VISTACARE, INC.
Form 10-Q
February 09, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
FORM 10-Q

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

For the quarterly period ended December 31, 2005

OR

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 No. 000-50118

VistaCare, Inc.

(*Exact name of registrant as specified in its charter*)

Delaware	**06-1521534**
(*State or other jurisdiction of incorporation or organization*)	(*I.R.S. Employer Identification No.*)
4800 North Scottsdale Road, Suite 5000 Scottsdale, Arizona	**85251**
(Address of principal executive offices)	(Zip code)

(480) 648-4545

(*Registrant s telephone number, including area code*)

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, as amended (the Exchange Act), 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. þ Yes o No

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

As of February 6, 2005, there were outstanding 16,392,143 shares of the issuer s Class A Common Stock, $0.01 par value per share.

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PART I FINANCIAL INFORMATION
Item 1. Financial Statements.

VISTACARE, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share information)

	December 31, 2005 (unaudited)	September 30, 2005 (note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 13,686	$ 25,962
Short-term investments	27,573	27,413
Patient accounts receivable (net of allowance for denials of $2,001 and $1,594 at December 31, 2005 and September 30, 2005, respectively)	28,953	20,202
Patient accounts receivable room & board (net of allowance for denials of $1,138 and $1,527 at December 31, 2005 and September 30, 2005, respectively)	4,650	9,149
Prepaid expenses	4,904	3,811
Tax receivable	4,271	4,329
Deferred tax assets	9,666	8,826
Total current assets	93,703	99,692
Fixed assets, net	7,046	5,757
Goodwill	24,002	24,002
Other assets	6,986	7,310
Total assets	$ 131,737	$ 136,761
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 34	$ 1,445
Accrued Medicare Cap	13,161	18,057
Accrued expenses	25,064	27,652
Total current liabilities	38,259	47,154
Deferred tax liability-non-current	4,555	2,745
Stockholders equity:		
Class A Common Stock, $0.01 par value; authorized 33,000,000 shares; 16,392,143 and 16,376,529 shares issued and outstanding at December 31, 2005 and September 30, 2005, respectively	164	164
Additional paid-in capital	108,093	108,054
Deferred compensation		(555)
Accumulated deficit	(19,334)	(20,801)
Total stockholders equity	88,923	86,862
Total liabilities and stockholders equity	$ 131,737	$ 136,761

See accompanying notes to consolidated financial statements.

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VISTACARE, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)
(in thousands, except per share information)

	Three Months Ended December 31,	
	2005	**2004**
Net patient revenue	$ 59,673	$ 56,615
Operating expenses:		
Patient care expenses	35,921	35,108
Sales, general and administrative expenses	20,197	19,321
Depreciation	614	452
Amortization	648	603
Total operating expenses	57,380	55,484
Operating income	2,293	1,131
Non-operating income (expense):		
Interest income	309	217
Interest expense		(7)
Other expense	(94)	(177)
Total non-operating income	215	33
Net income before income taxes	2,508	1,164
Income tax expense	1,041	456
Net income	$ 1,467	$ 708
Net income per common share:		
Basic net income per common share	$ 0.09	$ 0.04
Diluted net income per common share	$ 0.09	$ 0.04
Weighted average shares outstanding:		
Basic	16,381	16,214
Diluted	16,738	16,814

See accompanying notes to consolidated financial statements.

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VISTACARE, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(in thousands)

	Three Months Ended December 31, 2005	2004
Operating activities		
Net income	$ 1,467	$ 708
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation	614	452
Amortization	648	603
Share-based compensation	454	103
Deferred income tax expense (benefit)	970	(163)
Loss on disposal of assets	16	132
Changes in operating assets and liabilities:		
Patient accounts receivable, net	(4,251)	2,862
Prepaid expenses and other	(1,035)	(237)
Payment of Medicare Cap assessments decrease in accrued Medicare Cap	(6,121)	(4,938)
Increase in accrual for Medicare Cap	1,225	1,500
Accounts payable and accrued expenses	(3,999)	(4,047)
Net cash used in operating activities	(10,012)	(3,025)
Investing activities		
Short-term investments purchased	(1,801)	(14,254)
Short-term investments sold	1,641	4,105
Purchases of equipment	(1,977)	(717)
Internally developed software expenditures	(112)	(436)
Increase in other assets	(154)	(271)
Net cash used in investing activities	(2,403)	(11,573)
Financing activities		
Proceeds from issuance of common stock from exercise of stock options and employee stock purchase plan	139	122
Net cash provided by financing activities	139	122
Net decrease in cash	(12,276)	(14,476)
Cash and cash equivalents, beginning of period	25,962	28,687
Cash and cash equivalents, end of period	$ 13,686	$ 14,211
Cash and short-term investments, end of period	$ 41,259	$ 57,525

See accompanying notes to consolidated financial statements.

