

CORVEL CORP  
Form 10-Q  
August 05, 2013  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
WASHINGTON, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2013

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 0-19291

**CORVEL CORPORATION**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**33-0282651**  
(IRS Employer  
Identification No.)

**2010 Main Street, Suite 600**

**Irvine, CA**  
(Address of principal executive office)

**92614**  
(zip code)

**Registrant's telephone number, including area code: (949) 851-1473**

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, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (check one)

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

The number of shares outstanding of the registrant's Common Stock, \$0.0001 par value per share, as of July 24, 2013 was 21,178,834.

**Table of Contents**

**CORVEL CORPORATION**

**FORM 10-Q**

**TABLE OF CONTENTS**

	Page
<b><u>PART I FINANCIAL INFORMATION</u></b>	
<b>Item 1. <u>Financial Statements</u></b>	
<u>Consolidated Balance Sheets – March 31, 2013 and June 30, 2013 (unaudited)</u>	3
<u>Consolidated Income Statements (unaudited) – Three months ended June 30, 2012 and 2013</u>	4
<u>Consolidated Statements of Cash Flows (unaudited) – Three months ended June 30, 2012 and 2013</u>	5
<u>Notes to Consolidated Financial Statements – June 30, 2013</u>	6
<b>Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u></b>	15
<b>Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u></b>	24
<b>Item 4. <u>Controls and Procedures</u></b>	25
<b><u>PART II. OTHER INFORMATION</u></b>	
<b>Item 1. <u>Legal Proceedings</u></b>	25
<b>Item 1A. <u>Risk Factors</u></b>	25
<b>Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u></b>	33
<b>Item 3. <u>Defaults Upon Senior Securities</u></b>	33
<b>Item 4. <u>Mine Safety Disclosures</u></b>	33
<b>Item 5. <u>Other Information</u></b>	33
<b>Item 6. <u>Exhibits</u></b>	34
<u>Signatures</u>	35

**Table of Contents**

## Part I Financial Information

## Item 1. Financial Statements

**CORVEL CORPORATION****CONSOLIDATED BALANCE SHEETS**

	March 31, 2013	June 30, 2013 (Unaudited)
<b>Assets</b>		
Current Assets		
Cash and cash equivalents (Note A)	\$ 19,822,000	\$ 25,034,000
Customer deposits	10,107,000	11,327,000
Accounts receivable, net	49,105,000	50,758,000
Prepaid taxes and expenses	7,418,000	4,539,000
Deferred income taxes	6,448,000	6,610,000
Total current assets	92,900,000	98,268,000
Property and equipment, net	46,584,000	50,509,000
Goodwill	36,814,000	36,814,000
Other intangibles, net (Note F)	5,663,000	5,545,000
Other assets	421,000	247,000
<b>TOTAL ASSETS</b>	<b>\$ 182,382,000</b>	<b>\$ 191,383,000</b>
<b>Liabilities and Stockholders Equity</b>		
Current Liabilities		
Accounts and taxes payable	\$ 13,587,000	\$ 19,510,000
Accrued liabilities	39,168,000	39,336,000
Total current liabilities	52,755,000	58,846,000
Deferred income taxes	18,225,000	18,225,000
Commitments and contingencies (Notes G and H)		
Stockholders Equity		
Common stock, \$.0001 par value: 120,000,000 shares authorized at March 31, 2013 and June 30, 2013; 52,837,262 shares issued (21,520,248 shares outstanding, net of Treasury shares) and 52,901,438 shares issued (21,298,885 shares outstanding, net of Treasury shares) at March 31, 2013 and June 30, 2013, respectively	3,000	3,000
Paid-in capital	110,924,000	112,533,000
Treasury Stock (31,317,014 shares at March 31, 2013 and 31,602,553 shares at June 30, 2013)	(301,301,000)	(308,609,000)
Retained earnings	301,776,000	310,385,000
Total stockholders equity	111,402,000	114,312,000
<b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	<b>\$ 182,382,000</b>	<b>\$ 191,383,000</b>

See accompanying notes to consolidated financial statements.



