

RENAL CARE GROUP INC

Form 10-Q

May 04, 2005

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

**FORM 10-Q**

(Mark One)

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

**For the Quarterly Period Ended March 31, 2005**

**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 No. 0-27640**

**RENAL CARE GROUP, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**62-1622383**

(I.R.S. Employer Identification No.)

**2525 West End Avenue, Suite 600, Nashville, Tennessee 37203**

(Address of principal executive offices) (Zip code)

**Registrant's telephone number, including area code: (615) 345-5500**

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 is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes  No

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

Class	Outstanding at April 29, 2005
Common Stock, \$.01 par value	67,997,913

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**Table of Contents****PART I FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS****RENAL CARE GROUP, INC.****Condensed Consolidated Balance Sheets  
(in thousands, except per share data)**

	<b>December 31, 2004</b>	<b>March 31, 2005 (unaudited)</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 17,931	\$ 12,900
Accounts receivable, net	275,373	275,365
Inventories	23,359	25,771
Prepaid expenses and other current assets	26,817	23,033
Deferred income taxes	29,604	33,435
Total current assets	373,084	370,504
Property, plant and equipment, net	316,532	332,361
Intangible assets, net	34,320	35,407
Goodwill	694,264	717,746
Other assets	10,780	10,371
Total assets	\$ 1,428,980	\$ 1,466,389
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 139,929	\$ 140,529
Due to third-party payors	80,007	88,061
Current portion of long-term debt	23,969	25,624
Total current liabilities	243,905	254,214
Long-term debt, net of current portion	479,645	474,909
Deferred income taxes	51,419	45,815
Other long-term liabilities	16,271	15,740
Minority interest	45,619	48,028
Total liabilities	836,859	838,706
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.01 par value, 10,000 shares authorized, none issued		
Common stock, \$0.01 par value, 150,000 shares authorized, 82,317 and 82,770 shares issued at December 31, 2004 and March 31, 2005, respectively	823	828
	(372,249)	(381,635)

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Treasury stock, 14,514 and 14,766 shares of common stock at December 31, 2004 and March 31, 2005, respectively

Additional paid-in capital	411,888	421,945
Retained earnings	551,863	585,495
Accumulated other comprehensive (loss) income, net of tax	(204)	1,050
Total stockholders' equity	592,121	627,683
Total liabilities and stockholders' equity	\$ 1,428,980	\$ 1,466,389

See accompanying notes to condensed consolidated financial statements.

**Table of Contents****RENAL CARE GROUP, INC.****Condensed Consolidated Income Statements**  
**(in thousands, except per share data)**  
**(unaudited)**

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2004</b>	<b>2005</b>
Net revenue	\$ 278,028	\$ 373,509
Operating costs and expenses:		
Patient care costs	179,372	246,579
General and administrative expenses	22,676	30,631
Provision for doubtful accounts	7,110	8,203
Depreciation and amortization	12,163	16,787
Total operating costs and expenses	221,321	302,200
Income from operations	56,707	71,309
Interest expense, net	965	7,261
Income before minority interest and income taxes	55,742	64,048
Minority interest	7,214	9,362
Income before income taxes	48,528	54,686
Provision for income taxes	18,441	21,054
Net income	\$ 30,087	\$ 33,632
Net income per share:		
Basic	\$ 0.44	\$ 0.50
Diluted	\$ 0.42	\$ 0.48
Weighted average shares outstanding:		
Basic	68,910	67,863
Diluted	71,223	70,361

See accompanying notes to condensed consolidated financial statements.

**Table of Contents****RENAL CARE GROUP, INC.****Condensed Consolidated Statements of Cash Flows**  
**(in thousands)**  
**(unaudited)**

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2004</b>	<b>2005</b>
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 30,087	\$ 33,632
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	12,163	16,787
Loss on sale of property and equipment	154	394
Distributions to minority shareholders	(3,561)	(8,077)
Income applicable to minority interest	7,214	9,362
Deferred income taxes		(1,257)
Changes in operating assets and liabilities, net of effects from acquisitions	(600)	14,289
Net cash provided by operating activities	45,457	65,130
<b>INVESTING ACTIVITIES</b>		
Purchases of property and equipment	(19,118)	(22,161)
Cash paid for acquisitions, net of cash acquired	(55,768)	(44,013)
Change in other assets	(3,173)	1,388
Net cash used in investing activities	(78,059)	(64,786)
<b>FINANCING ACTIVITIES</b>		
Net proceeds from issuance of long-term debt	120,000	
Payments on long-term debt		(4,063)
Net borrowings under line of credit and capital leases	25,921	982
Net proceeds from issuance of common stock	9,628	7,092
Repurchase of treasury shares	(135,636)	(9,386)
Net cash provided by (used in) financing activities	19,913	(5,375)
Decrease in cash and cash equivalents	(12,689)	(5,031)
Cash and cash equivalents at beginning of period	50,295	17,931
Cash and cash equivalents at end of period	\$ 37,606	\$ 12,900

See accompanying notes to condensed consolidated financial statements.

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**RENAL CARE GROUP, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**MARCH 31, 2005**

(dollars in thousands, except per share data)

(unaudited)

**1. Basis of Presentation**

**Overview**

Renal Care Group, Inc. (the Company) provides dialysis services to patients with chronic kidney failure, also known as end-stage renal disease. As of March 31, 2005, the Company provided dialysis and ancillary services to over 30,400 patients through more than 425 owned outpatient dialysis centers in 34 states, in addition to providing acute dialysis services at more than 210 hospitals.

Renal Care Group's net revenue has been derived primarily from the following sources:

outpatient hemodialysis services;

ancillary services associated with dialysis, primarily the administration of Epogen® (erythropoietin alfa, which we refer to as EPO);

home dialysis services;

inpatient hemodialysis services provided to acute care hospitals and skilled nursing facilities;

laboratory services; and

management contracts with hospital-based and medical university dialysis programs.

Most patients with end-stage renal disease receive three dialysis treatments each week in an outpatient setting. Reimbursement for these services is provided primarily by the Medicare ESRD program based on rates established by the Centers for Medicare and Medicaid Services (CMS). For the three months ended March 31, 2005 and 2004, approximately 55% of the Company's net revenue was derived from reimbursement under the Medicare and Medicaid programs. Medicare reimbursement is subject to rate and other legislative changes by Congress and periodic changes in regulations, including changes that may reduce payments under the ESRD program. Neither Congress nor CMS approved an increase in the composite rate for 2003 or 2004. Congress approved an increase of 1.6% in the Medicare ESRD composite rate for 2005, as well as changes in the way we are paid for separately billable drugs.

The Medicare composite rate applies to a designated group of outpatient dialysis services, including the dialysis treatment, supplies used for the treatment, certain laboratory tests and medications, and most of the home dialysis services we provide. Renal Care Group receives separate reimbursement outside the composite rate for some other services, drugs, including specific drugs such as EPO and some physician-ordered tests, including laboratory tests, provided to dialysis patients.

Congress mandated a change in the way we are paid beginning in 2005 for some of the drugs, including EPO, that we bill for outside of the flat composite rate. This change results in lower reimbursement for these



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drugs and a higher composite rate. Under recently adopted regulations, in 2005 we are reimbursed for the top ten separately billable ESRD drugs at average acquisition cost, and we are reimbursed for other separately billable ESRD drugs at the rate of average sales price plus 6.0%. In addition, the composite rate has increased by 8.7% in 2005. These regulations also include a case-mix adjustment that became effective in April 2005, a geographic adjustment to the composite rate and a budget-neutrality adjustment. Management believes these changes coupled with the 1.6% increase in the Medicare composite rate in 2005 will be neutral to Renal Care Group's revenue per treatment and earnings.

If a patient is younger than 65 years old and has private health insurance, then that patient's treatment is typically reimbursed at rates significantly higher than Medicare during the first 30 months of care. After that period, Medicare becomes the primary payor. Reimbursement for dialysis services provided pursuant to a hospital contract is negotiated with the individual hospital and is usually higher than the Medicare composite rate. Because dialysis is a life-sustaining therapy to treat a chronic disease, utilization is predictable and is not subject to seasonal fluctuations.

Renal Care Group derives a significant portion of our revenue and earnings from the administration of EPO. EPO is manufactured by a single company, Amgen, Inc. EPO is used to treat anemia, a medical complication frequently experienced by dialysis patients. Changes in the Company's contract with Amgen for 2005 along with changes in Amgen's packaging practices for EPO may result in an increase in the Company's cost of EPO in 2005. The estimated impact of these changes was incorporated and communicated in Renal Care Group's corporate goals for 2005. Net revenue from the administration of EPO was 24% and 26% of the net revenue of the Company for the three months ended March 31, 2005 and 2004, respectively.

## **Interim Financial Statements**

Management believes the information contained in this quarterly report on Form 10-Q reflects all adjustments necessary to make the results of operations for the interim periods a fair representation of such operations. All such adjustments are of a normal recurring nature. Operating results for interim periods are not necessarily indicative of results that may be expected for the year as a whole. We suggest that you read these financial statements in conjunction with our consolidated financial statements and the related notes thereto included in our annual report on Form 10-K for the year ended December 31, 2004, as filed with the SEC on March 2, 2005.

## **Reclassifications**

Certain prior year balances have been reclassified to conform to the current year presentation. These reclassifications had no effect on the results of operations as previously reported.

