

CHEMED CORP
Form 10-Q
August 02, 2012

UNITED STATES

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

(Mark One)

X Quarterly Report Under Section 13 or 15 (d) of the Securities Exchange Act of 1934 For the Quarterly Period Ended June 30, 2012

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

Commission File Number: 1-8351

CHEMED CORPORATION
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

31-0791746
(IRS Employer Identification No.)

255 E. Fifth Street, Suite 2600, Cincinnati, Ohio 45202
(Address of principal executive offices) (Zip code)

(513) 762-6500
(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 during the preceding 12 months (or for such shorter periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X 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).

Yes X No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer X Accelerated filer Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

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Yes No X

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Amount	Date
Capital Stock \$1 Par Value	19,099,057 Shares	June 30, 2012

CHEMED CORPORATION AND
SUBSIDIARY COMPANIES

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
CHEMED CORPORATION AND SUBSIDIARY COMPANIES
UNAUDITED CONSOLIDATED BALANCE SHEET
(in thousands, except share and per share data)

	June 30, 2012	December 31, 2011
ASSETS		
Current assets		
Cash and cash equivalents	\$59,966	\$38,081
Accounts receivable less allowances of \$11,414 (2011 - \$11,524)	81,811	77,924
Inventories - net	8,146	8,668
Current deferred income taxes	13,226	12,540
Prepaid income taxes	4,187	2,131
Prepaid expenses	10,737	11,409
Total current assets	178,073	150,753
Investments of deferred compensation plans	33,215	31,629
Properties and equipment, at cost, less accumulated depreciation of \$155,406 (2011 - \$146,709)	88,571	82,951
Identifiable intangible assets less accumulated amortization of \$29,654 (2011 - \$28,904)	57,635	58,262
Goodwill	461,965	460,633
Other assets	11,669	11,677
Total Assets	\$831,128	\$795,905
LIABILITIES		
Current liabilities		
Accounts payable	\$51,002	\$48,225
Income taxes	167	90
Accrued insurance	36,786	37,147
Accrued compensation	39,729	41,087
Other current liabilities	14,906	18,851
Total current liabilities	142,590	145,400
Deferred income taxes	25,257	29,463
Long-term debt	170,769	166,784
Deferred compensation liabilities	33,149	30,693
Other liabilities	11,918	9,881
Total Liabilities	383,683	382,221
STOCKHOLDERS' EQUITY		
Capital stock - authorized 80,000,000 shares \$1 par; issued 31,142,442 shares (2011 - 30,936,925 shares)	31,142	30,937
Paid-in capital	410,957	398,094
Retained earnings	582,316	546,757
Treasury stock - 12,141,664 shares (2011 - 11,880,051)	(579,013)	(564,091)
Deferred compensation payable in Company stock	2,043	1,987

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Total Stockholders' Equity	447,445	413,684
Total Liabilities and Stockholders' Equity	\$831,128	\$795,905

See accompanying notes to unaudited consolidated financial statements.

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CHEMED CORPORATION AND SUBSIDIARY COMPANIES
 UNAUDITED CONSOLIDATED STATEMENT OF INCOME
 (in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Service revenues and sales	\$354,170	\$333,360	\$707,113	\$664,278
Cost of services provided and goods sold (excluding depreciation)	257,368	239,597	514,813	477,055
Selling, general and administrative expenses	49,770	50,424	102,937	106,078
Depreciation	6,380	6,358	12,621	12,646
Amortization	1,127	1,139	2,240	2,109
Total costs and expenses	314,645	297,518	632,611	597,888
Income from operations	39,525	35,842	74,502	66,390
Interest expense	(3,672)	(3,461)	(7,289)	(6,705)
Other income/(expense) - net	(970)	714	1,125	2,816
Income before income taxes	34,883	33,095	68,338	62,501
Income taxes	(13,609)	(12,809)	(26,619)	(24,114)
Net income	\$21,274	\$20,286	\$41,719	\$38,387
Earnings Per Share				
Net income	\$1.12	\$0.96	\$2.20	\$1.82
Average number of shares outstanding	18,998	21,115	18,976	21,067
Diluted Earnings Per Share				
Net income	\$1.10	\$0.94	\$2.16	\$1.78
Average number of shares outstanding	19,369	21,637	19,357	21,586
Cash Dividends Per Share	\$0.16	\$0.14	\$0.32	\$0.28

See accompanying notes to unaudited consolidated financial statements.

