KINDRED HEALTHCARE, INC
Form 10-Q
May 08, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2018

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: 001-14057

KINDRED HEALTHCARE, INC.

(Exact name of registrant as specified in its charter)

Delaware	61-1323993
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

680 South Fourth Street Louisville, KY	40202
(Address of principal executive offices)	(Zip Code)

(502) 596-7300

(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 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, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer	Emerging growth company
Non-accelerated filer	Smaller reporting company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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.

Class of Common Stock	Outstanding at April 30, 2018
Common stock, $0.25 par value	91,260,624 shares

KINDRED HEALTHCARE, INC.

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KINDRED HEALTHCARE, INC.

CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS

(Unaudited)

(In thousands, except per share amounts)

	Three months ended March 31, 2018	2017
Revenues	$1,513,789	$1,539,490
Salaries, wages and benefits	845,854	839,813
Supplies	75,008	80,101
Building rent	62,488	64,656
Equipment rent	8,689	8,887
Other operating expenses	135,717	158,824
General and administrative expenses (exclusive of depreciation and amortization expense included below)	265,372	275,503
Other (income) expense	(607)	30
Impairment charges	-	474
Restructuring charges	8,109	10,006
Depreciation and amortization	24,789	29,820
Interest expense	61,032	59,328
Investment income	(197)	(509)
	1,486,254	1,526,933
Income from continuing operations before income taxes	27,535	12,557
Provision for income taxes	1,228	2,234
Income from continuing operations	26,307	10,323
Discontinued operations, net of income taxes:		
Income (loss) from operations	(8,770)	5,059
Loss on divestiture of operations	(5,790)	(6,166)
Loss from discontinued operations	(14,560)	(1,107)
Net income	11,747	9,216
Earnings attributable to noncontrolling interests:		
Continuing operations	(12,792)	(10,483)
Discontinued operations	(660)	(4,481)
	(13,452)	(14,964)
Loss attributable to Kindred	$(1,705)	$(5,748)
Amounts attributable to Kindred stockholders:		
Income (loss) from continuing operations	$13,515	$(160)
Loss from discontinued operations	(15,220)	(5,588)
Net loss	$(1,705)	$(5,748)
Earnings (loss) per common share:		
Basic:		
Income (loss) from continuing operations	$0.15	$-

Discontinued operations:		
Income (loss) from operations	(0.11)	-
Loss on divestiture of operations	(0.06)	(0.07)
Loss from discontinued operations	(0.17)	(0.07)
Net loss	$(0.02)	$(0.07)
Diluted:		
Income (loss) from continuing operations	$0.15	$-
Discontinued operations:		
Income (loss) from operations	(0.11)	-
Loss on divestiture of operations	(0.06)	(0.07)
Loss from discontinued operations	(0.17)	(0.07)
Net loss	$(0.02)	$(0.07)
Shares used in computing earnings (loss) per common share:		
Basic	88,526	87,085
Diluted	88,526	87,085
Cash dividends declared and paid per common share	$-	$0.12

See accompanying notes.

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KINDRED HEALTHCARE, INC.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(Unaudited)

(In thousands)

	Three months ended March 31,	
	2018	2017
Net income	$11,747	$9,216
Other comprehensive income:		
Available-for-sale securities (Note 10):		
Change in unrealized investment gains	-	949
Reclassification of gains realized in net income	-	(1)
Net change	-	948
Interest rate swaps (Note 1):		
Change in unrealized gains	4,125	1,026
Reclassification of gains realized in net income, net of payments	(629)	(103)
Net change	3,496	923
Other comprehensive income	3,496	1,871
Comprehensive income	15,243	11,087
Earnings attributable to noncontrolling interests	(13,452)	(14,964)
Comprehensive income (loss) attributable to Kindred	$1,791	$(3,877)

See accompanying notes.

KINDRED HEALTHCARE, INC.

CONDENSED CONSOLIDATED BALANCE SHEET

(Unaudited)

(In thousands, except per share amounts)

	March 31, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 108,759	$ 160,254
Insurance subsidiary investments	22,407	22,546
Accounts receivable less allowance for loss of $67,227 March 31, 2018 and $96,899 December 31, 2017	1,165,044	1,122,532
Inventories	21,635	21,716
Income taxes	3,462	4,546
Assets held for sale	8,937	17,335
Other (Note 13)	69,828	60,610
	1,400,072	1,409,539
Property and equipment	1,686,791	1,682,965
Accumulated depreciation	(961,272)	(946,986)
	725,519	735,979
Goodwill	2,188,391	2,188,566
Intangible assets less accumulated amortization of $64,836 March 31, 2018 and $77,603 December 31, 2017	601,368	604,338
Insurance subsidiary investments	27,771	28,988
Other (Note 13)	263,242	265,307
Total assets (a)	$ 5,206,363	$ 5,232,717
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$ 147,143	$ 191,827
Salaries, wages and other compensation	337,838	352,179
Due to third party payors	26,772	35,321
Professional liability risks	60,671	60,767
Accrued lease termination fees	7,557	7,610
Other accrued liabilities (Note 13)	214,227	263,977
Long-term debt due within one year	14,482	14,638
	808,690	926,319
Long-term debt	3,266,364	3,146,972
Professional liability risks	276,551	276,829
Deferred tax liabilities	37,196	36,881
Deferred credits and other liabilities (Note 13)	492,170	497,954

Commitments and contingencies (Note 12)		
Equity:		
Stockholders' equity:		
Common stock, $0.25 par value; authorized 175,000 shares; issued 91,279 shares March 31, 2018 and 91,454 shares December 31, 2017	22,820	22,864
Capital in excess of par value	1,714,504	1,713,179
Accumulated other comprehensive income	9,675	6,179
Accumulated deficit	(1,632,432)	(1,618,896)
	114,567	123,326
Noncontrolling interests	210,825	224,436
Total equity	325,392	347,762
Total liabilities (a) and equity	$5,206,363	$5,232,717

(a) The Company's consolidated assets as of March 31, 2018 and December 31, 2017 include total assets of variable interest entities of $405.5 million and $405.8 million, respectively, which can only be used to settle the obligations of the variable interest entities. The Company's consolidated liabilities as of March 31, 2018 and December 31, 2017 include total liabilities of variable interest entities of $43.5 million and $43.9 million, respectively. See note 1 of the notes to unaudited condensed consolidated financial statements.

See accompanying notes.

KINDRED HEALTHCARE, INC.

