Addus HomeCare Corp
Form 10-Q
November 09, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2016

OR

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

For the transition period from to

Commission file number 001-34504

ADDUS HOMECARE CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**20-5340172**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
2300 Warrenville Rd.	
Downers Grove, IL	**60515**
(Address of principal executive offices)	**(Zip code)**

630-296-3400

(Registrant s telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. 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 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, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (check one):

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

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

Common Stock $0.001 par value

Shares outstanding at October 31, 2016: 11,463,501

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

ADDUS HOMECARE CORPORATION

AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

As of September 30, 2016 and December 31, 2015

(Amounts and Shares in Thousands, Except Per Share Data)

	(Unaudited) September 30, 2016	(Audited) December 31, 2015
Assets		
Current assets		
Cash	$ 39,446	$ 4,104
Accounts receivable, net of allowances of $7,208 and $4,850 at September 30, 2016 and December 31, 2015, respectively	80,454	84,959
Prepaid expenses and other current assets	4,485	4,858
Deferred tax assets	8,640	8,640
Total current assets	133,025	102,561
Property and equipment, net of accumulated depreciation and amortization	5,993	8,619
Other assets		
Goodwill	73,851	68,844
Intangibles, net of accumulated amortization	16,671	10,351
Investment in joint venture	900	900
Other assets		1,337
Total other assets	91,422	81,432
Total assets	$ 230,440	$ 192,612
Liabilities and stockholders equity		
Current liabilities		
Accounts payable	$ 4,268	$ 4,748
Current portion of long-term debt, net of debt issuance costs	2,244	1,109
Current portion of contingent earn-out obligation		1,250
Accrued expenses	43,929	35,082
Total current liabilities	50,441	42,189
Long-term liabilities		
Deferred tax liabilities	6,815	6,815
Long-term debt, less current portion, net of debt issuance costs	22,723	1,882

Total long-term liabilities	29,538	8,697
Total liabilities	79,979	50,886
Stockholders equity		
Common stock $.001 par value; 40,000 authorized and 11,464 and 11,108 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	12	11
Additional paid-in capital	91,354	87,076
Retained earnings	59,095	54,639
Total stockholders equity	150,461	141,726
Total liabilities and stockholders equity	$ 230,440	$ 192,612

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited)

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ADDUS HOMECARE CORPORATION

AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

For the Three and Nine Months Ended September 30, 2016 and 2015

(Amounts and Shares in Thousands, Except Per Share Data)

(Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
Net service revenues	$ 103,502	$ 84,331	$ 297,032	$ 252,055
Cost of service revenues	76,079	60,809	219,594	182,925
Gross profit	27,423	23,522	77,438	69,130
General and administrative expenses	23,207	18,041	64,953	52,617
Depreciation and amortization	1,721	1,197	4,943	3,504
Total operating expenses	24,928	19,238	69,896	56,121
Operating income	2,495	4,284	7,542	13,009
Interest income	(16)	(12)	(46)	(22)
Interest expense	648	175	1,760	527
Total interest expense, net	632	163	1,714	505
Other income	126		126	
Income before income taxes	1,989	4,121	5,954	12,504
Income tax expense	290	1,234	1,498	4,202
Net income	$ 1,699	$ 2,887	$ 4,456	$ 8,302
Net income per common share				
Basic income per share	$ 0.15	$ 0.26	$ 0.40	$ 0.76
Diluted income per share	$ 0.15	$ 0.26	$ 0.40	$ 0.74
Weighted average number of common shares and potential common shares outstanding:				
Basic	11,367	11,007	11,190	10,978
Diluted	11,417	11,247	11,227	11,183

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited)

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ADDUS HOMECARE CORPORATION

AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

For the Nine Months Ended September 30, 2016

(Amounts and Shares in Thousands)

(Unaudited)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Total Stockholders Equity
Balance at December 31, 2015	11,108	$ 11	$ 87,076	$ 54,639	$ 141,726
Issuance of shares of common stock under restricted stock award agreements	88				
Forfeiture of shares of common stock under restricted stock award agreements	(79)				
Stock-based compensation			1,263		1,263
Exercise of stock options	347	1	3,015		3,016
Net income				4,456	4,456
Balance at September 30, 2016	11,464	$ 12	$ 91,354	$ 59,095	$ 150,461