CHEMED CORPORATION AND SUBSIDIARY COMPANIES
UNAUDITED CONSOLIDATED STATEMENT OF CASH FLOWS
(in thousands)

	Six Months Ended June 30,	
	2012	2011
Cash Flows from Operating Activities		
Net income	\$41,719	\$38,387
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	14,861	14,755
Deferred income taxes	(4,895)	(18)
Provision for uncollectible accounts receivable	4,730	4,365
Amortization of discount on convertible notes	3,985	3,724
Stock option expense	4,312	4,495
Noncash long-term incentive compensation	-	2,595
Changes in operating assets and liabilities, excluding amounts acquired in business combinations:		
Increase in accounts receivable	(8,543)	(9,271)
Decrease/(increase) in inventories	522	(954)
Decrease/(increase) in prepaid expenses	672	(59)
Decrease in accounts payable and other current liabilities	(3,593)	(6,603)
Increase/(decrease) in income taxes	(1,029)	3,738
Increase in other assets	(2,283)	(5,652)
Increase in other liabilities	4,493	4,514
Excess tax benefit on share-based compensation	(1,069)	(3,339)
Other sources	773	450
Net cash provided by operating activities	54,655	51,127
Cash Flows from Investing Activities		
Capital expenditures	(18,474)	(14,960)
Business combinations, net of cash acquired	(1,500)	(3,689)
Other sources/(uses)	357	(869)
Net cash used by investing activities	(19,617)	(19,518)
Cash Flows from Financing Activities		
Dividends paid	(6,160)	(5,967)
Purchases of treasury stock	(12,841)	(25,482)
Proceeds from issuance of capital stock	3,670	7,698
Excess tax benefit on share-based compensation	1,069	3,339
Increase/(decrease) in cash overdrafts payable	985	(7,814)
Debt issuance costs	-	(2,723)
Other sources	124	364
Net cash used by financing activities	(13,153)	(30,585)
Increase in Cash and Cash Equivalents	21,885	1,024
Cash and cash equivalents at beginning of year	38,081	49,917
Cash and cash equivalents at end of period	\$59,966	\$50,941

See accompanying notes to unaudited consolidated financial statements.

CHEMED CORPORATION AND SUBSIDIARY COMPANIES

Notes to Unaudited Consolidated Financial Statements

1. Basis of Presentation

As used herein, the terms "We," "Company" and "Chemed" refer to Chemed Corporation or Chemed Corporation and its consolidated subsidiaries.

We have prepared the accompanying unaudited consolidated financial statements of Chemed in accordance with Rule 10-01 of SEC Regulation S-X. Consequently, we have omitted certain disclosures required under generally accepted accounting principles in the United States ("GAAP") for complete financial statements. The December 31, 2011 balance sheet data were derived from audited financial statements but do not include all disclosures required by GAAP. However, in our opinion, the financial statements presented herein contain all adjustments, consisting only of normal recurring adjustments, necessary to present fairly our financial position, results of operations and cash flows. These financial statements are prepared on the same basis as and should be read in conjunction with the Consolidated Financial Statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2011.

2. Revenue Recognition

Both the VITAS segment and the Roto-Rooter segment recognize service revenues and sales when the earnings process has been completed. Generally, this occurs when services are provided or products are delivered. VITAS recognizes revenue at the estimated realizable amount due from third-party payers. Medicare payments are subject to certain limitations, as described below.

