CHEMED CORP
Form 10-Q
May 02, 2014

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 March 31, 2014

o 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 (Address of principal executive offices)	45202 (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 o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes x No o

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	o	Non-accelerated filer	o	Smaller reporting company	o

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

Yes o No 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	17,539,101 Shares	March 31, 2014

CHEMED CORPORATION AND
SUBSIDIARY COMPANIES

Index

EX – 101.INS
EX – 101.SCH
EX – 101.CAL
EX – 101.DEF
EX – 101.LAB
EX – 101.PRE

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)

	March 31, 2014	December 31, 2013
ASSETS		
Current assets		
Cash and cash equivalents	$39,479	$84,418
Accounts receivable less allowances of $13,824 (2013 - $12,590)	116,152	91,770
Inventories	6,676	6,703
Current deferred income taxes	13,769	20,257
Prepaid income taxes	3,406	3,690
Prepaid expenses	18,930	17,818
Total current assets	198,412	224,656
Investments of deferred compensation plans	45,732	42,465
Properties and equipment, at cost, less accumulated depreciation of $185,056 (2013 - $180,550)	93,575	92,955
Identifiable intangible assets less accumulated amortization of $32,380 (2013 - $32,055)	56,276	56,556
Goodwill	466,961	466,871
Other assets	7,664	10,198
Total Assets	$868,620	$893,701
LIABILITIES		
Current liabilities		
Accounts payable	$38,599	$41,758
Current portion of long-term debt	185,825	183,564
Income taxes	3,967	111
Accrued insurance	39,391	41,859
Accrued compensation	38,233	48,323
Accrued legal	7,154	23,210
Other current liabilities	24,682	25,161
Total current liabilities	337,851	363,986
Deferred income taxes	28,232	27,301
Deferred compensation liabilities	45,498	42,348
Other liabilities	11,106	11,176
Total Liabilities	422,687	444,811
Commitments and contingencies		
STOCKHOLDERS' EQUITY		
Capital stock - authorized 80,000,000 shares $1 par; issued 32,621,360 shares (2013 - 32,245,226 shares)	32,621	32,245
Paid-in capital	504,883	481,011
Retained earnings	703,385	686,114
Treasury stock - 15,180,456 shares (2013 - 14,660,427)	(797,141)	(752,634)
Deferred compensation payable in Company stock	2,185	2,154

Total Stockholders' Equity	445,933	448,890
Total Liabilities and Stockholders' Equity	$868,620	$893,701

See accompanying notes to unaudited consolidated financial statements.

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

	Three Months Ended March 31,	
	2014	2013
Service revenues and sales	$358,300	$366,641
Cost of services provided and goods sold (excluding depreciation)	257,819	264,307
Selling, general and administrative expenses	55,671	55,560
Depreciation	7,149	6,795
Amortization	1,009	1,127
Total costs and expenses	321,648	327,789
Income from operations	36,652	38,852
Interest expense	(3,815)	(4,094)
Other income - net	816	1,706
Income before income taxes	33,653	36,464
Income taxes	(13,079)	(14,186)
Net income	$20,574	$22,278
Earnings Per Share		
Net income	$1.17	$1.20
Average number of shares outstanding	17,510	18,522
Diluted Earnings Per Share		
Net income	$1.12	$1.17
Average number of shares outstanding	18,305	19,000
Cash Dividends Per Share	$0.20	$0.18

See accompanying notes to unaudited consolidated financial statements.

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

	Three Months Ended March 31, 2014	Three Months Ended March 31, 2013
Cash Flows from Operating Activities		
Net income	$20,574	$22,278
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8,158	7,922
Deferred income taxes	6,841	(681)
Provision for uncollectible accounts receivable	3,304	2,967
Amortization of discount on convertible notes	2,261	2,114
Stock option expense	1,309	1,491
Amortization of debt issuance costs	337	780
Noncash long-term incentive compensation	373	612
Changes in operating assets and liabilities, excluding amounts acquired in business combinations:		
Increase in accounts receivable	(27,700)	(36,706)
Decrease in inventories	27	499
Increase in prepaid expenses	(1,112)	(1,092)
Decrease in accounts payable and other current liabilities	(32,561)	(698)
Increase in income taxes	5,322	10,139
Increase in other assets	(1,069)	(3,071)
Increase in other liabilities	3,080	3,282
Excess tax benefit on share-based compensation	(1,399)	(1,891)
Other sources	409	196
Net cash provided/(used) by operating activities	(11,846)	8,141
Cash Flows from Investing Activities		
Capital expenditures	(8,131)	(5,406)
Business combinations, net of cash acquired	(250)	-
Other sources	29	78
Net cash used by investing activities	(8,352)	(5,328)
Cash Flows from Financing Activities		
Purchases of treasury stock	(32,982)	-
Dividends paid	(3,303)	(3,367)
Capital stock surrendered to pay taxes on stock-based compensation	(2,916)	(3,389)
Proceeds from exercise of stock options	13,193	10,168
Excess tax benefit on share-based compensation	1,399	1,891
Increase/(decrease) in cash overdrafts payable	369	(3,165)
Debt issuance costs	-	(1,107)
Other uses	(501)	(419)
Net cash provided/(used) by financing activities	(24,741)	612
Increase/(Decrease) in Cash and Cash Equivalents	(44,939)	3,425
Cash and cash equivalents at beginning of year	84,418	69,531
Cash and cash equivalents at end of period	$39,479	$72,956

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, 2013 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 state 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 audited Consolidated Financial Statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2013.

