	70,814
Retained earnings	172,757	161,168
	(3,696)	(3,800)

Common stock in treasury, at cost, 564 and 582 shares at March 31, 2011 and December 31, 2010, respectively		
Total stockholders’ equity	241,943	228,203
Total liabilities and stockholders’ equity	$501,003	$479,892

See accompanying notes to condensed consolidated financial statements.

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THE ENSIGN GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except per share data)
(Unaudited)

	Three Months Ended March 31,	
	2011	2010
Revenue	$182,943	$154,174
Expense:		
Cost of services (exclusive of facility rent and depreciation and amortization shown separately below)	143,155	123,183
Facility rent—cost of services	3,616	3,575
General and administrative expense	7,401	5,774
Depreciation and amortization	5,059	3,955
Total expenses	159,231	136,487
Income from operations	23,712	17,687
Other income (expense):		
Interest expense	(2,727)	(2,280)
Interest income	55	67
Other expense, net	(2,672)	(2,213)
Income before provision for income taxes	21,040	15,474
Provision for income taxes	8,294	6,126
Net income	$12,746	$9,348
Net income per share:		
Basic	$0.61	$0.45
Diluted	$0.59	$0.44
Weighted average common shares outstanding:		
Basic	20,854	20,686
Diluted	21,516	21,074

See accompanying notes to condensed consolidated financial statements.

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THE ENSIGN GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended March 31,	
	2011	2010
Cash flows from operating activities:		
Net income	$12,746	$9,348
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,059	3,955
Amortization of deferred financing fees and debt discount	168	191
Deferred income taxes	294	(715)
Provision for doubtful accounts	2,227	1,550
Stock-based compensation	831	649
Excess tax benefit from share based compensation	(441)	(333)
Loss on disposition of property and equipment	(3)	21
Change in operating assets and liabilities		
Accounts receivable	(9,264)	(8,316)
Prepaid income taxes	1,333	1,242
Prepaid expenses and other current assets	502	632
Insurance subsidiary deposits and investments	607	(175)
Accounts payable	1,236	(419)
Accrued wages and related liabilities	(4,186)	(1,388)
Income taxes payable	6,592	—
Other accrued liabilities	(119)	2,149
Accrued self-insurance	1,396	1,481
Deferred rent liability	(289)	453
Net cash provided by operating activities	18,689	10,325
Cash flows from investing activities:		
Purchase of property and equipment	(9,001)	(6,415)
Cash payment for business acquisitions	(37,074)	(7,617)
Cash payment for asset acquisitions	(7,339)	—
Escrow deposits	—	(500)
Escrow deposits used to fund business acquisitions	14,422	7,595
Cash proceeds from the sale of fixed assets	51	58
Restricted and other assets	(278)	1
Net cash used in investing activities	(39,219)	(6,878)
Cash flows from financing activities:		
Payments on long term debt	(715)	(542)
Issuance of treasury stock upon exercise of options	103	132
Issuance of common stock upon exercise of options	775	264
Dividends paid	(1,150)	(1,032)
Excess tax benefit from share based compensation	441	333
Payments of deferred financing costs	(39)	(5)
Net cash used in financing activities	(585)	(850)
Net decrease in cash and cash equivalents	(21,115)	2,597
Cash and cash equivalents beginning of period	72,088	38,855

Cash and cash equivalents end of period	$50,973	41,452
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$2,900	$2,222
Income taxes	$7,870	$6,065
Accrued capital expenditures	$895	$—

See accompanying notes to condensed consolidated financial statements.

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THE ENSIGN GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars and shares in thousands, except per share data)
(Unaudited)

1. DESCRIPTION OF BUSINESS

The Company — The Ensign Group, Inc., through its subsidiaries (collectively, Ensign or the Company), provides skilled nursing and rehabilitative care services through the operation of 86 facilities and one home health and hospice operation as of March 31, 2011, located in California, Arizona, Texas, Washington, Utah, Colorado and Idaho. All of these facilities are skilled nursing facilities, other than five stand-alone assisted living facilities in California, Arizona, Texas and Colorado and seven campuses that offer both skilled nursing and assisted living services located in California, Texas, Arizona and Utah. The Company's facilities, each of which strives to be the facility of choice in the community it serves, provide a broad spectrum of skilled nursing and assisted living services, physical, occupational and speech therapies, and other rehabilitative and healthcare services, for both long-term residents and short-stay rehabilitation patients. The Company's facilities have a collective capacity of approximately 10,300 operational skilled nursing, assisted living and independent living beds. As of March 31, 2011, the Company owned 57 of its 86 facilities and operated an additional 29 facilities through long-term lease arrangements, and had options to purchase 8 of those 29 facilities.

The Ensign Group, Inc. is a holding company with no direct operating assets, employees or revenue. All of the Company's facilities are operated by separate, wholly-owned, independent subsidiaries, each of which has its own management, employees and assets. One of the Company's wholly-owned subsidiaries, referred to as the Service Center, provides centralized accounting, payroll, human resources, information technology, legal, risk management and other centralized services to the other operating subsidiaries through contractual relationships with such subsidiaries. The Company also has a wholly-owned captive insurance subsidiary (the Captive) that provides some claims-made coverage to the Company's operating subsidiaries for general and professional liability, as well as coverage for certain workers' compensation insurance liabilities.