As of June 30, 2012, VITAS has approximately \$510,000 in unbilled revenue included in accounts receivable (December 31, 2011 - \$720,000). The unbilled revenue at VITAS relates to hospice programs currently undergoing focused medical reviews ("FMR"). During FMR, surveyors working on behalf of the U.S. Federal government review certain patient files for compliance with Medicare regulations. During the time the patient file is under review, we are unable to bill for care provided to those patients. We make appropriate provisions to reduce our revenue and accounts receivable balance for potential denials of patient service revenue due to FMR activity.

We actively monitor each of our hospice programs, by provider number, as to their specific admission, discharge rate and median length of stay data in an attempt to determine whether they are likely to exceed the annual per-beneficiary Medicare cap ("Medicare cap"). Should we determine that revenues for a program are likely to exceed the Medicare cap based on projected trends, we attempt to institute corrective action to influence the patient mix or to increase patient admissions. However, should we project our corrective action will not prevent that program from exceeding its Medicare cap, we estimate the amount of revenue recognized during the period that will require repayment to the Federal government under the Medicare cap and record the amount as a reduction to patient revenue. The Medicare cap measurement period is from September 29 through September 28 of the following year for admissions and from November 1 through October 31 of the following year for revenue.

During the three-month period ended June 30, 2012, we did not record any Medicare cap liability. During the six-month period ended June 30, 2012, we reversed Medicare cap liability for amounts recorded in the fourth quarter of 2011 for three programs' projected 2012 measurement period liability. We reversed these amounts as improving admissions trends in these programs indicate that the liability had been eliminated.

Shown below is the Medicare cap liability activity for the periods ended (in thousands):

	June 30,
2012	2011

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Beginning balance January 1,	\$2,965	\$1,371
Reversal - 2012 measurement period	(2,577)	-
Expense - 2011 measurement period	-	299
Reversal - 2011 measurement period	-	(743)
Other	-	(198)
Ending balance June 30,	\$388	\$729

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Vitas provides charity care, in certain circumstances, to patients without charge when management of the hospice program determines, at the time services are performed, that the patient does not have the financial wherewithal to make payment. There is no revenue or associated accounts receivable in the accompanying consolidated financial statements related to charity care. The cost of charity care is calculated by taking the ratio of charity care days to total days of care and multiplying by total cost of care. The cost of charity care is as follows (in thousands):

Three months ended June 30,		Six months ended June 30,	
2012	2011	2012	2011
\$ 1,789	\$ 1,763	\$ 4,038	\$ 3,522

3. Segments

Service revenues and sales and after-tax earnings by business segment are as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Service Revenues and Sales				
VITAS	\$265,213	\$243,095	\$526,060	\$478,768
Roto-Rooter	88,957	90,265	181,053	185,510
Total	\$354,170	\$333,360	\$707,113	\$664,278
After-tax Earnings				
VITAS	\$20,433	\$18,589	\$40,060	\$36,714
Roto-Rooter	8,074	9,092	15,569	17,602
Total	28,507	27,681	55,629	54,316
Corporate	(7,233)	(7,395)	(13,910)	(15,929)
Net income	\$21,274	\$20,286	\$41,719	\$38,387

We report corporate administrative expenses and unallocated investing and financing income and expense not directly related to either segment as "Corporate".

4. Earnings per Share

Earnings per share ("EPS") are computed using the weighted average number of shares of capital stock outstanding. Earnings and diluted earnings per share are computed as follows (in thousands, except per share data):

For the Three Months Ended June 30,	Income	Net Income	
		Shares	Earnings per Share
2012			
Earnings	\$ 21,274	18,998	\$ 1.12
Dilutive stock options	-	288	
Nonvested stock awards	-	83	
Diluted earnings	\$ 21,274	19,369	\$ 1.10
2011			
Earnings	\$ 20,286	21,115	\$ 0.96
Dilutive stock options	-	433	
Nonvested stock awards	-	89	