## **2. Business Acquisitions**

### **2005 Acquisitions**

During the first quarter of 2005, we completed certain acquisitions. The combined net assets acquired and resulting net cash purchase price paid in these acquisitions were \$44,013. Each of the transactions involved the acquisition of the net assets of entities that provide care to ESRD patients through owned dialysis facilities. The acquired businesses either strengthened our existing market share within a specific geographic area or provided us with an entrance into a new market. We began recording the results of operations for each of these acquired businesses at the effective dates of the respective transactions.

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The following table summarizes the preliminarily estimated fair values of the assets acquired and liabilities assumed at the date of acquisition for the acquisitions completed during the first three months of 2005:

Accounts receivable, net	\$ 820
Inventory and other current assets	302
Property, plant and equipment, net	9,922
Intangible assets	2,034
Goodwill	32,270
Total assets acquired	45,348
Total liabilities assumed	1,335
Net assets acquired	\$ 44,013

Some of the estimated fair values of assets and liabilities are preliminary and may be adjusted. Items that may be adjusted include items such as deferred tax assets and liabilities, and the valuation of certain assets. Intangible assets primarily represent the value assigned to contracts such as non-competition agreements entered into in the transactions. Related amounts will be amortized over the lives of the contracts, which generally range from five to fifteen years.

**Pro Forma Data**

The following summary, prepared on a pro forma basis, combines our results of operations with those of the businesses we acquired in 2005. These pro forma results reflect the acquisitions as if consummated as of the beginning of the period presented, giving effect to adjustments such as amortization of intangibles, interest expense and related income taxes.

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2004</b>	<b>2005</b>
Pro forma net revenue	\$ 281,756	\$ 374,568
Pro forma net income	\$ 30,503	\$ 33,663
Pro forma net income per share:		
Basic	\$ 0.44	\$ 0.50
Diluted	\$ 0.43	\$ 0.48

The unaudited pro forma results of operations are not necessarily indicative of what actually would have occurred if the acquisitions had been completed prior to the beginning of the periods presented.

**Table of Contents****3. Long-Term Debt**

Long-term debt consisted of the following as of December 31, 2004 and March 31, 2005:

	<b>December 31, 2004</b>	<b>March 31, 2005</b>
Term loan facility, bearing interest at a variable rate (4.7% at March 31, 2005)	\$ 312,813	\$ 308,750
9% senior subordinated notes	159,685	159,685
Obligations under capital leases	4,151	3,774
Other	3,357	5,401
Total indebtedness, excluding fair value premium	480,006	477,610
Add: 9% senior subordinated notes fair value premium	23,608	22,923
Total long-term debt	503,614	500,533
Less: current portion	23,969	25,624
	\$ 479,645	\$ 474,909

**Credit Agreements**

On February 10, 2004, we entered into a new credit agreement (the 2004 Agreement) with a group of banks totaling up to \$700,000. The 2004 Agreement replaced both of our prior facilities. The 2004 agreement has a \$150,000 revolving credit facility, a \$325,000 term loan facility and a \$225,000 incremental term loan facility. Borrowings under the incremental term loan facility are subject to obtaining commitments from the banks and finalizing specific terms. The revolving credit facility and the \$325,000 term loan facility have a final maturity of February 10, 2009. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under the 2004 Agreement. Further, our obligations under the 2004 Agreement, and our subsidiaries' obligations under their guarantees, are secured by a pledge of the equity interests we hold in each of our subsidiaries. The 2004 Agreement includes financial covenants that are customary based on the amount and duration of the agreement.

The revolving credit facility under the 2004 Agreement may be used for acquisitions, repurchases of Company common stock, capital expenditures, working capital and general corporate purposes. Borrowings under the 2004 Agreement accrue interest at variable rates determined by the Company's leverage ratio. Effective June 30, 2004, we entered into interest rate swap agreements to hedge interest rate risk on \$150,000 of our term loan (See Interest Rate Swap below). The portion of our borrowings that is subject to variable rates carries a degree of interest rate risk. Specifically, the Company will face higher interest costs on this debt if interest rates rise.

**9% Senior Subordinated Notes**

With the acquisition of National Nephrology Associates, Inc. (NNA), we assumed all of NNA's outstanding debt including its 9% senior subordinated notes due 2011 (the Notes). We recorded the Notes at the face value of \$160,000 plus an additional \$25,600 representing the difference between the fair value of the Notes and the face amount on the

date of acquisition. Accordingly, the Notes were recorded at the estimated fair value of \$185,600. As of March 31, 2005, the carrying value of the Notes was \$182,608.

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The Notes bear interest at the rate of 9% per annum on the face amount. The fair value premium is being recognized over the life of the Notes using the effective interest method and is recorded as a reduction to interest expense. Accordingly, the effective interest rate on the Notes as of March 31, 2005 was 6.4%. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under these notes. The rights of the noteholders and our obligations under these notes are set forth in an indenture that NNA entered into in October 2003, which we assumed in connection with the NNA acquisition. The indenture includes customary financial covenants.

**Interest Rate Swap**

Effective June 30, 2004, the Company entered into interest rate swap agreements to hedge the interest rate risk on \$150,000 of our term loan. Under these interest rate swap agreements we will exchange fixed and variable rate interest payments based on a \$150,000 notional principal amount through March 30, 2007. The notional amount of \$150,000 and interest payments of 3.5% are fixed in the agreements. The interest payments are subject to adjustment based on our leverage ratio. The changes in cash flows under these agreements are expected to offset the changes in interest rate payments attributable to fluctuations in LIBOR. The hedge is structured to qualify for the shortcut method as prescribed by Statement of Financial Accounting Standard No. 133, *Accounting for Derivative Instruments and Hedging Activities*; therefore, we record changes in the fair value of the agreement directly in other comprehensive income. As of March 31, 2005, the notional amount of the swap agreements was \$150,000 and its fair value was \$1,707, resulting in an unrealized gain of \$1,254 during 2005 (net of a related tax expense of \$785).

**Obligations Under Capital Leases**

Obligations under capital leases consist primarily of capital leases for buildings and equipment maturing at various times through August 2015.

**Other**

The other long-term debt consists primarily of notes maturing at various times through February 2009.

**Maturities of Long-Term Debt**

The aggregate maturities of long-term debt, excluding the fair value premium, at March 31, 2005 are as follows:

2005	\$ 19,956
2006	30,858
2007	57,195
2008	156,664
2009	51,592
Thereafter	161,345
	\$ 477,610

**Table of Contents****Guarantor Information**

Our wholly-owned subsidiaries have guaranteed the Notes as well as our obligations under the 2004 Agreement. We conduct substantially all of our business through subsidiaries. Presented below is condensed consolidating financial information as of March 31, 2005 and December 31, 2004 and for the three months ended March 31, 2005 and 2004, respectively. The information segregates Renal Care Group, Inc. (the parent company), the combined wholly-owned subsidiary guarantors and the combined non-guarantor subsidiaries and reflects consolidating adjustments. All of the subsidiary guarantees are both full and unconditional, and joint and several.

**Condensed Consolidating Balance Sheets**

	<b>Parent Company</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>	<b>Consolidating Adjustments</b>	<b>Consolidated Total</b>
<b>As of December 31, 2004</b>					
Cash and cash equivalents	\$	\$	\$ 31,945	\$ (14,014)	\$ 17,931
Accounts receivable, net		198,778	76,595		275,373
Other current assets	45,749	23,320	10,711		79,780
Total current assets	45,749	222,098	119,251	(14,014)	373,084
Property, plant and equipment, net	29,542	189,434	96,408	1,148	316,532
Goodwill	1,483	574,815	117,666	300	694,264
Other assets	10,828	99,033	7,436	(72,197)	45,100
Total assets	\$ 87,602	\$ 1,085,380	\$ 340,761	\$ (84,763)	\$ 1,428,980
Current liabilities (including intercompany assets and liabilities)					
Long-term debt	\$ (699,042)	\$ 813,091	\$ 157,344	\$ (27,488)	\$ 243,905
Long-term liabilities	476,184	(259)	3,720		479,645
Minority interest	64,976	2,253	461		67,690
Stockholders equity		39,610	5,989	20	45,619
	245,484	230,685	173,247	(57,295)	592,121
Total liabilities and stockholders equity	\$ 87,602	\$ 1,085,380	\$ 340,761	\$ (84,763)	\$ 1,428,980
<b>As of March 31, 2005</b>					
Cash and cash equivalents	\$	\$	\$ 29,013	\$ (16,113)	\$ 12,900
Accounts receivable, net		196,292	79,073		275,365
Other current assets	46,354	24,203	11,682		82,239
Total current assets	46,354	220,495	119,768	(16,113)	370,504
Property, plant and equipment, net	37,678	194,735	99,594	354	332,361
Goodwill	1,483	593,117	122,846	300	717,746
Other assets	5,604	99,552	7,720	(67,098)	45,778

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Total assets	\$ 91,119	\$ 1,107,899	\$ 349,928	\$ (82,557)	\$ 1,466,389
Current liabilities (including intercompany assets and liabilities)	\$ (671,482)	\$ 799,131	\$ 156,598	\$ (30,033)	\$ 254,214
Long-term debt	471,592	(277)	3,594		474,909
Long-term liabilities	51,422	7,661	765	1,707	61,555
Minority interest		41,191	6,869	(32)	48,028
Stockholders equity	239,587	260,193	182,102	(54,199)	627,683
Total liabilities and stockholders equity	\$ 91,119	\$ 1,107,899	\$ 349,928	\$ (82,557)	\$ 1,466,389