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

(Unaudited)

(In thousands)

	Three months ended March 31, 2018	2017
Cash flows from operating activities:		
Net income	$11,747	$9,216
Add back loss from discontinued operations, net of income taxes	14,560	1,107
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation expense	22,322	25,191
Amortization of intangible assets	2,467	4,629
Amortization of stock-based compensation costs	4,261	3,026
Amortization of deferred financing costs	4,254	4,132
Payment of capitalized lender fees related to debt amendment	-	(5,403)
Provision for doubtful accounts	2,910	6,425
Deferred income taxes	411	1,227
Impairment charges	-	474
Other	270	6,258
Change in operating assets and liabilities:		
Accounts receivable	(77,785)	(79,752)
Inventories and other assets	(18,292)	(4,983)
Accounts payable	(19,680)	(10,425)
Income taxes	1,084	2,291
Due to third party payors	(8,135)	(4,745)
Other accrued liabilities	(38,743)	(42,973)
Net cash used in operating activities of discontinued operations	(34,054)	(8,293)
Net cash used in operating activities	(132,403)	(92,598)
Cash flows from investing activities:		
Routine capital expenditures	(15,910)	(10,346)
Development capital expenditures	(3,542)	(5,433)
Acquisitions, net of cash acquired	-	(3,150)
Sale of assets	13,225	-
Purchase of insurance subsidiary investments	-	(22,308)
Sale of insurance subsidiary investments	-	18,699
Net change in other investments	91	29
Other	(233)	154
Net cash provided by (used in) investing activities of discontinued operations	7,204	(1,601)
Net cash provided by (used in) investing activities	835	(23,956)
Cash flows from financing activities:		
Proceeds from borrowings under revolving credit	429,700	478,600
Repayment of borrowings under revolving credit	(310,200)	(343,400)

Repayment of term loan	(3,508)	(3,509)
Repayment of other long-term debt	(203)	(284)
Payment of deferred financing costs	(56)	(79)
Payment of dividend for mandatory redeemable preferred stock	-	(3,010)
Dividends paid	-	(10,228)
Contributions made by noncontrolling interests	165	-
Distributions to noncontrolling interests	(27,228)	(25,801)
Payroll tax payments for equity awards issuance	(3,044)	(2,255)
Net cash provided by financing activities	85,626	90,034
Change in cash, cash equivalents and restricted cash	(45,942)	(26,520)
Cash, cash equivalents and restricted cash at beginning of period	218,463	324,168
Cash, cash equivalents and restricted cash at end of period	$172,521	$297,648
Supplemental information:		
Interest payments	$76,283	$74,839
Income tax refunds	266	1,240
Distributions to noncontrolling interests:		
Continuing operations	(11,038)	(8,785)
Discontinued operations	(16,190)	(17,016)

See accompanying notes.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION

Business

Kindred Healthcare, Inc. is a healthcare services company that through its subsidiaries operates a home health, hospice and community care business, transitional care ("TC") hospitals, inpatient rehabilitation hospitals ("IRFs"), and a contract rehabilitation services business across the United States (collectively, the "Company" or "Kindred"). At March 31, 2018, the Company's Kindred at Home division primarily provided home health, hospice, and community care services from 606 sites of service in 40 states. The Company's hospital division operated 75 TC hospitals (certified as long-term acute care ("LTAC") hospitals under the Medicare program) in 17 states. The Company's Kindred Rehabilitation Services division operated 19 IRFs and 98 hospital-based acute rehabilitation units ("ARUs") (certified as IRFs), and provided rehabilitation services primarily in hospitals and long-term care settings in 45 states.

Recently issued accounting requirements

In February 2018, the Financial Accounting Standards Board (the "FASB") issued authoritative guidance which permits a company to reclassify the income tax effects of the Tax Cuts and Jobs Act of 2017 (the "Tax Reform Act") on items within accumulated other comprehensive income to retained earnings. The new guidance is effective for annual and interim periods beginning after December 15, 2018 and early adoption is permitted. The Company will not elect to early adopt and the adoption of this standard is not expected to have a material impact on the Company's business, financial position, results of operations or liquidity.

In August 2017, the FASB issued authoritative guidance with the objective of improving the financial reporting of hedging relationships under United States generally accepted accounting principles ("GAAP") to better portray economic results and to simplify the application of the current hedge accounting guidance. The new guidance is effective for annual and interim periods beginning after December 15, 2018 and early adoption is permitted. The adoption of this standard is not expected to have a material impact on the Company's business, financial position, results of operations or liquidity.

In January 2017, the FASB issued authoritative guidance that simplifies the measurement of goodwill impairment to a single-step test. The guidance removed step two of the goodwill impairment test, which required a hypothetical purchase price allocation. The measurement of goodwill impairment is now the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. Under the revised guidance, failing step one will always result in goodwill impairment. The new guidance is effective for annual and interim periods beginning after December 15, 2019 and early adoption is permitted. The Company adopted the new guidance on January 1, 2017 on a prospective basis. If the Company fails step one of the goodwill impairment test under the new guidance, the results could materially impact the Company's financial position and results of operations but not its business or liquidity.

In June 2016, the FASB issued authoritative guidance for accounting for credit losses on financial instruments. The new guidance introduces an approach based on expected losses to estimate credit losses on certain types of financial instruments and modifies the impairment model for available-for-sale debt securities. The new guidance is effective for annual periods beginning after December 15, 2019 and early adoption is permitted beginning after December 15,

2018. The adoption of this standard is not expected to have a material impact on the Company's business, financial position, results of operations, or liquidity.

In February 2016, the FASB issued amended authoritative guidance on accounting for leases. The new provisions require that a lessee of operating leases recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. The lease liability will be equal to the present value of lease payments, with the right-of-use asset based upon the lease liability. The classification criteria for distinguishing between finance (or capital) leases and operating leases are substantially similar to the previous lease guidance, but with no explicit bright lines. As such, operating leases will result in straight-line rent expense similar to current practice. For short-term leases (term of 12 months or less), a lessee is permitted to make an accounting election not to recognize lease assets and lease liabilities, which would generally result in lease expense being recognized on a straight-line basis over the lease term. The guidance is effective for annual and interim periods beginning after December 15, 2018, and will require application of the new guidance at the beginning of the earliest comparable period presented. The Company will not elect early adoption and will apply the modified retrospective approach as required. The adoption of this standard is expected to have a material impact on the Company's financial position. The Company does not expect an impact on its business, results of operations or liquidity.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION (Continued)

Revenue recognition

On January 1, 2018, the Company adopted Accounting Standards Codification ("ASC") 606, Revenue from Contracts with Customers, and all of the related amendments (the "New Revenue Standard"). The New Revenue Standard requires entities to recognize the amount of revenue it expects for the transfer of goods or services to customers. The adoption of this standard had an immaterial impact on the Company's reported total revenues as compared to what reported amounts would have been under the prior standard, and the Company expects the impact of adoption in future periods will be immaterial. The Company's accounting policies under the New Revenue Standard were applied prospectively and are noted below.

Revenues are recognized as performance obligations are satisfied, which is over time as patient services are rendered throughout the length of stay, in an amount that reflects the consideration the Company expects to receive in exchange for services. A performance obligation is defined as a promise in a contract to transfer a distinct good or service to the customer. Substantially all of the Company's contracts with patients and customers have a single performance obligation as the promise to transfer services is not distinct or separately identifiable from other promises in the contract.

The transaction price for the Company's contracts represents its best estimate of the consideration the Company expects to receive and includes assumptions regarding variable consideration as applicable. These variable considerations include estimated amounts due from patients and third party payors for healthcare services provided, including anticipated settlements under reimbursement agreements with Medicare, Medicaid, Medicare Advantage, Medicaid Managed, and other third party payors. Revenues under third party agreements are subject to examination and retroactive adjustment. Provisions for estimated third party adjustments are provided in the period the related services are rendered to the extent it is probable that a significant reversal of cumulative revenue will not occur. Any remaining differences between the amounts accrued and subsequent settlements are recorded in the periods in which the interim or final settlements are determined.

A summary of revenues by payor type follows (in thousands):

	Three months ended March 31,	
	2018	2017
Medicare	$791,842	$814,768
Medicaid	93,765	105,427
Medicare Advantage	142,224	116,503
Medicaid Managed	55,861	51,013
Other	452,063	475,385
	1,535,755	1,563,096
Eliminations	(21,966)	(23,606)

	$1,513,789	$1,539,490

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION (Continued)

Revenue recognition (Continued)

A summary of revenues by business segment follows (in thousands):

	Three months ended March 31, 2018	2017
Revenues:		
Kindred at Home:		
Home health	$453,759	$450,831
Hospice	183,628	179,378
	637,387	630,209
Hospital division	547,630	556,646
Kindred Rehabilitation Services:		
Kindred Hospital Rehabilitation Services	178,219	178,115
RehabCare	172,519	198,126
	350,738	376,241
	1,535,755	1,563,096
Eliminations:		
Kindred Hospital Rehabilitation Services	(19,321)	(21,148)
RehabCare	(1,993)	(1,878)
Hospitals	(652)	(580)
	(21,966)	(23,606)
	$1,513,789	$1,539,490

ASC 606 adoption impact

On January 1, 2018, the Company adopted the New Revenue Standard using the modified retrospective transition method. The Company recognized the cumulative effect of initially applying the New Revenue Standard to all contracts not completed as of the date of adoption, resulting in an $11.8 million adjustment, net of taxes, on January 1, 2018 to accounts receivable and accumulated deficit. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

The impact of adoption of the New Revenue Standard was primarily related to the following: (i) recognizing contractual revenues due to variable considerations subject to estimation during the period of service within the Kindred at Home division (included within the Medicare and Medicare Advantage payor types) and (ii) recognizing contractual revenues earlier due to variable considerations arising from the historical collectability of the Company's hospital division's private payor portfolio (included within the other payor type).

The Company reclassified approximately $3.8 million of other operating expenses to contractual revenues for the three months ended March 31, 2018 as a result of the New Revenue Standard. The Company reclassified the net hospice room and board charges previously recorded as other operating expenses to contractual revenues. In accordance with the New Revenue Standard definition of performance obligations, the Company does not view the room and board charges as separate and distinct from the patient services, and as such, classifies the net charges as contractual revenues. The remaining reclassifications resulted from certain bad debts considered implicit price concessions or contractual revenues under the New Revenue Standard, while the remaining bad debts recorded in other operating expenses are related to credit risk or limitations on a customer's ability to pay.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION (Continued)

ASC 606 adoption impact (Continued)

The impact of adoption on the Company's accompanying unaudited condensed consolidated statement of operations and unaudited condensed consolidated balance sheet was as follows (in thousands):

	Three months ended March 31, 2018		
	As reported	Without adoption of ASC 606	Effect of change
Statement of operations:			
Revenues	$1,513,789	$ 1,517,196	$(3,407)
Other operating expenses	135,717	139,581	(3,864)
Income from continuing operations before income taxes	27,535	27,078	457
	As of March 31, 2018		
Balance sheet:			
Current assets:			
Accounts receivable less allowance for loss	$1,165,044	$ 1,176,354	$(11,310)
Equity:			
Accumulated deficit	$(1,632,432)	$ (1,621,122)	$(11,310)

Equity

The following table sets forth the changes in equity attributable to noncontrolling interests and equity attributable to Kindred stockholders for the three months ended March 31, 2018 and 2017 (in thousands):

For the three months ended March 31, 2018	Amounts attributable to Kindred stockholders	Noncontrolling interests	Total equity
Balance at December 31, 2017	$ 123,326	$ 224,436	$347,762
Adoption of the New Revenue Standard as of January 1, 2018	(11,767)	-	(11,767)
Comprehensive income (loss):			
Net income (loss)	(1,705)	13,452	11,747
Other comprehensive income	3,496	-	3,496
	1,791	13,452	15,243
Shares tendered by employees for statutory tax withholdings upon issuance of common stock	(3,044)	-	(3,044)
Stock-based compensation amortization	4,261	-	4,261

Distributions to noncontrolling interests	-	(27,228)	(27,228)
Contributions made by noncontrolling interests	-	165	165
Balance at March 31, 2018	$ 114,567	$ 210,825	$ 325,392
For the three months ended March 31, 2017			
Balance at December 31, 2016	$ 812,551	$ 228,970	$ 1,041,521
Comprehensive income (loss):			
Net income (loss)	(5,748)	14,964	9,216
Other comprehensive income	1,871	-	1,871
	(3,877)	14,964	11,087
Shares tendered by employees for statutory tax withholdings upon issuance of common stock	(2,255)	-	(2,255)
Stock-based compensation amortization	3,132	-	3,132
Dividends paid	(10,228)	-	(10,228)
Distributions to noncontrolling interests	-	(25,801)	(25,801)
Balance at March 31, 2017	$ 799,323	$ 218,133	$ 1,017,456

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KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION (Continued)

Cash, cash equivalents and restricted cash

Beginning in 2018, the Company adopted the authoritative guidance that simplifies the disclosure of restricted cash within the statement of cash flows. The following table provides a reconciliation of cash and cash equivalents, as reported in our accompanying unaudited condensed consolidated balance sheet, to cash, cash equivalents and restricted cash, as reported in our accompanying unaudited condensed consolidated statement of cash flows (in thousands):

	March 31, 2018	December 31, 2017
Cash and cash equivalents	$ 108,759	$ 160,254
Restricted cash:		
Insurance subsidiary investments (current)	22,407	22,546
Other assets (current)	425	1,675
Insurance subsidiary investments (long-term)	27,771	28,988
Other assets (long-term)	13,159	5,000
Cash, cash equivalents and restricted cash	$ 172,521	$ 218,463

Property and equipment

Beginning April 1, 2017, the Company changed the estimated useful life of certain information technology equipment and software based upon a detailed review of actual utilization. Following the acquisition of Gentiva Health Services, Inc. (“Gentiva”), a home health and hospice company acquired by the Company on February 2, 2015 (the “Gentiva Merger”), the Company made significant investments in information technology and software. The actual usage and longevity of these assets supports longer lives than previously estimated. The change in estimate extended the expected useful life by one to two years depending on the asset category and has been accounted for prospectively. The impact from this change in accounting estimate was an increase to income from continuing operations before income taxes of approximately $3.5 million in the first quarter of 2018.

Derivative financial instruments

In January 2016, the Company entered into three interest rate swap agreements to hedge its floating interest rate on an aggregate of $325 million of debt outstanding under its Term Loan Facility (as defined in Note 11), which replaced the previous $225 million aggregate swap that expired on January 11, 2016. The interest rate swaps have an effective date of January 11, 2016, and expire on January 9, 2021. The Company is required to make payments based upon a fixed interest rate of 1.862% and 1.855% calculated on the notional amount of $175 million and $150 million, respectively. In exchange, the Company will receive interest on $325 million at a variable interest rate that is based upon the three-month London Interbank Offered Rate (“LIBOR”), subject to a minimum rate of 1.0%.

In March 2014, the Company entered into an interest rate swap agreement to hedge its floating interest rate on an aggregate of $400 million of debt outstanding under its Term Loan Facility. On April 8, 2014, the Company completed a novation of a portion of its $400 million swap agreement to two new counterparties, each in the amount of $125 million. The original swap contract was not amended, terminated, or otherwise modified. The interest rate swap had an effective date of April 9, 2014, expired on April 9, 2018, and applied to the Term Loan Facility. The Company made payments based upon a fixed interest rate of 1.867% calculated on the notional amount of $400 million. In exchange, the Company received interest on $400 million at a variable interest rate that was based upon the three-month LIBOR, subject to a minimum rate of 1.0%.

The interest rate swaps were assessed for hedge effectiveness for accounting purposes and the Company determined the interest rate swaps qualify for cash flow hedge accounting treatment at March 31, 2018. The Company records the effective portion of the gain or loss on these derivative financial instruments in accumulated other comprehensive income (loss) as a component of stockholders' equity and records the ineffective portion of the gain or loss on these derivative financial instruments as interest expense. For the three months ended March 31, 2018 and 2017, there was no ineffectiveness related to the interest rate swaps.

The aggregate fair value of the interest rate swaps recorded in other current assets was $6.6 million and $2.5 million at March 31, 2018 and December 31, 2017, respectively. The fair value was determined by reference to a third party valuation and is considered a Level 2 input within the fair value hierarchy.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION (Continued)

Variable interest entities

The Company follows the provisions of the authoritative guidance for determining whether an entity is a variable interest entity (“VIE”). In order to determine if the Company is a primary beneficiary of a VIE for financial reporting purposes, it must consider whether it has the power to direct activities of the VIE that most significantly impact the performance of the VIE and whether the Company has the obligation to absorb losses or the right to receive returns that would be significant to the VIE. The Company consolidates a VIE when it is the primary beneficiary.

Of the Company’s 19 operating IRFs, 17 are partnerships subject to an operating and management services agreement. Under GAAP, the Company determined that 14 of these 17 partnerships qualify as VIEs and concluded that the Company is the primary beneficiary in all but one partnership. The Company holds an ownership interest and acts as manager in each of the partnerships. Through the management services agreement, the Company is delegated necessary responsibilities to provide management services, administrative services and direction of the day-to-day operations. Based upon the Company’s assessment of the most significant activities of the IRFs, the manager has the ability to direct the majority of those activities in 13 of the partnerships.

The analysis upon which the consolidation determination rests can be complex, can involve uncertainties, and requires judgment on various matters, some of which could be subject to different interpretations.

The carrying amounts and classifications of the assets and liabilities of the consolidated VIEs are as follows (in thousands):

	March 31, 2018	December 31, 2017
Assets:		
Current assets:		
Cash and cash equivalents	$ 48,575	$ 43,734
Accounts receivable, net	43,252	47,034
Inventories	1,541	1,541
Other	2,337	2,899
	95,705	95,208
Property and equipment, net	13,645	14,160
Goodwill	275,375	275,375
Intangible assets, net	20,793	21,002
Other	6	6
Total assets	$ 405,524	$ 405,751
Liabilities:		
Current liabilities:		

Accounts payable	$26,716	$26,533
Salaries, wages and other compensation	2,468	3,092
Other accrued liabilities	3,942	4,066
Long-term debt due within one year	448	604
	33,574	34,295
Long-term debt	330	378
Deferred credits and other liabilities	9,643	9,235
Total liabilities	$43,547	$43,908

Other information

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions for quarterly reports on Form 10-Q of Regulation S-X and do not include all of the disclosures normally required by GAAP or those normally required in annual reports on Form 10-K. Accordingly, these financial statements should be read in conjunction with the audited consolidated financial statements of the Company for the year ended December 31, 2017 filed with the Securities and Exchange Commission (the “SEC”) on Form 10-K. The accompanying condensed consolidated balance sheet at December 31, 2017 was derived from audited consolidated financial statements, but does not include all disclosures required by GAAP.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION (Continued)

Other information (Continued)

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the Company’s customary accounting practices. Management believes that financial information included herein reflects all adjustments necessary for a fair statement of interim results and, except as otherwise disclosed, all such adjustments are of a normal and recurring nature.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with GAAP and include amounts based upon the estimates and judgments of management. Actual amounts may differ from those estimates.

Reclassifications

Certain prior period amounts have been reclassified to conform with the current period presentation.

NOTE 2 – PLANNED ACQUISITION OF KINDRED

Merger Agreement

On December 19, 2017, the Company announced that its Board of Directors (the “Board”) approved a definitive agreement under which the Company will be acquired by a consortium of three companies: TPG Capital (“TPG”), Welsh, Carson, Anderson & Stowe (“WCAS”) and Humana Inc. (“Humana”). Subject to the terms and conditions of an Agreement and Plan of Merger (the “Merger Agreement”) among the Company, Kentucky Hospital Holdings, LLC (“HospitalCo Parent”), Kentucky Homecare Holdings, Inc. (“Parent”) and Kentucky Homecare Merger Sub, Inc. (“Merger Sub”), Merger Sub will be merged with and into Kindred (the “Merger”), with Kindred continuing as the surviving company in the Merger (the “Surviving Entity”). See Note 5 for a description of restructuring charges associated with the Merger.

At the effective time of the Merger, each share of the Company’s common stock, par value $0.25 per share (“Common Stock”) issued and outstanding immediately prior to the effective time of the Merger (other than shares held by Parent, HospitalCo Parent, Merger Sub or Kindred and their respective wholly owned subsidiaries (which will be cancelled) and shares that are owned by stockholders who have properly exercised and perfected a demand for appraisal rights under Delaware law), will be cancelled and converted into the right to receive $9.00 in cash, without interest.

The Merger Agreement contains customary representations, warranties and covenants for a transaction of this nature. The Merger Agreement also contains customary covenants, including, among others, covenants (i) providing for the Company and its respective subsidiaries to conduct business in all material respects in the ordinary course and not to take certain actions without Merger Sub’s consent and (ii) for each of the parties to use reasonable best efforts to cause the transactions contemplated by the Merger Agreement to be consummated. Additionally, the Merger Agreement provides for customary pre-closing covenants, including covenants not to solicit proposals relating to alternative transactions or, subject to certain exceptions, enter into discussions concerning or provide information in connection with alternative transactions, covenants to call and hold a meeting of the Company's stockholders and a covenant to recommend that its stockholders adopt the Merger Agreement, subject to certain exceptions to permit the Company's directors to satisfy their applicable fiduciary duties.

Consummation of the Merger is subject to various conditions, including, among others, adoption of the Merger Agreement by the requisite vote of the Company's stockholders (this condition was satisfied on April 5, 2018), the receipt of certain licensure and regulatory approvals, the expiration of the waiting period under the Hart-Scott-Rodino Antitrust Improvement Act of 1976, as amended (this condition was satisfied on February 20, 2018), the consummation of the purchase of the two remaining skilled nursing facilities from Ventas, Inc. ("Ventas") and payment of corresponding expense reimbursement to Ventas (this condition was satisfied on December 21, 2017), the satisfaction of the closing conditions to the Separation Agreement (as defined below) and certain related entity conversions, the absence of any material adverse effect on each of the Company, its home health, hospice and community care business, and its TC hospitals, IRFs and contract rehabilitation services business, and certain other customary closing conditions.

The Merger Agreement also contains certain termination rights for the Company and Merger Sub (including if the Merger is not consummated by August 17, 2018 (the "End Date")) and provides that upon termination of the Merger Agreement under specified circumstances, including, among others, following a change in recommendation of the Board or its termination of the Merger Agreement to enter into a written definitive agreement for a "superior proposal," the Company will be required to pay Merger Sub a termination fee of $29 million and reimburse the documented out-of-pocket expenses of Parent, HospitalCo Parent and certain of their affiliates in connection with the Merger Agreement up to $10 million.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 2 – PLANNED ACQUISITION OF KINDRED (Continued)

Merger Agreement (Continued)

Parent will be required to pay the Company a reverse termination fee of $61.5 million, and to reimburse certain of the Company’s expenses, including the reasonable and documented out-of-pocket expenses the Company incurred in connection with the implementation of the Separation Transactions (as defined in the Separation Agreement), up to $13.5 million, in the event the Merger Agreement is terminated (i) by the Company, subject to certain limitations set forth in the Merger Agreement, if (A) there has been a breach of a representation, warranty or covenant of Parent or Merger Sub that would cause the related closing condition to be incapable of being satisfied or cured by the End Date or, if curable, is not cured by Parent or Merger Sub by the earlier of 30 days after receipt of written notice of such breach and the End Date, (B) the conditions to Parent, HospitalCo Parent and Merger Sub’s obligations to consummate the closing have been satisfied (other than those conditions that by their terms are to be satisfied at or immediately prior to the closing, provided that such conditions are then capable of being satisfied at the closing), the Company has irrevocably confirmed to Parent in writing that the Company is prepared and able to consummate the closing, and Parent and Merger Sub fail to consummate the Merger by the later of the date the closing should have occurred and three business days following the date of the notice from the Company described above, or (ii) by the Company or Parent if the Merger has not occurred by the End Date and at the time of termination all of the conditions to Parent, HospitalCo Parent and Merger Sub’s obligations to consummate the closing have been satisfied (other than those conditions that by their terms are to be satisfied by actions taken at the closing, provided that such conditions are then capable of being satisfied at the closing) other than those relating to obtaining specified licensure and regulatory approvals and/or there being any injunction or other order by a governmental entity charged with jurisdiction over the granting of such approvals.

In connection with the Merger Agreement, Parent and HospitalCo Parent have obtained equity and debt financing commitments for the transactions contemplated by the Merger Agreement and the Separation Agreement, the aggregate proceeds of which will be sufficient to consummate the transactions contemplated by the Merger Agreement and the Separation Agreement on the closing date, including the payment of any amounts required to be paid by Parent pursuant to the Merger Agreement on the closing date, the repayment of the Company’s existing indebtedness, and the payment of all fees and expenses reasonably expected to be incurred in connection therewith. Pursuant to equity commitment letters executed and delivered concurrently with the Merger Agreement, subject to the terms and conditions set forth therein, Humana, TPG, WCAS and Port-aux-Choix Private Investments Inc. (“PSP”), have committed, severally but not jointly, to capitalize Parent, and TPG, WCAS and PSP have committed, severally but not jointly, to capitalize HospitalCo Parent, with the aggregate amount of the equity financing. In addition, each of Humana, TPG, WCAS and PSP have provided us limited guarantees, guaranteeing Parent’s obligation to pay the reverse termination fee and certain other reimbursement obligations of the Parent and Merger Sub pursuant to the Merger Agreement.

Separation Agreement

Concurrently with the execution and delivery of the Merger Agreement, on December 19, 2017, Kindred, Parent, HospitalCo Parent, and Kentucky Hospital Merger Sub, Inc., entered into a Separation Agreement (the “Separation Agreement”), pursuant to which, promptly following the effective time of the Merger, the Surviving Entity will be separated from the Company's home health, hospice and community care services business and acquired by HospitalCo Parent.

The Separation Agreement relates to, among other things (i) certain restructuring transactions that are to take place with respect to the Company and its subsidiaries, (ii) procedures concerning the transfer of certain assets used and employees employed in the Company's respective businesses and (iii) the allocation of costs and expenses related to the separation of the Surviving Entity from the Homecare Business (as defined in the Separation Agreement). The Separation Agreement requires, among other things, the Company to take certain actions and expend certain efforts prior to the closing of the Merger in preparation for such separation transactions.

NOTE 3 – DIVESTITURES

Skilled nursing facility business exit

On June 30, 2017, the Company entered into a definitive agreement with BM Eagle Holdings, LLC, a joint venture led by affiliates of BlueMountain Capital Management, LLC ("BlueMountain"), under which the Company agreed to sell its skilled nursing facility business for $700 million in cash (the "SNF Divestiture"). The SNF Divestiture included 89 nursing centers with 11,308 licensed beds and seven assisted living facilities with 380 licensed beds in 18 states. Through March 31, 2018, the Company completed the sale or closed 86 of the skilled nursing facilities and all seven of the assisted living facilities.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 3 – DIVESTITURES (Continued)

Skilled nursing facility business exit (Continued)

Thirty-six of the skilled nursing facilities were previously leased from Ventas (the “Ventas Properties”). The Company had an option to acquire the real estate of the Ventas Properties for aggregate consideration of $700 million, which the Company exercised as it closed on the sale of the Ventas Properties in connection with the SNF Divestiture during 2017. On each respective closing date, the Company paid to Ventas the allocable portion of the $700 million purchase price for the Ventas Properties and Ventas conveyed the real estate for the applicable Ventas Property to BlueMountain or its designee.

The completion of the sales of the remaining three nursing centers is subject to customary conditions to closing, including the receipt of all licensure, regulatory and other approvals. The Company expects that all of the remaining closings will be completed during 2018.

In accordance with authoritative guidance for assets held for sale and discontinued operations accounting, the skilled nursing facility business is reported as assets held for sale and was moved to discontinued operations for all periods presented. See Note 4.

During the first quarter of 2018, the Company recorded $5.8 million of pretax charges related to the SNF Divestiture, including $3.7 million of transaction and other costs and $2.1 million of retention costs. During the first quarter of 2017, the Company recorded $6.2 million of pretax charges related to the SNF Divestiture, including $5.8 million of retention costs and $0.4 million of transaction and other costs.

In connection with the SNF Divestiture, the Company entered into an interim management agreement in the third quarter of 2017 with certain affiliates of BlueMountain in the state of California whereby the Company would lease its license of certain operations to such affiliates until licensure approval is obtained. Because the Company has continuing involvement in the business through purveying certain rights of ownership of the assets while under the interim management agreement and license sublease, the Company does not meet the requirements for a sale-leaseback transaction as described in ASC 840-40, Leases - Sale-Leaseback Transactions. Under the failed-sale-leaseback accounting model, the Company is deemed under GAAP to still own certain real estate assets sold to BlueMountain, which the Company must continue to reflect in its consolidated balance sheet and depreciate over the assets’ remaining useful life. The Company also must treat a portion of the pretax cash proceeds from the SNF Divestiture as though it were the result of a $140.8 million other long-term liability financing obligation in its accompanying unaudited condensed consolidated balance sheet, and also must defer a $17.9 million gain associated with some of these assets until continuing involvement ceases. The lease will terminate upon licensure approval, at which time the Company will cease to recognize the remaining other long-term liability financing obligation, as well as the remaining net book value of the real estate assets and will recognize the gain.

NOTE 4 – DISCONTINUED OPERATIONS

In accordance with the authoritative guidance for the impairment or disposal of long-lived assets, the divestitures of unprofitable businesses have been accounted for as discontinued operations. Accordingly, the operating results of these businesses and the losses or impairments associated with these transactions were classified as discontinued operations, net of income taxes, in the accompanying unaudited condensed consolidated statement of operations for all periods. Effective January 1, 2015, the authoritative guidance modified the requirements for reporting discontinued operations. A disposal is now required to be reported in discontinued operations only if the disposal represents a strategic shift that has (or will have) a major effect on the Company’s operations and financial results. At March 31, 2018, the Company had three nursing centers held for sale classified as discontinued operations.

In connection with the SNF Divestiture, direct overhead and the profits from applicable RehabCare contracts servicing the Company’s skilled nursing facility business that were not retained with new operators were moved to discontinued operations for all periods presented. The Company has reclassified certain retained businesses and expenses previously reported in the nursing center division to other business segments, including hospital-based sub-acute units and a skilled nursing facility to the hospital division and a small therapy business to the Kindred Hospital Rehabilitation Services operating segment for all periods presented. See Note 3.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 4 – DISCONTINUED OPERATIONS (Continued)

The following table summarizes (in thousands) the SNF Divestiture liability activity (included in current liabilities) during the three months ended March 31, 2018, which does not include non-cash charges of $3.2 million related to other costs:

	Retention	Transaction and other costs	Total
Liability balance at December 31, 2017	$ 5,436	$ 5,600	$ 11,036
Expense	2,117	486	2,603
Payments	(3,723)	(2,669)	(6,392)
Liability balance at March 31, 2018	$ 3,830	$ 3,417	$ 7,247

A summary of discontinued operations follows (in thousands):

	Three months ended March 31, 2018	2017
Revenues	$ 9,198	$ 255,683
Salaries, wages and benefits	6,293	95,424
Supplies	248	10,513
Building rent	1,693	20,438
Equipment rent	34	2,097
Other operating expenses	3,354	72,583
General and administrative expenses	4,966	43,954
Other income	(285)	(264)
Impairment charges	-	683
Depreciation and amortization	1,699	5,140
Interest expense	1	5
Investment income	(35)	(17)
	17,968	250,556
Income (loss) from operations before income taxes	(8,770)	5,127
Provision for income taxes	-	68
Income (loss) from operations	(8,770)	5,059
Loss on divestiture of operations	(5,790)	(6,166)
Loss from discontinued operations	(14,560)	(1,107)
Earnings attributable to noncontrolling interests	(660)	(4,481)
Loss attributable to Kindred	$ (15,220)	$ (5,588)

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 4 – DISCONTINUED OPERATIONS (Continued)

The following table sets forth certain discontinued operating data by business segment (in thousands):

	Three months ended March 31, 2018	2017
Revenues:		
Nursing center division	$8,646	$255,181
Hospital division	552	502
	$9,198	$255,683
Segment adjusted operating income (loss):		
Nursing center division	$(5,908)	$32,506
Hospital division	530	967
	$(5,378)	$33,473
Rent:		
Nursing center division:		
Building rent	$1,217	$19,973
Equipment rent	34	2,097
	1,251	22,070
Hospital division:		
Building rent	476	465
Equipment rent	-	-
	476	465
Totals:		
Building rent	1,693	20,438
Equipment rent	34	2,097
	$1,727	$22,535
Depreciation and amortization:		
Nursing center division	$1,699	$5,140
Hospital division	-	-
	$1,699	$5,140

The following table sets forth a summary of assets held for sale related to the SNF Divestiture (in thousands):

	March 31, 2018	December 31, 2017
Long-term assets:		
Property and equipment, net	$ 7,071	$ 15,711

Other	1,866	1,624
	8,937	17,335
Current liabilities (included in other accrued liabilities)	(417)	(417)
	$ 8,520	$ 16,918

NOTE 5 – RESTRUCTURING CHARGES

The Company has initiated various restructuring activities whereby it has incurred costs associated with reorganizing its operations, including the divestiture, swap, closure and consolidation of its business, facilities and branches, reduced headcount and realigned operations in order to improve operations, cost efficiencies and capital structure in response to changes in the healthcare industry, increasing leverage and to partially mitigate reductions in reimbursement rates from third party payors. The costs associated with these activities are reported as restructuring charges in the accompanying unaudited condensed consolidated statement of operations and would have been recorded as general and administrative expense or rent expense if not classified as restructuring charges.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 5 – RESTRUCTURING CHARGES (Continued)

The following table sets forth the restructuring charges incurred by business segment (in thousands):

	Three months ended March 31,	
	2018	2017
Kindred at Home:		
Home health	$291	$5,932
Hospice	519	2,386
	810	8,318
Hospital division	923	972
Kindred Rehabilitation Services:		
Kindred Hospital Rehabilitation Services	-	-
RehabCare	-	-
	-	-
Support center	6,376	716
	$8,109	$10,006

Restructuring Activities

Planned Acquisition of Kindred

During the fourth quarter of 2017, the Company announced that the Board had approved the Merger Agreement as described in Note 2. The costs incurred related to the Merger Agreement are expected to be substantially completed in 2018.

The composition of the restructuring costs that the Company has incurred for these restructuring initiatives is as follows (in thousands):

	Three months ended March 31,	
	2018	2017
Merger costs	$6,143	$ -
Retention and severance	407	-
	$6,550	$ -

The following table (in thousands) summarizes the Merger restructuring liability activity (included in other accrued liabilities):

	Merger costs
Liability balance at December 31, 2017	$7,907
Expense	6,143
Payments	(9,659)
Liability balance at March 31, 2018	$4,391

LTAC Hospital Portfolio Repositioning 2017 Plan

During the third quarter of 2017, the Company approved phase two of the LTAC hospital portfolio repositioning plan that incorporated the closure and conversion of certain LTAC hospitals as part of its mitigation strategies in response to the new patient criteria for LTAC hospitals under the Pathway for SGR Reform Act of 2013 (the "LTAC Legislation"). The activities related to the LTAC hospital portfolio repositioning 2017 plan will be substantially completed in 2018.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 5 – RESTRUCTURING CHARGES (Continued)

Restructuring Activities (Continued)

LTAC Hospital Portfolio Repositioning 2017 Plan (Continued)

The composition of the restructuring charges that the Company has incurred for these activities is as follows (in thousands):

	Three months ended March 31, 2018	2017
Lease termination costs	$451	$ -
Asset write-offs	418	-
Gain on disposal	(370)	-
Severance	(48)	
	$451	$ -

The following table (in thousands) summarizes the Company's LTAC hospital portfolio repositioning 2017 plan liability activity (included in current liabilities, and deferred credits and other liabilities) during the three months ended March 31, 2018, which does not include non-cash charges of $0.1 million related to asset write-offs and gain on disposal. The lease termination costs were recorded as a liability discounted at the Company's credit-adjusted risk-free rate through the end of 2025, which is the original lease term of the leased hospital.

	Lease termination costs
Liability balance at December 31, 2017	$ 31,645
Expense	451
Payments	(1,265)
Liability balance at March 31, 2018	$ 30,831

LTAC Hospital Portfolio Repositioning 2016 Plan

During the first quarter of 2016, the Company approved the LTAC hospital portfolio repositioning 2016 plan that incorporated the divestiture, swap or closure of certain LTAC hospitals as part of its mitigation strategies to prepare for new patient criteria for LTAC hospitals under the LTAC Legislation. The activities related to the LTAC hospital portfolio repositioning 2016 plan were substantially completed during 2016.

The composition of the restructuring charges that the Company has incurred for these activities is as follows (in thousands):

	Three months ended March 31, 2018	2017
Lease termination costs	$472	$740
Facility closure costs	-	232
	$472	$972

The following table (in thousands) summarizes the Company's LTAC hospital portfolio repositioning 2016 plan liability activity (included in current liabilities, and deferred credits and other liabilities) during the three months ended March 31, 2018. The majority of the lease termination costs were recorded as a liability discounted at the Company's credit-adjusted risk-free rate through the end of 2025, which is the original lease term of the leased hospitals.

	Lease termination costs
Liability balance at December 31, 2017	$ 33,945
Expense	472
Payments	(2,628)
Liability balance at March 31, 2018	$ 31,789

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 5 – RESTRUCTURING CHARGES (Continued)

Restructuring Activities (Continued)

Kindred at Home 2017 Efficiency Initiative

During the first quarter of 2017, the Kindred at Home division approved and initiated a cost and operations efficiency initiative to address increases in labor costs associated with competitive labor markets and the integration of pay practices from acquisitions across the Kindred at Home portfolio. This initiative includes the consolidation and closure of under-performing branches and a reduction in force associated with the restructuring of divisional and regional support teams. These activities were substantially completed during 2017.

The composition of the restructuring costs that the Company has incurred for these considerations is as follows (in thousands):

	Three months ended March 31,	
	2018	2017
Asset write-offs	$319	$2,888
Lease termination costs	194	616
Loss on disposal	50	-
Severance	12	1,417
	$575	$4,921

The following table (in thousands) summarizes the related restructuring liability activity (included in current liabilities) during the three months ended March 31, 2018, which does not include non-cash charges of $0.4 million related to asset write-offs and loss on disposal:

	Lease termination costs
Liability balance at December 31, 2017	$ 960
Expense	194
Payments	(227)
Liability balance at March 31, 2018	$ 927

Kindred at Home Branch Consolidations and Closures

During the first quarter of 2015, the Company approved and initiated branch consolidations and closures in specific markets to improve operations and cost efficiencies in the Kindred at Home division. The branch consolidations and closures included branches that served both the home health and hospice business segment operations. Gentiva initiated similar branch consolidations and closures prior to the Gentiva Merger and these activities and acquired liabilities are included herein. These activities were substantially completed during 2016.

The composition of the restructuring costs that the Company has incurred for these consolidations is as follows (in thousands):

	Three months ended March 31,	
	2018	2017
Lease termination costs	$61	$549
Asset write-offs	-	2,240
Severance	-	608
	$61	$3,397

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 6 – EARNINGS (LOSS) PER SHARE AND DIVIDENDS

Earnings (loss) per common share are based upon the weighted average number of common shares outstanding during the respective periods. The Company follows the provisions of the authoritative guidance for determining whether instruments granted in share-based payment transactions are participating securities, which requires that unvested restricted stock that entitles the holder to receive nonforfeitable dividends before vesting be included as a participating security in the basic and diluted earnings per common share calculation pursuant to the two-class method. Because the Company reported a loss from continuing operations attributable to the Company for the three months ended March 31, 2017, there was no allocation to participating unvested restricted stockholders for such period.

	Three months ended March 31,			
	2018		2017	
	Basic	Diluted	Basic	Diluted
Earnings (loss):				
Amounts attributable to Kindred stockholders:				
Income (loss) from continuing operations:				
As reported in Statement of Operations	$13,515	$13,515	$(160)	$(160)
Allocation to participating unvested restricted stockholders	(447)	(447)	-	-
Available to common stockholders	$13,068	$13,068	$(160)	$(160)
Discontinued operations, net of income taxes:				
Income (loss) from operations:				
As reported in Statement of Operations	$(9,430)	$(9,430)	$578	$578
Allocation to participating unvested restricted stockholders	312	312	-	-
Available to common stockholders	$(9,118)	$(9,118)	$578	$578
Loss on divestiture of operations:				
As reported in Statement of Operations	$(5,790)	$(5,790)	$(6,166)	$(6,166)
Allocation to participating unvested restricted stockholders	191	191	-	-
Available to common stockholders	$(5,599)	$(5,599)	$(6,166)	$(6,166)
Loss from discontinued operations:				
As reported in Statement of Operations	$(15,220)	$(15,220)	$(5,588)	$(5,588)
Allocation to participating unvested restricted stockholders	503	503	-	-
Available to common stockholders	$(14,717)	$(14,717)	$(5,588)	$(5,588)
Net loss:				
As reported in Statement of Operations	$(1,705)	$(1,705)	$(5,748)	$(5,748)
Allocation to participating unvested restricted stockholders	56	56	-	-
Available to common stockholders	$(1,649)	$(1,649)	$(5,748)	$(5,748)
Shares used in the computation:				
Weighted average shares outstanding - basic computation	88,526	88,526	87,085	87,085
Dilutive effect of employee stock options		-		-
Dilutive effect of tangible equity units		-		-
Adjusted weighted average shares outstanding -		88,526		87,085

diluted computation				
Earnings (loss) per common share:				
Income (loss) from continuing operations	$0.15	$0.15	$-	$-
Discontinued operations:				
Income (loss) from operations	(0.11)	(0.11)	-	-
Loss on divestiture of operations	(0.06)	(0.06)	(0.07)	(0.07)
Loss from discontinued operations	(0.17)	(0.17)	(0.07)	(0.07)
Net loss	$(0.02)	$(0.02)	$(0.07)	$(0.07)
Number of antidilutive stock options and tangible equity units excluded from				
shares used in the diluted earnings (loss) per common share computation		557		1,380