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Diluted earnings	\$	20,286	21,637	\$	0.94
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For the Six Months Ended June 30, 2012	Income	Net Income	
		Shares	Earnings per Share
Earnings	\$ 41,719	18,976	\$ 2.20
Dilutive stock options	-	294	
Nonvested stock awards	-	87	
Diluted earnings	\$ 41,719	19,357	\$ 2.16
2011			
Earnings	\$ 38,387	21,067	\$ 1.82
Dilutive stock options	-	433	
Nonvested stock awards	-	86	
Diluted earnings	\$ 38,387	21,586	\$ 1.78

For the three and six-month periods ended June 30, 2012, 1.4 million stock options were excluded from the computation of diluted earnings per share as their exercise prices were greater than the average market price for most of the period. For the three and six-month period ended June 30, 2011, 970,000 stock options were excluded from the computation of diluted earnings per share.

Diluted earnings per share may be impacted in the future as the result of the issuance of our 1.875% Senior Convertible Notes (the "Notes") and related purchased call options and sold warrants. Per FASB's authoritative guidance on the effect of contingently convertible instruments on diluted earnings per share and convertible bonds with an issuer option to settle for cash upon conversion, we will not include any shares related to the Notes in our calculation of diluted earnings per share until our average stock price for a quarter exceeds the current conversion price. We would then include in our diluted earnings per share calculation those shares issuable using the treasury stock method. The amount of shares issuable is based upon the amount by which the average stock price for the quarter exceeds the conversion price. The purchased call option does not impact the calculation of diluted earnings per share as it is always anti-dilutive. The sold warrants become dilutive when our average stock price for a quarter exceeds the strike price of the warrant.

The following table provides examples of how changes in our stock price impact the number of shares that would be included in our diluted earnings per share calculation at June 30, 2012. It also shows the impact on the number of shares issuable upon conversion of the Notes and settlement of the purchased call options and sold warrants:

Share Price	Shares Underlying 1.875%		Total Treasury Method	Shares Due to the Company	Incremental Shares Issued/Received by the Company upon Conversion (b)
	Convertible Notes	Warrant Shares	Incremental Shares (a)	under Notes Hedges	
\$ 80.73	40,072	-	40,072	(42,868)	(2,796)
\$ 90.73	295,315	-	295,315	(315,919)	(20,604)
\$ 100.73	499,879	-	499,879	(534,756)	(34,877)
\$ 110.73	667,495	120,403	787,898	(714,066)	73,832
\$ 120.73	807,344	319,182	1,126,526	(863,672)	262,854
\$ 130.73	925,798	487,550	1,413,348	(990,391)	422,957

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- a) Represents the number of incremental shares that must be included in the calculation of fully diluted shares under U.S. GAAP.
- b) Represents the number of incremental shares to be issued by the Company upon conversion of the 1.875% Convertible Notes, assuming concurrent settlement of the note hedges and warrants.

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5. Long-Term Debt

On March 1, 2011, we replaced our existing credit agreement with our Revolving Credit Facility (“2011 Credit Agreement”). Terms of the 2011 Credit Agreement consist of a five-year, \$350 million revolving credit facility. This 2011 Credit Agreement has a floating interest rate that is currently LIBOR plus 175 basis points. The 2011 Credit Agreement also includes a \$150 million expansion feature. The 2011 Credit Agreement contains the following quarterly financial covenants:

Description	Requirement
Leverage Ratio (Consolidated Indebtedness/Consolidated Adj. EBITDA)	< 3.50 to 1.00
Fixed Charge Coverage Ratio (Consolidated Free Cash Flow/Consolidated Fixed Charges)	> 1.50 to 1.00
Annual Operating Lease Commitment	< \$30.0 million

We are in compliance with all debt covenants as of June 30, 2012. We have issued \$29.4 million in standby letters of credit as of June 30, 2012 for insurance purposes. Issued letters of credit reduce our available credit under the 2011 Credit Agreement. As of June 30, 2012, we have approximately \$320.6 million of unused lines of credit available and eligible to be drawn down under our revolving credit facility, excluding the \$150 million expansion feature.