**Table of Contents****Condensed Consolidating Income Statements**

	<b>Parent Company</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>	<b>Consolidating Adjustments</b>	<b>Consolidated Total</b>
<b>For the three months ended March 31, 2004</b>					
Net revenue	\$ 187	\$ 187,654	\$ 91,386	\$ (1,199)	\$ 278,028
Total operating costs and expenses	10,306	141,123	71,091	(1,199)	221,321
Income (loss) from operations	(10,119)	46,531	20,295		56,707
Interest expense, net	965				965
Minority interest		6,586	628		7,214
Provision (benefit) for income taxes	(4,212)	15,179	7,474		18,441
Net income (loss)	\$ (6,872)	\$ 24,766	\$ 12,193	\$	\$ 30,087

	<b>Parent Company</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>	<b>Consolidating Adjustments</b>	<b>Consolidated Total</b>
<b>For the three months ended March 31, 2005</b>					
Net revenue	\$ 1,377	\$ 260,093	\$ 113,760	\$ (1,721)	\$ 373,509
Total operating costs and expenses	14,857	203,934	85,130	(1,721)	302,200
Income (loss) from operations	(13,480)	56,159	28,630		71,309
Interest expense, net	7,345	(303)	219		7,261
Minority interest		8,482	880		9,362
Provision (benefit) for income taxes	(8,018)	18,472	10,600		21,054
Net income (loss)	\$ (12,807)	\$ 29,508	\$ 16,931	\$	\$ 33,632

**Table of Contents****Condensed Consolidating Statements of Cash Flows**

	<b>Parent Company</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>	<b>Consolidating Adjustments</b>	<b>Consolidated Total</b>
<b>For the three months ended March 31, 2004</b>					
Cash flows from operating activities:					
Net income (loss)	\$ (6,872)	\$ 24,766	\$ 12,193	\$	\$ 30,087
Changes in operating and intercompany assets and liabilities and non-cash items included in net income	(28,729)	44,586	6,197	(6,684)	15,370
Net cash provided by (used in) operating activities	(35,601)	69,352	18,390	(6,684)	45,457
Net cash (used in) provided by investing activities	(4,469)	(66,291)	(12,168)	4,869	(78,059)
Net cash provided by financing activities	19,913				19,913
Increase (decrease) in cash and cash equivalents	(20,157)	3,061	6,222	(1,815)	(12,689)
Cash and cash equivalents, at beginning of period	20,157	2,646	27,492		50,295
Cash and cash equivalents, at end of period	\$	\$ 5,707	\$ 33,714	\$ (1,815)	\$ 37,606

	<b>Parent Company</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>	<b>Consolidating Adjustments</b>	<b>Consolidated Total</b>
<b>For the three months ended March 31, 2005</b>					
Cash flows from operating activities:					
Net income (loss)	\$ (12,808)	\$ 29,508	\$ 16,932	\$	\$ 33,632
Changes in operating and intercompany assets and liabilities and non-cash items included in net income	32,261	5,038	189	(5,990)	31,498
Net cash provided by (used in) operating activities	19,453	34,546	17,121	(5,990)	65,130
Net cash (used in) provided by investing activities	(19,578)	(34,236)	(11,766)	794	(64,786)
Net cash provided by (used in) financing activities	125	(310)	(8,287)	3,097	(5,375)
Decrease in cash and cash equivalents			(2,932)	(2,099)	(5,031)
Cash and cash equivalents, at beginning of period			31,945	(14,014)	17,931

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Cash and cash equivalents, at end of period	\$	\$	\$	29,013	\$	(16,113)	\$	12,900
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**Table of Contents****4. Net Income per Share**

The following table sets forth the computation of basic and diluted net income per share (shares in thousands):

	<b>Three Months Ended March 31</b>	
	<b>2004</b>	<b>2005</b>
Numerator:		
Numerator for basic and diluted net income per share net income	\$ 30,087	\$ 33,632
Denominator:		
Denominator for basic net income per share weighted-average shares	68,910	67,863
Effect of dilutive securities:		
Stock options	2,313	2,498
Denominator for diluted net income per share adjusted weighted-average shares and assumed conversions	71,223	70,361
Net income per share:		
Basic	\$ 0.44	\$ 0.50
Diluted	\$ 0.42	\$ 0.48

**5. Stockholders Equity***Stock-based Compensation*

We account for stock-based compensation to employees and directors using the intrinsic value method in accordance with the provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. Accordingly, we recognize no compensation expense when we grant fixed options to employees and directors, because the exercise price of the stock options equals or exceeds the market price of the underlying stock on the dates of grant. Option grants to medical directors and non-vested stock grants are expensed over their vesting periods.

The following table presents the pro forma effect on net income and net income per share as if we had applied the fair value based method and recognition provisions of Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation*, (SFAS No. 123) to stock-based compensation to employees and directors:

	<b>Three Months Ended March 31,</b>	
	<b>2004</b>	<b>2005</b>
Net income, as reported	\$ 30,087	\$ 33,632
Add: stock-based compensation expense, net of related tax effects, included in the determination of net income as reported	31	56
Less: stock-based compensation expense, net of related tax effects, determined by the fair value-based method	(2,387)	(2,479)

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Pro forma net income	\$ 27,731	\$ 31,209
Net income per share:		
Basic, as reported	\$ 0.44	\$ 0.50
Basic, pro forma	\$ 0.40	\$ 0.46
Diluted, as reported	\$ 0.42	\$ 0.48
Diluted, pro forma	\$ 0.39	\$ 0.44

The effects of applying SFAS No. 123 for providing pro forma disclosures are not likely to be representative of the effects on reported net income for future periods.

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### *Stock Split*

On April 27, 2004, we announced a three-for-two stock split in the form of a stock dividend distributed to shareholders of record as of May 7, 2004. On May 24, 2004 we issued one share for every two shares held by shareholders as of the record date. The par value of our common stock remained unchanged at \$0.01.

### *Authorized Shares*

On June 9, 2004, our shareholders approved an amendment to the certificate of incorporation increasing the number of authorized shares of common stock from 90,000 to 150,000.

## **6. Contingencies**

On October 25, 2004, the Company received a subpoena from the office of the United States Attorney for the Eastern District of New York. The subpoena requires the production of documents related to numerous aspects of the Company's business and operations, including those of RenaLab, Inc., the Company's laboratory. The subpoena includes specific requests for documents related to testing for parathyroid hormone (PTH) levels and vitamin D therapies. To the Company's knowledge no proceedings have been initiated against the Company at this time, although the Company cannot predict whether or when proceedings might be initiated. The Company intends to cooperate with the government's investigation. Compliance with the subpoena will require the Company to incur legal expenses and will require management attention. The Company cannot predict whether legal proceedings will be initiated against it in connection with this investigation or, if initiated, the outcome of any proceedings.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Company believes that it is in compliance with all applicable laws and regulations governing the Medicare and Medicaid programs. The Company is not aware of any pending or threatened investigations involving allegations of potential noncompliance with applicable laws or regulations. While no regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

The Company is involved in other litigation and regulatory investigations arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, these matters will be resolved without material adverse effect on the Company's consolidated financial position or results of operations.

## **7. Subsequent Event**

On May 3, 2005 the Company entered into a definitive merger agreement with Fresenius Medical Care AG in which Fresenius Medical Care will acquire all of the Company's outstanding stock. Fresenius Medical Care will pay \$48.00 for each share of outstanding common stock of the Company. Fresenius Medical Care will acquire the Company subject to its outstanding indebtedness of approximately \$500.5 million. The transaction is expected to close in the second half of 2005.

The Board of Directors of the Company and the management and supervisory boards of Fresenius Medical Care have approved the transaction. Completion of the transaction is subject to the approval of the Company's stockholders as well as customary conditions to closing, including the termination or expiration of the waiting period under the Hart-Scott Rodino Antitrust Improvements Act of 1976, as amended.

## **8. Recent Accounting Pronouncements**

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS No. 123(R)), which is a revision of SFAS No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123). SFAS No. 123(R) supersedes APB Opinion No. 25, *Accounting for Stock*

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*Issued to Employees*, and amends SFAS No. 95, *Statement of Cash Flows*. Generally, the approach in SFAS No. 123(R) is similar to the approach described in SFAS No. 123. However, SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values. Pro forma disclosure is no longer an alternative. On April 14, 2005, the United States Securities and Exchange Commission announced it would permit most registrants subject to its oversight additional time to implement the requirements in SFAS No. 123(R). As announced, the SEC will permit companies to implement SFAS No. 123(R) at the beginning of their next fiscal year (instead of their next reporting period) that begins after June 15, 2005. The Company is evaluating the requirements of SFAS No. 123(R) and expects that the adoption of SFAS No. 123(R), effective January 1, 2006, will have an impact on its consolidated results of operations and earnings per share. The Company has not yet determined the method of adoption or the potential financial impact of adopting SFAS No. 123(R).

