

LHC Group, Inc
Form 10-Q/A
August 08, 2007

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q/A
(Amendment No. 1)**

Quarterly report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2007

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _____ to _____

Commission file number: 0-8082

LHC GROUP, INC.

(Exact Name of Registrant as Specified in Charter)

**Delaware
(State or Other Jurisdiction of
Incorporation or Organization)**

**71-0918189
(I.R.S. Employer Identification No.)**

**420 West Pinhook Rd, Suite A
Lafayette, LA 70503**

(Address of principal executive offices including zip code)

(337) 233-1307

(Registrant's telephone number, including area code)

Indicate by check mark whether the issuer (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 a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated Filer Non-accelerated filer

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

Number of shares of common stock, par value \$0.01, outstanding as of May 3, 2007: 17,998,246 shares

**LHC GROUP, INC.
INDEX**

	Page
<u>Part I. Financial Information</u>	
<u>Explanatory Note</u>	ii
<u>Item 1. Financial Statements (unaudited)</u>	1
<u>Consolidated Balance Sheets March 31, 2007 (unaudited) (restated) and December 31, 2006</u>	1
<u>Consolidated Statements of Income (unaudited) Three months ended March 31, 2007 (restated) and 2006</u>	2
<u>Consolidated Statements of Cash Flows (unaudited) Three months ended March 31, 2007 (restated) and 2006</u>	3
<u>Notes to Consolidated Financial Statements (unaudited)</u>	4
<u>Item 4. Controls and Procedures</u>	17
<u>Signatures</u>	18
<u>EX-31.1 SECTION 302 CERTIFICATION OF THE CEO</u>	
<u>EX-31.2 SECTION 302 CERTIFICATION OF THE CFO</u>	
<u>EX-32 SECTION 906 CERTIFICATIONS OF THE CEO AND CFO</u>	

Table of Contents

EXPLANATORY NOTE

We are filing this Amendment No. 1 to Form 10-Q for the quarterly period ended March 31, 2007, as originally filed with the SEC on May 9, 2007, to restate our Consolidated Balance Sheet and Statements of Income and Cash Flows and corresponding financial information for the quarterly period ended March 31, 2007. These financial statements have been restated to include a contractual adjustment which reduces net service revenue \$783,000, and recognize the related income tax benefit of \$305,000.

In an effort to improve our processes and controls in billing and collections, during the second quarter of 2007 we engaged outside consulting expertise to evaluate the billing process related to the Long-Term Acute Care Hospitals (LTACHs). The review identified claims which had been collected, but had remaining claim amounts left on the books. In some cases, these remaining amounts related to contractual adjustments which had not been recorded or which had been incorrectly calculated and recorded at discharge. This information led management to determine that the Company had underestimated its revenue adjustments related to certain commercial payers in our LTACHs. Therefore the Company has made the following adjustment to the facility-based segment:

Increased the contractual adjustment in the first quarter by \$783,000 pre-tax which reduces net service revenue.

Pursuant to Rule 12b-15 under the Securities Exchange Act of 1934, as amended, the complete text of Item 1 and Item 4 of Part I is set forth below and Item 6 of Part II is amended to contain updated certifications from our Chief Executive Officer and Chief Financial Officer. This Amendment No. 1 continues to speak as of the date of the original Form 10-Q for the quarterly period ended March 31, 2007 and only reflects the changes to Part I and Part II discussed above. We have not updated or amended the disclosures contained herein to reflect events that have occurred since the filing of the Form 10-Q, or modified or updated those disclosures in any way other than as described above. Accordingly, this Amendment No. 1 should be read in conjunction with our filings made with the SEC subsequent to the filing of the original Form 10-Q on May 9, 2007.

Table of Contents**PART I**

FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS.
LHC GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	March 31, 2007 (unaudited) (as restated, see Note 1)	December 31, 2006
ASSETS		
Current assets:		
Cash	\$ 20,856	\$ 26,877
Receivables:		
Patient accounts receivable, less allowance for uncollectible accounts of \$7,378, and \$5,769 at March 31, 2007 and December 31, 2006, respectively	61,922	50,029
Other receivables	2,359	3,367
Employee receivables	134	34
Amounts due from governmental entities	2,518	2,518
	66,933	55,948
Deferred income taxes	2,953	1,935
Prepaid expenses and other current assets	3,133	4,120
Assets held for sale	374	1,171
Total current assets	94,249	90,051
Property, building, and equipment, net	12,006	11,705
Goodwill	44,913	39,681
Intangible assets, net	9,294	8,262
Other assets	3,559	2,995
Total assets	\$ 164,021	\$ 152,694