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited)

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ADDUS HOMECARE CORPORATION

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Nine Months Ended September 30, 2016 and 2015

(Amounts and Shares in Thousands)

(Unaudited)

	For the Nine Months Ended September 30, 2016	2015
Cash flows from operating activities:		
Net income	$ 4,456	$ 8,302
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,943	3,504
Non-cash restructuring	2,554	
Deferred income taxes		(13)
Stock-based compensation	1,263	1,162
Amortization of debt issuance costs	261	46
Provision for doubtful accounts	5,089	2,974
Revaluation of contingent consideration		130
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable	5,540	(12,085)
Prepaid expenses and other current assets	1,136	(468)
Accounts payable	(577)	698
Accrued expenses	6,326	4,536
Net cash provided by operating activities	30,991	8,786
Cash flows from investing activities:		
Acquisitions of businesses	(20,449)	(4,250)
Acquisition of customer list		(146)
Purchases of property and equipment	(1,168)	(1,316)
Net cash (used in) investing activities	(21,617)	(5,712)
Cash flows from financing activities:		
Cash received from exercise of stock options	3,016	305
Borrowings on revolver	27,000	
Borrowings on term loan	25,000	
Payments for debt issuance costs	(495)	(86)
Payments on capital leases	(828)	(779)
Payments on term loan	(625)	
Payments on revolver	(27,000)	
Payment on contingent earn-out obligation	(100)	(1,000)
Net cash provided by (used in) financing activities	25,968	(1,560)
Net change in cash	35,342	1,514
Cash, at beginning of period	4,104	13,363

Cash, at end of period	$	39,446	$	14,877
Supplemental disclosures of cash flow information:				
Cash paid for interest	$	1,748	$	528
Cash paid for income taxes		3,236		575
Supplemental disclosures of non-cash investing and financing activities				
Tax benefit related to the amortization of tax goodwill in excess of book basis		120		120
Property and equipment acquired through capital lease obligations				378

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited)

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ADDUS HOMECARE CORPORATION

AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation and Description of Business

The condensed consolidated financial statements include the accounts of Addus HomeCare Corporation (Holdings) and its subsidiaries (together with Holdings, the Company or we). The Company operates as one reportable business segment and is a provider of comprehensive personal care services, which are provided primarily in the home. The Company s personal care services provide assistance with activities of daily living and adult day services. The Company s consumers are primarily persons who are at risk of hospitalization or institutionalization, such as the elderly, chronically ill and disabled. The Company s payor clients include federal, state and local governmental agencies, managed care organizations, commercial insurers and private individuals. As of September 30, 2016, the Company provided personal care services to over 34,000 consumers through 118 locations across 24 states, including three adult day services centers in Illinois.

Principles of Consolidation

All intercompany balances and transactions have been eliminated in consolidation. The Company s investment in entities with less than 20% ownership or in which the Company does not have the ability to influence the operations of the investee are accounted for using the cost method and are included in investments in joint ventures.

Revenue Recognition

The Company generates net service revenues by providing services directly to consumers. The Company receives payments for providing services from federal, state and local governmental agencies, managed care organizations, commercial insurers and private consumers. The Company s operations are principally provided based on authorized hours, determined by the relevant agency, at an hourly rate specified in agreements or fixed by legislation and recognized as revenues at the time services are rendered. Net service revenues are reimbursed by state, local and other governmental programs which are partially funded by Medicaid or Medicaid waiver programs, with the remainder reimbursed through private individuals and various insurance programs.

Allowance for Doubtful Accounts

The Company establishes its allowance for doubtful accounts to the extent it is probable that a portion or all of a particular account will not be collected. The Company establishes its provision for doubtful accounts primarily by analyzing historical trends and the aging of receivables. In its evaluation, the Company considers other factors including: delays in payment trends in individual states due to budget or funding issues; billing conversions related to acquisitions or internal systems; resubmission of bills with required documentation and disputes with specific payors. An allowance for doubtful accounts is maintained at a level that the Company s management believes is sufficient to cover potential losses. However, actual collections could differ from the Company s estimates.