The following amounts are included in our consolidated balance sheet related to the Notes:

	June 30, 2012	December 31, 2011
Principal amount of convertible debentures	\$ 186,956	\$ 186,956
Unamortized debt discount	(16,187)	(20,172)
Carrying amount of convertible debentures	\$ 170,769	\$ 166,784
Additional paid in capital (net of tax)	\$ 31,310	\$ 31,310

The following amounts comprise interest expense included in our consolidated income statement (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Cash interest expense	\$ 1,350	\$ 1,288	\$ 2,683	\$ 2,440
Non-cash amortization of debt discount	2,009	1,878	3,985	3,724
Amortization of debt costs	313	295	621	541
Total interest expense	\$ 3,672	\$ 3,461	\$ 7,289	\$ 6,705

The unamortized debt discount is being amortized using the effective interest method over the remaining life of the Notes. The effective rate on the Notes is approximately 6.875%.

6. Other Income/(Expense) -- Net

Other income/(expense) -- net comprises the following (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Market value gains/(losses) on assets held in deferred compensation trust	\$ (948	) \$ 743	\$ 1,185	\$ 2,807
Gain/(loss) on disposal of property and equipment	(67	) 32	(148	) 11
Interest income	59	62	110	123
Other - net	(14	) (123	) (22	) (125
Other income/(expense) - net	\$ (970	) \$ 714	\$ 1,125	\$ 2,816

7. Stock-Based Compensation Plans

On February 17, 2012, the Compensation/Incentive Committee of the Board of Directors ("CIC") approved a grant of 35,969 shares of restricted stock to certain key employees. The restricted shares cliff vest four years from the date of issuance. The cumulative compensation expense related to the restricted stock award is \$2.3 million and will be recognized ratably over the 4 year vesting period. We assumed no forfeitures in determining the cumulative compensation expense of the grant.

On February 17, 2012, the CIC approved a grant of 442,350 stock options to certain employees. The stock options vest ratably over three years from the date of issuance. The cumulative compensation expense related to the stock option grant is \$7.1 million and will be recognized over the 3 year vesting period. We used the Black-Scholes option valuation method to determine the cumulative compensation expense of the grant.

8. Independent Contractor Operations

The Roto-Rooter segment sublicenses with 65 independent contractors to operate certain plumbing repair and drain cleaning businesses in lesser-populated areas of the United States and Canada. We had notes receivable from our independent contractors as of June 30, 2012 totaling \$1.1 million (December 31, 2011 - \$1.1 million). In most cases these loans are fully or partially secured by equipment owned by the contractor. The interest rates on the loans range from 0% to 8% per annum and the remaining terms of the loans range from 2 months to 5 years at June 30, 2012. We recorded the following from our independent contractors (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Revenues	\$ 6,809	\$ 6,528	\$ 13,491	\$ 13,039
Pretax profits	3,732	3,402	6,813	6,389

9. Pension and Retirement Plans

All of the Company's plans that provide retirement and similar benefits are defined contribution plans. These expenses include the impact of market gains and losses on assets held in deferred compensation plans. Expenses for the Company's pension and profit-sharing plans, excess benefit plans and other similar plans are as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
\$	1,162	\$ 2,871	\$ 5,854	\$ 6,954

10. Legal and Regulatory Matters

Litigation

On March 1, 2010 Anthony Morangelli and Frank Ercole filed a class action lawsuit in federal district court for the Eastern District of New York seeking unpaid minimum wages and overtime service technician compensation from Roto-Rooter and Chemed. They also seek payment of penalties, interest and plaintiffs' attorney fees. We contest these allegations. In September 2010, the Court conditionally certified a nationwide class of service technicians, excluding those who signed dispute resolution agreements in which they agreed to arbitrate claims arising out of their employment. We are unable to estimate our potential liability, if any, with respect to this case.