Like the Company's facilities, the Service Center and the Captive are operated by separate, wholly-owned, independent subsidiaries that have their own management, employees and assets. References herein to the consolidated "Company" and "its" assets and activities, as well as the use of the terms "we," "us," "our" and similar verbiage in this quarterly report is not meant to imply that The Ensign Group, Inc. has direct operating assets, employees or revenue, or that any of the facilities, the Service Center or the Captive are operated by the same entity.

Other Information — The accompanying condensed consolidated financial statements as of March 31, 2011 and for the three months ended March 31, 2011 and 2010 (collectively, the Interim Financial Statements), are unaudited. Certain information and footnote disclosures normally included in annual consolidated financial statements have been condensed or omitted, as permitted under applicable rules and regulations. Readers of the Interim Financial Statements should refer to the Company's audited consolidated statements and notes thereto for the year ended December 31, 2010 which are included in the Company's annual report on Form 10-K, File No. 001-33757 (the Annual Report) filed with the Securities and Exchange Commission (the SEC). Management believes that the Interim Financial Statements reflect all adjustments which are of a normal and recurring nature necessary to present fairly the Company's financial position and results of operations in all material respects. The results of operations presented in the Interim Financial Statements are not necessarily representative of operations for the entire year.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation — The accompanying Interim Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The Company is the sole member or shareholder of various consolidated limited liability companies and corporations; each established to operate various acquired skilled nursing and assisted living facilities. All intercompany transactions and balances have been eliminated in consolidation.

Estimates and Assumptions — The preparation of Interim Financial Statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods. The most significant estimates in the Company’s Interim Financial Statements relate to revenue, allowance for doubtful accounts, intangible assets and goodwill, impairment of long-lived assets, general and professional liability, worker’s compensation, and healthcare claims included in accrued self-insurance liabilities and income taxes. Actual results could differ from those estimates.

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Business Segments — The Company has a single reportable segment — long-term care services, which includes the operation of skilled nursing and assisted living facilities, home health, and related ancillary services. The Company's single reportable segment is made up of several individual operating segments grouped together principally based on their geographical locations within the United States. Based on the similar economic and other characteristics of each of the operating segments, management believes the Company meets the criteria for aggregating its operating segments into a single reporting segment.

Fair Value of Financial Instruments — The Company's financial instruments consist principally of cash and cash equivalents, debt security investments, accounts receivable, insurance subsidiary deposits, accounts payable and borrowings. The Company believes all of the financial instruments' recorded values approximate fair values because of their nature and respective short durations. The Company's fixed-rate debt instruments do not actively trade in an established market. The fair values of this debt are estimated by discounting the principal and interest payments at rates available to the Company for debt with similar terms and maturities. See further discussion of debt security investments at Note 4.

Revenue Recognition — The Company recognizes revenue when the following four conditions have been met: (i) there is persuasive evidence that an arrangement exists; (ii) delivery has occurred or service has been rendered; (iii) the price is fixed or determinable; and (iv) collection is reasonably assured. Revenue from the Medicare and Medicaid programs accounted for approximately 76% of the Company's revenue for the three months ended March 31, 2011 and 2010. The Company records revenue from these governmental and managed care programs as services are performed at their expected net realizable amounts under these programs. The Company's revenue from governmental and managed care programs is subject to audit and retroactive adjustment by governmental and third-party agencies. Consistent with healthcare industry accounting practices, any changes to these governmental revenue estimates are recorded in the period the change or adjustment becomes known based on final settlements. The Company recorded retroactive adjustments that increased revenue by $546 and $315 for the three months ended March 31, 2011 and 2010, respectively.

The Company's service specific revenue recognition policies are as follows:

Skilled Nursing Revenue

The Company's revenue is derived primarily from providing long-term healthcare services to residents and is recognized on the date services are provided at amounts billable to individual residents. For residents under reimbursement arrangements with third-party payors, including Medicaid, Medicare and private insurers, revenue is recorded based on contractually agreed-upon amounts on a per patient, daily basis. The Company records revenue from private pay patients, at the agreed upon rate, as services are performed.

Home Health and Hospice Revenue Recognition

Episodic Based Revenue — Net service revenue is typically recorded on a 60-day episode payment rate. The Company makes adjustments to revenue on completed episodes to reflect differences between estimated and actual payment amounts, an inability to obtain appropriate billing documentation or authorizations acceptable to the payor and other reasons unrelated to credit risk. The Company records an estimate for the impact of such payment adjustments based on its historical experience. In addition to revenue recognized on completed episodes, the Company also recognizes a portion of revenue associated with episodes in progress. Episodes in progress are 60-day episodes of care that begin during the reporting period, but were not completed as of the end of the period. The Company estimates this revenue on a monthly basis based upon historical trends. The primary factors underlying this estimate are the number of episodes in progress at the end of the reporting period, expected Medicare revenue per episode and the Company's estimate of the average percentage complete based on days completed of the episode of care.

Non-episodic Based Revenue — Gross revenue is recorded on an accrual basis based upon the date of service at amounts equal to our established or estimated per-visit rates, as applicable.

