

ADCARE HEALTH SYSTEMS INC  
Form 10-Q  
November 09, 2011  
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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2011

**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 001-33135

**AdCare Health Systems, Inc.**

(Exact name of registrant as specified in its charter)

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**Ohio**  
(State or Other Jurisdiction  
of Incorporation)

**31-1332119**  
(IRS Employer Identification Number)

**5057 Troy Rd, Springfield, OH 45502-9032**

(Address of principal executive offices)

**(937) 964-8974**

(Registrant's telephone number)

**NA**

(Former name, former address, or 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 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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  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 definition 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

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

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

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As of September 30, 2011: 12,169,852 shares of common stock with no par value were outstanding

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**AdCare Health Systems, Inc.**

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## Item 1. Financial Statements

**ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

## CONSOLIDATED BALANCE SHEETS

	September 30, 2011 (Unaudited)	December 31, 2010
<b><u>ASSETS</u></b>		
Current Assets:		
Cash and cash equivalents	\$ 10,049,883	\$ 3,911,140
Restricted cash and cash equivalents	3,313,000	1,047,454
Accounts receivable:		
Long-term care resident receivables, net	18,708,063	10,943,963
Management receivables, net	189,534	271,224
Prepaid expenses and other	1,312,394	1,243,663
Total current assets	33,572,874	17,417,444
Restricted cash and investments	4,455,568	3,099,936
Property and equipment, net	83,802,347	37,606,301
Intangibles, net	26,336,253	16,159,845
Goodwill	2,679,482	2,679,482
Escrow deposits for acquisitions	700,000	1,725,086
Lease deposits	2,193,442	1,670,282
Other assets	4,545,571	2,600,530
Total assets	\$ 158,285,537	\$ 82,958,906
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
Current Liabilities:		
Current portion of notes payable and other debt	\$ 11,078,424	\$ 3,633,401
Accounts payable	10,094,939	3,411,772
Accrued expenses	11,798,044	9,664,325
Total current liabilities	32,971,407	16,709,498
Notes payable and other debt, net of current portion	101,148,162	47,210,995
Derivative liability	2,057,152	2,905,750
Other liabilities	1,641,269	1,267,429
Deferred tax liability	491,294	255,141
Total liabilities	138,309,284	68,348,813
Commitments and contingencies (Note 4)		
Stockholders' equity:		
Preferred stock, no par value; 1,000,000 shares authorized; no shares issued or outstanding		
Common stock and additional paid-in capital, no par value; 29,000,000 shares authorized; 12,169,852 and 8,766,657 shares issued and outstanding	34,701,655	26,611,870

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Accumulated deficit	(14,183,047)	(12,548,870)
Total stockholders' equity	20,518,608	14,063,000
Noncontrolling interest in subsidiaries	(542,355)	547,093
Total equity	19,976,253	14,610,093
Total liabilities and stockholders' equity	\$ 158,285,537	\$ 82,958,906

See notes to consolidated financial statements

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## CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
<b>Revenues:</b>				
Patient care revenues	\$ 40,543,732	\$ 12,741,701	\$ 105,879,393	\$ 24,308,760
Management revenues	328,731	532,985	1,312,254	1,564,657
Total revenues	40,872,463	13,274,686	107,191,647	25,873,417
<b>Expenses:</b>				
Payroll and related payroll costs	21,963,988	8,243,065	59,182,571	16,269,039
Other operating expenses	14,372,765	4,618,960	36,547,834	8,810,591
Lease expense	1,981,332	869,400	5,830,923	1,158,933
Depreciation and amortization	840,116	303,190	2,201,083	779,164
Salary retirement and continuation costs			621,605	
Total expenses	39,158,201	14,034,615	104,384,016	27,017,727
Income (Loss) from Operations	1,714,262	(759,929)	2,807,631	(1,144,310)
<b>Other Income (Expense):</b>				
Interest expense, net	(2,230,211)	(420,448)	(5,524,682)	(1,005,908)
Acquisition costs, net of gains	(1,146,651)	(402,850)	(789,432)	1,226,854
Derivative gain	4,744,694		806,657	
Loss on extinguishment of debt	(58,440)		(135,840)	
Other income (expense)	(28,846)	(49,795)	558,101	(79,352)
Total other income (expense)	1,280,546	(873,093)	(5,085,196)	141,594
Income (Loss) Before Income Taxes	2,994,808	(1,633,022)	(2,277,565)	(1,002,716)
Income Tax Expense	(214,424)	(10,641)	(446,060)	(31,925)
Net Income (Loss)	2,780,384	(1,643,663)	(2,723,625)	(1,034,641)
Net Loss (Income) Attributable to Noncontrolling Interests	747,605	143,899	1,089,448	(665,663)
Net Income (Loss) Attributable to AdCare Health Systems	\$ 3,527,989	\$ (1,499,764)	\$ (1,634,177)	\$ (1,700,304)
Net Income (Loss) Per Share, Basic	\$ 0.33	\$ (0.18)	\$ (0.17)	\$ (0.25)
Net Income (Loss) Per Share, Diluted	\$ 0.29	\$ (0.18)	\$ (0.17)	\$ (0.25)
<b>Weighted Average Common Shares Outstanding,</b>				
Basic	10,738,093	8,321,768	9,450,507	6,754,786
Diluted	12,689,231	8,321,768	9,450,507	6,754,786