Property and Equipment

Property and equipment are recorded at cost and depreciated over the estimated useful lives of the related assets by use of the straight-line method. Maintenance and repairs are charged to expense as incurred. The estimated useful lives of the property and equipment are as follows:

Computer equipment	3 5 years
Furniture and equipment	5 7 years
Transportation equipment	5 years
Computer software	5 10 years
Leasehold improvements	Lesser of useful life or lease term, unless probability of lease renewal is likely

Goodwill

The Company s carrying value of goodwill is the residual of the purchase price over the fair value of the net assets acquired from various acquisitions including the acquisition of Addus HealthCare, Inc. (Addus HealthCare). In accordance with Accounting Standards Codification (ASC) Topic 350, *Goodwill and Other Intangible Assets*, goodwill and intangible assets with indefinite useful lives are not amortized. The Company tests goodwill for impairment at the reporting unit level on an annual basis, as of October 1, or whenever potential impairment triggers occur, such as a significant change in business climate or regulatory changes that would indicate that an impairment may have occurred. The Company may use a qualitative test, known as Step 0, or a two-step quantitative method to determine whether impairment has occurred. In Step 0, the Company can elect to perform Step 0, an optional qualitative analysis, and based on the results, skip the remaining two steps. In 2015, the Company elected to implement Step 0 and was not required to conduct the remaining two step analysis. The results of the Company s Step 0 assessment indicated that it was more likely than not that the fair value of its reporting unit exceeded its carrying value and therefore the Company concluded that there were no impairments for the year ended December 31, 2015. No impairment charges were recorded for the three and nine months ended September 30, 2016 or 2015.

Intangible Assets

The Company s identifiable intangible assets consist of customer and referral relationships, trade names, trademarks, state licenses and non-compete agreements. Amortization is computed using straight-line and accelerated methods based upon the estimated useful lives of the respective assets, which range from two to twenty-five years.

Intangible assets with finite lives are amortized using the estimated economic benefit method over the useful life and assessed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The Company would recognize an impairment loss when the estimated future non-discounted cash flows associated with the intangible asset is less than the carrying value. An impairment change would then be recorded for the excess of the carrying value over the fair value. The Company estimates the fair value of these intangible assets using the income approach. No impairment charge was recorded for the three and nine months ended September 30, 2016 or 2015.

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The income approach, which the Company uses to estimate the fair value of its intangible assets (other than goodwill), is dependent on a number of factors including estimates of future market growth and trends, forecasted revenue and costs, expected periods the assets will be utilized, appropriate discount rates and other variables. The Company bases its fair value estimates on assumptions the Company believes to be reasonable but which are unpredictable and inherently uncertain. Actual future results may differ from those estimates.

The Company also has indefinite-lived intangible assets that are not subject to amortization expense such as certificates of need and licenses to conduct specific operations within geographic markets. The Company s management has concluded that certificates of need and licenses have indefinite lives, as management has determined that there are no legal, regulatory, contractual, economic or other factors that would limit the useful life of these intangible assets, and the Company intends to renew and operate the certificates of need and licenses indefinitely. The certificates of need and licenses are tested annually for impairment. No impairment was recorded for the three and nine months ended September 30, 2016 or 2015.

Debt Issuance Costs

The Company amortizes debt issuance costs on a straight-line method over the term of the related debt. This method approximates the effective interest method. The Company has classified the debt issuance costs as current portion of long-term debt or long term debt, less current portion as of September 30, 2016. For the year ended December 31, 2015, debt issuance costs are included in other assets on the Condensed Consolidated Balance Sheets as the Company had no long-term debt outstanding during the year to offset the debt issuance costs.

Workers Compensation Program

The Company s workers compensation program has a $0.4 million deductible component. The Company recognizes its obligations associated with this program in the period the claim is incurred. The cost of both the claims reported and claims incurred but not reported, up to the deductible, have been accrued based on historical claims experience, industry statistics and an actuarial analysis performed by an independent third party. The future claims payments related to the workers compensation program are secured by letters of credit.

Interest Income

Legislation enacted in Illinois entitles designated service program providers to receive a prompt payment interest penalty based on qualifying services approved for payment that remain unpaid after a designated period of time. As the amount and timing of the receipt of these payments are not certain, the interest income is recognized when received and reported in the statement of income as interest income. For the three and nine months ended September 30, 2016 and 2015, the Company did not receive any prompt payment interest. While the Company may be owed additional prompt payment interest, the amount and timing of receipt of such payments remains uncertain, and the Company has determined that it will continue to recognize prompt payment interest income when received.