**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Results of Operations****Three Months Ended March 31, 2004 Compared to Three Months Ended March 31, 2005**

*Net Revenue.* Net revenue increased from \$278.0 million for the three months ended March 31, 2004 to \$373.5 million for the three months ended March 31, 2005, an increase of \$95.5 million, or 34.3%. This increase resulted primarily from a 33.2% increase in the number of treatments we performed from 860,249 in the 2004 period to 1,146,233 in the 2005 period. This growth in treatments is the result of our acquisition of NNA on April 2, 2004 and other dialysis facilities along with a 3.0% increase in same-market treatments for the 2005 period over the 2004 period. In addition, average patient revenue per treatment increased slightly from \$323 in 2004 to \$324 in 2005. During the first quarter of 2004 we resolved several contractual issues with payors that increased our net revenue per treatment by approximately \$6 per treatment. Excluding the impact of these contractual issues with payors, the average patient revenue per treatment increased 2.2% from \$317 in 2004 to \$324 in 2005. The increase was largely due to the impact of our annual price increase implemented in the fourth quarter of 2004, favorable renegotiations of some of our managed care contracts, the net impact of Medicare's 1.6% composite rate increase and changes in its reimbursement for separately billable drugs, along with an increase in the utilization of certain ancillary drugs.

*Patient Care Costs.* Patient care costs consist of costs directly related to the care of patients, including direct labor, drugs and other medical supplies, and operational costs of facilities. Patient care costs increased from \$179.4 million for the three months ended March 31, 2004, to \$246.6 million for the three months ended March 31, 2005, an increase of 37.5%. This increase was due principally to the increase in the number of treatments we performed during the period, which resulted in corresponding increases in the use of labor, drugs and supplies. Patient care costs as a percentage of revenue increased from 64.5% in the 2004 period to 66.0% in the 2005 period. This increase is due to generally higher salary and benefit costs and routine supply costs experienced in the former NNA facilities. Patient care costs per treatment increased 2.9% from \$209 in the 2004 period to \$215 in the 2005 period. This increase was largely due to the higher cost structure in the former NNA facilities. Management believes that the Company will continue to face increases in the cost of labor through the remainder of 2005.

*General and Administrative Expenses.* General and administrative expenses include corporate office costs and other costs not directly related to the care of patients, including facility administration, accounting, billing and information systems. General and administrative expenses increased from \$22.7 million for the three months ended March 31, 2004 to \$30.6 million for the three months ended March 31, 2005, an increase of 35.1%. The increase in general and administrative expenses over 2004 was due to increased costs associated with acquisitions closed subsequent to the first quarter of 2004. General and administrative expenses as a percentage of net revenue remained unchanged at 8.2% in 2005.

*Provision for Doubtful Accounts.* Management determines the provision for doubtful accounts as a function of payor mix, billing practices and other factors. We reserve for doubtful accounts in the period when we recognize revenue based upon a variety of factors. These factors include, but are not limited to, analysis of the revenues generated from payor sources, performing subsequent collection testing and regularly reviewing detailed accounts receivable agings. Management makes adjustments to the allowance for doubtful accounts as necessary based on the results of management's reviews of the net collectibility of accounts receivable. The provision for doubtful accounts increased from \$7.1 million for the three months ended March 31, 2004 to \$8.2 million for the three

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months ended March 31, 2005, an increase of \$1.1 million, or 15.4%. The provision for doubtful accounts as a percentage of net revenue decreased from 2.6% in the 2004 period to 2.2% in the 2005 period. The decrease in the provision for doubtful accounts as a percentage of net revenue was due to continued improvements in the Company's collection experience which is partially attributable to improvements in the amount of self-pay balances.

*Depreciation and Amortization.* Depreciation and amortization increased from \$12.2 million for the three months ended March 31, 2004 to \$16.8 million for the three months ended March 31, 2005, an increase of 38.0%. This increase was due to the start-up of dialysis facilities, the normal replacement costs of dialysis facilities and equipment, purchase of information systems, and the amortization of separately identifiable intangible assets associated with acquisitions. Depreciation and amortization as a percentage of net revenue increased slightly from 4.4% in 2004 to 4.5% in 2005.

*Income from Operations.* Income from operations increased from \$56.7 million for the three months ended March 31, 2004 to \$71.3 million for the three months ended March 31, 2005, an increase of 25.7%. Income from operations as a percentage of net revenue decreased from 20.4% in the 2004 period to 19.1% in the 2005 period principally as a result of the acquisition of NNA, which had generally lower margins than the remainder of our operations as a result of NNA's lower revenue per treatment, higher patient care costs and other factors discussed above.

*Interest Expense, Net.* Interest expense increased from \$965,000 for the three months ended March 31, 2004 to \$7.3 million for the three months ended March 31, 2005. This increase was due to higher average borrowings outstanding during the quarter, which were primarily associated with the completion of our program to repurchase \$250.0 million in common stock between November 2003 and March 2004, our acquisitions after January 1, 2004 and the assumption of NNA's \$160.0 million of 9% senior subordinated notes.

*Minority Interest.* Minority interest represents the proportionate equity interest of other owners in the consolidated entities that we do not wholly own. The financial results of those entities are included in the Company's consolidated results. Minority interest as a percentage of net revenue decreased from 2.6% in the 2004 period to 2.5% in the 2005 period. The change in minority interest expense as a percentage of revenue occurred based on a slight decline in the overall profitability of our facilities that operate as joint ventures. As of March 31, 2005, we were the majority and controlling owner in 70 joint ventures, as compared to 53 as of March 31, 2004.

*Provision for Income Taxes.* Income tax expense increased from \$18.4 million for the three months ended March 31, 2004 to \$21.1 million for the three months ended March 31, 2005, an increase of \$2.6 million or 14.2%. The increase is a result of higher pre-tax earnings described above. Our effective tax rate increased from 38.0% for the 2004 period to 38.5% in the 2005 period.

*Net Income.* Net income increased from \$30.1 million for the three months ended March 31, 2004 to \$33.6 million for the three months ended March 31, 2005, an increase of \$3.5 million or 11.8%. The increase is a result of the items discussed above.

## **Liquidity and Capital Resources**

We require capital primarily to acquire and develop dialysis centers, to purchase property and equipment for existing centers, to repurchase shares of our common stock and to finance working capital needs. At March 31, 2005, our working capital was \$116.3 million, cash and cash equivalents were \$12.9 million, and our current ratio was approximately 1.5 to 1.0.

Net cash provided by operating activities was \$65.1 million for the three months ended March 31, 2005. Cash provided by operating activities consists of net income before depreciation and amortization expense and

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income applicable to minority interest, adjusted for changes in components of working capital. Net cash used in investing activities was \$64.8 million for the three months ended March 31, 2005. Net cash used in investing activities consisted primarily of \$44.0 million cash paid for acquisitions, net of cash acquired, as well as \$22.2 million in purchases of property and equipment. Net cash used in financing activities was \$5.4 million for the three months ended March 31, 2005. Net cash used in financing activities primarily reflects net proceeds of \$7.1 million from the issuance of common stock, offset by \$9.4 million in repurchases of our common stock.

On February 10, 2004, we entered into a new credit agreement (the 2004 Agreement) with a group of banks totaling up to \$700.0 million. The 2004 Agreement replaced both of our prior facilities. The 2004 Agreement has a \$150.0 million revolving credit facility, a \$325.0 million term loan facility and a \$225.0 million incremental term loan facility. Borrowings under the incremental term loan facility are subject to obtaining commitments from the banks and finalizing specific terms. The revolving credit facility and the \$325.0 million term loan facility have a final maturity of February 10, 2009. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under the 2004 Agreement. Further, our obligations under the 2004 Agreement, and our subsidiaries' obligations under their guarantees, are secured by a pledge of the equity interests we hold in each of our subsidiaries. The 2004 Agreement includes financial covenants that are customary based on the amount and duration of the agreement.

Borrowings under the \$150.0 million revolving credit facility may be used for acquisitions, repurchases of our stock, capital expenditures, working capital and general corporate purposes. As of March 31, 2005, we can borrow up to \$150.0 million under the revolving credit facility but cannot borrow any additional amounts under the \$325.0 million term loan facility. At March 31, 2005, our outstanding indebtedness was \$500.5 million, including a remaining balance of \$308.8 million under the term loan facility, \$4.6 million under the revolving credit facility, \$182.6 million of 9.0% senior subordinated notes assumed in the NNA transaction and \$4.5 million of other indebtedness, primarily capital leases.

Borrowings under the 2004 Agreement bear interest at variable rates determined by our leverage ratio. These variable rate debt instruments carry a degree of interest rate risk and we will face higher interest costs on this debt if interest rates rise.

Effective June 30, 2004, we entered into interest rate swap agreements to hedge the interest rate risk on \$150.0 million of our term loan. Under these interest rate swap agreements we exchange fixed and variable rate interest payments based on a \$150.0 million notional principal amount through March 30, 2007. The notional amount of \$150.0 million and the interest rate of 3.5% are fixed in the agreements. The changes in cash flows under these agreements are expected to offset the changes in interest rate payments attributable to fluctuations in LIBOR. The hedge is structured to qualify for the shortcut method; therefore, we record changes in the fair value of the agreement directly in other comprehensive income. The interest payments under this agreement are settled on a net basis each calendar quarter.