Hospice Revenue — Gross revenue is recorded on an accrual basis based upon the date of service at amounts equal to the estimated payment rates. The estimated payment rates are daily rates for each of the levels of care we deliver. The

Company makes adjustments to revenue for an inability to obtain appropriate billing documentation or authorizations acceptable to the payor and other reasons unrelated to credit risk. The Company estimates the impact of these adjustments based on its historical experience, which primarily includes historical collection rates on Medicare claims, and records it during the period services are rendered as an estimated revenue adjustment and as a reduction to its outstanding patient accounts receivable. Additionally, as Medicare hospice revenue is subject to an inpatient cap limit and an overall payment cap, the Company monitors its provider numbers and estimate amounts due back to Medicare if a cap has been exceeded. The Company records these adjustments as a reduction to revenue and increases other accrued liabilities.

Accounts Receivable — Accounts receivable consist primarily of amounts due from Medicare and Medicaid programs, other government programs, managed care health plans and private payor sources. Estimated provisions for doubtful accounts are recorded to the extent it is probable that a portion or all of a particular account will not be collected.

In evaluating the collectability of accounts receivable, the Company considers a number of factors, including the age of the accounts, changes in collection patterns, the composition of patient accounts by payor type and the status of ongoing disputes with third-party payors. The percentages applied to the aged receivable balances are based on the Company's historical experience and time limits, if any, for managed care, Medicare and Medicaid. The Company periodically refines its procedures for estimating the allowance for doubtful accounts based on experience with the estimation process and changes in circumstances.

Property and Equipment — Property and equipment are initially recorded at their historical cost. Repairs and maintenance are expensed as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the depreciable assets (ranging from three to 30 years). Leasehold improvements are amortized on a straight-line basis over the shorter of their estimated useful lives or the remaining lease term.

Impairment of Long-Lived Assets — The Company reviews the carrying value of long-lived assets that are held and used in the Company's operations for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of these assets is determined based upon expected undiscounted future net cash flows from the operations to which the assets relate, utilizing management's best estimate, appropriate assumptions, and projections at the time. If the carrying value is determined to be unrecoverable from future operating cash flows, the asset is deemed impaired and an impairment loss would be recognized to the extent the carrying value exceeded the estimated fair value of the asset. The Company estimates the fair value of assets based on the estimated future discounted cash flows of the asset. Management has evaluated its long-lived assets and has not identified any impairment during the three months ended March 31, 2011 or 2010.

Intangible Assets and Goodwill — Intangible assets consist primarily of favorable lease, lease acquisition costs, patient base, trade names and other indefinite-lived intangibles. Favorable leases and lease acquisition costs are amortized over the life of the lease of the facility, typically ranging from ten to 20 years. Patient base is amortized over a period of three to eight months, depending on the classification of the patients and the level of occupancy in a new acquisition on the acquisition date. Trade names at facilities are amortized over 30 years.

Goodwill represents the excess of the purchase price over the fair value of identifiable net assets acquired in business combinations. Goodwill is subject to annual testing for impairment. In addition, goodwill is tested for impairment if events occur or circumstances change that would reduce the fair value of a reporting unit below its carrying amount. The Company defines reporting units as the individual facilities. The Company performs its annual test for impairment during the fourth quarter of each year. The Company did not record any impairment charges during the three months ended March 31, 2011.

Self-Insurance — The Company is partially self-insured for general and professional liability up to a base amount per claim (the self-insured retention) with an aggregate, one time deductible above this limit. Losses beyond these amounts are insured through third-party policies with coverage limits per occurrence, per location and on an aggregate basis for the Company. For claims made after April 1, 2011, the combined self-insured retention was $500 per claim with an aggregate $1,750 deductible limit. For all facilities, except those located in Colorado, the third-party coverage above these limits was $1,000 per occurrence, $3,000 per facility, with a $10,000 blanket aggregate and an additional state-specific aggregate where required by state law. In Colorado, the third-party coverage above these limits was $1,000 per occurrence and $3,000 per facility, which is independent of the $10,000 blanket aggregate applicable to our other 82 facilities.

The self-insured retention and deductible limits for general and professional liability and worker's compensation are self-insured through the Captive, the related assets and liabilities of which are included in the accompanying Interim Financial Statements. The Captive is subject to certain statutory requirements as an insurance provider. These requirements include, but are not limited to, maintaining statutory capital. The Company’s policy is to accrue amounts equal to the actuarially estimated costs to settle open claims of insureds, as well as an estimate of the cost of insured claims that have been incurred but not reported. The Company develops information about the size of the ultimate claims based on historical experience, current industry information and actuarial analysis, and evaluates the estimates for claim loss exposure on a quarterly basis. Accrued general liability and professional malpractice liabilities recorded on an undiscounted basis in the accompanying condensed consolidated balance sheets were $27,423 and $26,037 as of March 31, 2011 and December 31, 2010, respectively.

The Company's operating subsidiaries are self-insured for workers' compensation liability in California. To protect itself against loss exposure in California with this policy, the Company has purchased individual stop-loss insurance coverage that insures individual claims that exceed $500 for each claim. In Texas, the operating subsidiaries have elected non-subscriber status for workers' compensation claims and, effective February 1, 2011, the Company has purchased individual stop-loss coverage that insures individual claims that exceed $750 for each claim. The Company's operating subsidiaries in other states have third party guaranteed cost coverage. In California and Texas, the Company accrues amounts equal to the estimated costs to settle open claims, as well as an estimate of the cost of claims that have been incurred but not reported. The Company uses actuarial valuations to estimate the liability based on historical experience and industry information. Accrued workers' compensation liabilities are recorded on an undiscounted basis in the accompanying condensed consolidated balance sheets and were $9,332 and $9,203 as of March 31, 2011 and December 31, 2010, respectively.