**Table of Contents****CORVEL CORPORATION****CONSOLIDATED INCOME STATEMENTS    UNAUDITED**

	Three Months Ended June 30,	
	2012	2013
<b>REVENUES</b>	<b>\$ 104,606,000</b>	<b>\$ 118,113,000</b>
Cost of revenues	81,425,000	91,195,000
<b>Gross profit</b>	<b>23,181,000</b>	<b>26,918,000</b>
General and administrative expenses	12,174,000	12,842,000
<b>Income before income tax provision</b>	<b>11,007,000</b>	<b>14,076,000</b>
Income tax provision	4,411,000	5,467,000
<b>NET INCOME</b>	<b>\$ 6,596,000</b>	<b>\$ 8,609,000</b>
Net income per common and common equivalent share		
Basic	\$ 0.29	\$ 0.40
Diluted	\$ 0.29	\$ 0.40
Weighted average common and common equivalent shares		
Basic	22,626,000	21,396,000
Diluted	22,852,000	21,584,000

See accompanying notes to consolidated financial statements.

**Table of Contents****CORVEL CORPORATION****CONSOLIDATED STATEMENTS OF CASH FLOWS UNAUDITED**

	Three Months Ended June 30,	
	2012	2013
<b><i>Cash flows from Operating Activities</i></b>		
<b>NET INCOME</b>	\$ 6,596,000	\$ 8,609,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,359,000	4,012,000
Loss on disposal of assets	8,000	1,000
Stock compensation expense	297,000	405,000
Write-off of uncollectible accounts	438,000	320,000
Deferred income tax	(120,000)	(162,000)
Changes in operating assets and liabilities		
Accounts receivable	2,565,000	(1,973,000)
Customer deposits	(986,000)	(1,220,000)
Prepaid taxes and expenses	3,244,000	2,879,000
Other assets	137,000	174,000
Accounts and taxes payable	(1,725,000)	3,580,000
Accrued liabilities	(1,347,000)	168,000
Net cash provided by operating activities	13,466,000	16,793,000
<b><i>Cash Flows from Investing Activities</i></b>		
Purchase of property and equipment	(3,404,000)	(5,477,000)
Net cash (used in) investing activities	(3,404,000)	(5,477,000)
<b><i>Cash Flows from Financing Activities</i></b>		
Purchase of treasury stock	(3,673,000)	(7,308,000)
Tax effect of stock option exercises	489,000	337,000
Exercise of common stock options	1,093,000	867,000
Net cash (used in) financing activities	(2,091,000)	(6,104,000)
<b><i>Increase (decrease) in cash and cash equivalents</i></b>	<b>7,971,000</b>	<b>5,212,000</b>
Cash and cash equivalents at beginning of period	6,597,000	19,822,000
Cash and cash equivalents at end of period	\$ 14,568,000	\$ 25,034,000
<b>Supplemental Cash Flow Information:</b>		
Income taxes paid	\$ 110,000	\$ 300,000
Purchase of software license under finance agreement	\$	\$ 2,343,000
See accompanying notes to consolidated financial statements.		

**Table of Contents**

**CORVEL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2013**

**Note A Basis of Presentation and Summary of Significant Accounting Policies**

The unaudited financial statements herein have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission. The accompanying interim financial statements have been prepared under the presumption that users of the interim financial information have either read or have access to the audited financial statements for the latest fiscal year ended March 31, 2013. Accordingly, footnote disclosures which would substantially duplicate the disclosures contained in the March 31, 2013 audited financial statements have been omitted from these interim financial statements.

The Company evaluated all subsequent events or transactions through the date of filing this report. During the period subsequent to June 30, 2013, the Company repurchased 125,293 shares for \$3,882,000 for an average of \$30.98 per share. These shares were repurchased under the Company's ongoing share repurchase program described in Note C.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the three months ended June 30, 2013 are not necessarily indicative of the results that may be expected for the fiscal year ending March 31, 2014. For further information, refer to the consolidated financial statements and footnotes for the fiscal year ended March 31, 2013 included in the Company's Annual Report on Form 10-K.

*Basis of Presentation:* The consolidated financial statements include the accounts of CorVel and its subsidiaries. Significant intercompany accounts and transactions have been eliminated in consolidation.

*Use of Estimates:* The preparation of financial statements in compliance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the accompanying financial statements. Actual results could differ from those estimates. Significant estimates include the values assigned to intangible assets, capitalized software development, the allowance for doubtful accounts, accrual for income taxes, share-based payments related to performance based awards, loss contingencies, estimated claims for claims administration revenue recognition, estimates used in stock options valuations, and accrual for self-insurance reserves.