Interest Expense

The Company s interest expense consists of interest costs on its credit facility, capital lease obligations and amortization of debt issuance costs and is reported in the statement of income when incurred.

Other Income

Other income consists of income distributions received from the investment in joint venture. The Company accounts for this income in accordance with ASC Topic 325, *Investments Other.* The Company recognizes the net accumulated earnings only to the extent distributed by the joint venture on the date received.

Income Tax Expense

The Company accounts for income taxes under the provisions of ASC Topic 740, *Income Taxes.* The objective of accounting for income taxes is to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in its financial statements or tax returns. Deferred taxes, resulting from differences between the financial and tax basis of the Company s assets and liabilities, are also adjusted for changes in tax rates and tax laws when changes are enacted. ASC Topic 740 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion or all of the deferred tax asset will not be realized. ASC Topic 740, also prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. In addition, ASC Topic 740 provides guidance on derecognition, classification, accounting in interim periods and disclosure requirements for uncertain tax positions.

Stock-based Compensation

The Company has two stock incentive plans that provide for stock-based employee compensation, the 2006 Stock Incentive Plan (the 2006 Plan) and the 2009 Stock Incentive Plan, as amended and restated (the 2009 Plan). The Company accounts for stock-based compensation in accordance with ASC Topic 718, *Stock Compensation*. Compensation expense is recognized on a graded method under the 2006 Plan and on a straight-line basis under the 2009 Plan over the vesting period of the awards based on the fair value of the options and restricted stock awards. Under the 2006 Plan, the Company historically used the Black-Scholes option pricing model to estimate the fair value of its stock based payment awards, but beginning October 28, 2009 under its 2009 Plan the Company began using an enhanced Hull-White Trinomial model. The determination of the fair value of stock-based payments utilizing the Black-Scholes model and the enhanced Hull-White Trinomial model is affected by Holdings stock price and a number of assumptions, including expected volatility, risk-free interest rate, expected term, expected dividends yield, expected forfeiture rate, expected turn-over rate and the expected exercise multiple.

Diluted Net Income Per Common Share

Diluted net income per common share, calculated on the treasury stock method, is based on the weighted average number of shares outstanding during the period. The Company s outstanding securities that may potentially dilute the common stock are stock options and restricted stock awards.

Included in the Company s calculation of diluted earnings per share for the three and nine months ended September 30, 2016 were approximately 469,000 stock options outstanding, of which approximately 39,000 and 29,000, respectively, were dilutive. In addition, there were approximately 97,000 restricted stock awards outstanding, of which approximately 11,000 and 7,000 were dilutive for the three and nine months ended September 30, 2016, respectively.

Included in the Company s calculation of diluted earnings per share for the three and nine months ended September 30, 2015 were approximately 650,000 stock options outstanding, of which approximately 217,000 and 199,000, respectively, were dilutive. In addition, there were approximately 89,000 restricted stock awards outstanding, approximately 23,000 and 5,000 of which were dilutive for the three and nine months ended September 30, 2015, respectively.

Estimates

The financial statements are prepared by management in conformity with U.S. Generally Accepted Accounting Principles (GAAP) and include estimated amounts and certain disclosures based on assumptions about future events. Accordingly, actual results could differ from those estimates.

Fair Value of Financial Instruments

The Company s financial instruments consist of cash, accounts receivable, payables and debt. The carrying amounts reported in the condensed consolidated balance sheets for cash, accounts receivable, accounts payable and accrued expenses approximate fair value because of the short-term nature of these instruments. The carrying value of the Company s long-term debt with variable interest rates approximates fair value based on instruments with similar terms.

The Company applies fair value techniques on a non-recurring basis associated with valuing potential impairment losses related to goodwill and indefinite-lived intangible assets and also when determining the fair value of contingent considerations. To determine the fair value in these situations, the Company uses Level 3 inputs, such as discounted cash flows, or if available, what a market participant would pay on the measurement date.

The Company utilizes the income approach to estimate the fair value of its intangible assets derived from acquisitions. At the date of acquisition, a contingent earn-out obligation is recorded at its fair value, which is calculated as the present value of the Company s maximum obligation based on probability-weighted estimates of achievement of performance targets defined in the earn-out agreements. The Company reviews the fair valuation periodically and adjusts the fair value for any changes in the maximum earn-out obligation based on probability-weighted estimates of achievement of certain performance targets defined in the earn-out agreements. In addition, discounted cash flows were used to estimate the fair value of the Company s investment in joint ventures.