The Company provides self-insured medical (including prescription drugs) and dental healthcare benefits to the majority of its employees. The Company is fully liable for all financial and legal aspects of these benefit plans. To protect itself against loss exposure with this policy, the Company has purchased individual stop-loss insurance coverage that insures individual claims that exceed $250 for each covered person with an aggregate individual stop loss deductible of $75. These limits reset every plan year subject to a lifetime maximum of $5,000 per each covered person on the Preferred Provider Organization (PPO) and Exclusive Provider Organization (EPO) plans and an unlimited lifetime plan maximum on the Health Maintenance Organization (HMO) plan. The aforementioned coverage only applies to claims paid during the plan year. The Company's accrued liability under these plans recorded on an undiscounted basis in the accompanying condensed consolidated balance sheets was $2,041 and $2,160 at March 31, 2011 and December 31, 2010, respectively.

In addition, in accordance with guidance provided by the Financial Accounting Standards Board (FASB) in August 2010, the Company recorded an asset and equal liability of $2,965, in order to present the ultimate costs of malpractice claims and the anticipated insurance recoveries on a gross basis. Prior to fiscal year 2011, these liabilities were recorded net of anticipated insurance recoveries. See additional discussion in "Adoption of New Accounting Pronouncements" below.

The Company believes that adequate provision has been made in the Interim Financial Statements for liabilities that may arise out of patient care, workers' compensation, healthcare benefits and related services provided to date. The amount of the Company's reserves was determined based on an estimation process that uses information obtained from both company-specific and industry data. This estimation process requires the Company to continuously monitor and evaluate the life cycle of the claims. Using data obtained from this monitoring and the Company's assumptions about emerging trends, the Company, with the assistance of an independent actuary, develops information about the size of ultimate claims based on the Company's historical experience and other available industry information. The most significant assumptions used in the estimation process include determining the trend in costs, the expected cost of claims incurred but not reported and the expected costs to settle or pay damage awards with respect to unpaid claims. The self-insured liabilities are based upon estimates, and while management believes that the estimates of loss are reasonable, the ultimate liability may be in excess of or less than the recorded amounts. Due to the inherent volatility of actuarially determined loss estimates, it is reasonably possible that the Company could experience changes in estimated losses that could be material to net income. If the Company's actual liability exceeds its estimates of loss, its future earnings and financial condition would be adversely affected.

Income Taxes — Deferred tax assets and liabilities are established for temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities at tax rates in effect when such temporary differences are expected to reverse. The Company generally expects to fully utilize its deferred tax assets; however, when necessary, the Company records a valuation allowance to reduce its net deferred tax assets to the amount that is more likely than not to be realized.

In determining the quarterly income tax rate for financial statements, the Company must consider expected annual income, permanent differences between financial reporting and tax recognition of income or expense and other factors. When the Company takes uncertain income tax positions that do not meet the recognition criteria, it records a liability for underpayment of income taxes and related interest and penalties, if any. In considering the need for and magnitude of a liability for such positions, the Company must consider the potential outcomes from a review of the positions by the taxing authorities

In determining the need for a valuation allowance, the annual income tax rate for interim periods, or the need for and magnitude of liabilities for uncertain tax positions, the Company makes certain estimates and assumptions. These estimates and assumptions are based on, among other things, knowledge of operations, markets, historical trends and likely future changes and, when appropriate, the opinions of advisors with knowledge and expertise in certain fields. Due to certain risks associated with the Company's estimates and assumptions, actual results could differ.

Stock-Based Compensation — The Company measures and recognizes compensation expense for all share-based payment awards made to employees and directors including employee stock options based on estimated fair values, ratably over the requisite service period of the award. Net income has been reduced as a result of the recognition of the fair value of all stock options and restricted stock awards issued on and subsequent to January 1, 2006, the amount of which is contingent upon the number of future grants and other variables.

New Accounting Pronouncements — In December, 2010, the FASB amended its view on performing step two of a goodwill impairment analysis. The amendment does not prescribe a specific method of calculating the carrying value of a reporting unit in the performance of step one of the goodwill impairment test and requires entities with a zero or negative carrying value to assess, considering qualitative factors such as those listed in Accounting Standards Codification (ASC) 350-20-35-30 Intangibles - Goodwill and Other, whether it is more likely than not that a goodwill impairment exists. If an entity concludes that it is more likely than not that a goodwill impairment exists, the entity must perform step two of the goodwill impairment test. For public entities, these amendments are effective for impairment tests performed during entities' fiscal years that begin after December 15, 2010. The Company will adopt this amendment during it's goodwill impairment analysis in the fourth quarter of the current year. The Company does not believe the adoption of this amendment will have a material effect on its financial statements.
Adoption of New Accounting Pronouncements — In August 2010, the Financial Accounting Standards Board clarified that health care entities should not net insurance recoveries against related claim liability. Further, such entities should determine the claim liability without considering insurance recoveries. Further, it was determined a cumulative-effect adjustment should be recognized in opening retained earnings in the period of adoption if a difference exists between any liabilities and insurance receivables recorded as a result of applying these amendments. These amendments are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2010. The Company adopted this guidance during the quarter ended March 31, 2011. See further discussion in Note 2 to the Condensed Consolidated Financial Statements under "Self-Insurance."