*Cash and Cash Equivalents:* Cash and cash equivalents consist of short-term highly-liquid investment-grade interest-bearing securities with maturities of 90 days or less when purchased. The carrying amounts of the Company's financial instruments approximate their fair values at March 31, 2013 and June 30, 2013.

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**Table of Contents**

**CORVEL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2013**

**Note A Basis of Presentation and Summary of Significant Accounting Policies (continued)**

*Fair Value of Financial Instruments:* The Company applies Accounting Standards Codification ( ASC ) 820, Fair Value Measurements and Disclosures, which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements with respect to fair value measurements of (a) nonfinancial assets and liabilities that are recognized or disclosed at fair value in the Company's Consolidated Financial Statements on a recurring basis (at least annually) and (b) all financial assets and liabilities. ASC 820 prioritizes the inputs used in measuring fair value into the following hierarchy:

Level 1 Quoted market prices in active markets for identical assets or liabilities;

Level 2 Observable inputs other than those included in Level 1 (for example, quoted prices for similar assets in active markets or quoted prices for identical assets in inactive markets); and

Level 3 Unobservable inputs reflecting management's own assumptions about the inputs used in estimating the value of the asset.

The carrying amount of the Company's financial instruments (i.e. cash, accounts receivable, accounts payable, etc.) are all Level 1 and approximate their fair values at March 31, 2013 and June 30, 2013. The Company has no Level 2 or Level 3 assets.

*Goodwill:* The Company accounts for its business combinations in accordance with the Financial Accounting Standards Board ( FASB ) ASC 805-10 through ASC 805-50 Business Combinations, which requires that the purchase method of accounting be applied to all business combinations and addresses the criteria for initial recognition of intangible assets and goodwill. In accordance with FASB ASC 350-10 through ASC 350-30, goodwill and other intangible assets with indefinite lives are not amortized but are tested for impairment annually, or more frequently if circumstances indicate the possibility of impairment. If the carrying value of goodwill or an intangible asset exceeds its fair value, an impairment loss shall be recognized.

*Revenue Recognition:* The Company recognizes revenue when there is persuasive evidence of an arrangement, the services have been provided to the customer, the sales price is fixed or determinable, and collectability is reasonably assured. For the Company's services, as the Company's professional staff performs work, they are contractually permitted to bill for fees earned in fraction of an hour increments worked or by units of production. The Company recognizes revenue as the time is worked or as units of production are completed, which is when the revenue is earned and realized. Labor costs are recognized as the costs are incurred. The Company derives its revenue from the sale of Network Solutions and Patient Management services. Network Solutions and Patient Management services may be sold individually or combined. When a sale combines multiple elements, the Company accounts for multiple element arrangements in accordance with the guidance included in ASC 605-25.

Management evaluates agreements with customers in accordance with the provision of the revenue recognition topic ASC 605 that addresses multiple-deliverable revenue arrangements. The multiple-deliverable arrangements entered into consist of bundled managed care which included various units of accounting such as network solutions, and patient management which includes claims administration. Such elements are considered separate units of accounting due to each element having value to the customer on a stand-alone basis. The selling price for each unit of accounting is determined using contract price and management estimates. When the Company's customers purchase several products the pricing of the products sold is generally the same as if the products were sold on an individual basis. Revenue is recognized as the work is performed in accordance with the Company's customer contracts. Based upon the nature of the Company's products, bundled managed care elements are generally delivered in the same accounting period. The Company recognizes revenue for patient management claims administration services over the life of the customer contract. The Company estimates, based upon prior experience in managing claims, the deferral amount from when the claim is received to when the customer contract expires.



**Table of Contents**

**CORVEL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2013**

**Note A Basis of Presentation and Summary of Significant Accounting Policies (continued)**

*Recent Accounting Pronouncements:* In July 2012, the FASB issued guidance that revises the requirements regarding how entities test indefinite-lived intangible assets, other than goodwill, for impairment. The guidance allows companies to perform a qualitative assessment before calculating the fair value of the reporting unit. If entities determine, on the basis of qualitative factors, that the fair value of the indefinite-lived intangible asset is more likely than not greater than the carrying amount, a quantitative calculation would not be needed. The guidance became effective for the Company at the beginning of its first quarter of fiscal 2014. The adoption of this guidance did not have a material impact on the Company's financial statements.