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VISTACARE, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
December 31, 2005

Description of Business

VistaCare, Inc. (VistaCare, Company or we or similar pronoun), is a Delaware corporation providing medical care designed to address the physical, emotional, and spiritual needs of patients with a terminal illness and the support of their family members. Hospice services are provided predominately in the patient s home or other residence of choice, such as a nursing home or assisted living facility, or in a hospital or in-patient unit. VistaCare provides in-patient services at its in-patient units and through leased beds at unrelated hospitals and skilled nursing facilities on a per diem basis. VistaCare provides services in Alabama, Arizona, Colorado, Georgia, Indiana, Massachusetts, New Mexico, Nevada, Ohio, Oklahoma, Pennsylvania, South Carolina, Texas and Utah.

The accompanying interim consolidated financial statements of VistaCare have been prepared in conformity with U.S. generally accepted accounting principles, consistent in all material respects with those applied in the Company s Annual Report on Form 10-K for the fiscal year ended September 30, 2005 (fiscal 2005), except for the adoption of Statement of Financial Accounting Standards No. 123(R), Share-Based Payment (SFAS No. 123(R)) See Note 1.

1. Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements include accounts of VistaCare and its wholly owned subsidiaries: VistaCare USA, Inc., Vista Hospice Care, Inc., and FHI Health Services, Inc. (including its wholly-owned subsidiaries). Intercompany transactions and balances have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary, consisting of normal recurring accruals, for a fair presentation have been included. Operating results for the three months ended December 31, 2005 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2006.

The balance sheet at September 30, 2005 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in VistaCare, Inc. s Form 10-K for the year ended September 30, 2005.

Per Share Information

Basic net income per common share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per common share is computed by dividing net income by the weighed average number of shares outstanding during the period plus the effect of potentially dilutive securities, including shares and employee stock options of 16.7 million shares and 16.8 million shares for three months ended December 31, 2005 and December 31, 2004, respectively. The effect of dilutive securities not included because they would have been antidilutive were 2.0 million shares and 1.2 million shares for the three months ended December 31, 2005 and December 31, 2004, respectively.

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Stock Based Compensation

At December 31, 2005, the Company had two active share-based employee compensation plans. Stock option awards granted from these plans are granted at the fair market value on the date of grant, and vest over a period determined at the time the options are granted, ranging from one to five years, and generally have a maximum term of ten years. When options are exercised, new shares of the Company s Class A common stock are issued.

Prior to October 1, 2005, the Company accounted for the plans under the measurement and recognition provisions of APB Opinion No. 25, *Accounting for Stock Issued to Employees,* and related Interpretations, as permitted by FASB Statement No. 123, *Accounting for Stock-Based Compensation*. Under APB Opinion No. 25, stock options granted at market required no recognition of compensation cost and a share-based compensation proforma disclosure regarding the proforma effect on net earnings assuming compensation cost had been recognized in accordance with Statement of Financial Accounting Standard No. 123 Stock-Based Compensation.

		Three Months Ended December 31, 2004
Net income to common stockholders:		
As reported:	$	708
Deduct total stock-based employee compensation expense determined under fair value method for all awards, net of tax impact		(812)
Pro forma net loss to common stockholders	$	(104)
Basic net income (loss) per common share:		
As reported	$	0.04
Pro forma		(0.01)
Diluted net income (loss) per common share:		
As reported	$	0.04
Pro forma		(0.01)
Weighted average shares used in computation:		
Basic		16,214
Diluted		16,814