In November 2010, the FASB provided clarification regarding pro forma revenue and earnings disclosure requirements for business combinations. These amendments specify that if a public entity presents comparative financial statements, the entity should disclose only revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year has occurred as of the beginning of the comparable prior annual reporting period. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period on or after December 15, 2010. The Company adopted these amendments on January 1, 2011, noting they did not have a material impact on the Company's financial statements.

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3. COMPUTATION OF NET INCOME PER COMMON SHARE

Basic net income per share is computed by dividing net income attributable to common shares by the weighted average number of outstanding common shares for the period. The computation of diluted net income per share is similar to the computation of basic net income per share except that the denominator is increased to include contingently returnable shares and the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued.

A reconciliation of the numerator and denominator used in the calculation of basic net income per common share follows:

	Three Months Ended March 31,	
	2011	2010
Numerator:		
Net income	$12,746	$9,348
Denominator:		
Weighted average shares outstanding for basic net income per share	20,854	20,686
Basic net income per common share	$0.61	$0.45

A reconciliation of the numerator and denominator used in the calculation of diluted net income per common share follows:

	Three Months Ended March 31,	
	2011	2010
Numerator:		
Net income	$12,746	$9,348
Denominator:		
Weighted average common shares outstanding	20,854	20,686
Plus: incremental shares from assumed conversion (1)	662	388
Adjusted weighted average common shares outstanding	21,516	21,074
Diluted net income per common share	$0.59	$0.44

(1) For the three months ended March 31, 2011 and 2010, the Company had 9 and 776, respectively, options outstanding which are anti-dilutive and therefore not factored into the weighted average common shares amount above.

4. INSURANCE SUBSIDIARY DEPOSITS AND INVESTMENTS

On February 10, 2009, the Company purchased three separate AAA rated debt security investments for an aggregate purchase price of $12,183 with insurance subsidiary deposits and cash from the Captive. The debt securities had maturity dates in December 2010, July 2011 and December 2011 and were guaranteed by the Federal Deposit Insurance Corporation (FDIC) under the Temporary Liquidity Guarantee Program upon maturity.

On December 1, 2010, the first of the three debt security investments matured and the funds of $4,000 were reinvested in a new debt security which matures on June 8, 2012. The new debt security investment is also AAA rated, and is backed by the FDIC.

At March 31, 2011, the Company had approximately $12,095 in debt security investments, which are held to maturity and carried at amortized cost. The fair value of the investments is determined based on “Level 1” inputs, which consist of unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets. The carrying value of the debt securities approximates fair value. The Company has the intent and the ability to hold these debt securities to maturity.

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THE ENSIGN GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

5. REVENUE AND ACCOUNTS RECEIVABLE

Revenue for the three months ended March 31, 2011 and 2010 is summarized in the following tables:

	Three Months Ended March 31,					
	2011			2010		
	Revenue	% of Revenue		Revenue	% of Revenue	
Medicaid	$66,225	36.2	%	$61,653	40.0	%
Medicare	67,643	37.0	%	51,122	33.2	%
Medicaid — skilled	4,411	2.4	%	4,418	2.8	%
Total Medicaid and Medicare	138,279	75.6	%	117,193	76.0	%
Managed care	24,141	13.2	%	20,569	13.4	%
Private and other payors	20,523	11.2	%	16,412	10.6	%
Revenue	$182,943	100.0	%	$154,174	100.0	%

Accounts receivable as of March 31, 2011 and December 31, 2010 is summarized in the following table:

	March 31, 2011		December 31, 2010	
Medicaid	$22,234		$20,712	
Managed care	24,046		22,764	
Medicare	26,913		22,826	
Private and other payors	14,137		12,928	
	87,330		79,230	
Less allowance for doubtful accounts	(10,856	)	(9,793	)
Accounts receivable	$76,474		$69,437	

6. ACQUISITIONS

The Company’s acquisition policy is generally to purchase or lease facilities to complement the Company’s existing portfolio of long-term care facilities. The results of all the Company’s operations are included in the accompanying Interim Financial Statements subsequent to the date of acquisition. Acquisitions are typically paid for in cash and are accounted for using the acquisition method of accounting. Where the Company enters into facility lease agreements, the Company typically does not pay any material amount to the prior facility operator nor does the Company acquire any assets or assume any liabilities, other than rights and obligations under the lease and operations transfer agreement, as part of the transaction. Some leases include options to purchase the facilities. As a result, from time to time, the Company will acquire facilities that the Company has been operating under third-party leases.

During the three months ended March 31, 2011, the Company acquired two skilled nursing facilities which also offer assisted living and independent living services, one independent living facility and one assisted living facility. The aggregate purchase price of the three business acquisitions was approximately $37,074, which was paid in cash. The facilities acquired during the three months ended March 31, 2011 are as follows:

- On January 1, 2011, the Company purchased one skilled nursing facility which also offers assisted living and independent living services and one independent living facility in Texas for approximately $14,580 which was paid in cash. This acquisition added 123 operational skilled nursing beds, 77 assisted living units, 72 independent living units and 20 independent living cottages to the Company's operations. The Company also entered into a separate operations transfer agreement with the prior tenant as part of this transaction.