LIABILITIES AND STOCKHOLDERS EQUITY

Current liabilities:		
Accounts payable and other accrued liabilities	\$ 5,268	\$ 5,903
Salaries, wages, and benefits payable	12,835	10,572
Amounts due to governmental entities	3,162	3,223
Amounts payable under cooperative endeavor agreements	56	51
Income taxes payable	4,155	1,219
Current portion of capital lease obligations	164	211

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Current portion of long-term debt	430	428
Total current liabilities	26,070	21,607
Deferred income taxes, less current portion	2,525	2,104
Capital lease obligations, less current portion	128	147
Long-term debt, less current portion	3,010	3,051
Minority interests subject to exchange contracts and/or put options	285	317
Other minority interests	3,928	3,579
Stockholders' equity:		
Common stock \$0.01 par value: 40,000,000 shares authorized; 20,700,211 and 20,682,317 shares issued and 17,750,142 and 17,732,258 shares outstanding at March 31, 2007 and December 31, 2006, respectively	177	177
Treasury stock 2,950,059 shares at cost	(2,856)	(2,856)
Additional paid-in capital	80,639	80,273
Retained earnings	50,115	44,295
Total stockholders' equity	128,075	121,889
Total liabilities and stockholders' equity	\$ 164,021	\$ 152,694

See accompanying notes.

- 1 -

Table of Contents

LHC GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended March 31,	
	2007	2006
	(as restated, see Note 1)	
	(in thousands, except share and per share data)	
Net service revenue	\$ 69,251	\$ 46,468
Cost of service revenue	35,194	24,860
Gross margin	34,057	21,608
General and administrative expenses	23,038	15,247
Operating income	11,019	6,361
Interest expense	83	86
Non-operating income, including (gain) on sales of assets	(293)	(166)
Income from continuing operations before income taxes and minority interest and cooperative endeavor allocations	11,229	6,441
Income tax expense	3,634	1,697
Minority interest and cooperative endeavor allocations	1,807	995
Income from continuing operations	5,788	3,749
Gain (Loss) from discontinued operations (net of income taxes (benefit) of \$(2) and \$(129) in the three months ended March 31, 2007 and 2006, respectively)	(3)	(210)
Gain on sale of discontinued operations (net of income taxes of \$365 for the three months ended March 31, 2006)		597
Net income	5,785	4,136
Redeemable minority interests	35	843
Net income available to common stockholders	\$ 5,820	\$ 4,979
Earnings per share basic:		
Income from continuing operations	\$ 0.33	\$ 0.23
Gain (Loss) from discontinued operations, net		(0.01)
Gain on sale of discontinued operations, net		0.04
Net income	0.33	0.26
Redeemable minority interests		0.05
Net income available to common shareholders	\$ 0.33	\$ 0.31
Earnings per share diluted:		

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Income from continuing operations	\$	0.33	\$	0.23
Gain (Loss) from discontinued operations, net				(0.01)
Gain on sale of discontinued operations, net				0.04
Net income		0.33		0.26
Redeemable minority interests				0.05
Net income available to common shareholders	\$	0.33	\$	0.31

Weighted average shares outstanding:

Basic	17,748,369	16,557,828
Diluted	17,807,338	16,563,368

See accompanying notes.

- 2 -

Table of Contents

LHC GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three months Ended	
	March 31,	
	2007	2006
	(as	
	restated,	
	see	
	Note 1)	
	(in thousands)	
Operating activities		
Net income	\$ 5,785	\$ 4,136
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	710	532
Provision for bad debts	1,816	841
Stock-based compensation expense	227	96
Minority interest in earnings of subsidiaries	1,756	1,028
Deferred income taxes	(596)	(290)
Gain on divestitures and sale of assets		(963)
Changes in operating assets and liabilities, net of acquisitions:		
Receivables	(12,801)	(2,431)
Prepaid expenses, other assets	526	63
Accounts payable and accrued expenses	4,614	1,963
Net amounts due under cooperative endeavor agreements	5	23
Net amounts due governmental entities	(61)	598
Net cash provided by operating activities	1,981	5,596
Investing activities		
Purchases of property, building, and equipment	(716)	(991)
Proceeds from sale of entities		1,200
Cash paid for acquisitions, primarily goodwill and intangible assets	(5,865)	(3,269)
Net cash used in investing activities	(6,581)	(3,060)
Financing activities		
Principal payments on debt	(39)	(603)
Payments on capital leases	(66)	(109)
Proceeds from employee stock purchase plan	88	
Minority interest distributions, net	(1,404)	(1,089)
Net cash used in financing activities	(1,421)	(1,801)
Change in cash	(6,021)	735
Cash at beginning of period	26,877	17,398
Cash at end of period	\$ 20,856	\$ 18,133