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)* , which requires an entity to recognize the amount of revenue for which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in GAAP. In July 2015, the FASB agreed to defer the effective date of the standard from January 1, 2017, to January 1, 2018, with an option that permits companies to adopt the standard as early as the original effective date. Early application prior to the original effective date is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its condensed consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

In August 2014, the FASB issued ASU 2014-15, *Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern*, which will explicitly require management to assess an entity s ability to continue as a going concern and to provide related footnote disclosures in certain circumstances. Currently, there is no guidance in GAAP about management s responsibility to evaluate whether there is substantial doubt about an entity s ability to continue as a going concern or to provide related footnote disclosures. The amendments in this update provide that guidance. In doing so, the amendments should reduce diversity in the timing and content of footnote disclosures. The amendments require management to assess an entity s ability to continue as a going concern by incorporating and expanding upon certain principles that are currently in U.S. auditing standards. Specifically, the amendments (1) provide a definition of the term substantial doubt , (2) require an evaluation every reporting period including interim periods, (3) provide principles for considering the mitigating effect of management s plans, (4) require certain disclosures when substantial doubt is alleviated as a result of consideration of management s plans, (5) require an express statement and other disclosures when substantial doubt is not alleviated and (6) require an assessment for a period of one year after the date that the financial statements are issued (or available to be issued). The amendments in this update are effective for the first annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. The Company is currently evaluating the impact of adopting this update on its consolidated financial statements.

In November 2015, the FASB issued ASU 2015-17, *Balance Sheet Classification of Deferred Taxes*, which simplifies the presentation of deferred income taxes by eliminating the need for entities to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. This amendment is effective for annual periods beginning after December 15, 2016. The Company is currently evaluating the potential impact that ASU 2015-17 may have on its financial position and results of operations. The adoption of this standard is not expected to have an impact on the Company s financial position, results of operations or financial statement disclosures, except the deferred tax assets will be reclassified from current to long-term assets.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the impact of its pending adoption of the new standard on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. ASU 2016-09 allows for simplification of several aspects of the accounting for share-based payment transactions including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Under ASU 2016-09, all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) should be recognized as income tax expense or benefit in the income statement. ASU 2016-09 also requires recognition of excess tax benefits regardless of whether the benefit reduces taxes payable in the current period. ASU 2016-09 further permits the withholding of an amount up to employees maximum individual tax rate in the relevant jurisdiction without resulting in a liability classification. ASU 2016-09 also requires any excess tax benefits be classified along with other income tax cash flows as an operating activity and cash paid by an employer when directly withholding shares for tax-withholding purposes to be classified as a financing activity. ASU 2016-09 is effective for public companies for interim and annual periods beginning after December 15, 2016. The Company is currently evaluating the impact of ASU 2016-09 on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments (Topic 326) Credit Losses.* ASU 2016-13 changes the impairment model for most financial assets and certain other instruments. Under the new standard, entities holding financial assets and net investment in leases that are not accounted for at fair value through net income are to be presented at the net amount expected to be collected. An allowance for credit losses will be a valuation account that will be deducted from the amortized cost basis of the financial asset to present the net carrying value at the amount expected to be collected on the financial asset. ASU 2016-13 is effective as of January 1, 2020. Early adoption is permitted. The Company is currently evaluating the impact of ASU 2016-13. The adoption of this standard is not expected to have a material impact on the Company s consolidated financial statements or footnote disclosures.

2. Acquisitions

Effective February 23, 2016, the Company acquired certain assets of Lutheran Social Services of Illinois (LSSI) for approximately $0.1 million, in order to expand its adult day services business within the State of Illinois. The results of operations from the acquisition of LSSI is included in the Company s statement of income from the date of the acquisition. The LSSI acquisition accounted for $0.3 million and $0.7 million of net service revenues for the three and nine months ended September 30, 2016, respectively.