VITAS is party to a class action lawsuit filed in the Superior Court of California, Los Angeles County, in September 2006 by Bernadette Santos, Keith Knoche and Joyce White. This case alleges failure to pay overtime and failure to provide meal and rest periods to a purported class of California admissions nurses, chaplains and sales representatives. The case seeks payment of penalties, interest and Plaintiffs' attorney fees. We contest these allegations. In December 2009, the trial court denied Plaintiffs' motion for class certification. In July 2011, the Court of Appeals affirmed denial of class certification on the travel time, meal and rest period claims, and reversed the trial court's denial on the off-the-clock and sales representation exemption claims. Plaintiffs have filed an appeal of this decision. We are unable to estimate our potential liability or potential range of loss, if any, with respect to this case.

On January 12, 2012, the Greater Pennsylvania Carpenters Pension Fund filed a putative class action lawsuit in the United States District Court for the Southern District of Ohio against the Company, Kevin McNamara, David Williams, and Timothy O'Toole. On April 9, 2012, the Court issued orders (a) renaming the suit as In re Chemed Corp. Securities Litigation, Civil Action No. 1:12-cv-28 (S.D. Ohio), (b) appointing the Greater Pennsylvania Carpenters Pension Fund and the Electrical Workers Pension Fund, Local 103, I.B.E.W. as Lead Plaintiffs; and (c) approving Lead Plaintiffs' selection of Labaton Sucharow LLP and Robbins Geller Rudman & Dowd LLP as Co-Lead Counsel. On June 18, 2012, Lead Plaintiffs filed an amended complaint alleging violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 against all Defendants, and violation of Section 20(a) of the Securities Exchange Act of 1934 against Messrs. McNamara, Williams and O'Toole. The suit's allegations concern the VITAS hospice segment of the Company's business. Lead Plaintiffs seek, on behalf of a putative class of purchasers of Chemed Capital Stock between February 15, 2010 and November 16, 2011, compensatory damages in an unspecified amount and attorneys' fees and expenses, arising from Defendants' failure to disclose an alleged fraudulent scheme to enroll ineligible hospice patients and to fraudulently obtain payments from the federal government. Defendants are required to move or otherwise respond to the amended complaint on or before August 17, 2012. Defendants believe the claims are without merit, and intend to defend vigorously against them.

Regardless of outcome, defense of litigation adversely affects us through defense costs, diversion of our time and related publicity.

Regulatory Matters

In June 2012, VITAS received an administrative subpoena from the Office of the Inspector General ("OIG") of the U.S. Department of Health and Human Services in connection with an investigation of possible improper claims submitted to the Medicare and Medicaid Programs. It seeks production to the OIG of various categories of documents concerning the provision of hospice services, for headquarters and its Southern California programs, for the period January 1, 2007 through the date of the subpoena. The categories of documents include policy, procedure and training manuals; documents concerning patient eligibility for hospice care, including referrals, admissions, certification, revocations and census information; documents concerning claims submitted to government programs; certain information concerning employees and their compensation; and documents concerning VITAS' financial performance. We are conferring with the U.S. Attorney's Office for the Central District of California regarding the document requests. We cannot predict the timing or outcome of this investigation, or estimate our potential liability, if any.