- On February 1, 2011, the Company purchased one skilled nursing facility in Utah, which also offers assisted living and independent living services for approximately $16,569 which was paid in cash. This acquisition added 233 operational skilled nursing beds, 48 assisted living units and 68 independent living apartments to the Company's operations. The Company also entered into a separate operations transfer agreement with the prior tenant as part of this transaction.

- On March 18, 2011, the Company purchased one assisted living facility in California for approximately $5,925, which was paid in cash. This acquisition added 125 assisted living units to the Company's operations. The Company also entered into a separate operations transfer agreement with the prior tenant as part of this transaction.

In addition, the Company purchased the underlying assets of one of its skilled nursing facilities in Ventura, California as part of the March 18 transaction. The facility was purchased for approximately $7,339, which was paid in cash. This acquisition did not impact the Company's operational skilled nursing bed count.

The Company expensed $71 in acquisition related costs during the three months ended March 31, 2011.

The table below presents the allocation of the purchase price for the facilities acquired in business combinations during the three months ended March 31, 2011 and 2010:

	March 31, 2011	2010
Land	$4,905	$841
Building and improvements	30,503	6,387
Equipment, furniture, and fixtures	1,016	289
Other intangible assets	650	100
	$37,074	$7,617

The Company’s acquisition strategy has been focused on identifying both opportunistic and strategic acquisitions within its target markets that offer strong opportunities for return on invested capital. The facilities acquired by the Company are frequently underperforming financially and can have regulatory and clinical challenges to overcome. Financial information, especially with underperforming facilities, is often inadequate, inaccurate or unavailable. Consequently, the Company believes that prior operating results are not meaningful, representative of the Company’s current operating results or indicative of the integration potential of its newly acquired facilities. The four businesses acquired during the three months ended March 31, 2011 were not material acquisitions to the Company individually or in the aggregate. Accordingly, pro forma financial information is not presented. These acquisitions have been included in the March 31, 2011 condensed consolidated balance sheet of the Company, and the operating results have been included in the condensed consolidated statement of income of the Company since the dates the Company gained effective control.

7. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	March 31, 2011	December 31, 2010
Land	$53,611	$46,900
Buildings and improvements	218,433	179,189
Equipment	53,109	47,983
Furniture and fixtures	8,603	8,271
Leasehold improvements	24,558	24,147
Construction in progress	9,370	7,587
	367,684	314,077
Less accumulated depreciation	(56,312)	(51,550)
Property and equipment, net	$311,372	$262,527

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8. INTANGIBLE ASSETS — Net

Intangible Assets	Weighted Average Life (Years)	March 31, 2011 Gross Carrying Amount	Accumulated Amortization	Net	December 31, 2010 Gross Carrying Amount	Accumulated Amortization	Net
Lease acquisition costs	15.5	$910	$ (607)	$303	$910	$ (592)	$318
Favorable lease	20.0	3,573	(534)	3,039	3,573	(482)	3,091
Patient base	0.6	1,428	(948)	480	778	(728)	50
Trade name	30.0	733	(128)	605	733	(122)	611
Total		$6,644	$ (2,217)	$4,427	$5,994	$ (1,924)	$4,070

Amortization expense was $293 and $328 for the three months ended March 31, 2011 and 2010, respectively. Of the $293 in amortization expense incurred during the three months ended March 31, 2011, approximately $220 related to the amortization of patient base intangible assets at recently acquired facilities, which is typically amortized over a period of three to eight months, depending on the classification of the patients and the level of occupancy in a new acquisition on the acquisition date.

Estimated amortization expense for each of the years ending December 31 is as follows:

Year	Amount
2011 (remainder)	$697
2012	291
2013	291
2014	289
2015	269
2016	248
Thereafter	2,342
	$4,427

9. RESTRICTED AND OTHER ASSETS

Restricted and other assets consist primarily of capital reserves and deposits. Capital reserves are maintained as part of the mortgage agreements of the Company and certain of its landlords with the U.S. Department of Housing and Urban Development. These capital reserves are restricted for capital improvements and repairs to the related facilities.

Restricted and other assets consist of the following:

	March 31, 2011	December 31, 2010
Deposits with landlords	$739	$736
Capital improvement reserves with landlords and lenders	3,751	3,477
Debt issuance costs, net	2,197	2,296
Other assets	1,978	—
Restricted and other assets	$8,665	$6,509

Included in Other assets, as of March 31, 2011, are the Company's general and professional liability claims and related anticipated insurance recoveries recorded on a gross rather than net basis in accordance with an Accounting Standards Update issued by the FASB. Prior to fiscal year 2011, insurance claims liabilities were recorded net of anticipated recoveries. This balance represents the long term portion of the insurance claims recoverable asset.

10. OTHER ACCRUED LIABILITIES

Other accrued liabilities consist of the following:

	March 31, 2011	December 31, 2010
Quality assurance fee	$1,478	$1,706
Resident refunds payable	2,792	3,122
Deferred resident revenue	1,132	1,313
Cash held in trust for residents	1,506	1,523
Dividends payable	1,157	1,152
Property taxes	1,097	1,325
Other	4,283	3,416
Other accrued liabilities	$13,445	$13,557

Quality assurance fee represents amounts payable to California, Utah and Idaho in respect of a mandated fee based on resident days. Resident refunds payable includes amounts due to residents for overpayments and duplicate payments. Deferred resident revenue occurs when the Company receives payments in advance of services provided. Cash held in trust for residents reflects monies received from, or on behalf of, residents. Maintaining a trust account for residents is a regulatory requirement and, while the trust assets offset the liability, the Company assumes a fiduciary responsibility for these funds. The cash balance related to this liability is included in other current assets in the accompanying condensed consolidated balance sheets.