Effective October 1, 2005, the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), *Share-Based Payment* (SFAS No. 123(R)), which requires companies to measure and recognize compensation expense for all share-based payments at fair value. SFAS No. 123(R) eliminates the ability to account for share-based compensation transactions using APB Opinion No. 25, and generally requires that such transactions be accounted for using prescribed fair-value-based methods. SFAS No. 123(R) permits public companies to adopt its requirements using one of two methods: (a) a modified prospective method in which compensation costs are recognized beginning with the effective date based on the requirements of SFAS No. 123(R) for all share-based payments granted or modified after the effective date, and based on the requirements of SFAS No. 123(R) for all awards granted to employees prior to the effective date of SFAS No. 123(R) that remain unvested on the effective date or (b) a modified retrospective method which includes the requirements of the modified prospective method described above, but also permits companies to restate based on the amounts previously recognized under SFAS No. 123(R) for purposes of pro forma disclosures either for all periods presented or prior interim periods of the year of adoption. Effective October 1, 2005, the Company adopted SFAS No. 123(R) using the modified prospective method. Other than certain options previously issued at an amount determined to be below fair value for financial accounting purposes, no share-based employee compensation cost has been reflected in net income prior to the adoption of SFAS No. 123(R). The Company calculates the fair value of stock options using the Black-Scholes model. Results for prior periods have not been restated.

The adoption of SFAS No. 123(R) reduced income before income tax expense for the three months ended December 31, 2005 by approximately $0.4 million and reduced net income for the three months ended December 31, 2005 by approximately $0.3 million. Basic and diluted net income per common share for the three months ended December 31, 2005 would have been $0.12 and $0.12, respectively, if the Company had not adopted SFAS No. 123(R), compared to reported basic and diluted net income per common share of $0.09 and $0.09, respectively. The total value of the stock options awards and stock options granted and stock options that were deemed to be granted in the money using regression analysis after the Company became publicly traded is expensed ratably over the service period of the employees receiving the awards. As of December 31, 2005, total unrecognized compensation cost related to stock option awards was approximately $5.9 million and the related weighted-average period over which it is expected to be recognized is approximately 2.6 years.

Prior to the adoption of SFAS No. 123(R), the Company presented all benefits of tax deductions resulting from the exercise of share-based compensation as operating cash flows in the Statement of Cash Flows. SFAS No. 123(R) requires the benefits of tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. Such amounts were immaterial for the company during the three months ended December 31, 2005.

Compensation expense related to share-based awards is generally amortized over the vesting period with 10% recorded as patient care expenses and 90% recorded in selling, general & administrative expenses in the consolidated statements of operations.

A Summary of stock options within the Company s share-based compensation plans and changes for the three months ended December 31, 2005 is as follows:

	Number of Shares Under Option	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Balance at September 30, 2005	2,638,814	$ 16.72		
Granted	42,300	12.48		
Exercised	(4,800)	3.80		
Terminated/expired	(120,208)	24.22		
Balance at December 31, 2005	2,556,106	$ 16.33	7.49	(8,669,148)

The intrinsic value of options exercised during the three months ended December 5, 2005 was $0.1 million. Options exercisable under the Company s share-based compensation plans at December 31, 2005 were 1.6 million shares with an average exercise price of $18.02, an average remaining contractual term of 7 years, and an aggregate intrinsic value of $(12.9) million. Cash received by the Company related to the exercise of options during the three months ended December 31, 2005 amounted to $0.1 million.

A summary of restricted stock activity within the Company s share-based compensation plans and changes for the three months ended December 31, 2005 is as follows:

Nonvested Shares	Shares	Weighted-Average Grant-Date Fair Value
Nonvested at September 30, 2005	15,000	$ 16.00
Granted	97,000	$ 12.99
Vested	0	$
Forfeited	0	$
Nonvested at December 31, 2005	112,000	$ 13.70

The total fair value of restricted shares vested during the three months ended December 31, 2005 and December 31, 2004 was $0.0 million and $0.0 million, respectively.

The fair value of each stock option award is estimated on the date of the grant using the Black-Scholes option pricing model with the following assumptions:

	Three Months Ended December 31, 2005	Three Months Ended December 31, 2004

Expected dividend yield	0.0%	0.0%
Expected stock price volatility	0.51	0.55
Risk-free interest rate	3.94%	3.64%
Expected life of options	7.5 years	5 years

The risk-free interest rate is based on the U.S. treasury security rate in effect as of the date of grant. The expected lives of options for the three months ended December 31, 2005 and December 31, 2004 is an average of the contractual terms and vesting periods, and historical data, respectively. The weighted average fair value of stock options granted during the three months ended December 31, 2005 and December 31, 2004 was $7.32 and $7.14, respectively. The expected stock price volatility is based on historical data of the Company.