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.

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.

During the three month period ended March 31, 2014, we reversed Medicare cap liability of $847,000 for amounts recorded in the fourth quarter of 2013 for two programs' projected 2014 measurement period liability. We reversed these amounts as improving admissions trends in these programs indicate that the liability had been eliminated for one program and partially eliminated for the other program.

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

	March 31,	
	2014	2013
Beginning balance January 1,	$8,260	$1,261
2014 measurement period	(847)	-
2013 measurement period	-	(873)
Ending balance March 31,	$7,413	$388

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 March 31,	
2014	2013
$1,699	$1,929

3. Segments

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

	Three months ended March 31, 2014	2013
Service Revenues and Sales		
VITAS	$260,412	$271,326
Roto-Rooter	97,888	95,315
Total	$358,300	$366,641
After-tax Earnings		
VITAS	$18,159	$20,142
Roto-Rooter	10,033	9,624
Total	28,192	29,766
Corporate	(7,618)	(7,488)
Net income	$20,574	$22,278

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 March 31,	Net Income: Income	Shares	Earnings per Share
2014			
Earnings	$ 20,574	17,510	$ 1.17
Dilutive stock options	-	362	
Nonvested stock awards	-	148	
Conversion of Notes	-	285	
Diluted earnings	$ 20,574	18,305	$ 1.12
2013			
Earnings	$ 22,278	18,522	$ 1.20
Dilutive stock options	-	371	
Nonvested stock awards	-	107	
Diluted earnings	$ 22,278	19,000	$ 1.17

For the three-month period ended March 31, 2014, 329,000 stock options were excluded from the computation of diluted earnings per share because they would have been anti-dilutive. For the three-month period ended March 31, 2013, 11,000 stock options were excluded from the computation of diluted earnings per share.

Diluted earnings per share was impacted as the result of our 1.875% Senior Convertible Notes (the "Notes"). Beginning March 1, 2014, the Notes can be converted into our Capital Stock in accordance with the terms of the Notes. At March 31, 2014, our share price exceeded the Convertible Note price. Using the treasury method, the diluted share count was 285,000 shares higher assuming 100% of the Notes are presumed for net share settlement. The purchased call option is anticipated to offset any shares issued at the maturity of the Notes. Under generally accepted accounting principles the purchased call option does not impact the calculation of diluted earnings per share as it is always anti-dilutive. There is no economic dilution anticipated upon conversion as a result of our purchased call options.

5. Long-Term Debt

On January 18, 2013, we replaced our existing credit agreement with our Revolving Credit Facility ("2013 Credit Agreement"). Terms of the 2013 Credit Agreement consist of a five-year, $350 million revolving credit facility. This 2013 Credit Agreement has a floating interest rate that is currently LIBOR plus 125 basis points. The 2013 Credit Agreement also includes a $150 million expansion feature. Debt issuance costs associated with the existing credit agreement were not material. With respect to the 2013 Credit Agreement, deferred financing costs are immaterial. The 2013 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 March 31, 2014. We have issued $35.0 million in standby letters of credit as of March 31, 2014 for insurance purposes. Issued letters of credit reduce our available credit under the 2013 Credit Agreement. As of March 31, 2014, we have approximately $315.0 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:

	March 31, 2014	December 31, 2013
Principal amount of convertible debentures	$ 186,956	$ 186,956
Unamortized debt discount	(1,131)	(3,392)
Carrying amount of convertible debentures	$ 185,825	$ 183,564
Additional paid in capital (net of tax)	$ 31,310	$ 31,310

In the second quarter of 2013, the principal amount of the convertible debentures was reclassified to current as the amounts are due in May 2014.

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

	Three months ended March 31, 2014	2013
Cash interest expense	$ 1,217	$ 1,200
Non-cash amortization of debt discount	2,261	2,114
Amortization and write-off of debt costs	337	780
Total interest expense	$ 3,815	$ 4,094

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% as of March 31, 2014.