*Accounts Receivable:* The majority of the Company's accounts receivable are due from companies in the property and casualty insurance industries, self-insured employers, and government entities. Accounts receivable are generally due within 30 days and are stated as amounts due from customers net of an allowance for doubtful accounts. Those accounts outstanding longer than the contractual payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company and the condition of the general economy and the industry as a whole. No one customer accounted for 10% or more of accounts receivable at either March 31, 2013 or June 30, 2013. No one customer accounted for 10% or more of revenue during the three months ended June 30, 2012 or 2013.

*Property and Equipment:* Additions to property and equipment are recorded at cost. Depreciation and amortization are provided using the straight-line method over the estimated useful lives of the related assets, which range from one to seven years. The Company accounts for internally developed software costs in accordance with FASB ASC 350-40, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use, which allows for the capitalization of software developed for internal use. These costs are included in computer software in property and equipment and are amortized over a period of five years.

*Long-Lived Assets:* The carrying amount of all long-lived assets is evaluated periodically to determine if adjustment to the depreciation and amortization period or to the unamortized balance is warranted. Such evaluation is based principally on the expected utilization of the long-lived assets and the projected, undiscounted cash flows of the operations in which the long-lived assets are deployed.

*Income Taxes:* The Company provides for income taxes in accordance with provisions specified in ASC 740, Accounting for Income Taxes. Accordingly, deferred income tax assets and liabilities are computed for differences between the financial statement and tax bases of assets and liabilities. These differences will result in taxable or deductible amounts in the future, based on tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which temporary differences become deductible. In making an assessment regarding the probability of realizing a benefit from these deductible differences, management considers the Company's current and past performance, the market environment in which the Company operates, tax-planning strategies and the length of carry-forward periods for loss carry-forwards, if any. Valuation allowances are established when necessary to reduce deferred tax assets to amounts that are more likely than not to be realized. Further, the Company provides for income tax issues not yet resolved with federal, state and local tax authorities. The balance of the unrecognized tax benefits as of March 31, 2013 and June 30, 2013 was \$772,000 and \$869,000, respectively.

**Table of Contents****CORVEL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****June 30, 2013****Note A Basis of Presentation and Summary of Significant Accounting Policies (continued)**

*Earnings Per Share:* Earnings per common share-basic is based on the weighted average number of common shares outstanding during the period. Earnings per common share-diluted is based on the weighted average number of common shares and common share equivalents outstanding during the period. In calculating earnings per share, earnings are the same for the basic and diluted calculations. Weighted average shares outstanding decreased in the June 2013 quarter compared to the same quarter of the prior year primarily due to repurchase of shares under the Company's share repurchase program. See also Note D.

*Stock Split:* During the quarter ended June 30, 2013, the Company's Board of Directors declared a two-for-one stock split in the form of a 100% stock dividend with a record date of June 12, 2013 and a distribution date of June 26, 2013. All prior period share and per share calculations in these financial statements and elsewhere in this report have been retroactively adjusted to reflect this split.

**Note B Stock Based Compensation and Stock Options**

Under the Company's Restated Omnibus Incentive Plan (formerly the Restated 1988 Executive Stock Option Plan) (the Plan) as in effect at June 30, 2013, options for up to 19,365,500 shares of the Company's common stock may be granted over the life of the Plan to key employees, non-employee directors and consultants at exercise prices not less than the fair market value of the stock at the date of grant. Options granted under the Plan are non-statutory stock options and generally vest 25% one year from date of grant and the remaining 75% vesting ratably each month for the next 36 months. The options granted to employees and the board of directors expire at the end of five years and ten years from date of grant, respectively.

The Company records compensation expense for employee stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes option-pricing model with the assumptions included in the table below. The Company uses historical data among other factors to estimate the expected volatility, the expected option life, and the expected forfeiture rate. The risk-free rate is based on the interest rate paid on a U.S. Treasury issue with a term similar to the estimated life of the option. Based upon the historical experience of options cancellations, the Company has estimated an annualized forfeiture rate of 11.70% and 12.84% for the three months ended June 30, 2012 and 2013, respectively. Forfeiture rates will be adjusted over the requisite service period when actual forfeitures differ, or are expected to differ, from the estimate. The following assumptions were used to estimate the fair value of options granted during the three months ended June 30, 2012 and 2013 using the Black-Scholes option-pricing model:

	Three Months Ended June 30,	
	2012	2013
Risk-free interest rate	0.62%	0.66%
Expected volatility	47%	47%
Expected dividend yield	0.00%	0.00%
Expected forfeiture rate		