Income Taxes

VistaCare accounts for income taxes under the liability method as required by Financial Accounting Standards Board Statement No. 109, *Accounting for Income Taxes.* Under the liability method, deferred taxes are determined based on temporary differences between financial statement and tax bases of assets and liabilities existing at each balance sheet date using enacted tax rates for years in which the related taxes are expected to be paid or recovered.

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Reclassifications

Certain amounts have been reclassified to conform to the current presentation.

2. Fixed Assets

A summary of fixed assets follows (in thousands):

	December 31, 2005	September 30, 2005
Equipment	$ 9,644	$ 9,249
Furniture and fixtures	2,799	2,515
Leasehold improvements	1,800	1,449
Construction in progress	1,133	278
Total fixed assets	15,376	13,491
Less accumulated depreciation	(8,330)	(7,734)
Net fixed assets	$ 7,046	$ 5,757

3. Other Assets

A summary of other assets follows (in thousands):

	December 31, 2005	September 30, 2005
Internally developed software, net of amortization of $4,692 and $4,209 as of December 31, 2005 and September 30, 2005, respectively	$ 2,976	$ 3,380
Workers compensation, restricted cash	1,409	1,842
Covenant-not-to compete, net of amortization of $105 and $35 as of December 31, 2005 and September 30, 2005, respectively	1,295	1,365
Refundable deposits	419	415
Computer software, net of amortization of $2,106 and $2,035 as of December 31, 2005 and September 30, 2005, respectively	269	273
Other	618	35
Total other assets	$ 6,986	$ 7,310

4. Accrued Expenses

A summary of accrued expenses follows (in thousands):

	December 31, 2005	September 30, 2005
Patient care expenses	$ 12,743	$ 13,186
Administrative expenses	4,807	3,713
Salaries and payroll taxes	2,866	4,888
Paid time-off	2,154	2,115
Self-insurance health expenses	1,644	3,011
Taxes	850	739

Total accrued expenses	$ 25,064	$ 27,652

5. Long-Term Debt

In December 2004, VistaCare renewed a $30.0 million revolving line of credit and entered into a $20.0 million term loan (credit facility). The credit facility is collateralized by substantially all of VistaCare s assets including cash, accounts receivable and equipment. Loans under the revolving line of credit bear interest at an annual rate equal to the one-month London Interbank Borrowing Rate in effect from time to time plus 3.0-5.0%. Accrued interest under the revolving line of credit is due weekly.

Under the revolving line of credit, VistaCare may borrow, repay and re-borrow an amount equal to the lesser of: (i) $30.0 million or (ii) 85% of the net value of eligible accounts receivable. Under the term loan, borrowings are based on allowable total indebtedness based on a multiplier of cash flow as defined in the loan agreement. The maturity date of the credit facility is December 22, 2009. As of December 31, 2005, there was no balance outstanding on the revolving line of credit or on the term loan.

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The credit facility contains certain customary covenants including those that restrict the ability of VistaCare to incur additional indebtedness, pay dividends under certain circumstances, permit liens on property or assets, make capital expenditures, make certain investments, and prepay or redeem debt or amend certain agreements relating to outstanding indebtedness. The Company was in compliance with the financial debt service coverage covenants as of December 31, 2005.

6. Related Party Transactions

On September 27, 2005, the Board of Directors, at a special meeting, agreed to aid in the relocation of Mr. David Elliot, Chief Operating Officer, to the Phoenix, Arizona metropolitan area by purchasing Mr. Elliot s house in Minnesota for $940,000. The purchase price was based on three independent real estate appraisals. An agreement for the sale of the house to the Company was executed on October 11, 2005. Pursuant to the terms of this agreement, if the house sold for less than $940,000, Mr. Elliot was to pay the Company the difference between $940,000 and the sales price. On December 15, 2005, the Company closed on the house sale to an unrelated third party for $900,000. Mr. Elliot has agreed to reimburse the Company for the difference of approximately $40,000 by March 31, 2006.