The 9% senior subordinated notes we assumed in the NNA transaction bear interest at the rate of 9% per annum on the face amount that was \$160.0 million at the date of acquisition. As of March 31, 2005 these notes have a remaining face value of \$159.7 million and are recorded at their carrying value of \$182.6 million. These notes do not provide for scheduled principal amortization and are scheduled to mature on November 1, 2011. Each of our wholly-owned subsidiaries has guaranteed all of our obligations under these notes. The rights of the noteholders and our obligations under these notes are set forth in an indenture that NNA entered into in October 2003, which we assumed in connection with the NNA acquisition. The indenture includes customary financial covenants.

As a result of our indebtedness, we will incur substantial interest expense in 2005. Based on our outstanding indebtedness of \$477.6 million, excluding the unamortized fair value premium of \$22.9 million on



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the 9% senior subordinated notes, the aggregate maturities of our borrowings are as follows: 2005 \$20.0 million; 2006 \$30.9 million; 2007 \$57.2 million; 2008 \$156.6 million; 2009 \$51.6 million; and thereafter \$161.3 million.

A significant component of our growth strategy is the acquisition and development of dialysis facilities. There can be no assurance that we will be able to identify suitable acquisition candidates or to close acquisitions on acceptable terms. Management believes that existing cash and funds from operations, together with funds available under our credit facility, will be sufficient to meet our acquisition, expansion, capital expenditure and working capital needs for the foreseeable future. However, in order to finance certain large strategic acquisition opportunities, we may need to incur additional short and long-term bank indebtedness or to issue equity or debt securities. The availability and terms of any future financing will depend on market and other conditions. There can be no assurance that we will be able to secure additional financing, if required, on acceptable terms.

We plan to make capital expenditures of between \$85.0 million and \$95.0 million in 2005, primarily for equipment replacement, expansion of existing dialysis facilities and construction of de novo facilities. As of March 31, 2005, we had made approximately \$22.2 million of capital expenditures for these purposes in 2005. We expect to fund these capital expenditures with cash provided by operating activities and our existing credit facilities. Management believes that capital resources available to us will be sufficient to meet the needs of our business, both on a short- and long-term basis.

Management, from time to time, determines the appropriateness of repurchasing common stock in accordance with a repurchase plan initially authorized by the Board of Directors in October 2000. In 2001, we began repurchasing shares of our common stock by purchasing 150,000 shares of common stock for approximately \$3.1 million. In 2002, we repurchased 4.3 million shares of our common stock for approximately \$90.9 million. In October 2003, we announced that the Board of Directors had approved an increase in the repurchase plan to allow the purchase of up to a total of \$450.0 million in common stock, and we announced that we intended to repurchase \$250.0 million in common stock between November 1, 2003 and March 31, 2004. During 2003, we repurchased 5.5 million shares of common stock for \$140.5 million. During 2004, we repurchased 4.6 million shares for \$137.8 million and in the first quarter of 2005 we repurchased 252,000 shares of common stock for approximately \$9.4 million. As of March 31, 2005, we had repurchased an aggregate of 14.8 million shares under the plan, for a total of approximately \$381.6 million.

**Critical Accounting Policies**

The Securities and Exchange Commission (SEC) issued a financial reporting release, FR-60, *Cautionary Advice Regarding Disclosure About Critical Accounting Policies*. In accordance with that release, management has identified accounting policies that it considers critical to the business of Renal Care Group. Those policies include net revenue and contractual provisions, provision for doubtful accounts, self-insurance accruals, impairment of goodwill and long-lived assets, and income taxes. These policies were identified as critical based on their importance to the consolidated financial statements as well as on the degrees of subjectivity and complexity involved in these policies. There have been no changes in Renal Care Group's critical accounting policies or in the application of those policies from those described in the annual report on Form 10-K for the year ended December 31, 2004, as filed with the SEC on March 2, 2005.

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**RISK FACTORS**

*You should carefully consider the risks described below before investing in Renal Care Group. The risks and uncertainties described below **are not** the only ones facing Renal Care Group. Other risks and uncertainties that we have not predicted or assessed may also adversely affect us.*

*If any of the following risks occurs, our earnings, financial condition or business could be materially harmed, and the trading price of our common stock could decline, resulting in the loss of all or part of your investment.*

**Our profits are dependent on the services we provide to a small portion of our patients who are covered by private insurance.**

In recent reviews of dialysis reimbursement, the Medicare Payment Advisory Commission, also known as MedPAC, determined that Medicare payments for dialysis services are less than the average costs that providers incur to provide the services. Since Medicaid rates are comparable to those of Medicare and because Medicare only pays us 80% of the Medicare allowable amount (the patient or secondary insurance being responsible for the remaining 20%), the amount we receive from Medicare and Medicaid is less than our average cost per treatment. As a result, the payments we receive from private payors both subsidize the losses we incur on services for Medicare and Medicaid patients and generate all the profits we report. In fact, much of our profit is generated from private-pay patients for whom we are paid at amounts equal to several times Medicare rates. We estimate that Medicare and Medicaid are the primary payors for approximately 80% of the patients to whom we provide care but that 45% of our net revenue in 2003, 47% of our net revenue in 2004 and 45% of our net revenue for the three months ended March 31, 2005 were derived from sources other than Medicare and Medicaid. Therefore, if the private payors who pay for the care of the other 20% of our patients reduce their payments for our services, or if we experience a shift in our revenue mix toward Medicare or Medicaid reimbursement, then our revenue, cash flow and earnings would decrease, and our cash flow and profits would be disproportionately impacted.

We have been able to implement annual price increases for private insurers and managed care organizations, but government reimbursement has remained flat or has been increased only modestly. Management believes that health insurance pricing is cyclical and that we may be at or near the top of the cycle. As a result, management believes that our ability to maintain or raise rates to private insurers and managed care companies may be more limited over the next several years than it has been in the recent past. Management believes that the reductions in reimbursement by commercial insurers, along with pricing pressure from other commercial insurers and managed care organizations could adversely impact our revenue per treatment and earnings per share in 2005. Any of the following events could have a material adverse effect on our revenue and earnings:

any number of economic or demographic factors could cause private insurers, hospitals or managed care companies to reduce the rates they pay us or to refuse to pay price increases or to work to reduce the rate of our price increases;

a portion of our business that is currently reimbursed by private insurers or hospitals may become reimbursed by managed care organizations, which generally have lower rates for our services; or

a portion of our business that is currently reimbursed by private insurers at rates based on our billed charges may become reimbursed under a contract at lower rates.

**If Congress or CMS changes the Medicare or Medicaid programs for dialysis, then our net revenue and earnings could decrease.**

If the government changes the Medicare, Medicaid or similar government programs or the rates those programs pay for our services, then our revenue and earnings may decline. We estimate that approximately 55% of our net revenue for 2003, 53% of our net revenue for 2004, and 55% of our net revenue for the three months ended March 31, 2005 consisted of reimbursements from Medicare, Medicaid and comparable state programs, including reimbursement for the administration of EPO. Any of the following actions in connection with government programs could cause our revenue and earnings to decline:

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a reduction of the amount paid to us under government programs;

an increase in the costs associated with performing our services that are subject to inflation, such as labor and supply costs, without a corresponding increase in reimbursement rates;

the inclusion of some or all ancillary services, for which we are now reimbursed separately, in the flat composite rate for a dialysis treatment; or

changes in laws, or the interpretations of laws, which could cause us to modify our operations.

Specifically, the President's proposed budget for fiscal 2006 proposes substantial cuts in federal Medicaid spending. We cannot predict whether any of the proposed cuts will be made or how they will affect us. In addition, Congress and CMS have proposed expanding the drugs and services that are included in the flat composite rate. CMS has indicated that it believes such a mechanism would be fairer and easier to administer. In addition, Congress mandated a change in the way we are paid beginning in 2005 for some of the drugs, including EPO, that we bill for outside of the flat composite rate. This change results in lower reimbursement for these drugs and a higher composite rate. Under recently adopted regulations, in 2005 we are reimbursed for the top ten separately billable ESRD drugs (including EPO) at the rate of average acquisition cost, and we are reimbursed for other separately billable ESRD drugs at the rate of average sales price plus 6.0%. In addition, the composite rate will be increased by 8.7% in 2005. These regulations also include a case-mix adjustment that became effective in April 2005, a geographic adjustment to the composite rate and a budget-neutrality adjustment. Management believes these changes coupled with the 1.6% increase in the Medicare composite rate in 2005 will be neutral to our Medicare revenue per treatment.

**The implementation of the case-mix adjustment could adversely affect our cash flow and working capital.**

Under the regulations adopted pursuant to the MMA, CMS has adopted a case-mix adjustment for the ESRD composite rate, under which the Medicare composite rate will be adjusted based on a patient's age, body mass index and body surface area. These regulations became effective April 1, 2005. Management believes implementing these case-mix adjustments will require significant systems changes for the Medicare fiscal intermediaries that process and pay Medicare claims. If the required systems changes are not made on a timely basis, then the Medicare fiscal intermediaries may delay the payment of claims or may not pay claims correctly, either of which could have an adverse effect on our cash flow and working capital.

**If states lower Medicaid reimbursement, then we would be less profitable.**

The Medicaid programs in Alaska and New Mexico, two states in which we operate, currently reimburse us at rates higher than those paid by Medicare. These programs may reduce payment levels to be at or close to Medicare rates. In addition, a number of the states in which we operate are experiencing budget shortfalls, and some of these states may consider reducing Medicaid reimbursement, changing their Medicaid programs or not paying claims to address these shortfalls and cut costs. We are unable to predict whether and, if so, when any reductions in Medicaid reimbursement might occur and what their precise effect will be.