During the three months ending March 31, 2017, the Company paid a cash dividend of $0.12 per common share. The Board elected to discontinue paying dividends on the Company's Common Stock following the March 31, 2017 payment and instead redirected funds to repay debt and invest in growth.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 6 – EARNINGS (LOSS) PER SHARE AND DIVIDENDS (Continued)

The Company made an installment payment on the Company's 172,500 tangible equity units (the "Units") of $18.75 per Unit on March 1, 2017. Each Unit was composed of a prepaid stock purchase contract (a "Purchase Contract") and one share of 7.25% Mandatory Redeemable Preferred Stock, Series A (the "Mandatory Redeemable Preferred Stock") which had a final preferred stock installment payment date of December 1, 2017. On December 1, 2017, the remaining holders of 87,379 Purchase Contracts were mandatorily redeemed. As a result, holders thereof received 50.6329 shares of Common Stock per Purchase Contract, resulting in approximately 4.4 million shares of Common Stock being issued on such date. Holders of the Mandatory Redeemable Preferred Stock were previously entitled to receive a quarterly "preferred stock installment payment" in cash, shares of Common Stock, or a combination thereof. All shares of Mandatory Redeemable Preferred Stock were redeemed on December 1, 2017 as planned pursuant to their terms.

NOTE 7 – BUSINESS SEGMENT DATA

The Company is organized into three operating divisions: the Kindred at Home division, the hospital division, and the Kindred Rehabilitation Services division. Based upon the authoritative guidance for business segments, the Company's operating divisions represent five reportable operating segments, including (1) home health services, (2) hospice services, (3) hospitals, (4) Kindred Hospital Rehabilitation Services, and (5) RehabCare. These reportable operating segments are consistent with information used by the Company's President and Chief Executive Officer and its Chief Operating Officer to assess performance and allocate resources. The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies.

The Company has reclassified certain retained businesses and expenses previously reported in the nursing center division, including hospital-based sub-acute units and a skilled nursing facility to the hospital division and a small therapy business to the Kindred Hospital Rehabilitation Services operating segment for all periods presented.

For segment purposes, the Company defines segment adjusted operating income as earnings before interest, income taxes, depreciation, amortization, and total rent reported for each of the Company's operating segments, excluding impairment charges, restructuring charges, and the allocation of support center overhead.

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 7 – BUSINESS SEGMENT DATA (Continued)

The following table sets forth certain data by business segment (in thousands):

	Three months ended March 31, 2018	2017
Revenues:		
Kindred at Home:		
Home health	$453,759	$450,831
Hospice	183,628	179,378
	637,387	630,209
Hospital division	547,630	556,646
Kindred Rehabilitation Services:		
Kindred Hospital Rehabilitation Services	178,219	178,115
RehabCare	172,519	198,126
	350,738	376,241
	1,535,755	1,563,096
Eliminations:		
Kindred Hospital Rehabilitation Services	(19,321)	(21,148)
RehabCare	(1,993)	(1,878)
Hospitals	(652)	(580)
	(21,966)	(23,606)
	$1,513,789	$1,539,490
Income from continuing operations:		
Segment adjusted operating income:		
Kindred at Home:		
Home health	$59,512	$63,750
Hospice	28,943	27,581
	88,455	91,331
Hospital division	104,250	93,438
Kindred Rehabilitation Services:		
Kindred Hospital Rehabilitation Services	53,409	51,760
RehabCare	3,931	8,704
	57,340	60,464
Support center expenses	(57,600)	(60,014)
Impairment charges	-	(474)
Restructuring charges	(6,931)	(8,101)
Building rent	(62,488)	(64,656)
Equipment rent	(8,689)	(8,887)
Restructuring charges - rent	(1,178)	(1,905)

Depreciation and amortization	(24,789)	(29,820)
Interest, net	(60,835)	(58,819)
Income from continuing operations before income taxes	27,535	12,557
Provision for income taxes	1,228	2,234
	$26,307	$10,323

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 7 – BUSINESS SEGMENT DATA (Continued)

	Three months ended March 31,	
	2018	2017
Rent:		
Kindred at Home:		
Home health:		
Building	$8,025	$8,147
Equipment	272	306
	8,297	8,453
Hospice:		
Building	4,278	4,256
Equipment	78	84
	4,356	4,340
Hospital division:		
Building	41,072	43,271
Equipment	7,289	7,474
	48,361	50,745
Kindred Rehabilitation Services:		
Kindred Hospital Rehabilitation Services:		
Building	8,647	8,423
Equipment	526	375
	9,173	8,798
RehabCare:		
Building	340	323
Equipment	494	621
	834	944
Support center:		
Building	126	236
Equipment	30	27
	156	263
Totals:		
Building	62,488	64,656
Equipment	8,689	8,887
	$71,177	$73,543
Depreciation and amortization:		
Kindred at Home:		

Home health	$2,101	$3,128
Hospice	867	1,285
	2,968	4,413
Hospital division	10,042	10,874
Kindred Rehabilitation Services:		
Kindred Hospital Rehabilitation Services	3,566	3,843
RehabCare	427	1,845
	3,993	5,688
Support center	7,786	8,845
	$24,789	$29,820

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KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 7 – BUSINESS SEGMENT DATA (Continued)

	Three months ended March 31, 2018	2017
Capital expenditures, excluding acquisitions (including discontinued operations):		
Kindred at Home:		
Home health:		
Routine	$1,835	$1,038
Development	-	-
	1,835	1,038
Hospice:		
Routine	655	629
Development	-	-
	655	629
Hospital division:		
Routine	6,924	3,123
Development	102	-
	7,026	3,123
Kindred Rehabilitation Services:		
Kindred Hospital Rehabilitation Services:		
Routine	1,197	418
Development	610	482
	1,807	900
RehabCare:		
Routine	315	187
Development	-	-
	315	187
Support center:		
Routine:		
Information systems	4,837	4,109
Other	147	842
	4,984	4,951
Development	2,830	4,951
	7,814	9,902
Discontinued operations - nursing centers:		
Routine	500	1,595
Development	-	6

	500	1,601
Totals:		
Routine	16,410	11,941
Development	3,542	5,439
	$19,952	$17,380

KINDRED HEALTHCARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

NOTE 7 – BUSINESS SEGMENT DATA (Continued)

	March 31, 2018	December 31, 2017
Assets at end of period (including discontinued operations):		
Kindred at Home:		
Home health	$1,547,395	$ 1,540,010
Hospice	912,179	