See notes to consolidated financial statements





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## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended September 30,	
	2011	2010
Cash flows from operating activities:		
Net loss	\$ (2,723,625)	\$ (1,034,641)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	2,201,082	779,164
Warrants issued for services	162,496	9,626
Stock based compensation expense	578,969	637,705
Provision for leases in excess of cash	558,069	
Amortization of deferred financing costs	599,318	37,674
Amortization of debt discounts	663,279	
Derivative gain	(806,657)	
Loss on debt extinguishment	135,840	
Deferred tax expense	236,153	31,925
Loss on disposal of assets	126,015	1,303
Gain on acquisitions	(1,104,486)	(1,805,740)
Noncash acquisition costs	206,394	171,961
Provision for bad debts	585,404	17,806
Other noncash items	58,638	
Changes in certain assets and liabilities, net of acquisitions:		
Accounts receivable	(8,267,814)	(1,451,473)
Prepaid expenses and other	(166,147)	(173,162)
Other assets	(524,813)	(806,378)
Accounts payable and accrued expenses	8,775,946	2,591,366
Other liabilities	(264,458)	(95,504)
Net cash provided by (used in) operating activities	1,029,603	(1,088,368)
Cash flows from investing activities:		
Change in restricted cash and investments	546,222	158,716
Escrow deposits for acquisitions	(990,000)	(2,735,301)
Acquisitions	(10,059,914)	(3,730,747)
Purchase of property and equipment	(2,732,034)	(692,492)
Net cash used in investing activities	(13,235,726)	(6,999,824)
Cash flows from financing activities:		
Proceeds from debt	7,312,954	3,096,015
Proceeds from exercise of warrants/options	6,797,758	331,100
Debt issuance costs	(388,389)	
Change in line of credit	5,770,283	
Proceed from public stock offering		6,109,725
Repayment of notes payable	(1,147,740)	(475,034)
Net cash provided by financing activities	18,344,866	9,061,806
Net Change in Cash	6,138,743	973,614
Cash, Beginning	3,911,140	4,481,100
Cash, Ending	\$ 10,049,883	\$ 5,454,714

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### Supplemental Disclosure of Cash Flow Information:

Cash paid during the period for income taxes	\$	197,000		
Cash paid during the period for interest	\$	4,246,116	\$	997,343
Supplemental Disclosure of Noncash Activities:				
Noncash change in fair value of PP&E from acquisition	\$		\$	750,287
Acquisitions in exchange for debt		48,825,540		6,365,000
Warrants issued for financings costs		329,901		
Other assets acquired in exchange for debt		5,062,656		

See notes to consolidated financial statements.