Supplemental disclosures of cash flow information

Interest paid	\$ 83	\$ 86
Income taxes paid	\$ 1,240	\$ 105

See accompanying notes.

- 3 -

Table of Contents

LHC GROUP, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Organization

LHC Group, Inc. (the Company) is a healthcare provider specializing in the post-acute continuum of care primarily for Medicare beneficiaries in rural markets in the southern United States. The Company provides home-based services, primarily through home nursing agencies and hospices, and facility-based services, primarily through long-term acute care hospitals and outpatient rehabilitation clinics. As of the date of this report, the Company, through its wholly and majority-owned subsidiaries, equity joint ventures, and controlled affiliates, operated in Louisiana, Alabama, Arkansas, Mississippi, Texas, West Virginia, Kentucky, Florida, Georgia and Tennessee.

Unaudited Interim Financial Information

The consolidated balance sheet as of March 31, 2007 and the related consolidated statements of income and cash flows for the three months ended March 31, 2007 and 2006 and related notes (interim financial information) have been prepared by LHC Group, Inc. and are unaudited. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation in accordance with accounting principles generally accepted in the United States have been included. Operating results for the three months ended March 31, 2007 are not necessarily indicative of the results that may be expected for the year ended December 31, 2007.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted from the interim financial information presented. These consolidated financial statements should be read in conjunction with the notes to the consolidated financial statements included in the Company's Consolidated Financial Statements in the Company's Annual Report as filed with the Securities and Exchange Commission on Form 10-K for the year ended December 31, 2006, which includes information and disclosures not included herein.

Restatement of Financial Statements

Subsequent to the issuance of the Company's Quarterly Report on Form 10-Q for the period ended March 31, 2007, management determined that the accounting for certain contractual adjustments related to the commercial contracts in the LTACHs was in error. The Company previously disclosed in a Current Report on Form 8-K dated July 31, 2007, that it would restate its financial statements to correct the accounting for contractual adjustments. The effects of the restatement adjustments on the Company's originally reported results of operations for the three months ended March 31, 2007 are summarized below.

1. Consolidated Balance Sheet

- a. Patient accounts receivable decreased by \$783,000 which decreases Total current assets and Total assets by the same amount.
- b. Income taxes payable decreased by \$305,000 which decreases Total current liabilities by the same amount.
- c. Retained earnings decreased by \$478,000 which decreases Total stockholders' equity by the same amount.
- d. Total liabilities and stockholders' equity decreased by \$783,000.

2. Consolidated Statement of Income

- a. Net service revenue decreased by \$783,000 which decreases Gross margin, Operating income, and Income from continuing operations before income taxes and minority interest and cooperative endeavor allocations by the same amount.
- b. Income tax expense decreased by \$305,000.
- c.

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Income from continuing operations decreased \$478,000 which decreases Net income and Net income available to common stockholders by the same amount.

- d. Earnings per share decreased \$0.02 and fully diluted earnings per share decreased \$0.02.
- 3. Consolidated Statement of Cash Flows
 - a. Net income decreased by \$478,000.

- 4 -

Table of Contents

- b. Changes in operating assets and liabilities, net of acquisitions: Receivables decreased by \$783,000.
- c. Changes in operating assets and liabilities, net of acquisitions: Accounts payable and accrued expenses decreased by \$305,000.

2. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenue and expenses during the reported period. Actual results could differ from those estimates.

Critical Accounting Policies

The most critical accounting policies relate to the principles of consolidation, revenue recognition, accounts receivable and allowances for uncollectible accounts, and accounting for goodwill and intangible assets.