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11. INCOME TAXES

The provision for income taxes for the three months ended March 31, 2011 and 2010 is summarized as follows:

	Three Months Ended March 31, 2011	2010
Current:		
Federal	$6,622	$5,771
State	1,378	1,070
	8,000	6,841
Deferred:		
Federal	319	(567)
State	(25)	(148)
	294	(715)
Total	$8,294	$6,126

The Company's deferred tax assets and liabilities as of March 31, 2011 and December 31, 2010 are summarized as follows:

	March 31, 2011	December 31, 2010
Deferred tax assets (liabilities):		
Accrued expenses	$16,048	$15,968
Allowance for doubtful accounts	4,525	4,082
State taxes	—	533
Tax credits	1,039	1,063
Total deferred tax assets	21,612	21,646
State taxes	(640)	—
Depreciation and amortization	(4,791)	(4,973)
Prepaid expenses	(1,512)	(1,711)
Total deferred tax liabilities	(6,943)	(6,684)
Net deferred tax assets	$14,669	$14,962

The Company is not currently under examination by any major income tax jurisdiction. In 2011, the statute of limitations will lapse on the Company's 2006 and 2007 income tax years for state and Federal purposes, respectively; however, the Company does not believe this lapse will significantly impact unrecognized tax benefits for any uncertain tax positions. The Company is not aware of any other event that might significantly impact the balance of unrecognized tax benefits in the next twelve months. The net balance of unrecognized tax benefits was not material to the Interim Financial Statements for the three months ended March 31, 2011 or 2010.

12. DEBT

On December 31, 2010, four of the Company's real estate holding subsidiaries executed a promissory note with RBS Asset Finance, Inc. (RBS) as Lender for an aggregate of $35,000 (RBS Loan). The RBS Loan was secured by Commercial Deeds of Trust, Security Agreements, Assignment of Leases and Rents and Fixture Fillings on the four properties and other related instruments and agreements, including without limitation a promissory note and a Company guaranty. The RBS Loan bears interest at a fixed rate of 6.04%. Amounts borrowed under the RBS Loan may be prepaid starting after the second anniversary of the note subject to prepayment fees of 5.0% of the principal balance on the date of prepayment. These prepayment fees are reduced by 1.0% a year for years three through seven of the loan. The term of the RBS Loan is for seven years, with monthly principal and interest payments commencing on February 1, 2011 and the balance due on January 1, 2018.

Among other things, under the RBS Loan, the Company must maintain compliance with specified financial covenants measured on a quarterly basis, including a minimum debt service coverage ratio, an average occupancy rate and a minimum project yield. The loan documents also include certain additional affirmative and negative covenants, including limitations on the disposition of the Borrowers and the collateral.

On November 6, 2009, the Company finalized the Fourth Amended and Restated Loan Agreement (Amended Term Loan) with General Electric Capital Corporation (GECC) which increased the borrowing capacity of the Amended Term Loan by $40,000, further referred to as the Six Project Loan. The Six Project Loan will mature on September 30, 2014 and is secured by, among other things, a perfected first priority mortgage/deed of trust on the fee simple interest in six of the Company’s skilled nursing facilities (the Property). The Amended Term Loan, which includes both the Ten Project Note (as described below) and the Six Project Loan, is cross collateralized and cross defaulted with the existing Second Amended and Restated Loan and Security Agreement (the Revolver). The interest rate on the loan is calculated at the current five year swap rate on the date of closing plus 585 basis points for half of the loan balance and the three year swap rate on the date of closing plus 585 basis points and thereafter floating at 90-day LIBOR plus 575 basis points, reset monthly and subject to a LIBOR floor of 2.0% for the remaining half of the loan balance. The Amended Term Loan did not modify any of the existing terms of the Ten Project Note.

On October 1, 2009, four subsidiaries of The Ensign Group, Inc. entered into four separate promissory notes with Johnson Land Enterprises, LLC, for an aggregate of $10,000, as a part of the Company’s acquisition of three skilled nursing facilities in Utah. The unpaid balance of principal and accrued interest from these notes is due on September 30, 2019. The notes bear interest at a rate of 6.0% per annum. As a part of this transaction, the Company recorded a discount to the debt balance in the form of imputed interest of $1,218. This amount will be amortized over the term of the promissory notes, or ten years.

In addition, on October 1, 2009, a subsidiary of The Ensign Group, Inc. in West Jordan, Utah assumed the obligation to pay the remaining principal and interest on bonds which were originally sold to finance the construction of the facility. These bonds were assumed as a part of the Company’s acquisition of three skilled nursing facilities in Utah. The unpaid balance of principal and accrued interest from these bonds is due on July 1, 2015. The bonds bear interest at an annual rate equal to sixty percent of the rate announced from time to time by Bank of America as its prime rate, which was 2.1% on March 31, 2011.