- 8 -

6. Other Income – Net

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

	Three months ended March 31, 2014	2013
Market value gains on assets held in deferred compensation trust	$ 1,162	$ 1,472
Loss on disposal of property and equipment	(278)	(78)
Interest income - net	(50)	303
Other - net	(18)	9
Total other income - net	$ 816	$ 1,706

7. Stock-Based Compensation Plans

On February 21, 2014, the Compensation/Incentive Committee of the Board of Directors ("CIC") granted 10,340 Performance Stock Units ("PSUs") contingent upon the achievement of certain total shareholders return ("TSR") targets as compared to the TSR of a group of peer companies for the three-year period ending December 31, 2016, the date at which such awards may vest. The cumulative compensation cost of the TSR-based PSUs award to be recorded over the three year service period is $1.2 million.

On February 21, 2014, the CIC also granted 14,061 PSUs contingent upon the achievement of certain earnings per share ("EPS") targets for the three-year period ending December 31, 2016. At the end of each reporting period, the Company estimates the number of shares that it believes will ultimately be earned and records that expense over the service period of the award. We currently estimate the cumulative compensation cost of the EPS-based PSUs to be recorded over the three year service period is $1.2 million.

8. Independent Contractor Operations

The Roto-Rooter segment sublicenses with 68 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 March 31, 2014 totaling $1.5 million (December 31, 2013 - $1.5 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 March 31, 2014. We recorded the following from our independent contractors (in thousands):

	Three months ended March 31, 2014	2013
Revenues	$ 9,023	$ 8,210
Pretax profits	5,159	4,258

9. 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 March 31, 2014	2013

$3,897	$4,296

10. Legal and Regulatory Matters

The VITAS segment of the Company's business operates in a heavily-regulated industry. As a result, the Company is subjected to inquiries and investigations by various government agencies, as well as to lawsuits, including qui tam actions. The following sections describe the various ongoing material lawsuits and investigations of which the Company is currently aware. It is not possible at this time for us to estimate either the timing or outcome of any of those matters, or whether any potential loss, or range of potential losses, is probable or estimable.

Regulatory Matters and Litigation

On January 12, 2012, a putative class action lawsuit was filed in the U.S. District Court for the Southern District of Ohio against the Company, Kevin McNamara, David Williams, and Timothy O'Toole, In re Chemed Corp. Securities Litigation, Civil Action No. 1:12-cv-28 (S.D. Ohio). On June 18, 2012, an amended complaint was filed 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. Plaintiffs seek, on behalf of a putative class of purchasers of Chemed Capital Stock, compensatory damages in an unspecified amount and attorneys' fees and expenses, arising from Defendants' alleged failure to disclose an alleged fraudulent scheme at VITAS to enroll ineligible hospice patients and to fraudulently obtain payments from the federal government. Defendants filed motions to dismiss the amended complaint on August 17, 2012, which were pending when the parties reached an agreement to settle the action. On June 7, 2013, following the filing of U.S. v. VITAS, discussed below, Plaintiffs filed a motion for leave to file a second amended complaint. Defendants opposed this motion. On September 16, 2013, Plaintiffs executed a Settlement Term Sheet with Defendants, reaching an agreement in principle to settle this case subject to Court approval. On February 6, 2014, Plaintiffs, on behalf of a putative class of purchasers of Chemed Capital Stock between February 15, 2010 and May 2, 2013, inclusive, executed a stipulation of settlement with defendants, agreeing to settle this case in full and with prejudice, and to provide Defendants with full releases of all claims that are or could have been asserted by Plaintiffs in exchange for payment of $6.0 million by our insurer into a settlement fund for the benefit of the putative settlement class ("Settlement"). The Settlement of $6.0 million has been recorded as an accrual and offsetting prepaid in the accompanying Consolidated Balance Sheet. This Settlement received preliminary Court approval on March 27, 2014 and is scheduled for a final hearing on July 19, 2014. Defendants agreed to enter into this Settlement in order to eliminate the burden, expense and distraction of further litigation.

In June 2011, the U.S. Attorney provided the Company with a partially unsealed qui tam complaint filed under seal in the U.S. District Court for the Western District of Texas, United States, et al. ex rel. Urick v. VITAS HME Solutions, Inc. et al., 5:08-cv-0663 ("Urick"). The U.S. Attorney filed a notice in May 2012 stating that it had decided not to intervene in the case at that time but indicating that it continues to investigate the allegations. In June 2012, the complaint was unsealed. The complaint asserts violations of the federal False Claims Act and the Texas Medicaid Fraud Prevention Act based on allegations of a conspiracy to submit to Medicare and Medicaid false claims involving hospice services for ineligible patients, unnecessary medical supplies, failing to satisfy certain prerequisites for payment, and altering patient records, including backdating patient revocations. The suit was brought by Barbara Urick, a registered nurse in VITAS's San Antonio program, against VITAS, certain of its affiliates, and several former VITAS employees, including physicians Justo Cisneros and Antonio Cavasos and nurses Sally Schwenk, Diane Anest, and Edith Reed. In September 2012 and July 2013, the plaintiff dismissed all claims against the individual defendants. The complaint was served on the VITAS entities on April 12, 2013.