Principles of Consolidation

The consolidated financial statements include all subsidiaries and entities controlled by the Company. Control is generally defined by the Company as ownership of a majority of the voting interest of an entity. The consolidated financial statements include entities in which the Company absorbs a majority of any losses, receives a majority of any residual returns, or both, as a result of ownership, contractual or other financial interests in the entity.

All significant inter-company accounts and transactions have been eliminated in consolidation. Business combinations, which are accounted for as purchases, have been included in the consolidated financial statements from the respective dates of acquisition.

Table of Contents

The following describes the Company's consolidation policy with respect to its various ventures excluding wholly-owned subsidiaries:

Equity Joint Ventures

The Company's joint ventures are structured as limited liability companies in which the Company typically owns a majority equity interest ranging from 51% to 99%. Each member of all but one of the Company's equity joint ventures participates in profits and losses in proportion to their equity interests. The Company has one joint venture partner whose participation in losses is limited. The Company consolidates these entities as the Company absorbs a majority of any losses, receives a majority of any residual returns and generally has voting control over the entity.

Cooperative Endeavors

The Company has arrangements with certain partners that involve the sharing of profits and losses. Unlike the equity joint ventures, the Company owns 100% of the equity in these cooperative endeavors. In these cooperative endeavors, the Company possesses interests in the net profits and losses ranging from 67% to 70%. The Company has one cooperative endeavor partner whose participation in losses is limited. The Company consolidates these entities as the Company owns 100% of the outstanding equity and the Company absorbs a majority of any losses and receives a majority of any residual returns.

License Leasing Arrangements

The Company, through wholly-owned subsidiaries, leases home health licenses necessary to operate certain of its home nursing agencies. As with wholly-owned subsidiaries, the Company owns 100% of the equity of these entities and consolidates them based on such ownership as well as the Company's right to receive a majority of any residual returns and the Company's obligation to absorb a majority of any losses.

Management Services

The Company has various management services agreements under which the Company manages certain operations of agencies and facilities. The Company does not consolidate these agencies or facilities, as the Company does not have an ownership interest and does not have a right to receive a majority of any residual returns or an obligation to absorb a majority of any losses.

The following table summarizes the percentage of net service revenue earned by type of ownership or relationship the Company had with the operating entity:

	Three Months Ended March 31,	
	2007	2006
Wholly-owned subsidiaries	45.2%	38.3%
Equity joint ventures	41.1	47.5
Cooperative endeavors	1.2	1.7
License leasing arrangements	9.7	11.1
Management services	2.8	1.4
	100.0%	100.0%

Revenue Recognition

The Company reports net service revenue at the estimated net realizable amount due from Medicare, Medicaid, commercial insurance, managed care payors, patients, and others for services rendered. Under Medicare, the Company's home nursing patients are classified into a group referred to as a home health resource group prior to the receipt of services. Based on this home health resource group, the Company is entitled to receive a prospective Medicare payment for delivering care over a 60-day period referred to as an episode. Medicare adjusts these prospective payments based on a variety of factors, such as low utilization, patient transfers, changes in condition and the level of services provided. In calculating the Company's reported net service revenue from home nursing services, the Company adjusts the prospective Medicare payments by an estimate of the adjustments. The Company calculates the adjustments based on a historical average of these types of adjustments. For home nursing services, the Company

recognizes revenue based on the number of days elapsed during the episode of care.

- 6 -

Table of Contents

For the Company's long-term acute care hospitals, revenue is recognized as services are provided. Under Medicare, patients in the Company's long-term acute care facilities are classified into long-term diagnosis-related groups. Based on this classification, the Company is then entitled to receive a fixed payment from Medicare. This fixed payment is also subject to adjustment by Medicare due to factors such as short stays. In calculating reported net service revenue for services provided in the Company's long-term acute care hospitals, the Company reduces the prospective payment amounts by an estimate of the adjustments. The Company calculates the adjustment based on a historical average of these types of adjustments for claims paid.

For hospice services, the Company is paid by Medicare under a per diem payment system. The Company receives one of four predetermined daily or hourly rates based upon the level of care the Company furnished. The Company records net service revenue from hospice services based on the daily or hourly rate. The Company recognizes revenue for hospice as services are provided.

Under Medicare, the Company is reimbursed for rehabilitation services based on a fee schedule for services provided adjusted by the geographical area in which the facility is located. The Company recognizes revenue as these services are provided.