The Company has the Revolver with GECC under which the Company may borrow up to the lesser of $50,000 or 85% of the eligible accounts receivable. The Revolver will expire on February 21, 2013. At March 31, 2011 and December 31, 2010, there were no outstanding borrowings under the Revolver. As of March 31, 2011, the amount of borrowing capacity pledged to secure outstanding letters of credit and reserves against collateral for actual and contingent liabilities was $2,133 and $6,000, respectively. In addition, in the event of the Company's default under the Amended Term Loan, GECC has the right to take control of the Company's facilities encumbered by the loan to the extent necessary to make such payments and perform such acts that are required under the loan.

Long-term debt consists of the following:

	March 31, 2011	December 31, 2010
Ten Project Note with GECC, multiple-advance term loan, principal and interest payable monthly; interest is fixed at time of draw at 10-year treasury note rate plus 2.25% (rates in effect at March 31, 2011 range from 6.95% to 7.50%), balance due June 2016, collateralized by deeds of trust on real property, assignments of rents, security agreements and fixture financing statements.	$51,961	$52,229
Six Project Loan with GECC, principal and interest payable monthly, interest defined above, balance due September 30, 2014, collateralized by deeds of trust on real property, assignments of rents, security agreements and fixture financing statements.	39,359	39,495
Promissory note with RBS, principal and interest payable monthly and continuing through January 2018, interest at a fixed rate of 6.04%, collateralized by real property, assignment of rents and Company guaranty.	34,849	35,000
Promissory notes, principal, and interest of $69 payable monthly and continuing through September 2019, interest at fixed rate of 6.0%, collateralized by deed of trust on real property, assignment of rents and security agreement.	9,662	9,724
Bond, principal and interest of $20 payable monthly and continuing through July 2015, interest at a fixed rate of 60% of the Prime Rate (as defined by the agreement).	988	1,038
Mortgage note, principal, and interest of $54 payable monthly and continuing through February 2027, interest at fixed rate of 7.5%, collateralized by deed of trust on real property, assignment of rents and security agreement.	6,037	6,086
	142,856	143,572
Less current maturities	(3,165)	(3,055)
Less debt discount	(1,035)	(1,066)
	$138,656	$139,451

The Company is subject to standard reporting requirements and other typical covenants for loans of these types. As of March 31, 2011, the Company was in compliance with such loan covenants.

The carrying value of the Company's long-term debt is considered to approximate the fair value of such debt for all periods presented based upon the interest rates that the Company believes it can currently obtain for similar debt.

13. OPTIONS AND AWARDS

Stock-based compensation expense consists of share-based payment awards made to employees and directors, including employee stock options and restricted stock awards, based on estimated fair values. Stock-based compensation expense recognized in the Company's condensed consolidated statements of income for the three months ended March 31, 2011 and 2010 does not include compensation expense for share-based payment awards granted prior to, but not yet vested as of, January 1, 2006, but does include compensation expense for the share-based payment awards granted on or subsequent to January 1, 2006 based on the grant date fair value. As stock-based compensation expense recognized in the Company's condensed consolidated statements of income for the three months ended March 31, 2011 and 2010 was based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. The Company estimates forfeitures at the time of grant and, if necessary, revises the estimate in subsequent periods if actual forfeitures differ.

The Company has three option plans, the 2001 Stock Option, Deferred Stock and Restricted Stock Plan (2001 Plan), the 2005 Stock Incentive Plan (2005 Plan) and the 2007 Omnibus Incentive Plan (2007 Plan), all of which have been approved by the stockholders. In the 2001 Plan and the 2005 Plan, options may be exercised for unvested shares of common stock, which have full stockholder rights including voting, dividend and liquidation rights. The Company retains the right to repurchase any or all unvested shares at the exercise price paid per share of any or all unvested shares should the optionee cease to remain in service while holding such unvested shares. The total number of shares available under all of the Company’s stock incentive plans was 1,639 as of March 31, 2011.

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The Company uses the Black-Scholes option-pricing model to recognize the value of stock-based compensation expense for all share-based payment awards. Determining the appropriate fair-value model and calculating the fair value of stock-based awards at the grant date requires considerable judgment, including estimating stock price volatility, expected option life and forfeiture rates. The Company develops estimates based on historical data and market information, which can change significantly over time. The Company granted 9 options and 47 restricted stock awards during the three month period ended March 31, 2011.

The Company used the following assumptions for stock options granted during the three months ended March 31, 2011 and 2010:

Grant Year	Plan	Options Granted	Weighted Average Risk-Free Rate		Expected Life	Weighted Average Volatility		Weighted Average Dividend Yield	
2011	2007	9	2.53	%	6.5 years	55	%	0.93	%
2010	2007	106	2.82	%	6.5 years	55	%	1.08	%

For the three months ended March 31, 2011 and 2010, the following represents the weighted average exercise price, grant date intrinsic value and fair value displayed at grant date for stock option grants:

Grant Year	Granted	Weighted Average Exercise Price	Weighted Average Fair Value of Options
2011	9	$24.36	$12.42
2010	106	$17.47	$8.86

The weighted average exercise price equaled the weighted average fair value of common stock on the grant date for all options granted during the periods ended March 31, 2011 and 2010 and therefore, the intrinsic value was $0 at date of grant.

The following table represents the employee stock option activity during the three months ended March 31, 2011: