PARTICIPANTS

Corporate Participants

Mary Ann Arico – Chief Investor Relations Officer, HealthSouth Corp.
Jay Grinney – President and Chief Executive Officer, HealthSouth Corp.
Douglas E. Coltharp – Chief Financial Officer & Executive Vice President, HealthSouth Corp.
Mark J. Tarr – Chief Operating Officer & Executive Vice President, HealthSouth Corp.
John P. Whittington – Secretary, Executive VP & General Counsel, HealthSouth Corp.

Other Participants

Whit Mayo – Analyst, Robert W. Baird & Co. Equity Capital Markets
Sheryl R. Skolnick – Analyst, CRT Capital Group LLC
Frank G. Morgan – Analyst, RBC Capital Markets LLC
Joshua R. Raskin – Analyst, Barclays Capital, Inc.
Darren Lehrich – Analyst, Deutsche Bank Securities, Inc.
Rob M. Mains – Analyst, Stifel, Nicolaus & Co., Inc.
Chris D. Rigg – Analyst, Susquehanna Financial Group LLLP
A.J. Rice – Analyst, UBS Securities LLC
Gary Lieberman – Analyst, Wells Fargo Securities LLC
Stephen C. Baxter – Analyst, Bank of America Merrill Lynch

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to HealthSouth First Quarter 2014 Earnings Conference Call. At this time, I would like to inform all participants that their lines will be in a listen-only mode. After the speakers' remarks, there will be a question-and-answer period. [Operator Instructions] You will be limited to one question and one follow-up question. Today's conference call is being recorded. If you have any objections, you may disconnect at this time.

I will now turn the call over to Mary Ann Arico, Chief Investor Relations Officer.

Mary Ann Arico, Chief Investor Relations Officer

Thank you operator and Good morning everyone. Thank you for joining us today for the HealthSouth First Quarter 2014 Earnings Call. With me on the call in Birmingham today are Jay Grinney, President and Chief Executive Officer; Doug Coltharp, Executive Vice President and Chief Financial Officer; Mark Tarr, Executive Vice President and Chief Operating Officer; John Whittington, Executive Vice President, General Counsel and Corporate Secretary; Andy Price, Chief Accounting Officer; Ed Fay, Treasurer; Julie Duck, Senior Vice President, Financial Operations.

Before we begin, if you do not already have a copy, the press release, financial statements, the related 8-K filing with the SEC and the supplemental slides are available on our website at www.healthsouth.com.

Moving to slide two to Safe Harbor, which is also set forth in greater detail on the last page of the earnings release. During the call, we will make forward-looking statements which are subject to risks and uncertainties, many of which are beyond our control. Certain risks, uncertainties and other factors that could cause actual results to differ materially from management's projections, forecasts, estimates and expectations are discussed in the company's SEC filings, including in the Form 10-K

for 2013 and the Form 10-Q for first quarter 2014 when filed and previous filings with the SEC. We encourage you to read them.

You are cautioned not to place undue reliance on the estimates, projections, guidance and other forward-looking information presented. Statements made throughout the presentation are based on current estimates of future events and speak only as of today. The company does not undertake a duty to update or correct these forward-looking statements.

Our slide presentation and discussion on this call will include certain non-GAAP financial measures. For such measures, reconciliation to the most directly comparable GAAP measure is available at the end of the slide presentation or at the end of the related press release, both of which are available on our website and as part of the Form 8-K filed last night with the SEC.

Before I turn it over to Jay, I would like to remind you that we will strictly adhere to the one question and one follow-up question rule to allow everyone time to submit a question. If you have additional questions, please feel free to put yourself back in the queue.

And with that, I will turn the call over to Jay.

Jay Grinney, President and Chief Executive Officer

Great. Thank you Mary Ann and good morning to everyone joining today's call. We are very pleased to report that our first quarter results were very good despite the negative effect of sequestration and the disruption to operations resulting from the unusual winter storms. As noted in our release, sequestration, which anniversaried on April 1, created a $9 million revenue and an $8 million adjusted EBITDA headwind in the quarter. Although the winter storms affected many hospitals across our portfolio, they were especially disruptive to our West Virginia, Virginia, Pennsylvania and South Carolina markets. While as reported, discharge growth for the quarter was 2.4%, we estimate the negative impact these storms had on our discharges was approximately 100 basis points, all of which affected same-store facilities. Normalizing for this effect, total discharge growth would have been approximately 3.4% and same-store growth would have been approximately 1.4%.

Adjusted EBITDA for the quarter came in at $144.1 million, a 3.4% increase over Q1 of 2013 despite the $8 million negative effect of sequestration I mentioned earlier.

We also continued to return capital to shareholders in the first quarter through the repurchase of 808,880 shares of HealthSouth common stock under our $250 million repurchase authorization and the payment of an $0.18 per share common dividend.

Looking at the remainder of the year, we believe our full-year results will be at the high-end of both our adjusted EBITDA guidance range of $555 million to $565 million and our EPS guidance range of a $1.86 to $1.91 per diluted share.

Discharges in April are on track, and we expect full-year discharge growth to be between 2.5% and 3.5% despite the weather-related impact in the first quarter. This full-year discharge growth also incorporates discharge growth comps of 6.3% and 5.7%, respectively, in the second and third quarters.

On the development front, the announcement of our joint venture with Mountain States Health Alliance to own and operate Quillen Rehabilitation Hospital brings to four the number of new hospitals we expect to add to our portfolio this year. Our development pipeline remains quite strong and we anticipate announcing other portfolio additions by year-end.

Finally, for those of you who may have missed it, we filed an 8-K after the market closed last Friday disclosing we received additional subpoenas in connection with the previously disclosed DOJ investigation. We have been expecting these new subpoenas for months, and it seeks substantially similar information as the earlier subpoenas from seven additional hospitals. Obviously, since this is an ongoing investigation, we can't provide any commentary beyond what we have disclosed in our reports filed with the SEC. However, what I can say is that we have devoted significant resources, including training and education, to assist our hospitals in complying with the multitude of rules and regulation in our industry, and we're cooperating fully with this investigation.

I'll now turn the agenda over to Doug to provide more commentary on the quarter. After Doug's remarks, we'll open the lines for Q&A.

Douglas E. Coltharp, Chief Financial Officer & Executive Vice President

Thank you, Jay, and good morning everyone. As in the past, during my remarks I'll be making frequent reference to the supplemental slides accompanying our earnings release, so you may find it helpful to have those available.

Revenue in Q1 increased by 3.2% driven by inpatient growth of 3.9% offset by a 7% or $2.5 million decrease in outpatient and other revenue. Discharge growth for Q1 was 2.4%, and as Jay mentioned, we estimate the negative impact attributable to the severe winter storms at approximately 100 basis points, all of which was felt in same-store markets. Same-store growth for the quarter was 0.4% and new store growth was 2%. Revenue for Q1 was also negatively impacted by approximately $9 million attributable to sequestration, and as Jay stated, as a reminder, sequestration anniversaried on April 1 of this year.

The decline in outpatient revenue was primarily attributable to three fewer satellite clinics and seven fewer hospital-based units in operation in Q1 of this year as compared to Q1 of 2013. And revenue per discharge increased by 1.5%, 3.2% prior to the impact of sequestration.

In our Q4 2013 earnings, we devoted a fair bit of time to discussing the establishment reserves against revenue related to post-payment reviews by RAC auditors focused on medical necessity criteria. During Q1, the successful resolution of certain claims under review together with the CMS mandated cessation of further RAC audits until contract rebidding is completed obviated any additions to our previously established reserves.

Bad debt as a percent of revenue for Q1 was 1.3%, flat with the comparable period in 2013.

Prepayment reviews also focused on medical necessity criteria and conducted by fiscal intermediaries, often referred to MACs, have continued, and substantial delays in the adjudication process at the administrative law judge hearing level remain unabated. Accordingly, our bad debt outlook for 2014 remains at 1.3% to 1.5% of net revenues.

During Q1, we continued to exhibit disciplined expense management. SWB as a percent of revenue was 48.4%, up 40 basis points in Q1 last year, but would have declined by 30 basis points if not for sequestration. In a similar vein, hospital-related expenses as a percent of revenue were 20.5%, an increase of 20 basis points from Q1 2013 but would have declined by 10 basis points if not for sequestration.

We also continued our focus on labor productivity during Q1, as employees per occupied bed, or EPOB, was essentially flat at 3.32 in spite of the challenges presented by the severe winter storms.

Adjusted EBITDA for Q1 of $144.1 million increased 3.4% over the same period last year. Adjusted EBITDA was negatively impacted by approximately $8 million related to sequestration and was also impacted by the lower volumes resulting from the winter storms, although quantifying the weather impact on adjusted EBITDA is difficult. Adjusted EBITDA for Q1 included approximately $2 million in gains stemming from the sale of two investments.

Consistent with our expectations, interest expense for Q1 increased by $3.7 million over the same period last year to $27.9 million, primarily as a result of the exchange of the 2% convertible senior subordinated notes for shares of our 6.5% convertible perpetual preferred stock completed in Q4 2013. As a reminder, although the exchange results in an increase of reported interest expense, it reduces our preferred dividend, creating an annualized cash flow benefit of approximately $10 million.

Also as anticipated, our D&A expense for Q1 increased by $4.3 million from Q1 last year to $26.4 million, primarily due to our recent capital expenditures including the investments we have been making in our new clinical information system.

Our diluted earnings per share for Q1 was $0.48, flat to last year, as the current year included higher stock-based compensation expense and an asset impairment charge. The year-over-year EPS comparison can be found on slide 13 of the supplemental slides.

The strength and consistency of our cash flow generation was again evidenced in Q1 with adjusted free cash flow of $65.1 million. As compared to Q1 last year, the benefit of higher adjusted EBITDA was offset by increases in net working capital and maintenance CapEx. The approximate $16 million increase in working capital had two primary components: a decline in payroll liabilities attributable to tax withholding payments related to the vesting of employee restricted stock grants and year-over-year timing differences in our accounts payable. As may be seen on slide 19 of the supplemental slides, we continue to anticipate the full-year increase in working capital for 2014 in a range of $15 million to $25 million.

Maintenance CapEx for Q1 of $30.2 million increased by $11.3 million over Q1 2013. As discussed in our February earnings call, this was primarily attributable to approximately $12 million in hospital equipment purchases that were made in Q4 2013 but which were paid for in January 2014 and therefore are included as Q1 maintenance CapEx. We continue to estimate maintenance CapEx for the full-year 2014 in a range of $90 million to $100 million.

Discretionary CapEx for Q1 was $33.4 million as compared to $30.3 million in Q1 of last year. Our Q1 discretionary CapEx included approximately $17.3 million for the purchase of the real estate of our San Antonio hospital which had previously been subject to a lease agreement. We now own the property associated with 76 of our 103 hospitals.

Our significant free cash flow continued to provide flexibility to return capital to our shareholders, and we did so in Q1 via the payment of the quarterly $0.18 per share dividend on our common stock as well as by repurchasing approximately 809,000 common shares using $26.3 million under our $250 million share buyback authorization.

Substantial investments in our business and returns to our shareholders notwithstanding, we ended the quarter with funded debt and our leverage ratio modestly reduced from year end 2013 levels and with just $43 million outstanding under our $600 million revolving credit facility.

And we'll now open the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Whit Mayo of Robert Baird.

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: Hey, thanks. First question, I just was wondering if you guys could maybe reflect for a minute on the recent de novos over the past two years or so; just wondering if you could frame up maybe returns that you've achieved versus expectations, margins, occupancy, just any way to give us a sense of sort of what the returns have been versus your internal expectations?

<A – Jay Grinney – HealthSouth Corp.>: Yeah, I would say the returns have been quite impressive. We do have a page in our Investor Reference Book that shows all of the recent de novos. I think there may be 8 or 9 of them that we've highlighted there, and we show not only how quickly did each hospital get to certain occupancy levels but we also then indicate when each of them are achieving positive sustained EBITDA. And so, as you can see on that page, and I'm sorry I don't have that reference right away, but we'll get it to you shortly, so those of you who have the Investor Reference Book can look at that. But it is – it's page 73 in the IRB, and you can see that virtually all of the hospitals achieved positive sustained EBITDA in months 3 through 8, and most of the hospitals achieved the average occupancy of the company, which is just under 70% within the first year.

As a reminder, all of the hospitals that we're building are private room facilities, so the expectation would be that maximum occupancy in those hospitals would be much closer to the 95% level because we have much more flexibility in all private rooms.

In terms of actual returns that we've set out, I'll ask Doug to respond.

<A – Doug Coltharp – HealthSouth Corp.>: Yeah, as we've stated previously, we target for our de novos and acquisitions a pre-tax return of at least 15%, and we've been fortunate that the de novos that we have added to our portfolio over the last several years have exceeded that return metric.

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: Great. And this is really a segue to my second question, too, and it just relates to LTACs, and it just seems so clear that CMS is redefining the role of that particular sector and really pointing the industry towards the most medically complex cases out there, and given your JV strategy on the rehab side, the success with the de novos, it just seems like it makes a lot of sense that many hospitals could benefit from dedicated ICU vent facilities and these seem to be so complementary to what you're doing on rehab. So, I'm just kind of curious how you're thinking about that maybe over the next two or three years?

<A – Jay Grinney – HealthSouth Corp.>: Thinking about what?

<Q – Whit Mayo – Robert W. Baird & Co. Equity Capital Markets>: LTACs.

<A – Jay Grinney – HealthSouth Corp.>: You know, as a provider of healthcare services, we recognize the benefit that LTACs provide to patients who need those services. We are familiar with how to own and operate LTACs; we've done that previously, as most of you know. I will say that the new patient criteria is welcomed because it now creates some certainty with respect to the next several years, but it is a little troubling to us as you look at the transition, and we believe that the transition from current state to future state is going to be a little bumpy.

We look at – and we've done a pretty deep dive on LTACs throughout the country, and we've done a heat map to show where are the compliant hospitals, where are the noncompliant hospitals, and well over half of the LTACs out there are currently not compliant. The fact that there's going to have to be such a large transformation is concerning.

That doesn't mean that we are not monitoring the LTAC environment, we are, but frankly, we think it's a little early to be judging whether or not this is going to present huge upside for the LTAC segment. The biggest concern in our mind is the fact that the non-compliant patients will be paid at the lower of the IPPS or cost. So the best case is they get paid at cost, which means there's no margin on those patients, the worst case is that the acute care rate is less than cost, in which case if the costs aren't mitigated, the LTAC provider will be losing money on those.

So I think there are going to be some winners and some losers, as we would expect. And so, our position is it's a very attractive, very – a highly needed service, but it's one that requires a little more monitoring to see how this transition is going to play out.

Operator: Our next question comes from the line of Sheryl Skolnick of CRT Capital.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Good morning. Thank you very much. I know you can't comment terribly much about the situation with the OIG and the subpoenas, but I'm wondering if you could update us on your levels of compliance with the 60% rule as you have done in the past, and your thoughts around the process that you've gone through to ensure that you have compliance with the updated parameters in 2009 and any other descriptions of your current operations and posture with respect to the lower-acuity patients specifically targeted in those admission criteria or excluded from those admission criteria, if you [inaudible] …

<A – Jay Grinney – HealthSouth Corp.>: Okay, you faded a little bit at the end, Sheryl, but I think I caught the question. I'll take the last part of the question first, and then I'll ask Mark to respond to where we are with respect to overall compliance.

But I think as everybody knows, all of us who operate in the healthcare environment are subject to a lot of regulations, many of which come out with certain rules and regulations associated with it. It requires a fair amount of analysis to understand exactly what the new rules mean, then establishing training material, utilizing outside parties when necessary, going to CMS for clarification when necessary, and then attempting to get those new regulations out across the entire portfolio.

I think we've done a pretty good job with that. We feel very confident that we are on top of the regulations at the proposed stage. We're on top of it once they are actually promulgated. We pay a lot of attention to that, and want to make sure that those rules and regulations are complied with. And we put training materials together, we have onsite training, we have online training, and we really try to do the very best we can to ensure compliance.

Terms of our overall 60% compliance, I'm going to ask Mark to address that.

<A – Mark Tarr – HealthSouth Corp.>: Yeah, Sheryl, our overall compliance of the company is 76%. That is, as you can imagine, a number that we monitor very closely at each individual hospital to make sure that each hospital is in full compliance with the 60% guidelines. And to the extent that a hospital gets closer to the 60%, then they will closely monitor those patients coming in and make sure that we had a higher percentage of compliant cases to make sure that we have a little bit of a buffer there.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Can you just clarify on that – the 76% overall, meaning that overall for the company as a whole, you're at 76% versus the 60% total rate, or does it mean that 76% of your facilities are compliant with the 60%?

<A – Mark Tarr – HealthSouth Corp.>: That's 76% overall on the compliance percentage.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Okay.

<A – Mark Tarr – HealthSouth Corp.>: All-in.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Okay. That's great. Thank you very much. And...

<A – Jay Grinney – HealthSouth Corp.>: Sheryl?

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Yeah. Oh, and I just wanted to say thank you for releasing that disclosure as soon as you got it. That's really a best practice, and it's very much appreciated.

<A – Jay Grinney – HealthSouth Corp.>: You're welcome. Sorry that it was on a Friday, but we got it on Friday. So wanted to make sure that today, we want to make sure that everybody saw that.

<Q – Sheryl Skolnick – CRT Capital Group LLC>: Thank you.

Operator: Our next question comes from the line of Frank Morgan of RBC Capital Markets.

<Q – Frank Morgan – RBC Capital Markets LLC>: Good morning.

<A – Jay Grinney – HealthSouth Corp.>: Morning.

<Q – Frank Morgan – RBC Capital Markets LLC>: Hey, within your guidance on the volume side, 2.5% to 3.5%, how much of that would you say is implied to be same-store?

<A – Jay Grinney – HealthSouth Corp.>: You know, we haven't broken that out, but historically there's been a roughly 40%/60%, somewhere in that range of new store and same-store, but that fluctuates, Frank. And that – so it's very hard for us to precisely say every single quarter same-store is going to X percent, and new store is going to Y percent. As you know, when we bring on new hospitals, and for instance this year, we're going to be bringing on new hospitals, three new hospitals in the fourth quarter. Well, clearly, that will have a disproportionate impact on overall discharge growth as we go into 2015, and there will be a disproportionate impact on new stores.

Now, similarly, in years gone by, we've added hospitals more spread out throughout the year, and so the impact is a little bit less. But if you think about it historically, and again, we provide this information in the Investor Reference Book on page 12. If you look at it overall, you can see there's a lot of variation in the new store. A new store can be as low as 0.4%, it can be as high as 2.5% or 2.8%, and same-store can be as low as 0.6% as it was in Q3 of 2010, as high as 5% in Q1 of 2012. So I think if you could look at the page 12 in our Investor Reference Book, you'll see that it's very hard to say with any certainty – or I should not certainty, with any precision in some sort of formulaic way if you look at our overall growth, it will consist of X percent same-store and Y percent new store. There's a lot of variability in those numbers.

<Q – Frank Morgan – RBC Capital Markets LLC>: I got you. Thanks. And in terms of just – as far as a generalization though, understanding that you're having, you know, you're coming up against difficult comps, 2.5% to 3%, would you say that's a good, kind of normalized sustainable run rate on the company, and then – or is there anything else that you're seeing out there, either new capacity coming online, new competitor, any other shift that you're seeing that might influence volume, or do you think this 2.5% to 3.5% is a good long-term number that we should model off of? Thanks.

<A – Jay Grinney – HealthSouth Corp.>: We – yeah, we think that that's a good long-term number that you can model off of for the planning horizon that we outlined in our business outlook which is found on page 22 of the supplemental slides and would take us out through 2016.

<Q – Frank Morgan – RBC Capital Markets LLC>: Okay. Thanks.

<A – Jay Grinney – HealthSouth Corp.>: Um-hmm.

Operator: Our next question comes from Josh Raskin of Barclays.

<Q – Josh Raskin – Barclays Capital, Inc.>: and Jack Meehan as well. So, first question just, you know, the update on the guidance moving towards the high end, understand there was a couple million dollar gain, I think the $2 million, but my guess is weather was probably $1.5 million to $2 million as well. So maybe what's driving the comfort towards the higher end of the range relative to what you guys knew a little more than two months ago?

<A – Jay Grinney – HealthSouth Corp.>: You know, it's just the fact that we're two and a half months down the road. And even though we did see the disruption to discharges in Q1 as a result of the winter storms, as I mentioned, we're feeling pretty good about the discharge growth in April. It's only one month out of the quarter, but we're back on track and so we feel that now we have a little more visibility, little more confidence in the overall numbers, and feel that guiding to the high-end is the appropriate thing to do.

<Q>: Got you. And hi, guys, it's Jack. I just want to follow-up operationally with the weather. How does that directly affect the business? Is it more on the admission side bringing people in because you're downstream from acute care providers, or is it more, you know, of a length of stay issue, you can't necessarily discharge someone with the weather. I'd imagine that the acuity, just the type of population that you're seeing, that's not going to change much, you're going to still obviously have the same sort of traumatic injuries each quarter, right?

<A – Jay Grinney – HealthSouth Corp.>: Yeah, let me begin, and then I'm going to ask Mark to give you a little more color commentary. I mean, the easiest way to think about this, because this was the way it happened, is these storms literally locked down the communities that they hit. It made getting out on the roads virtually impossible. So in those communities, in the markets that were hit by these storms, and as I think all of us know, there were multiple storms, sometimes days apart. During the build up to and certainly during those storms, these communities shut down. Roads were closed, people couldn't get in or out of their homes, they couldn't get in or out of hospitals, be it acute cares and going in terms of admissions, acute cares in terms of discharges. We couldn't get our liaisons to the acute care hospitals and we couldn't get patients into our hospitals. There were facilities that had to keep patients longer than we would have otherwise wanted to or certainly longer than the patients would have wanted to. So, the impact was multifaceted. There wasn't any just one specific thing that happened, but what we did see was that it occurred in those hospitals, those markets that I mentioned, multiple times, particularly in late January and into February.

<A – Mark Tarr – HealthSouth Corp.>: Yeah, this is Mark. Operationally, the biggest challenge is just getting the patients in. We can have a referral from the acute care hospital, but then the storm hits, and then having the ability to actually move the patient from the acute care hospital into our hospital is where the challenges really came into play. And as Jay alluded, it shuts down the entire marketplace, so we couldn't discharge patients out, although we didn't see a huge increase in our overall length of stay for the company as a whole, in those hospitals impacted, there was a bit of an impact there. But the greatest challenge is just getting patients into the hospital and get that conversion, we call it, from the point of having a patient referral to the point of a patient admission.

<Q>: Got it. Okay, thanks, guys.

Operator: Our next question comes from Darren Lehrich of Deutsche Bank.

<Q – Darren Lehrich – Deutsche Bank Securities, Inc.>: Thanks. Good morning, everybody.

<A – Jay Grinney – HealthSouth Corp.>: Good morning.

<Q – Darren Lehrich – Deutsche Bank Securities, Inc.>: I just wanted to ask a little bit more about the Mountain States JV, and just the overall JV opportunity. It looks like based on your comments this was a freestanding facility, and I guess I'd be curious just to get your thoughts on the end market and the overall market opportunity for hospitals that own these kinds of freestanding IRFs, or if this is something different that you'll be converting it to that. And then, just more broadly, get your thoughts on other JVs with hospital-based units of IRFs. So, I'm just interested in your commentary on the JV potential here.

<A – Jay Grinney – HealthSouth Corp.>: I'm going to ask Mark in a minute to comment on the Mountain States opportunity, which we do think is a terrific opportunity for us to partner with an outstanding organization and to enhance the overall rehabilitative services in that market.

To answer the broader question, we do see that there are increased opportunities to joint venture with acute care hospitals that are providing rehab services today. Some of those services offered by the acute care hospitals are in the form of free-standing hospitals, like Quillen. Most, however, are services that are offered in an HIH. What we are seeing is that many acute care hospitals are acknowledging that in today's reimbursement environment of reduced Medicare, Medicaid and commercial payments, it's hard for them to offer a consistently high quality level of rehab services and at the same time meet all of their medical, surgical and core business needs. Accordingly, we're seeing more inquiries and more responses to our inquiries about joint venturing those services to provide the full continuum of care but now doing it on a partnership basis. And so as I mentioned in my comments, we were very pleased to announce this joint venture, and we are looking forward to announcing additional additions to our portfolio in the balance of the year.

<A – Mark Tarr – HealthSouth Corp.>: Yeah, Darren, it's Mark. We're very excited about the Quillen opportunity. That particular hospital, the building itself was built to be a free-standing rehab hospital. Over the years, it has had a couple different transitions. It currently houses both inpatient rehab hospital beds as well as SNF beds. The long-term prognosis is to continue to grow the rehab and the SNF beds will be transferred out. But needless to say, we're very excited about working with the team there, working with Mountain States, and continuing to grow in that marketplace.

<Q – Darren Lehrich – Deutsche Bank Securities, Inc.>: That's great. And then if I could just – I wanted to follow-up, Jay, you'd made mention of just the rulemaking process, and I'd be curious to know with the rules coming out soon, is there any expectations for the upcoming PPS rulemaking, anything that we should be on the lookout for that's been different this year? Thanks.

<A – Jay Grinney – HealthSouth Corp.>: Darren, we are not hearing anything about the proposed rule. We're not hearing anything positive, we're not hearing anything negative. So, we're not expecting anything that would be coming from left field, but we're going to be waiting expectedly just like everybody else is to get the proposed rule probably sometime in May.

<Q – Darren Lehrich – Deutsche Bank Securities, Inc.>: Got it. Thank you very much.

Operator: Our next question comes from Rob Mains of Stifel.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: Thanks. Good morning.

<A – Jay Grinney – HealthSouth Corp.>: Good morning.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: A question on the outpatient. I know we're talking 6% of revenues, you went over that there are 10 fewer clinics than last year. Was there a decline from the fourth quarter to the first quarter? Or is some of that decline also weather-related?

<A – Jay Grinney – HealthSouth Corp.>: Well, the weather-related hit in this first quarter, for sure. I mean, that was not something we put a number on Rob, but it was, it certainly impacted a significant number of – our outpatient business itself is located in those states, of which Pennsylvania is one of the higher states that we definitely saw an impact there.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: Okay. Fair enough. And then kind of a follow-up to Darren's question. We've got the latest Medicare imbroglio behind us. In your mind, what are the kind of legislative priorities that you're looking at both for HealthSouth and for the industry?

<A – Jay Grinney – HealthSouth Corp.>: You know, the legislative priorities really are the sustainable growth rate in 2015 and the debt ceiling debate that will go along with that. Our assessment is that legislatively, there's not going to be anything else occurring in 2014 because everybody's focus is on the midterm elections and each party wants to enhance their position in both the House and the Senate in terms of the number of Representatives and Senators that they have. So the next real priority is going to be what happens to the SGR in Q1 of 2015, and how does that fit within the overall debate of the debt ceiling? That – those, I should say, will be informed by what kind of – what the House and the Senate looks like in terms of leadership, which will be dictated by the midterms.

So that's the next sort of marker for us, and right now, we're just – when we go to Washington and we meet with members, we are trying to underscore the value proposition that inpatient rehabilitation services offers to their constituents, primarily the Medicare constituents, and that we're very pleased that that message is very well received. I think the members who represent our hospitals, many of whom come to our hospitals, they visit our hospitals, they see the services that we provide, they see the value that we're offering to the patients who need and deserve inpatient rehabilitative care, and so they get that we're an important part of the continuum.

But to answer your question, again, I think the next real milestone legislatively will be next year with SGR and debt ceiling.

<Q – Rob Mains – Stifel, Nicolaus & Co., Inc.>: Great. Thank you.

Operator: Our next question comes from Chris Rigg of Susquehanna Financial.

<Q – Chris Rigg – Susquehanna Financial Group LLLP>: Thanks for taking my questions. Just was hoping to get a quick refresher on the NOLs and whether there's been any change quarter-to-quarter here. I know sometimes that changes at year-end and whether – just update us on the timing as to when you think you'll be a full cash tax payer again. Thanks a lot.

<A – Doug Coltharp – HealthSouth Corp.>: It's Doug. And obviously the NOL does change from quarter-to-quarter as we're utilizing that to offset what otherwise would be the federal taxes due on our earnings. So, we've included in the supplemental slides on page – let's see. I've got it right here...

<Q – Chris Rigg – Susquehanna Financial Group LLLP>: 18?

<A – Doug Coltharp – HealthSouth Corp.>: On 18, what the balance was at the end of the first quarter, and that was at $866 million. Again, you can then utilize the effective tax rate assumption of roughly 40%, and then that will give you a sense as to how long we'll continue to have the benefit of those NOLs. And as we've stated here on page 18 as well, for the near-term, we continue to estimate that our annual cash taxes will be in that $10 million to $15 million range.

<Q – Chris Rigg – Susquehanna Financial Group LLLP>: Okay. And then just one other question. I know you can't say a lot about the DOJ investigations, but I just want to make sure I understand exactly what happened here, and it may just be legalese nuances, but it was OIG HHS for a number of quarters in your disclosures, and then in the 10-Q, it changed to the DOJ. In the disclosures from last week, the DOJ was in there. Has the DOJ always been involved, or did they get inserted into the process at some later date?

<A – John Whittington – HealthSouth Corp.>: Good morning, this is John Whittington. They've always been involved, and we've always disclosed their involvement from the beginning.

<Q – Chris Rigg – Susquehanna Financial Group LLLP>: Okay. It just looked like it's – in the 10-Ks and other it always said OIG HHS, and then the DOJ came into the disclosures later. But we can follow up offline. Thanks.

<A – John Whittington – HealthSouth Corp.>: They represent the government. They represent the healthcare administration.

<A – Jay Grinney – HealthSouth Corp.>: Yeah, it's always been in there.

<Q – Chris Rigg – Susquehanna Financial Group LLLP>: Okay.

<A – Jay Grinney – HealthSouth Corp.>: And Chris, what we'll do is we'll send the excerpts from the Qs and the 8-Ks to you just so you can confirm that.

<Q – Chris Rigg – Susquehanna Financial Group LLLP>: Thank you.

Operator: Our next question comes from the line of A.J. Rice from UBS.

<Q – A.J. Rice – UBS Securities LLC>: Hello, everybody.

<A – Jay Grinney – HealthSouth Corp.>: Good morning.

<Q – A.J. Rice – UBS Securities LLC>: Two quick questions. First of all, maybe just – is there any further color on what you're seeing with respect to your labor, particularly your therapists? I know you said EPOB was flat year-to-year, but how about turnover rates, availability of people? Has it tightened at all with the economy getting a little better, or not really?

<A – Jay Grinney – HealthSouth Corp.>: The answer is not really. We are very pleased with our ability to recruit and importantly, retain really top talent both in the nursing side as well as the therapy side, and our turnover in the therapy area has remained consistently in the single-digits for as long as I've been here. I mean, it's really been one of the things that I think makes this company unique, and we haven't seen any volatility in that.

On the nursing side, we also have very good retention rates, and part of that has been a push to ensure that as many of our registered nurses as possible seek and apply to become certified as a rehabilitation RN, and that's been a very successful program for us.

<Q – A.J. Rice – UBS Securities LLC>: Okay. And then the other follow-up, I guess, would be to – I think last quarter, you guys mentioned that you were sort of waiting to see how the doc fix shook out and so forth maybe with respect to the pace of share buybacks, and obviously you bought some in the first quarter. Do you see that now that we have some clarity around the Washington scene at least until next spring, do you see an acceleration in your pace on share repurchases? Any commentary along there would be helpful.

<A – Doug Coltharp – HealthSouth Corp.>: A.J., it's Doug. Obviously, we continue to have capacity for further share repurchases both in terms of the authorization that is in place from our board of directors and in terms of our balance sheet capacity, and specifically the amount of availability that we have under our revolving credit facility. And as we have stated I think pretty consistently here over the course of the last two years, shareholder distributions both in the form of the dividends that we're paying on our common stock and incremental share repurchases are going to continue to be an important component of our business model.

<Q – A.J. Rice – UBS Securities LLC>: Okay. Thanks a lot.

Operator: Our next question comes from the line of Gary Lieberman of Wells Fargo.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Good morning. Thanks for taking my question.

<A – Jay Grinney – HealthSouth Corp.>: Good morning.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Just a follow-up on your conversations that you had in DC. Did the idea or the concept of site-neutral payments come up when you're having your discussions, and sort of where are we on that front?

<A – Jay Grinney – HealthSouth Corp.>: They have not come up on a regular basis. They do come up from time-to-time. I think as most everybody knows, there was a bipartisan, bicameral discussion draft, if you will, that was issued earlier this year, the IMPACT Act, and that was to – really, it was an effort by the Finance Committee on the Senate side, Ways and Means on House side, to begin looking at post-acute payment reform and some options that might be part of that. Site-neutral payments would be included in that construct, but if you go in and you analyze what was said, basically, the conclusion was this is very complicated, there are a lot of additional steps that need to be followed, there needs to be the adoption of a common patient assessment tool. And in the IMPACT's outline, the draft bill's outline, the work that it would have to be done on this occurs from now until I think 2020 or 2022.

So, does it get some attention? Yes. Is it acknowledged that it is a very complicated transition to make? Yes. Are there any proposals that have been put on the table that say these would be the services or the CMGs that would be paid on a site-neutral vis-à-vis the services that – or CMGs that would not be? And the answer is no.

So I think it's very much in its infancy. But it's certainly a concept that's out there. And as we've said in the past, we don't necessarily believe that moving to site-neutral would be negative for HealthSouth because presumably in that calculation of what that site-neutral payment would be, especially if the comparison is between a rehabilitation payment and a nursing home payment, factors beyond just what is the per day payment would be included, and those factors would include items such as length of stay, return rates or readmission rates to acute care hospitals, and more importantly, outcomes. So, it is something that gets talked about. It's not something that is ready for prime time in our space. And as I've said, we're not looking at it as necessarily a big negative. It could be a real positive for us.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Okay. And then as a follow-up. You had said that you were expecting the subpoenas that you received that you announced on Friday. Are there any other subpoenas that you're anticipating regarding the investigation?

<A – John Whittington – HealthSouth Corp.>: Again, this is John Whittington. At this time, we don't have any reason to expect any additional subpoenas, but as you know, the government is free to investigate in the way it deems appropriate. But right now, we're not aware of any reason to expect new subpoenas, but I wouldn't rule anything out.

<Q – Gary Lieberman – Wells Fargo Securities LLC>: Okay. Great. Thanks very much.

Operator: Thank you. Our final question comes from the line of Kevin Fischbeck of Bank of America.

<Q – Steve Baxter – Bank of America Merrill Lynch>: Hey, this is Steve Baxter on for Kevin. Just a question on the payor mix. Fee-for-service Medicare continues to tick up, and managed care, which includes Medicare Advantage, continues to trend down a little bit. Given the growth in the MA program and the improving economy and the potential impact on commercial, that seems little bit surprising to me. So any color you could give, you know, is this volume dynamic or is there something going on with pricing on the managed care side that we should be thinking about. Any kind of update would be great. Thanks.

<A – Jay Grinney – HealthSouth Corp.>: Yeah, sure. So if you look at Q1 of 2013 versus Q1 of 2014, there was about a 1.8% decline in the number of Medicare Advantage discharges treated in our hospitals. And maybe that's kind of the number that you're focusing on. If you break that down, however, there are two buckets underneath managed Medicare. One would be the traditional fee-for-service payment, the other would be on a contracted where we go out and we negotiate with an MA plan to be an inpatient rehabilitation provider. The fee-for-service is a very small component of the overall Medicare Advantage numbers, but that bucket has actually gone down 29% year-over-year. Now, it's a small number to begin with, so we went from 375 discharges down to 265 discharges. On the other hand, the contracted bucket actually went up 2.5%.

<Q – Steve Baxter – Bank of America Merrill Lynch>: I appreciate the color.

Operator: And thank you. That was our final question. I will now turn the floor back over to Mary Ann Arico for any additional or closing remarks.

Mary Ann Arico, Chief Investor Relations Officer

Thank you. As a reminder, we will be filing the updated Investor Reference Book next week. If you have additional questions, I'll be available later today. You can reach me at 205-969-6175. Thank you.

Jay Grinney, President and Chief Executive Officer

Thanks everyone.

Operator: Thank you. This concludes today's HealthSouth first quarter 2014 earnings conference call. You may now disconnect, and have a wonderful day.

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