The Company's Medicaid reimbursement is based on a predetermined fee schedule applied to each service provided. Therefore, revenue is recognized for Medicaid services as services are provided based on this fee schedule. The Company's managed care payors reimburse the Company under the terms of the related contracts. Accordingly, the Company recognizes revenue from managed care payors consistent with those terms.

The Company records management services revenue as services are provided in accordance with the various management services agreements to which the Company is a party. The agreements generally call for the Company to provide billing, management, and other consulting services suited to and designed for the efficient operation of the applicable home nursing agency, hospice, or inpatient rehabilitation facility. The Company is responsible for the costs associated with the locations and personnel required for the provision of the services. The Company is generally compensated based on a percentage of net billings or an established base fee. In addition, for certain of the management agreements, the Company may earn incentive compensation.

Net service revenue was comprised of the following:

	Three Months Ended March 31,	
	2007	2006
Home-based services	79.5%	69.8%
Facility-based services	20.5	30.2
	100.0%	100.0%

The following table sets forth the percentage of net service revenue earned by category of payor:

	Three Months Ended March 31,	
	2007	2006
Payor:		
Medicare	81.7%	86.1%
Medicaid	6.1	5.2
Other	12.2	8.7
	100.0%	100.0%

Home-Based Services

Home Nursing Services. The Company receives a standard prospective Medicare payment for delivering care. The base payment, established through federal legislation, is a flat rate that is adjusted upward or downward based upon differences in the expected resource needs of individual patients as indicated by clinical severity, functional severity, and service utilization. The magnitude of the adjustment is determined by each patient's categorization into one of 80 payment groups, known as home health resource groups, and the costliness of care for patients in each group relative to the average patient. The Company's payment is also adjusted for differences in local prices using the hospital wage index. The Company performs payment variance analyses to verify the models utilized in projecting total net service revenue are accurately reflecting the payments to be received.

- 7 -

Table of Contents

Medicare rates are subject to change. Due to the length of the Company's episodes of care, a situation may arise where Medicare rate changes affect a prior period's net service revenue. In the event that Medicare rates experience change, the net effect of that change will be reflected in the current reporting period.

Final payments from Medicare may reflect one of five retroactive adjustments to ensure the adequacy and effectiveness of the total reimbursement: (a) an outlier payment if the patient's care was unusually costly; (b) a low utilization adjustment if the number of visits was fewer than five; (c) a partial payment if the patient transferred to another provider before completing the episode; (d) a change-in-condition adjustment if the patient's medical status changes significantly, resulting in the need for more or less care; or (e) a payment adjustment based upon the level of therapy services required in the population base. Management estimates the impact of these payment adjustments based on historical experience and records this estimate during the period the services are rendered.

Hospice Services. The Company's Medicare hospice reimbursement is based on an annually-updated prospective payment system. Hospice payments are also subject to two caps. One cap relates to individual programs receiving more than 20% of their total Medicare reimbursement from inpatient care services. The second cap relates to individual programs receiving reimbursements in excess of a cap amount, calculated by multiplying the number of beneficiaries during the period by a statutory amount that is indexed for inflation. The determination for each cap is made annually based on the 12-month period ending on October 31 of each year. This limit is computed on a program-by-program basis. None of the Company's hospices exceeded either cap during the three months ended March 31, 2007 or 2006.

Facility-Based Services

Long-Term Acute Care Services. The Company is reimbursed by Medicare for services provided under the long-term acute care hospital prospective payment system, which was implemented on October 1, 2002. Each patient is assigned a long-term care diagnosis-related group. The Company is paid a predetermined fixed amount applicable to that particular group. This payment is intended to reflect the average cost of treating a Medicare patient classified in that particular long-term care diagnosis-related group. For selected patients, the amount may be further adjusted based on length of stay and facility-specific costs, as well as in instances where a patient is discharged and subsequently readmitted, among other factors. Similar to other Medicare prospective payment systems, the rate is also adjusted for geographic wage differences.

Outpatient Rehabilitation Services. Outpatient therapy services are reimbursed on a fee schedule, subject to annual limitations. Outpatient therapy providers receive a fixed fee for each procedure performed, adjusted by the geographical area in which the facility is located. The Company recognizes revenue as the services are provided. There are also annual per Medicare beneficiary caps that limit Medicare coverage for outpatient rehabilitation services.