In May 2009, VITAS received an administrative subpoena from the U.S. Department of Justice requesting VITAS deliver to the OIG documents, patient records, and policy and procedure manuals for headquarters and its Texas programs concerning hospice services provided for the period January 1, 2003 to the date of the letter. In August 2009, the OIG selected medical records for 59 past and current patients from a Texas program for review. In February 2010, VITAS received a companion civil investigative demand (“CID”) from the State of Texas Attorney General’s Office, seeking related documents. In September 2010, it received a second CID and a second administrative subpoena seeking related documents. In April 2011, the U.S. Attorney provided the Company with a copy of qui tam complaint filed under seal in the U.S. District Court for the Northern District of Texas. The Court unsealed this complaint in November 2011. The U.S. Attorney and the Attorney General for the State of Texas filed a notice in November 2011 that they had decided not to intervene at that time in the case. They continue to investigate its allegations. It was brought by Michael Rehfelt, a former VITAS San Antonio program general manager, against VITAS, the program’s former Regional Vice President Keith Becker, its former Medical Director Justos Cisneros, and their current employers: Wellmed Medical Management, Care Level Management LLC, and Inspiris Inc. Plaintiff dismissed his case against their current employers in March of 2012. The case alleges admission and recertification of inappropriate patients, backdating revocations, and conspiring to admit inappropriate patients to hospice. In June 2011, the U.S. Attorney provided the Company with a partially unsealed second qui tam complaint filed under seal in the U.S. District Court for the Western District of Texas. In June 2011, the U.S. Attorney also provided the Company with a partially unsealed third qui tam complaint filed under seal in the Northern District of Illinois, Eastern Division. We are conferring with the U.S. Attorney regarding the Company’s defenses to each complaint’s allegations. We can neither predict the outcome of this investigation nor estimate our potential liability, if any.

In April 2005, the OIG served VITAS with civil subpoenas relating to VITAS' alleged failure to appropriately bill Medicare and Medicaid for hospice services. As part of this investigation, the OIG selected medical records for 320 past and current patients from VITAS' three largest programs for review. It also sought policies and procedures dating back to 1998 covering admissions, certifications, recertifications and discharges. During the third quarter of 2005 and again in May 2006, the OIG requested additional information from us. The Court dismissed a related qui tam complaint filed in U.S. District Court for the Southern District of Florida with prejudice in July 2007. The plaintiffs appealed this dismissal, which the Court of Appeals affirmed. The government continues to investigate the complaint's allegations. In March 2009, we received a letter from the government reiterating the basis of their investigations. In July 2012, we received an administrative subpoena from the Office of the Attorney General of Florida seeking documents from January 1, 2007 covering areas including billing, marketing, referrals, incentives, patient eligibility for hospice care, claims submitted to government programs, and VITAS' financial performance. We are conferring with the government's counsel regarding the document requests. We are unable to estimate the timing or outcome of this investigation or our potential liability, if any, with respect to this matter.

Regardless of outcome, responding to the subpoenas can adversely affect us through defense costs, diversion of our time and related publicity.

11. Concentration of Risk

VITAS has pharmacy services agreements ("Agreements") with Omnicare, Inc. and its subsidiaries ("OCR") whereby OCR provides specified pharmacy services for VITAS and its hospice patients in geographical areas served by both VITAS and OCR. The Agreements renew automatically for one-year terms. Either party may cancel the Agreements at the end of any term by giving 90 days prior written notice. VITAS made purchases from OCR of \$10.2 million and \$9.8 million for the three months ended June 30, 2012 and 2011, respectively. VITAS made purchases from OCR of \$20.3 million and \$19.1 million for the six months ended June 30, 2012 and 2011, respectively. For the three and six month periods ending June 30, 2012 and 2011, respectively, purchases from this vendor represent over 90% of all pharmacy services used by VITAS.

12. Cash Overdrafts and Cash Equivalents

Included in accounts payable at June 30, 2012 is cash overdrafts payable of \$11.3 million (December 31, 2011 - \$10.3 million).

From time to time throughout the year, we invest excess cash in money market funds with major commercial banks. We closely monitor the creditworthiness of the institutions with which we invest our overnight funds. We had \$53.4 million in cash equivalents as of June 30, 2012. There was \$32.5 million in cash equivalents as of December 31, 2011. The weighted average rate of return for our cash equivalents was 0.2% for June 30, 2012 and 0.1% for December 31, 2011.