On April 24, 2015, Addus HealthCare entered into a Securities Purchase Agreement with Margaret Coffey and Carol Kolar (the South Shore Sellers), South Shore Home Health Service Inc. (South Shore) and Acaring Home Care, LLC (Acaring), pursuant to which Addus HealthCare agreed to acquire all of the issued and outstanding securities of each of South Shore and Acaring. On February 5, 2016, Addus HealthCare completed its acquisition of all the outstanding securities of South Shore and Acaring for a total purchase price of $20.4 million (the South Shore Purchase Price). A portion of the South Shore Purchase Price was deposited into escrow to serve as a source of recovery for certain indemnification obligations of the South Shore Sellers. The related acquisition costs were $1.3 million and were expensed as incurred. The results of operations from South Shore and Acaring are included in the Company s statements of income from the date of the acquisition. Acaring was dissolved on March 1, 2016, and its assets were transferred to South Shore.

The Company s acquisition of South Shore and Acaring has been accounted for in accordance with ASC Topic 805, *Business Combinations,* and the resulting goodwill and other intangible assets was accounted for under ASC Topic 350 *Goodwill and Other Intangible Assets*. The acquisition was recorded at its fair value as of February 5, 2016. Under business combination accounting, the South Shore Purchase Price was $20.4 million and was allocated to South Shore s net tangible and identifiable intangible assets based on their estimated fair values. Management has preliminarily valued and allocated the purchase price as shown below. These preliminary estimates and assumptions could change during the purchase price measurement period as the Company finalizes the valuation, primarily related to working capital adjustments. Management anticipates this will be completed during the fourth quarter of 2016.

	Total
	(Amounts in Thousands)
Goodwill	$ 5,127
Identifiable intangible assets	9,957
Accounts receivable	6,124
Furniture, fixtures and equipment	66
Other current assets	763
Accrued liabilities	(1,491)
Accounts payable	(97)
Total purchase price allocation	$ 20,449

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Management s assessment of qualitative factors affecting goodwill for South Shore includes: estimates of market share at the date of purchase; ability to grow in the market; synergy with existing Company operations and the presence of managed care payors in the market.

Identifiable intangible assets acquired consist of trade names and trademarks, customer relationships and non-compete agreements. The estimated fair value of identifiable intangible assets was determined by the Company s management. It is anticipated that the net intangible and identifiable intangible assets, including goodwill, are deductible for tax purposes.

The South Shore acquisition accounted for $14.9 million and $36.7 million of net service revenues for the three and nine months ended September 30, 2016, respectively.

Effective November 9, 2015, the Company acquired certain assets of Five Points Healthcare of Virginia, LLC (Five Points), in order to further expand the Company s presence in the State of Virginia. The total consideration for the transaction was comprised of $4.1 million in cash. The related acquisition costs were $0.4 million and were expensed as incurred. The results of operations from the acquisition is included in the Company s statement of income from the date of the acquisition.

The Company s acquisition of Five Points has been accounted for in accordance with ASC Topic 805, *Business Combinations,* and the resulting goodwill and other intangible assets was accounted for under ASC Topic 350 *Goodwill and Other Intangible Assets*. The acquisition of Five Points was recorded at its fair value as of November 9, 2015. The total purchase price was $4.1 million. Under business combination accounting, the total purchase price was allocated to Five Points net tangible and identifiable intangible assets based on their estimated fair values. Based upon management s valuation, the total purchase price has been allocated as follows:

	Total
	(Amounts in Thousands)
Goodwill	$ 2,885
Identifiable intangible assets	920
Accounts receivable	472
Accrued liabilities	(155)
Accounts payable	(7)
Total purchase price allocation	$ 4,115

Management s assessment of qualitative factors affecting goodwill for Five Points includes: estimates of market share at the date of purchase; ability to grow in the market; synergy with existing Company operations and the presence of managed care payors in the market.

Identifiable intangible assets acquired consist of trade names and trademarks, customer relationships and non-compete agreements. The estimated fair value of identifiable intangible assets was determined by the Company s management. The net intangible and identifiable intangible assets, including goodwill, are deductible for tax purposes.

The Five Points acquisition accounted for $0.9 million and $3.1 million of net service revenues for the three and nine months ended September 30, 2016, respectively.

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The following table contains unaudited pro forma condensed consolidated income statement information assuming the Five Points and the South Shore and Acaring acquisitions closed on January 1, 2015.