Accounts Receivable and Allowances for Uncollectible Accounts

The Company reports accounts receivable net of estimated allowances for uncollectible accounts and adjustments. Accounts receivable are uncollateralized and primarily consist of amounts due from third-party payors and patients. To provide for accounts receivable that could become uncollectible in the future, the Company establishes an allowance for uncollectible accounts to reduce the carrying amount of such receivables to their estimated net realizable value. The credit risk for other concentrations of receivables is limited due to the significance of Medicare as the primary payor. The Company does not believe that there are any other significant concentrations of receivables from any particular payor that would subject it to any significant credit risk in the collection of accounts receivable.

The amount of the provision for bad debts is based upon the Company's assessment of historical and expected net collections, business and economic conditions, and trends in government reimbursement. Uncollectible accounts are written off when the Company has determined the account will not be collected.

A portion of the estimated Medicare prospective payment system reimbursement from each submitted home nursing episode is received in the form of a request for accelerated payment (RAP). The Company submits a RAP for 60% of the estimated reimbursement for the initial episode at the start of care. The full amount of the episode is billed after the episode has been completed. The RAP received for that particular episode is deducted from the final payment. If a final bill is not submitted within the greater of 120 days from the start of the episode, or 60 days from the date the RAP was paid, any RAPs received for that episode will be recouped by Medicare from any other claims

Table of Contents

in process for that particular provider. The RAP and final claim must then be re-submitted. For any subsequent episodes of care contiguous with the first episode for a particular patient, the Company submits a RAP for 50% instead of 60% of the estimated reimbursement. The Company has earned net service revenue in excess of billings rendered to Medicare. Only a nominal portion of the amounts due to the Medicare program represent cash collected in advance of providing services.

Our Medicare population is paid at a prospectively set amount that can be determined at the time services are rendered. Our Medicaid reimbursement is based on a predetermined fee schedule applied to each individual service we provide. Our managed care contracts are structured similar to either the Medicare or Medicaid payment methodologies. Because of our payor mix, we are able to calculate our actual amount due at the patient level and adjust the gross charges down to the actual amount at the time of billing. This negates the need for an estimated contractual allowance to be booked at the time we report net service revenue for each reporting period.

At March 31, 2007, our allowance for uncollectible accounts, as a percentage of patient accounts receivable, was approximately 10.5%. For the three months ended March 31, 2007, the provision for doubtful accounts increased to 2.6% of net service revenue compared to 1.8% of net service revenue for the same period in 2006. Adverse changes in general economic conditions, billing operations, payor mix, or trends in federal or state governmental coverage could affect our collection of accounts receivable, cash flows and results of operations.

The following table sets forth our aging of accounts receivable (based on the billing date) as of March 31, 2007:

Payor	0-30	31-60	61-90	91-120	121-150	151+	Total
				(in thousands)			
Medicare	\$ 20,383	\$ 4,736	\$ 2,548	\$ 1,202	\$ 1,888	\$ 9,103	\$ 39,860
Medicaid	1,348	1,512	543	377	640	3,921	8,341
Other	4,745	3,049	1,822	695	1,297	9,491	21,099
Total	\$ 26,476	\$ 9,297	\$ 4,913	\$ 2,274	\$ 3,825	\$ 22,515	\$ 69,300

Goodwill and Intangible Assets

Goodwill and other intangible assets with indefinite lives are reviewed annually for impairment or more frequently if circumstances indicate impairment may have occurred.

The Company estimates the fair value of its identified reporting units and compares those estimates against the related carrying value. For each of the reporting units, the estimated fair value is determined based on a multiple of earnings before interest, taxes, depreciation, and amortization or on the estimated fair value of assets in situations when it is readily determinable.

Included in intangible assets, net are other intangible assets such as licenses to operate home-based and/or facility-based services and trade names. The Company has valued these intangible assets separately from goodwill for each acquisition completed after January 1, 2006. The Company has concluded that these licenses and trade names have indefinite lives, as management has determined that there are no legal, regulatory, contractual, economic or other factors that would limit the useful life of these intangible assets and the Company intends to renew and operate the licenses and use these trade names indefinitely. Prior to January 1, 2006, the Company elected to recognize the fair value of indefinite-lived licenses and trade names together with goodwill as a single asset for financial reporting purposes.

Components of the Company's home nursing operating segment are generally represented by individual subsidiaries or joint ventures with individual licenses to conduct specific operations within geographic markets as limited by the terms of each license. Components of the Company's facility-based services are represented by individual operating entities. Effective January 1, 2004, management aggregates the components of these two segments into two reporting units for purposes of evaluating impairment.