Also in June 2011, the U.S. Attorney provided the Company with a partially unsealed qui tam complaint filed under seal in the U.S. District Court for the Northern District of Illinois, United States, et al. ex rel. Spottiswood v. Chemed Corp., 1:07-cv-4566 ("Spottiswood"). In April 2012, the complaint was unsealed. The U.S. Attorney and Attorney General for the State of Illinois filed notices in April and May 2012, respectively, stating that they had decided not to intervene in the case at that time but indicating that they continue to investigate the allegations. Plaintiff filed an amended complaint in November 2012. The complaint asserts violations of the federal False Claims Act and the Illinois Whistleblower Reward and Protection Act based on allegations that VITAS fraudulently billed Medicare and Medicaid for providing unwarranted continuous care services. The suit was brought by Laura Spottiswood, a former part-time pool registered nurse at VITAS, against Chemed, VITAS, and a VITAS affiliate. The complaint was served on the defendants on April 12, 2013. On May 29 and June 4, 2013, respectively, the Court granted the government's motion to partially intervene in Spottiswood and in Urick on the allegations that VITAS submitted or caused to be submitted false or fraudulent claims for continuous care and routine home care on behalf of certain ineligible Medicare beneficiaries. The Court also transferred them to the U.S. District Court for the Western District of Missouri under docket Nos. 4:13-cv-505 and 4:13-cv-563, respectively.

On May 2, 2013, the government filed a False Claims Act complaint against the Company and certain of its hospice-related subsidiaries in the U.S. District Court for the Western District of Missouri, United States v. VITAS Hospice Services, LLC, et al., No. 4:13-cv-00449-BCW (the "2013 Action"). Prior to that date, the Company received various subpoenas from the U.S. Department of Justice and OIG that have been previously disclosed. The 2013 Action alleges that, since at least 2002, VITAS, and since 2004, the Company, submitted or caused the submission of false claims to the Medicare program by (a) billing Medicare for continuous home care services when the patients were not eligible, the services were not provided, or the medical care was inappropriate, and (b) billing Medicare for patients who were not eligible for the Medicare hospice benefit because they did not have a life expectancy of six months or less if their illnesses ran their normal course. This complaint seeks treble damages, statutory penalties, and the costs of the action, plus interest. On August 1, 2013, the government filed its First Amended Complaint in the 2013 Action. The First Amended Complaint changed and supplemented some of the allegations, but did not otherwise expand the causes of action or the nature of the relief sought against VITAS. The defendants filed a motion to dismiss on September 24, 2013.

On May 6, 2013, the U.S. District Court for the Western District of Missouri, at the request of the government, unsealed a qui tam complaint against VITAS and VITAS Healthcare Corporation of California, United States ex rel. Charles Gonzales v. VITAS Healthcare Corporation, et al., CV 12-0761-R ("Gonzales"). The case was transferred from the Central District of California to the Western District of Missouri under docket No. 4:13-cv-344. The government partially intervened in Gonzales. The Gonzales complaint alleges that VITAS' Los Angeles program falsely certified and recertified patients as eligible for the Medicare Hospice Benefit. It alleges violations of the False Claims Act and seeks treble damages, civil penalties, recovery of costs, attorneys' fees and expenses, and pre- and post-judgment interest.

On September 25, 2013, the Court granted a joint motion by the government, the relators, and VITAS to consolidate the Spottiswood, Urick, and Gonzales complaints with the 2013 Action. As a result, the First Amended Complaint will govern the consolidated federal claims brought by the United States and the relators for all purposes. The relators and VITAS have stipulated that certain non-intervened claims will not be pursued by the relators. The Spottiswood relator filed an action under the Illinois False Claims Act, The State of Illinois ex rel. Laura Spottiswood v. Chemed Corporation, et al., No. 14 L 2786 in the Circuit Court of Cook County, Illinois on March 6, 2014. The Court granted the parties' joint motion to place this case on the its stay calendar, pending resolution of the 2013 Action.

VITAS has also received document subpoenas in related state matters. In February 2010, VITAS received a civil investigative demand ("CID") from the Texas Attorney General seeking documents from January 1, 2002 through the date of the CID, and interrogatory responses in connection with an investigation of possible fraudulent submission of Medicaid claims for non-qualifying patients and fraudulent shifting of costs from VITAS to the State of Texas and the United States. The CID requested similar information sought by prior Department of Justice subpoenas, including policy and procedure manuals and information concerning Medicare and Medicaid billing, patient statistics and sales and marketing practices, together with information concerning record-keeping and retention practices, and medical records concerning 117 patients. In September 2010, VITAS received a second CID from the Texas Attorney General seeking additional documents concerning business plans and results, revocation forms for certain patients, and electronic documents of 10 current and former employees. In July 2012, VITAS received an investigative subpoena from the Florida Attorney General seeking documents previously produced in the course of prior government investigations as well as, for the period January 1, 2007 through the date of production, billing records and procedures; information concerning business results, plans, and strategies; documents concerning patient eligibility for hospice care; and certain information concerning employees and their compensation.