**If reimbursement for EPO decreases, then we could be less profitable.**

If government or private payors reduce reimbursement rates for EPO, for which we are currently reimbursed separately outside of the flat composite rate, then our revenue and earnings will decline. Revenues from the administration of EPO were approximately 24% of our net revenue for 2003, 26% of our net revenue for 2004 and 24% of our net revenue for the three months ended March 31, 2005. Most of our payments for EPO



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come from government programs. For the three months ended March 31, 2005, Medicare and Medicaid reimbursement represented approximately 55% of the total revenue we derived from EPO. A reduction in the reimbursement rate for EPO or the inclusion of EPO in the list of items covered by the flat composite rate could materially and adversely affect our net revenue and earnings. As discussed above, Congress has mandated a change in the way we will be reimbursed for EPO, and CMS has adopted regulations to implement the change.

**If Amgen raises the price for EPO or if EPO becomes in short supply, then we could be less profitable.**

EPO is produced by a single manufacturer, Amgen, Inc. In April 2002, Amgen announced a 3.9% increase in the price of EPO. This price increase adversely affected our earnings in 2003, and changes in the rebate structure under our current contract with Amgen adversely affected our earnings in 2004. Changes in the rebate structure under our current contract with Amgen or in Amgen's packaging process for EPO, may adversely affect our earnings in 2005. If Amgen imposes additional EPO price increases or if Amgen or other factors interrupt the supply of EPO, then our net revenue and earnings will decline.

**If Amgen markets Aranesp® for ESRD patients, then we could be less profitable.**

Amgen has developed and obtained FDA approval for a drug to treat anemia that is marketed as Aranesp® (darbepoetin alfa). Aranesp® is a longer acting form of bio-engineered protein that, like EPO, can be used to treat anemia. EPO is usually administered in conjunction with each dialysis treatment. Aranesp® can remain effective for two to three weeks. If Amgen markets Aranesp® for the treatment of dialysis patients, then our earnings could be materially and adversely affected by either of the following factors:

our margins realized from the administration of Aranesp® could be lower than the margins realized on the administration of EPO; or

physicians could decide to administer Aranesp® in their offices, and we would not recognize net revenue or profit from the administration of EPO or Aranesp®.

**Changes in our clinical practices or reimbursement rules for EPO and other drugs could substantially reduce our revenue and earnings.**

The administration of EPO and other drugs accounted for approximately 35% of our net revenue in the first quarter of 2005. Changes in physician practices or prescription patterns, changes in private and governmental reimbursement criteria or the introduction of new drugs or new types of drug administration could materially reduce our net revenue and profits. For example, some Medicare fiscal intermediaries have implemented or may implement local medical review policies for EPO and other drugs that would effectively limit reimbursement for those drugs. In 2004, CMS proposed a national policy that would establish limits on reimbursement for EPO, but this proposal has not yet been finalized. We are unable to predict whether and, if so, when any such changes may occur, but if they do, they will likely have an adverse impact on our net revenue and earnings.

**If our business is alleged or found to violate health care or other applicable laws, our net revenue and earnings could decrease.**

We are subject to extensive federal, state and local regulation. The laws that apply to our operations include, but are not limited to, the following:

fraud and abuse prohibitions under state and federal health care laws;

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prohibitions and limitations on patient referrals;

billing and reimbursement rules, including false claims prohibitions under health care reimbursement laws;

rules regarding the collection, use, storage and disclosure of patient health information, including HIPAA, and state law equivalents of HIPAA;

facility licensure;

health and safety requirements;

environmental compliance; and

medical and toxic waste disposal.

Much of the regulation of our business, particularly in the areas of fraud and abuse and patient referral, is complex and open to differing interpretations. Due to the broad application of the statutory provisions and the absence in many instances of regulations or court decisions addressing the specific arrangements through which we conduct our business, including our arrangements with medical directors, physician stockholders and physician joint venture partners, governmental agencies could challenge some of our practices under these laws.

New regulations governing electronic transactions and the collection, use, storage, and disclosure of health information impose significant administrative and financial obligations on our business. If, after the required compliance date, we are found to have violated these regulations, we could be subject to:

criminal or civil penalties, including significant fines;

claims by people who believe their health information has been improperly used or disclosed; and

administrative penalties by payors.

Government investigations of health care providers, including dialysis providers, have continued to increase. We have been the subject of investigations in the past, and the government may investigate our business in the future. One of our competitors, DaVita, Inc., has announced that it is the subject of an investigation by the U.S. Attorney for the Eastern District of Pennsylvania. Another competitor, Gambro Healthcare, Inc., recently settled matters related to an investigation by the U.S. Attorney's Office in St. Louis, Missouri and paid approximately \$350.0 million in connection with the settlement. In addition, each of DaVita and Fresenius Medical Care AG has announced that it is the subject of an investigation by the U.S. Attorney's Office in St. Louis, Missouri.

On October 25, 2004, we received a subpoena from the office of the United States Attorney for the Eastern District of New York. The subpoena requires the production of documents related to numerous aspects of our business and operations, including those of RenaLab, Inc., our laboratory. The subpoena includes specific requests for documents related to testing for parathyroid hormone (PTH) levels and vitamin D therapies. Our competitors DaVita, Inc., Fresenius Medical Care AG, and Gambro Healthcare, Inc., as well as other participants in the dialysis industry, have announced that they have received similar subpoenas. If any of our operations is found to violate applicable laws, then we may be subject to severe sanctions, or we could be required to alter or

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discontinue the challenged conduct or both. If we are required to alter our practices, we may not be able to do so successfully. If any of these events occurs, our revenue and earnings could decline.

**If our joint ventures violate the law, our business could be damaged.**

A number of the dialysis centers we operate are owned by joint ventures in which we hold a controlling interest and one or more physicians or physician practice groups maintain a minority interest. The physician owners may also provide medical director services to those centers or other centers we own and operate. Our joint venture arrangements do not satisfy all elements of any safe harbor under the Anti-Kickback statutes. If one or more of our joint ventures were found to be in violation of the Anti-Kickback Statute or the Stark Law, we could be required to restructure them or refuse to accept referrals for designated health services from the physicians with whom those particular joint venture centers have a relationship. We also could be required to repay to Medicare amounts received by the joint ventures pursuant to prohibited referrals, and we could be subject to monetary penalties. If we are subject to any of these penalties, our business could be damaged.

**Changes in the health care delivery, financing or reimbursement systems could adversely affect our business.**

The health care industry in the United States may be entering a period of change and uncertainty. Health care organizations, public or private, may dramatically change the way they operate and pay for services. Our business is designed to function within the current health care financing and reimbursement system. During the past several years, the health care industry has been subject to increasing levels of government regulation of, among other things, reimbursement rates and relationships with referring physicians. In addition, proposals to reform the health care system have been considered by Congress. In light of the continued increases in the cost of health care and the current economic situation coupled with the federal budget deficit, there may be new proposals to change the health care system and control costs. These proposals, if enacted, could further increase the government's oversight role and involvement in health care, lower reimbursement rates and otherwise change the operating environment for health care companies. We cannot predict the likelihood of those events or what impact they may have on our business.

**If local physicians stop sending patients to our centers or were prohibited from doing so for regulatory reasons, then our revenue and earnings would decline.**

Our dialysis centers depend on local nephrologists sending patients to the centers. Typically, one or a few physicians' patients make up all or a significant portion of the patient base at each of our dialysis centers, and the loss of the patient base of one or more of these physicians could have a material adverse effect on the operations of that center. The loss of the patient base of a significant number of local physicians could cause our revenue and earnings to decline. In many instances, the primary referral sources for our centers are physicians who also serve as medical directors of our centers and may be shareholders. If the medical director relationship or stock ownership were found to violate applicable federal or state law, including fraud and abuse laws and laws prohibiting self-referrals, then the physicians acting as medical directors or owning our stock could be forced to stop referring patients to our centers.

A number of our medical director agreements will expire over the next three years, unless they are renewed or renegotiated. We did not renew or renegotiate a small number of our medical director agreements that expired in 2004, and we may not be able to renew or renegotiate expiring medical director agreements

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successfully, or we may not be able to enforce the non-competition provisions of some of our medical director or other agreements. Any of these factors could result in a loss of patients, since dialysis patients are typically treated at a center where their physician, or a member of his or her practice group serves as medical director. We believe that our future success will depend in part on our ability to attract and retain qualified physicians to serve as medical directors of our dialysis centers.

**The dialysis business is highly competitive. If we do not compete effectively in our markets, then we could lose market share and our rate of growth could slow.**

The dialysis industry is largely consolidated, and the consolidation trend continues as large providers acquire other providers. In December 2004, DaVita, Inc. and Gambro Healthcare, Inc. announced a definitive agreement under which DaVita will acquire Gambro's United States dialysis services business. If that transaction closes as agreed, then there will be three large dialysis companies (including Renal Care Group) that compete for the acquisition of outpatient dialysis centers and the development of relationships with referring physicians. The other two competitors will be significantly larger companies, which may enable them to pay more or otherwise compete more effectively for acquisitions. In addition, Fresenius Medical Care also manufactures dialysis equipment, which may allow them to benefit from lower equipment costs. We also face competition from new entrants into the market, including centers established by former medical directors or other referring physicians. We cannot assure you that we will be able to compete effectively with any of our competitors.