7. Litigation

Between August and September 2004, approximately five complaints were filed individually and on behalf of all others similarly situated in the United States District Court for the District of Arizona against the Company and two of our officers alleging violations of the federal securities laws arising out of declines in the Company s stock price in 2004. Specifically, the complaints alleged claims in connection with various statements and purported omissions to the public and to the securities markets relating to the Company s August 2004 announcement of our decision to accrue an increased amount for the quarter ended June 30, 2004 for potential liability due to the Medicare Cap on reimbursement for hospice services. The five lawsuits were consolidated in April 2005. The consolidated case is in the early stages of discovery. The Company intends to vigorously defend the lawsuit. No assurances can be made that the Company will be successful in defense of such claims. If the Company is not successful in defense of such claims, we could be forced to make significant payments to the class of stockholders set forth in the consolidated complaint and their lawyers, and such payments could have a material adverse effect on our business, financial condition, results of operations and cash flows if not covered by our insurance carrier. Even if such claims are not successful, the litigation could result in substantial costs and divert management s attention and resources, which could adversely affect our business, results of operations, financial position and cash flows.

Between August and September 2004, two shareholders filed separate derivative lawsuits purportedly on behalf of the Company against several present and former officers and members of the Board of Directors of the Company in the United States District Court for the District of Arizona. The two derivative complaints, which have been consolidated, allege breaches of fiduciary duties, abuse of control, mismanagement, waste of corporate assets and unjust enrichment, as a result of the same activities alleged in the lawsuits discussed above. The derivative complaint seeks attorney fees and the payment of damages to the Company. As of the date of this report, the defendants filed a motion to dismiss and no discovery has occurred.

We are also subject to a variety of other claims and suits that arise from time to time in the ordinary course of our business. While management currently believes that resolving all of the matters discussed in Note 7, individually or in aggregate, will not have a material adverse impact on our financial position or our results of operations, the litigation and other claims that we face are subject to inherent uncertainties and management s view of these matters may change in the future. Should an unfavorable final outcome occur, there exists the possibility of a material adverse impact on our financial position, results of operations and cash flows for the period in which the effect becomes probable and reasonably estimable.

8. Dilutive Securities

The following table presents the calculation of basic and diluted net income (loss) per common share (in thousands, except per share information):

	Three Months Ended December 31,	
	2005	**2004**

Numerator		
Net income	$ 1,467	$ 708
Denominator		
Denominator for basic net income per common share weighted average shares	16,381	16,214
Effect of dilutive securities:		
Employee stock options	358	600

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	Three Months Ended December 31,	
	2005	**2004**
Denominator for diluted net income per common share adjusted weighted average shares and assumed conversion	16,738	16,814
Net income per common share:		
Basic net income to common stockholders	$ 0.09	$ 0.04
Diluted net income to common stockholders	$ 0.09	$ 0.04

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VISTACARE, INC.
HIGHLIGHTS
(dollars in millions, except as noted)

	Three Months Ended December 31, 2005	Three Months Ended December 31, 2004	Twelve Months Ended September 30, 2005
Patient Statistics:			
Average Daily Census (ADC)	5,313	5,318	5,376
Ending census on last day of period	5,130	5,329	5,510
Patient days	488,784	489,225	1,960,638
In-patient days (general in-patient)	5,016	4,597	17,335
Admissions	3,996	4,314	17,275
Diagnosis mix of admitted patients:			
Cancer	33%	32%	31%
Alzheimers/Dementia	13%	11%	11%
Heart disease	18%	18%	18%
Respiratory	9%	8%	9%
Failure to thrive/Rapid decline	19%	23%	23%
All other	8%	8%	8%
Discharges	4,344	4,232	17,382
Average length of stay on discharged patients	115	114	113
Median length of stay on discharged patients	34	31	31
Program site Statistics:			
Programs	58	48	58
In-patient units (included within a program)	2	1	2
Medicare provider numbers	36	36	37
Programs by ADC size			
0-60 ADC	22	9	21
61-100 ADC	17	14	15
100-200 ADC	13	20	16
200+ ADC	6	5	6
Net patient revenue:			
Net patient revenue	$ 59.7	$ 56.6	$ 225.4
Net patient revenue per day of care	$ 122.08	$ 115.72	$ 114.89
Patient revenue payor %			
Medicare	92.5%	93.3%	92.5%
Medicaid	4.7%	3.8%	4.6%
Private insurers and managed care	2.8%	2.9%	2.9%
Level of care % of patient revenue			
Routine home care	94.7%	95.5%	95.4%
General in-patient care	4.5%	3.8%	3.7%
Continuous home care	0.6%	0.5%	0.7%
Respite in-patient care	0.2%		