13. Financial Instruments

FASB's authoritative guidance on fair value measurements defines a hierarchy which prioritizes the inputs in fair value measurements. Level 1 measurements are measurements using quoted prices in active markets for identical assets or liabilities. Level 2 measurements use significant other observable inputs. Level 3 measurements are measurements using significant unobservable inputs which require a company to develop its own assumptions. In recording the fair value of assets and liabilities, companies must use the most reliable measurement available.

The following shows the carrying value, fair value and the hierarchy for our financial instruments as of June 30, 2012 (in thousands):

	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Fair Value Measure Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mutual fund investments of deferred compensation plans held in trust	\$ 33,215	\$ 33,215	\$ -	\$ -
Long-term debt	170,769	187,984	-	-

For cash and cash equivalents, accounts receivable and accounts payable, the carrying amount is a reasonable estimate of fair value because of the liquidity and short-term nature of these instruments.

14. Capital Stock Transactions

We repurchased the following capital stock for the three and six-months ended June 30, 2012 and 2011:

	Three months ended June 30, 2012	2011	Six months ended June 30, 2012	2011
Shares repurchased	199,900	-	199,900	341,513
Weighted average price per share	\$ 55.72	\$ -	\$ 55.72	\$ 63.79

15. Business Combinations

In the first six months of 2012, we completed three business combinations within our Roto-Rooter segment for \$1.5 million in cash to increase our market penetration in Bend, Oregon; Shreveport, Louisiana; and Boise, Idaho. A substantial portion of this aggregate purchase price was allocated to goodwill. The operating results of these business combinations have been included in our results of operations since the acquisition date and are not material for the three and six-month periods ended June 30, 2012 nor for the comparable prior year periods.

16. Guarantor Subsidiaries

Our 1.875% Notes are fully and unconditionally guaranteed on an unsecured, jointly, and severally liable basis by certain of our 100% owned subsidiaries. The following unaudited, condensed, consolidating financial data presents the composition of the parent company (Chemed), the guarantor subsidiaries and the non-guarantor subsidiaries as of June 30, 2012 and December 31, 2011 for the balance sheet, the three and six months ended June 30, 2012 and June 30, 2011 for the income statement and the six months ended June 30, 2012 and June 30, 2011 for the statement of cash flows (dollars in thousands):

June 30, 2012	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
ASSETS					
Cash and cash equivalents	\$53,280	\$ (803)	\$ 7,489	\$ -	\$ 59,966
Accounts receivable, less allowances	1,082	80,120	609	-	81,811
Intercompany receivables	-	303,347	-	(303,347)	-
Inventories - net	-	7,414	732	-	8,146
Current deferred income taxes	(1,311)	14,329	208	-	13,226
Prepaid income taxes	4,701	(890)	376	-	4,187
Prepaid expenses	980	9,554	203	-	10,737
Total current assets	58,732	413,071	9,617	(303,347)	178,073
Investments of deferred compensation plans	-	-	33,215	-	33,215
Properties and equipment, at cost, less accumulated depreciation	11,203	74,761	2,607	-	88,571
Identifiable intangible assets less accumulated amortization	-	57,635	-	-	57,635
Goodwill	-	457,487	4,478	-	461,965
Other assets	7,010	1,733	2,926	-	11,669
Investments in subsidiaries	833,241	23,043	-	(856,284)	-
Total assets	\$910,186	\$ 1,027,730	\$ 52,843	\$ (1,159,631)	\$ 831,128
LIABILITIES AND STOCKHOLDERS' EQUITY					
Accounts payable	\$(748)	\$51,304	\$ 446	\$ -	\$ 51,002
Intercompany payables	298,601	-	4,746	(303,347)	-
Income taxes	-	-	167	-	167
Accrued insurance	402	36,384	-	-	36,786
Accrued compensation	2,020	37,166	543	-	39,729
Other current liabilities	1,992	12,618	296	-	14,906
Total current liabilities	302,267	137,472	6,198	(303,347)	142,590