**If we are unable to make acquisitions in the future, then our rate of growth will slow.**

Much of our historical growth has come from acquisitions. Although we intend to continue to pursue growth through the acquisition of dialysis centers, we may be unable to identify and complete suitable acquisitions at prices we are willing to pay, or we may be unable to obtain the necessary financing. Further, due to the increased size of our business, the amount that acquired businesses contribute to our revenue and profits will continue to be smaller on a percentage basis. Also, as a result of consolidation in the dialysis industry, if DaVita's acquisition of Gambro is completed, we believe the three largest providers of outpatient dialysis services (including Renal Care Group) will own approximately 67% of the outpatient dialysis facilities in the United States. We compete with these other companies to identify and complete suitable acquisitions. We believe this competition has intensified in light of the smaller pool of available acquisition candidates and other market forces. As a result, we believe it will be more difficult for us to acquire suitable companies on favorable terms. Further, the businesses we acquire may not perform well enough to justify our investment. If we are unable to make additional acquisitions on suitable terms, then we may not meet our growth expectations.

**If we fail to integrate acquired companies, then we will be less profitable.**

We have grown significantly by acquisitions of other dialysis providers since our formation. We recently acquired dialysis programs in Cape Girardeau, Missouri; Lansing, Michigan; and Beaverton, Oregon. We intend to pursue acquisitions of more dialysis businesses in the future. We are unable to predict the number and size of any future acquisitions. We face significant challenges in integrating an acquired company's management and other personnel, clinical operations, and financial and operating systems with ours, often without the benefit of continued services from key personnel of the acquired company, particularly in larger acquisitions. We may be unable to integrate the businesses we acquire successfully or to achieve anticipated benefits from an acquisition in a timely manner, which could lead to substantial costs and delays or other operational, technical or financial problems, including diverting management's attention from our existing business. Any of these results could damage our profitability and our prospects for future growth.



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**If acquired businesses have unknown liabilities, then we could be exposed to liabilities that could harm our business and profitability.**

Businesses we acquire may have unknown or contingent liabilities, including liabilities for failure to comply with health care laws. Although we attempt to identify practices that may give rise to unknown or contingent liabilities and conform them to our standards after the acquisition, private plaintiffs or governmental agencies may still assert claims. Even though we generally seek to obtain indemnification from the sellers of businesses we buy, unknown and contingent liabilities may not be covered by indemnification or may exceed contractual limits or the financial capacity of the indemnifying party.

**We may not have sufficient cash flow from our business to pay our substantial debt.**

As of March 31, 2005, we had total consolidated debt of approximately \$500.5 million, including a \$22.9 million fair value premium on the 9.0% senior subordinated notes, and cash of approximately \$12.9 million. Also, subject to limitations, including those in our credit facility and those included in the indenture for the 9.0% senior subordinated notes we assumed in the NNA acquisition, we are not and will not be prohibited from incurring additional debt.

Due to the large amount of our consolidated debt, we may not generate enough cash from our operations to meet these obligations or to fund other liquidity needs. Our ability to generate cash in the future is, to some extent, subject to risks and uncertainties that are beyond our control, including those described in this Risk Factors section. If we are unable to meet our debt obligations, we may need to refinance all or a portion of our indebtedness, sell assets or raise funds in the capital markets. However, we cannot assure you that, if we are unable to pay our debt, we will be able to refinance it, obtain additional equity capital or sell assets, in each case on commercially reasonable terms, or at all, or otherwise be able to fund our liquidity needs.

If for any reason we are unable to meet our debt obligations, we would be in default under the terms of the agreements governing our outstanding debt. If such a default were to occur, the lenders under our credit facility could elect to declare all amounts outstanding under the credit facility immediately due and payable, and the lenders would not be obligated to continue to advance funds to us under our credit facility. In addition, if such a default were to occur, the 9.0% senior subordinated notes would become immediately due and payable. If these debt obligations are accelerated, we cannot assure you that our assets will be sufficient to repay the money we owe to banks and other debt holders.

**The large amount and terms of our outstanding debt may prevent us from taking actions we would otherwise consider in our best interest.**

The indenture governing our 9.0% senior subordinated notes and our credit facility contain numerous financial and operating covenants that limit our ability to engage in activities such as:

incurring additional debt;

acquiring and developing new dialysis centers;

making investments;

creating liens;

creating restrictions on the ability of our subsidiaries to pay dividends or other amounts to us;



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disposing of assets;

paying dividends on our capital stock;

repurchasing our capital stock;

engaging in transactions with our affiliates; or

consolidating, merging or selling all or substantially all of our assets.

Our credit facility also requires us to comply with financial covenants, including a net worth test, a leverage ratio test and a fixed charge coverage ratio test. Our ability to comply with these covenants may be affected by events beyond our control, including those described in this Risk Factors section. A breach of any of the covenants contained in our credit facility or our inability to comply with the required financial covenants could result in an event of default, which would allow the lenders under our credit facility to declare all borrowings outstanding to be due and payable, and triggering an event of default under the indenture governing our 9.0% senior subordinated notes. In addition, our lenders could require us to apply all of our available cash to repay our borrowings or they could prevent us from making debt service payments on our 9.0% senior subordinated notes. If the amounts outstanding under our credit facility or these notes are accelerated, we cannot assure you that our assets would be sufficient to repay in full the money we owe the banks and our other debt holders.

The large amount of our outstanding debt and the limitations our credit facility impose on us could have adverse consequences, including:

having to use much of our cash flow for scheduled debt service rather than for operations, future business opportunities or other purposes, such as funding working capital and capital expenditures;

being unable to increase our borrowings under our credit facility or obtain other debt financing for future working capital, capital expenditures, acquisitions or other corporate purposes;

being less able to take advantage of significant business opportunities, including acquisitions or divestitures;

difficulty satisfying our obligations under our 9.0% senior subordinated notes;

increasing our vulnerability to general adverse economic and industry conditions; and

causing us to be at a competitive disadvantage to competitors with less debt.

**If a change of control occurs, we may have to spend a substantial amount of cash or incur additional indebtedness to satisfy our obligation to repurchase our 9.0% senior subordinated notes from holders who choose to tender their notes pursuant to certain procedures in the indenture.**

Upon specified change of control events the holders of our 9.0% senior subordinated notes have the right to require us to repurchase all or any part (equal to \$1,000 or an integral multiple thereof) of the notes they hold at an offer price in cash equal to 101.0% of the aggregate principal amount of the notes plus accrued and unpaid

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interest thereon, if any, to the date of purchase. Should a change of control occur, we may be unable to pay the purchase price for all of the notes tendered for repurchase. Our failure to purchase tendered notes would constitute an event of default under the indenture governing the 9.0% senior subordinated notes, which would constitute a default under our credit facility. In addition, the terms of our credit facility restrict our ability to purchase the 9.0% senior subordinated notes. Future credit agreements or other agreements relating to debt may contain similar or more restrictive provisions. We may not be able to secure the consent of our lenders to repurchase the 9.0% senior subordinated notes or refinance the borrowings that prohibit us from repurchasing the notes. If we do not obtain consent or repay the borrowings, we would be unable to repurchase the notes.

Alternatively, even if we were able to pay the purchase price for the notes tendered for repurchase, we might have to use a substantial amount of cash to do so, which would deplete our funds to meet our other cash obligations or cause us to incur additional indebtedness to repurchase the notes.

These repurchase requirements may also delay or make it harder for others to obtain control of Renal Care Group.

**If our costs of insurance and claims increase, then our earnings could decrease.**

We currently maintain programs of general and professional liability insurance and directors and officers insurance with significant deductible or self-insured retention amounts on each claim. In addition, we generally self-insure our employee health plan and workers compensation program, while maintaining excess insurance for some very large claims. We have accepted higher deductibles and self-insurance exposure in each of the last several years to offset part of the increases in premiums for the programs. These deductibles and premiums increased substantially in 2002 and 2003. The rate of increase in deductibles and premiums moderated somewhat in 2004, but there were some increases, and there may be larger increases in the future. Our earnings could be materially and adversely affected by any of the following:

further increases in premiums, deductibles and self-insurance retentions;

increases in the number of liability claims against us or the cost of settling or trying cases related to those claims; and

an inability to obtain one or more types of insurance on acceptable terms.

**If our board of directors does not approve an acquisition or change in control, then our shareholders may not realize the full value of their stock.**

Our certificate of incorporation and bylaws contain a number of provisions that may delay, deter or inhibit a future acquisition or change in control that is not first approved by our board of directors. This could occur even if our shareholders receive an attractive offer for their shares or if a substantial number or even a majority of our shareholders believe the takeover is in their best interest. These provisions are intended to encourage any person interested in acquiring us to negotiate with and obtain approval from our board of directors before pursuing a transaction. Provisions that could delay, deter or inhibit a future acquisition or change in control include the following:

a staggered board of directors that would require two annual meetings to replace a majority of the board of directors;

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restrictions on calling special meetings at which an acquisition or change in control might be brought to a vote of the shareholders;

blank check preferred stock that may be issued by our board of directors without shareholder approval and that may be substantially dilutive or contain preferences or rights objectionable to an acquiror; and

a poison pill that would substantially dilute the interest sought by an acquiror.