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(Unaudited)

	<b>Total</b>	<b>Accumulated Deficit</b>	<b>Common Stock and Additional Paid-in Capital</b>	<b>Noncontrolling Interest</b>
Balance, January 1, 2011	\$ 14,610,093	\$ (12,548,870)	\$ 26,611,870	\$ 547,093
Nonemployee warrants for services	394,981		394,981	
Nonemployee stock issuance for services	206,394		206,394	
Stock based compensation expense	578,969		578,969	
Exercises of options and warrants	6,797,757		6,797,757	
Stock issued from debt conversion	111,684		111,684	
Net loss	(2,723,625)	(1,634,177)		(1,089,448)
Balance, September 30, 2011	\$ 19,976,253	\$ (14,183,047)	\$ 34,701,655	\$ (542,355)

See notes to consolidated financial statements

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**ADCARE HEALTH SYSTEMS, INC. AND SUBSIDIARIES**

Notes to Consolidated Financial Statements (Unaudited)

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Basis of Presentation*

The consolidated financial statements are presented in accordance with accounting principles generally accepted in the United States. These statements include the accounts of AdCare Health Systems, Inc. ( AdCare ) and its controlled subsidiaries (collectively the Company or we ). Controlled subsidiaries include majority owned subsidiaries and variable interest entities in which we have control as the primary beneficiary. The Company delivers skilled nursing, assisted living and home health services. All inter-company accounts and transactions were eliminated in the consolidation. The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and notes required for complete annual financial statements and should be read in conjunction with the Company s audited consolidated financial statements and notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010 (the Annual Report ). In the opinion of the Company s management, all adjustments considered for a fair presentation are included and are of a normal recurring nature. Operating results for the nine months ended September 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. Certain prior year amounts have been reclassified to conform to the current year presentation.

*Earnings per Share*

Basic earnings per share is computed by dividing net income or loss by the weighted-average number of common shares outstanding during the period. Diluted earnings per share is similar to basic earnings per share except net income or loss is adjusted by the impact of the assumed issuance of convertible shares and the weighted-average number of common shares outstanding includes potentially dilutive securities, such as options, warrants, non-vested shares, and additional shares issuable under convertible notes outstanding during the period when such potentially dilutive securities are not anti-dilutive. Potentially dilutive securities from option, warrants and non-vested shares are calculated in accordance with the treasury stock method, which assumes that proceeds from the exercise of all options and warrants with exercise prices exceeding the average market value are used to repurchase common stock at market value. The incremental shares remaining after the proceeds are exhausted represent the potentially dilutive effect of the securities. Potentially dilutive securities from convertible debt are calculated based on the assumed issuance at the beginning of the period, as well as any adjustment to income that would result from their assumed issuance.

For the nine months ending September 30, 2011 and the three and nine month periods ending September 30, 2010, no potentially dilutive securities were included in the diluted earnings per share calculation because to do so would be anti-dilutive. The following table provides a reconciliation of net income (loss) and the number of common shares used in the computation of diluted earnings per share:

	<b>Three Months Ended September 30,</b>	
	<b>2011</b>	<b>2010</b>

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	Income (loss)	Shares (1)	Per Share	Income (loss)	Shares (1)	Per Share
Net income (loss) attributable to AdCare Health Systems	\$ 3,527,989	10,738,093	\$ 0.33	\$ (1,499,764)	8,321,768	\$ (0.18)
Effect from options, warrants and non-vested shares		1,057,905				
Effect from assumed issuance of convertible shares (2)	159,309	893,233				
Diluted net income (loss)	\$ 3,687,298	12,689,231	\$ 0.29	\$ (1,499,764)	8,321,768	\$ (0.18)

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*Earnings per Share (continued)*

	Nine Months Ended September 30,					
	Income (loss)	2011 Shares (1)	Per Share	Income (loss)	2010 Shares (1)	Per Share
Net income (loss) attributable to AdCare Health Systems	\$ (1,634,177)	9,450,507	\$ (0.17)	\$ (1,700,304)	6,754,786	\$ (0.25)
Effect from options, warrants and non-vested shares						
Effect from assumed issuance of convertible shares						
Diluted net income (loss)	\$ (1,634,177)	9,450,507	\$ (0.17)	\$ (1,700,304)	6,754,786	\$ (0.25)

(1) - The weighted average shares outstanding includes retroactive adjustments from the stock dividend (see Note 13).

(2) - The impacts of the conversion of the 2010 convertible note were excluded as the impact would be anti-dilutive.

*Intangible Assets and Goodwill*

There have been no required impairment adjustments to intangible assets and goodwill during the nine months ended September 30, 2011 and 2010.

Intangible assets consist of the following:

	September 30, 2011		December 31, 2010	
Gross	Net	Gross	Net	