	For the Three Months Ended September 30, (Amounts in Thousands)	
	2016	**2015**
Net service revenues	$ 103,502	$ 98,981
Operating income	2,495	5,898
Net income	1,699	3,952
Net income per common share		
Basic income per share	$ 0.15	$ 0.36
Diluted income per share	0.15	0.35

	For the Nine Months Ended September 30, (Amounts in Thousands)	
	2016	**2015**
Net service revenues	$ 301,867	$ 293,774
Operating income	7,923	17,594
Net income	4,512	10,476
Net income per common share		
Basic income per share	$ 0.41	$ 0.95
Diluted income per share	0.41	0.94

The pro forma disclosures in the table above include adjustments for amortization of intangible assets and tax expense and acquisition costs to reflect results that are more representative of the combined results of the transactions as if South Shore and Acaring and Five Points had been acquired effective January 1, 2015. This pro forma information is presented for illustrative purposes only and may not be indicative of the results of operations that would have actually occurred. In addition, future results may vary significantly from the results reflected in the pro forma information. The unaudited pro forma financial information does not reflect the impact of future events that may occur after the acquisition, such as anticipated cost savings from operating synergies.

Effective January 1, 2015, the Company acquired Priority Home Health Care, Inc. (PHHC), in order to further expand the Company s presence in the State of Ohio. The total consideration for the transaction was comprised of $4.3 million in cash. The related acquisition costs were $0.5 million and were expensed as incurred. The results of operations from this acquired entity are included in the Company s statement of income from the date of the acquisition.

The Company s acquisition of PHHC has been accounted for in accordance with ASC Topic 805, *Business Combinations,* and the resulting goodwill and other intangible assets were accounted for under ASC Topic 350 *Goodwill and Other Intangible Assets*. The acquisition was recorded at its fair value as of January 1, 2015. The total purchase price was $4.3 million. Under business combination accounting, the total purchase price was allocated to PHHC s net tangible and identifiable intangible assets based on their estimated fair values. Based upon management s valuation, the total purchase price has been allocated as follows:

	Total (Amounts in Thousands)
Goodwill	$ 1,862

Identifiable intangible assets		1,930
Accounts receivable		951
Furniture, fixtures and equipment		58
Other current assets		8
Accrued liabilities		(339)
Accounts payable		(220)
Total purchase price allocation	$	4,250

Management s assessment of qualitative factors affecting goodwill for PHHC includes: estimates of market share at the date of purchase; ability to grow in the market; synergy with existing Company operations and the presence of managed care payors in the market.

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Identifiable intangible assets acquired consist of trade names and trademarks, customer relationships and non-compete agreements. The estimated fair value of identifiable intangible assets was determined by the Company s management. The net intangible and identifiable intangible assets, including goodwill, are deductible for tax purposes.

The PHHC acquisition accounted for $1.8 million and $5.8 million of net service revenues for the three and nine months ended September 30, 2016 and $2.5 million and $7.2 million of net service revenues for the three and nine months ended September 30, 2015, respectively.

The Company had recorded a $1.3 million contingent earn-out obligation as a current liability related to its December 1, 2013 acquisition of Coordinated Home Health Care, LLC. This obligation was paid during the second quarter of 2016.

3. Goodwill and Intangible Assets

A summary of the goodwill activity for the nine months ended September 30, 2016 is provided below:

	Goodwill (Amounts in Thousands)
Goodwill, at December 31, 2015	$ 68,844
Additions for acquisitions	5,127
Adjustments to previously recorded goodwill	(120)
Goodwill, at September 30, 2016	$ 73,851

Adjustments to the previously recorded goodwill are primarily credits related to amortization of tax goodwill in excess of book basis.

The carrying amount and accumulated amortization of each identifiable intangible asset category consisted of the following as of September 30, 2016 and December 31, 2015:

	Customer and referral relationships	Trade names and trademarks	State licenses	Non-competition agreements	Total
			(Amounts in Thousands)		
Gross balance at December 31, 2015	$ 29,872	$ 8,161	$ 150	$ 2,098	$ 40,281
Accumulated amortization	(24,055)	(4,587)		(1,288)	(29,930)
Net Balance at December 31, 2015	5,817	3,574	150	810	10,351
Gross balance at January 1, 2016	29,872	8,161	150	2,098	40,281
Additions for acquisitions	4,800	5,100		57	9,957