These provisions could also discourage bids for our common stock at a premium and cause the market price of our common stock to decline.

### **Our stock price is volatile and as a result, the value of your investment may go down for reasons unrelated to the performance of our business.**

Our common stock is traded on the New York Stock Exchange. The market price of our common stock has been volatile, ranging from a low closing price of \$35.60 per share to a high closing price of \$40.00 per share for the three months ended March 31, 2005. The market price for our common stock could fluctuate substantially based on a variety of factors, including the following:

future announcements concerning us, our competitors or the health care market;

the threat, commencement or outcome of litigation or government investigation;

changes in government regulations; and

changes in earnings estimates by analysts.

Furthermore, stock prices for many companies fluctuate widely for reasons that may be unrelated to their operating results. These fluctuations, coupled with changes in demand or reimbursement levels for our services and general economic, political and market conditions, could cause the market price of our common stock to decline.

### **Forward-Looking Statements**

Some of the information in this quarterly report on Form 10-Q represents forward-looking statements that involve substantial risks and uncertainties. You can identify these statements by forward-looking words such as may, will, expect, anticipate, believe, intend, estimate and continue or similar words. You should read statements that contain these words carefully for the following reasons:

the statements discuss our future expectations;

the statements contain projections of our future earnings or of our financial condition; and

the statements state other forward-looking information.

We believe it is important to communicate our expectations to our investors. There may, however, be events in the future that we are not accurately able to predict or over which we have no control. The risk factors listed above, as well as any cautionary language in or incorporated by reference into this quarterly report on Form 10-Q, provide examples of risks, uncertainties and events that may cause our actual results to differ materially from the

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expectations we describe in our forward-looking statements. The SEC allows us to incorporate by reference the information we file with them, which means we can disclose important information to you by referring you to those documents. Before you invest in our common stock, you should be aware that the occurrence of any of the events described in the above risk factors, elsewhere in or incorporated by reference into this quarterly report on Form 10-Q and other events that we have not predicted or assessed could have a material adverse effect on our earnings, financial condition and business. If the events described above or other unpredicted events occur, then the trading price of our common stock could decline and you may lose all or part of your investment.

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**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The following discusses our exposure to market risk related to changes in interest rates.

**Cash balances**

We maintain all cash in United States dollars in highly liquid, interest-bearing, investment grade instruments with maturities of less than three months, which we consider cash equivalents; therefore, the Company has no market risk sensitive instruments.

**Outstanding debt**

As of March 31, 2005, we had outstanding debt of \$500.5 million, including a \$22.9 million fair value premium on the 9.0% senior subordinated notes. This debt consisted of \$308.8 million outstanding under the term facility in our 2004 credit agreement, \$182.6 million of indebtedness relating to the 9.0% senior subordinated notes due 2011 and approximately \$9.1 million outstanding under various capital leases and notes payable. Borrowings of \$158.8 million under the term loan bear interest at variable rates based on LIBOR rates or the prime rate that are determined by our leverage ratio. The remaining \$150.0 million under the term loan are fixed at a rate of 3.5% plus an additional spread based on the Company's leverage ratio under interest rate swap agreements that became effective on June 30, 2004. Our weighted average borrowing rate under the term loan as of March 31, 2005, was 4.7%. We expect this rate to rise in the future if interest rates rise on the portion that bears interest at floating rates. Outstanding senior subordinated notes bear nominal interest at 9.0% on the \$159.7 million outstanding face amount of the notes. The unamortized \$22.9 million fair value premium is being recognized over the life of the notes using the effective interest method and is recorded as a reduction to interest expense. Accordingly, the effective interest rate on the notes as of March 31, 2005 was 6.4%. At March 31, 2005, the fair value of our indebtedness under the credit facility and senior subordinated notes approximated carrying value. At the March 31, 2005 borrowing levels and giving effect to the impact of our interest rate swap agreements, if there had been a 1% increase in the variable interest rates, then our pre-tax income would have decreased by approximately \$420,000 for the three months ended March 31, 2005.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

(a) Our chief executive officer and chief financial officer evaluated our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the chief executive officer and chief financial officer have concluded that as of the end of the period covered by this report Renal Care Group maintains disclosure controls and procedures that are effective to provide reasonable assurance that information required to be disclosed in our reports under the Exchange Act is recorded, processed, summarized and reported within the periods specified in the SEC's rules and forms.

(b) There have been no changes in our internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably likely materially to affect, our internal control over financial reporting.

**Table of Contents****PART II OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS**

On October 25, 2004, the Company received a subpoena from the office of the United States Attorney for the Eastern District of New York. The subpoena requires the production of documents related to numerous aspects of the Company's business and operations, including those of RenaLab, Inc., the Company's laboratory. The subpoena includes specific requests for documents related to testing for parathyroid hormone (PTH) levels and vitamin D therapies. To the Company's knowledge no proceedings have been initiated against the Company at this time, although the Company cannot predict whether or when proceedings might be initiated. The Company intends to cooperate with the government's investigation.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

During the quarter ended March 31, 2005, we purchased shares of our common stock as part of a publicly announced program as follows:

<b>Period</b>	<b>Total Number of Shares Purchased</b>	<b>Average Price Paid per Share</b>	<b>Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs</b>
January 1, 2005 to January 31, 2005	252,000	\$ 37.21	252,000	\$ 68,364,671
February 1, 2005 to February 28, 2005				\$ 68,364,671
March 1, 2005 to March 31, 2005				\$ 68,364,671
<b>Total</b>	<b>252,000</b>	<b>\$ 37.21</b>	<b>252,000</b>	

The Registrant's share repurchase program was originally announced on October 2, 2000, and was amended by announcements on July 9, 2002, November 18, 2002, August 12, 2003 and October 28, 2003. The program permits repurchases of up to \$450.0 million of common stock. The program expires December 31, 2005. No share repurchase plan or program expired during the period covered by this quarterly report.

**ITEM 5. OTHER INFORMATION**

On February 3, 2005, the Company entered into an employment agreement with David M. Maloney, whereby Mr. Maloney was employed as Executive Vice President and Chief Information Officer of the Company effective as of that date for an initial term ending on December 31, 2007 (the Initial Period), subject to earlier termination by Mr. Maloney or the Company as provided in the agreement. The agreement automatically renews for additional

12-month terms unless either party provides notice of non-renewal. The base compensation under the agreement is \$300,000 per year and may be adjusted as provided for in the agreement. In addition, Mr. Maloney is entitled to an annual bonus of up to 75% of the base compensation for such year. The actual amount of the annual bonus paid will be determined based on the Company's and Mr. Maloney's achievement of performance goals reasonably established by the Compensation Committee. If the employment agreement is terminated by the Company without cause, or if Mr. Maloney terminates the agreement for good reason, as defined therein, then the Company will pay to Mr. Maloney, after the effective date of such termination, (1) an amount equal to (A) the base compensation (as then in effect) plus an amount of annual bonus equal to the target percentage of base compensation (as then in effect) multiplied by (B) two (or three if the termination occurs within 12 months following a Change in Control, as defined in the agreement), and (2) any unpaid bonus payable for the most recently completed calendar year. In addition, the employment agreement contains certain non-compete provisions during employment and for a period of 12 months thereafter within a 75-mile radius of any renal dialysis center, unit or facility owned or operated by the Company or an affiliate of the Company.

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**ITEM 6. EXHIBITS**

- 10.49 Employment Agreement, effective as of February 3, 2005, between the Company and David M. Maloney (incorporated by reference to Exhibit 10.49 to the Company's Annual Report on Form 10-K for the year ended December 31, 2004)
- 10.50 Supplemental Executive Retirement Plan for certain executive officers effective January 1, 2005
- 10.51 Limited Liability Company Agreement for Maumee Dialysis Services, LLC effective December 1, 2001
  - 10.51.1 Management Agreement dated December 1, 2001 between Maumee Dialysis Services, LLC and DMN of Indiana Corporation
  - 10.51.2 Amendment Number 1 to Limited Liability Company Agreement dated July 1, 2002 between Maumee Dialysis Services, LLC, RCG Indiana, LLC and Indiana Dialysis Management, P.C.
- 10.52 Limited Liability Company Agreement for Three Rivers Dialysis Services, LLC effective March 31, 2001
  - 10.52.1 Management Agreement dated March 31, 2001 between Three Rivers Dialysis Services, LLC and DMN of Indiana Corporation
  - 10.52.2 Amendment Number 1 to Limited Liability Company Agreement dated July 1, 2002 between Three Rivers Dialysis Services, LLC, RCG Indiana, LLC and Indiana Dialysis Management, P.C.
- 31.1 Certification pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1\* Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2\* Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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\* In accordance with Release No. 34-47551, this exhibit is furnished to the SEC as an accompanying document and is not deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that Section, and the document will not be deemed incorporated by reference into any filing under the Securities Act of 1933.

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**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

RENAL CARE GROUP, INC.  
(Registrant)

May 4, 2005

BY: /s/ David M. Dill  
David M. Dill  
Executive Vice President,  
Chief Financial Officer (Principal  
Financial Officer and Principal  
Accounting Officer)

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**RENAL CARE GROUP, INC.**

**EXHIBIT INDEX**

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