Other Significant Accounting Policies***Due to/from Governmental Entities***

The Company's critical access hospital and long-term acute care hospitals are reimbursed for certain activities based on tentative rates. Final reimbursement is determined based on submission of annual cost reports and audits

Table of Contents

by the fiscal intermediary. Adjustments are accrued on an estimated basis in the period the related services are rendered and further adjusted as final settlements are determined. These adjustments are accounted for as changes in estimates. There have been no significant changes in estimates during the three months ended March 31, 2007 and 2006.

Property, Building, and Equipment

Property, building, and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the individual assets, generally ranging from three to ten years and up to thirty-nine years on buildings. Depreciation expense for the three months ended March 31, 2007 and 2006 was \$710,000 and \$532,000, respectively.

Capital leases are included in equipment. Capital leases are recorded at the present value of the future rentals at lease inception and are amortized over the shorter of the applicable lease term or the useful life of the equipment. Amortization of assets under the capital lease obligations is included in depreciation and amortization expense.

Long-Lived Assets

The Company reviews the recoverability of long-lived assets whenever events or circumstances occur which indicate recorded costs may not be recoverable. If the expected future cash flows (undiscounted) are less than the carrying amount of such assets, the Company recognizes an impairment loss for the difference between the carrying amount of the assets and their estimated fair value.

Income Taxes

The Company accounts for income taxes using the liability method. Under the liability method, deferred taxes are determined based on differences between the financial reporting and tax bases of assets and liabilities, and are measured using the enacted tax laws that will be in effect when the differences are expected to reverse. Management provides a valuation allowance for any net deferred tax assets when it is more likely than not that a portion of such net deferred tax assets will not be recovered.

Minority Interest and Cooperative Endeavor Agreements

The interest held by third parties in subsidiaries owned or controlled by the Company is reported on the consolidated balance sheets as minority interest. Minority interest reported in the consolidated statements of income reflects the respective interests in the income or loss of the subsidiaries attributable to the other parties, the effect of which is removed from the Company's consolidated results of operations.

Several of the Company's home health agencies have cooperative endeavor agreements with third parties that allow the third parties to be paid or recover a fee based on the profits or losses of the respective agencies. The Company accrues for the settlement of the third party's profits or losses during the period the amounts are earned. Under the agreements, the Company has incurred net amounts due to the third parties of \$56,000 and \$65,000 for the three months ended March 31, 2007 and 2006, respectively. The cooperative endeavor agreements have terms expiring at the end of June 2008.

For agreements where the third party is a healthcare institution, the agreements typically require the Company to lease building and equipment and receive housekeeping and maintenance from the healthcare institutions. Ancillary services related to these arrangements are also typically provided by the healthcare institution.

Minority Interest Subject to Exchange Contracts and/or Put Options

The Company has a put option agreement with the minority interest holders of a majority-owned subsidiary, St. Landry Extended Care Hospital, LLC (St. Landry), which allows the minority interest holders to redeem their minority interests for cash. As of March 31, 2007, approximately 76.5% of the doctors have converted their minority interests to cash.

There were no redemptions in the three months ended March 31, 2007. In the three months ended March 31, 2007, the Company recorded a mark-to-market charge of \$35,000 for these redeemable minority interests. Included

Table of Contents

in minority interests subject to exchange contracts and/or put options liability at March 31, 2007 and December 31, 2006 is \$279,000 and \$314,000, respectively, related to these redeemable minority interests.

Stock-based Compensation

The Company has two stock option plans that are administered by the Compensation Committee of the Board of Directors, which selects persons eligible to receive awards and determines the number of shares and/or options subject to each award, the terms, conditions, performance measures and other provisions of the award. Readers should refer to note 6 of the Company's consolidated financial statements in its Annual Report on Form 10-K for the year ended December 31, 2006 for additional information related to these stock-based compensation plans.

The Company accounts for its stock-based compensation plans using the fair value recognition provisions of Statement of Financial Accounting Standards.

Earnings Per Share

Basic per share information is computed by dividing the item by the weighted-average number of shares outstanding during the period. Diluted per share information is computed by dividing the item by the weighted-average number of shares outstanding plus dilutive potential shares.