The net costs incurred related to U.S. v. Vitas and related regulatory matters were $748,000 and $1.0 million for the periods ending March 31, 2014 and 2013, respectively.

In November 2013, two shareholder derivative lawsuits were filed against the Company's current and former directors, as well as certain of its officers, both of which are covered by the Company's commercial insurance. On November 6, 2013, KBC Asset Management NV filed suit in the United States Distrct Court for the District of Delaware, KBC Asset Management NV, derivatively on behalf of Chemed Corp. v. McNamara, et al., No. 13 Civ. 1854 (LPS) (D. Del.). It sued Kevin McNamara, Joel Gemunder, Patrick Grace, Thomas Hutton, Walter Krebs, Andrea Lindell, Thomas Rice, Donald Saunders, Arthur Tucker, Jr., George Walsh III, Frank Wood, Timothy O'Toole, David Williams and Ernest Mrozek, together with the Company as nominal defendant. Plaintiff alleges that since at least 2004, Chemed, through VITAS, has submitted or caused the submission of false claims to Medicare. The suit alleges a claim for breach of fiduciary duty against the individual defendants, and seeks (a) a declaration that the individual defendants breached their fiduciary duties to the Company; (b) an order requiring those defendants to pay compensatory damages, restitution and exemplary damages, in unspecified amounts, to the Company; (c) an order directing the Company to implement new policies and procedures; and (d) costs and disbursements incurred in bringing the action, including attorneys' fees.

On November 14, 2013, Mildred A. North filed suit in the United States District Court for the Southern District of Ohio, North, derivatively on behalf of Chemed Corp. v. Kevin McNamara, el al., No. 13 Civ. 833 (MDB) (S.D. Ohio). She sued Kevin McNamara, David Williams, Timothy O'Toole, Joel Gemunder, Patrick Grace, Walter Krebs, Andrea Lindell, Thomas Rice, Donald Saunders, George Walsh III, Frank Wood and Thomas Hutton, together with the Company as nominal defendant. Plaintiff alleges that, between February 2010 and the present, the individual defendants breached their fiduciary duties as officers and directors of Chemed by, among other things, (a) allegedly causing VITAS to submit improper and ineligible claims to Medicare and Medicaid; and (b) allegedly misrepresenting the state of Chemed's internal controls. The suit alleges claims for breach of fiduciary duty, abuse of control and gross mismanagement against the individual defendants. The complaint also alleges unjust enrichment and insider trading against Messrs. McNamara, Williams and O'Toole. Plaintiff seeks (a) a declaration that the individual defendants breached their fiduciary duties to the Company; (b) an order requiring those defendants to pay compensatory damages, restitution and exemplary damages, in unspecified amounts, to the Company; (c) an order directing the Company to implement new policies and procedures; and (d) costs and disbursements incurred in bringing the action, including attorneys' fees.

On December 20, 2013, Plaintiff in the North action filed a motion before the Judicial Panel on Multidistrict Litigation seeking centralized treatment of her action and the KBC action in the U.S. District Court for the Southern District of Ohio. Defendants in both cases, as well as Plaintiff KBC, opposed that motion, consistent with Chemed's By-law 8.07, which requires all derivative suits brought in Chemed's name to proceed in federal or state court in Delaware. The MDL Panel denied the motion on April 2, 2014. On January 29, 2014 Defendants filed motions to transfer North to Delaware under 28 U.S.C § 1404 and to stay the case until after resolution of that motion and the MDL motion.

The Company intends to defend vigorously against the allegations in each of the above lawsuits. Regardless of the outcome of any of the preceding matters, responding to the subpoenas and dealing with the various regulatory agencies and opposing parties can adversely affect us through defense costs, potential payments, diversion of management time, and related publicity. Although the Company intends to defend them vigorously, there can be no assurance that those suits will not have a material adverse effect on the Company.

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 three-year terms. Either party may cancel the Agreements at the end of any term by giving 30 days prior written notice. VITAS made purchases from OCR of $8.8 million and $9.6 million for the three months ended March 31, 2014 and 2013, respectively. Purchases from OCR represent approximately 90% of all pharmacy services used by VITAS.

12. Cash Overdrafts and Cash Equivalents

Included in accounts payable at March 31, 2014 is cash overdrafts payable of $1.2 million (December 31, 2013 - $806,000).

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 $20.0 million in cash equivalents as of March 31, 2014. There was $23.1 million in cash equivalents as of December 31, 2013. The weighted average rate of return for our cash equivalents was 0.09% for March 31, 2014 and 0.08% for December 31, 2013.

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 March 31, 2014 (in thousands):

		Fair Value Measure		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mutual fund investments of deferred compensation plans held in trust	$ 45,498	$ 45,732	$ -	$ -
Long-term debt	185,825	209,157	-	-

The following shows the carrying value, fair value and the hierarchy for our financial instruments as of December 31, 2013 (in thousands):

		Fair Value Measure		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mutual fund investments of deferred compensation plans held in trust	$ 42,465	$ 42,465	$ -	$ -
Long-term debt	183,564	193,032	-	-

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 Repurchase Plan Transactions

We repurchased the following capital stock for the three months ended March 31, 2014 and 2013:

	Three months ended March 31,	
	2014	2013
Shares repurchased	382,934	-
Weighted average price per share	$ 86.13	$ -

In February 2014, the Board of Directors authorized an additional $100 million for stock repurchase under Chemed’s existing share repurchase program. We currently have $88.8 million of authorization remaining under this share repurchase plan.

15. 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 March 31, 2014 and December 31, 2013 for the balance sheet, the three months ended March 31, 2014 and December 31, 2013 for the income statement and the three months ended March 31, 2014 and March 31, 2013 for the statement of cash flows (dollars in thousands):

March 31, 2014	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
ASSETS					
Cash and cash equivalents	$41,808	$(11,336)	$ 9,007	$ -	$ 39,479
Accounts receivable, including intercompany	1,231	517,646	1,256	(403,981)	116,152
Inventories	-	6,148	528	-	6,676
Current deferred income taxes	-	14,720	264	(1,215)	13,769
Prepaid income taxes	9,155	-	7	(5,756)	3,406
Prepaid expenses	6,612	11,958	360	-	18,930
Total current assets	58,806	539,136	11,422	(410,952)	198,412
Investments of deferred compensation plans	-	-	45,732	-	45,732
Properties and equipment, at cost less accumulated depreciation	9,963	81,033	2,579	-	93,575
Identifiable intangible assets less accumulated amortization	-	56,276	-	-	56,276
Goodwill	-	462,687	4,274	-	466,961
Other assets	12,745	1,877	17,141	(24,099)	7,664
Investments in subsidiaries	964,753	28,007	-	(992,760)	-
Total assets	$1,046,267	$1,169,016	$ 81,148	$ (1,427,811)	$ 868,620
LIABILITIES AND STOCKHOLDERS' EQUITY					
Accounts payable, including intercompany	$398,529	$39,213	$ 4,838	$ (403,981)	$ 38,599
Current portion of long-term debt	185,825	-	-	-	185,825
Income taxes	-	7,663	2,060	(5,756)	3,967
Accrued insurance	1,433	37,958	-	-	39,391
Accrued compensation	1,086	36,807	340	-	38,233
Accrued legal	6,043	1,111	-	-	7,154
Other current liabilities	4,288	21,429	180	(1,215)	24,682
Total current liabilities	597,204	144,181	7,418	(410,952)	337,851
Deferred income taxes	-	52,331	-	(24,099)	28,232
Deferred compensation liabilities	-	-	45,498	-	45,498
Other liabilities	3,130	6,879	1,097	-	11,106
Stockholders' equity	445,933	965,625	27,135	(992,760)	445,933
Total liabilities and stockholders' equity	$1,046,267	$1,169,016	$ 81,148	$ (1,427,811)	$ 868,620

December 31, 2013	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
ASSETS					
Cash and cash equivalents	$84,005	$(8,777)	$ 9,190	$ -	$ 84,418
Accounts receivable, including intercompany	925	509,580	1,000	(419,735)	91,770
Inventories	-	6,246	457	-	6,703
Current deferred income taxes	-	21,307	126	(1,176)	20,257
Prepaid income taxes	3,710	1,176	349	(1,545)	3,690
Prepaid expenses	6,925	10,682	211	-	17,818
Total current assets	95,565	540,214	11,333	(422,456)	224,656
Investments of deferred compensation plans	-	-	42,465	-	42,465
Properties and equipment, at cost less accumulated depreciation	10,184	80,144	2,627	-	92,955
Identifiable intangible assets less accumulated amortization	-	56,556	-	-	56,556
Goodwill	-	462,489	4,382	-	466,871
Other assets	17,782	1,775	15,888	(25,247)	10,198
Investments in subsidiaries	945,450	27,564	-	(973,014)	-
Total assets	$1,068,981	$1,168,742	$ 76,695	$ (1,420,717)	$ 893,701
LIABILITIES AND STOCKHOLDERS' EQUITY					
Accounts payable, including intercompany	$417,593	$39,424	$ 4,476	$ (419,735)	$ 41,758
Current portion of long-term debt	183,564	-	-	-	183,564
Income taxes	1,106	210	340	(1,545)	111
Accrued insurance	784	41,075	-	-	41,859
Accrued compensation	5,047	42,905	371	-	48,323
Accrued legal	6,031	17,179	-	-	23,210
Other current liabilities	2,739	22,219	1,379	(1,176)	25,161
Total current liabilities	616,864	163,012	6,566	(422,456)	363,986
Deferred income taxes	-	52,548	-	(25,247)	27,301
Deferred compensation liabilities	-	-	42,348	-	42,348
Other liabilities	3,227	6,914	1,035	-	11,176
Stockholders' equity	448,890	946,268	26,746	(973,014)	448,890
Total liabilities and stockholders' equity	$1,068,981	$1,168,742	$ 76,695	$ (1,420,717)	$ 893,701

For the three months ended March 31, 2014	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
Continuing Operations					
Service revenues and sales	$-	$349,890	$ 8,410	$ -	$ 358,300
Cost of services provided and goods sold	-	253,052	4,767	-	257,819
Selling, general and administrative expenses	5,710	47,005	2,956	-	55,671
Depreciation	241	6,671	237	-	7,149
Amortization	445	564	-	-	1,009
Total costs and expenses	6,396	307,292	7,960	-	321,648
Income/ (loss) from operations	(6,396)	42,598	450	-	36,652
Interest expense	(3,663)	(152)	-	-	(3,815)
Other (expense)/income - net	3,672	(4,014)	1,158	-	816
Income/ (loss) before income taxes	(6,387)	38,432	1,608	-	33,653
Income tax (provision)/ benefit	2,137	(14,613)	(603)	-	(13,079)
Equity in net income of subsidiaries	24,824	1,028	-	(25,852)	-
Net income	$20,574	$24,847	$ 1,005	$ (25,852)	$ 20,574

For the three months ended March 31, 2013	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated
Continuing Operations					
Service revenues and sales	$-	$359,056	$ 7,585	$ -	$ 366,641
Cost of services provided and goods sold	-	259,977	4,330	-	264,307
Selling, general and administrative expenses	5,872	46,572	3,116	-	55,560
Depreciation	240	6,325	230	-	6,795
Amortization	482	645	-	-	1,127
Total costs and expenses	6,594	313,519	7,676	-	327,789
Income/ (loss) from operations	(6,594)	45,537	(91)	-	38,852
Interest expense	(3,975)	(105)	(14)	-	(4,094)
Other (expense)/income - net	4,273	(4,035)	1,468	-	1,706
Income/ (loss) before income taxes	(6,296)	41,397	1,363	-	36,464
Income tax (provision)/ benefit	2,133	(15,817)	(502)	-	(14,186)
Equity in net income of subsidiaries	26,441	910	-	(27,351)	-
Net income	$22,278	$26,490	$ 861	$ (27,351)	$ 22,278

For the three months ended March 31 2014	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidated
Cash Flow from Operating Activities:				
Net cash provided by operating activities	$(6,773)	$(5,370)	$ 297	$ (11,846)
Cash Flow from Investing Activities:				
Capital expenditures	(20)	(7,897)	(214)	(8,131)
Business combinations, net of cash acquired	-	(250)	-	(250)
Other sources/(uses) - net	(58)	62	25	29
Net cash used by investing activities	(78)	(8,085)	(189)	(8,352)
Cash Flow from Financing Activities:				
Increase /(decrease) in cash overdrafts payable	323	46	-	369
Change in intercompany accounts	(11,080)	10,850	230	-
Dividends paid	(3,303)	-	-	(3,303)
Debt issuance costs	-	-	-	-
Capital stock surrendered to pay taxes on stock-based compensation	(2,916)	-	-	(2,916)
Purchases of treasury stock	(32,982)	-	-	(32,982)
Proceeds from exercise of stock options	13,193	-	-	13,193
Excess tax benefit on share-based compensation	1,399	-	-	1,399
Other sources/(uses) - net	20	-	(521)	(501)
Net cash provided/(used) by financing activities	(35,346)	10,896	(291)	(24,741)
Net increase/(decrease) in cash and cash equivalents	(42,197)	(2,559)	(183)	(44,939)
Cash and cash equivalents at beginning of year	84,005	(8,777)	9,190	84,418
Cash and cash equivalents at end of period	$41,808	$(11,336)	$ 9,007	$ 39,479

For the three months ended March 31, 2013	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidated
Cash Flow from Operating Activities:				
Net cash provided by operating activities	$(4,511)	$12,302	$ 350	$ 8,141
Cash Flow from Investing Activities:				
Capital expenditures	(10)	(5,278)	(118)	(5,406)
Other sources/(uses) - net	(16)	71	23	78
Net cash provided/(used) by investing activities	(26)	(5,207)	(95)	(5,328)
Cash Flow from Financing Activities:				
Increase/(decrease) in cash overdrafts payable	(554)	(2,611)	-	(3,165)
Change in intercompany accounts	6,731	(6,570)	(161)	-
Dividends paid	(3,367)	-	-	(3,367)
Debt issuance	(1,107)	-	-	(1,107)
Capital stock surrendered to pay taxes on stock-based compensation	(3,389)	-	-	(3,389)
Purchases of treasury stock	-	-	-	-
Proceeds from exercise of stock options	10,168	-	-	10,168
Excess tax benefit on share-based compensation	1,891	-	-	1,891
Other sources/(uses) - net	(4)	-	(415)	(419)
Net cash provided/(used) by financing activities	10,369	(9,181)	(576)	612
Net increase in cash and cash equivalents	5,832	(2,086)	(321)	3,425
Cash and cash equivalents at beginning of year	56,342	4,674	8,515	69,531
Cash and cash equivalents at end of period	$62,174	$2,588	$ 8,194	$ 72,956

- 16 -

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Executive Summary

We operate through our two wholly-owned subsidiaries, VITAS Healthcare Corporation and Roto-Rooter Group, Inc. VITAS focuses on hospice care that helps make terminally ill patients' final days as comfortable as possible. Through its teams of doctors, nurses, home health aides, social workers, clergy and volunteers, VITAS provides direct medical services to patients, as well as spiritual and emotional counseling to both patients and their families. Roto-Rooter's services are focused on providing plumbing and drain cleaning services to both residential and commercial customers. Through its network of company-owned branches, independent contractors and franchisees, Roto-Rooter offers plumbing and drain cleaning service to over 90% of the U.S. population.

The following is a summary of the key operating results (in thousands except per share amounts):

	Three months ended March 31,					
		2014			2013	
Service revenues and sales	$	358,300		$	366,641	
Net income	$	20,574		$	22,278	
Diluted EPS	$	1.12		$	1.17	
Adjusted net income	$	23,713		$	26,140	
Adjusted diluted EPS	$	1.32		$	1.38	
Adjusted EBITDA	$	47,672		$	51,296	
Adjusted EBITDA as a % of revenue		13.3	%		14.0	%

Adjusted net income, adjusted diluted EPS, earnings before interest, taxes and depreciation and amortization ("EBITDA") and Adjusted EBITDA are not measures derived in accordance with GAAP. We use Adjusted Diluted EPS as a measure of earnings for our long-term incentive plan awards. We provide non-GAAP measures to help readers evaluate our operating results, compare our operating performance with that of similar companies that have different capital structures and help evaluate our ability to meet future debt service, capital expenditure and working capital requirements. Our non-GAAP measures should not be considered in isolation or as a substitute for comparable measures presented in accordance with GAAP. A reconciliation of our non-GAAP measures are presented on pages 25-26.

For the three months ended March 31, 2014, the decrease in consolidated service revenues and sales was driven by a 2.7% increase at Roto-Rooter and a 4.0% decrease at VITAS. The increase in service revenues at Roto-Rooter was driven by a 4.8% increase in price and mix shift offset by a 2.4% decrease in job count. The remaining difference relates to increases in contractor revenue. The decrease in service revenues at VITAS was a result of Medicare reimbursement rates increasing 1.4%, offset by a 2.0% decrease as a result of sequestration, decreased ADC of 0.8%, and geographical and level of care mix shift. Consolidated net income decreased 7.6% as a result of the lower revenue at VITAS and higher health insurance costs at Vitas as well as increased advertising expense at Roto-Rooter. Diluted EPS decreased 4.3% as a result of the decrease in net income offset by a lower number of shares outstanding. Adjusted EBITDA as a percent of revenue decreased 0.7% mainly as a result of lower revenue at VITAS. See page 27 for additional VITAS operating metrics.

On April 1, 2013, Medicare reduced hospice reimbursement rates 2.0%. Effective October 1, 2013, Medicare increased the average hospice rate approximately 1.4% This effectively reduced Medicare hospice reimbursement 0.6% in the first quarter of 2014 when compared to the prior year quarter. VITAS expects its full-year 2014 revenue growth, prior to Medicare cap, to be in the range of 1.0% to 3.0%. Admissions in 2014 are estimated to increase 3.0% to 4.0%. Adjusted EBITDA margin, prior to Medicare cap, is estimated to be 14.5% to 15.0%. Medicare cap is estimated to be $5.0 million in 2014. Roto-Rooter expects full-year 2014 revenue growth of 3.0% to 4.0%. The revenue estimate is a result of increased job pricing of approximately 2.0%. Adjusted EBITDA margin for 2014 is estimated in the range of 19.0% to 20.0%. We anticipate that our operating income and cash flows will be sufficient to operate our businesses and meet any commitments for the foreseeable future.

Financial Condition

Liquidity and Capital Resources

Material changes in the balance sheet accounts from December 31, 2013 to March 31, 2014 include the following:

- A $24.4 million increase in accounts receivable related to the timing of Medicare receipts.
- A $6.5 million decrease in current deferred income taxes mainly related to the payment of litigation settlements.
- A $10.1 million decrease in accrued compensation related to the payment of incentive compensation in the first quarter.
- A $16.1 million decrease in accrued legal due to the payment of litigation settlements.

Net cash provided by operating activities decreased $20.0 million primarily as a result of the decrease in accounts payable and other current liabilities offset by the increase in a