The following table sets forth shares used in the computation of basic and diluted per share information:

	Three Months Ended	
	March 31,	
	2007	2006
Weighted average number of shares outstanding for basic per share calculation	17,748,369	16,557,828
Effect of dilutive potential shares:		
Options	4,789	940
Restricted stock	54,180	4,600
Adjusted weighted average shares for diluted per share calculation	17,807,338	16,563,368

Recently Issued Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157), which defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements. SFAS No. 157 will be effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the requirements of this new standard and has not concluded its analysis on the impact to the Company's consolidated financial position or results of operations.

In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting (SFAS) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment to FASB Statement No. 115* (SFAS No. 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The Company is currently evaluating the requirements of this new standard and has not concluded its analysis on the impact to the Company's consolidated financial position or results of operations.

3. Acquisitions and Divestitures

The following acquisitions were completed pursuant to the Company's strategy of becoming the leading provider of post-acute healthcare services to Medicare patients in selected rural markets in the southern United States. The purchase price of each acquisition was determined based on the Company's analysis of comparable acquisitions and target market's potential cash flows. Goodwill generated from the acquisitions was recognized based on the expected contributions of each acquisition to the overall corporate strategy. The Company expects the goodwill recognized in connection with the acquisition of existing operations to be fully tax deductible.

Table of Contents*2007 Acquisitions*

During the three month period ended March 31, 2007, the Company acquired the existing operations of four entities for \$5,298,000 in cash and \$439,000 in acquisition costs. Goodwill of \$4.8 million and other intangibles of \$1.0 million were assigned to the home based services segment.

2007 Divestitures

The Company has reclassified the operations of one long-term acute care hospital out of discontinued operations in the three months ended March 31, 2007 and 2006. The facility had previously been identified as held for sale and accounted for in discontinued operations throughout the year ended December 31, 2006. Goodwill of \$402,000 and other assets related to this hospital were classified as assets held for sale at December 31, 2006. The operating results for the three months ended March 31, 2006, previously disclosed in discontinued operations, have been reclassified to continuing operations in the statement of income.

The Company has identified one pharmacy operation as held for sale as of March 31, 2007. The assets related to this operation are classified as assets held for sale on the balance sheet.

The following table summarizes the operating results of divestitures which have been presented as loss from discontinued operations in the accompanying consolidated statements of income:

	Three Months Ended March 31,	
	2007	2006
Net service revenue	\$ 542	\$ 1,594
Costs, expenses and minority interest and cooperative endeavor allocations	547	1,933
Gain (Loss) from discontinued operations before income taxes	(5)	(339)
Income taxes (benefit)	(2)	(129)
Gain (Loss) from discontinued operations	\$ (3)	\$ (210)

The changes in recorded goodwill by segment for the three month period ended March 31, 2007 were as follows:

	Three months Ended March 31, 2007 (in thousands)	
Home-based services segment:		
Balance at December 31, 2006	\$	35,740
Goodwill acquired during the period from acquisitions		4,830
Balance at March 31, 2007	\$	40,570
Facility-based services segment:		
Balance at December 31, 2006	\$	3,941
Goodwill classified as held for sale at December 31, 2006		402
Balance at March 31, 2007	\$	4,343

The above transactions were considered to be immaterial individually and in the aggregate. Accordingly, no supplemental pro forma information is required.

- 12 -

Table of Contents**4. Credit Arrangements****Long-Term Debt**

Long-term debt consisted of the following:

	March 31, 2007	December 31, 2006
	(in thousands)	
Notes payable:		
Due in yearly installments of \$50,000 through August 2010 at 6.25%	\$ 190	\$ 190
Due in monthly installments of \$20,565 through October 2015 at LIBOR plus 225 basis points (7.57% at March 31, 2007)	2,891	2,898
Due in monthly installments of \$12,500 through November 2009 at 3.08%	359	391
	3,440	3,479
Less current portion of long-term debt	430	428
	\$ 3,010	\$ 3,051

In August 2005, the Company entered into a promissory note with Bancorp Equipment Finance, Inc. to purchase an airplane, for a principal amount of \$2,975,000 with interest on any outstanding principal balance at the one month LIBOR rate plus 225 basis points (7.57% at March 31, 2007). The note is collateralized by the Company's airplane and is payable in 119 monthly installments of \$20,565 followed by one balloon installment in the amount of \$1,920,565.

In August 2005, the Company entered into a promissory note with the seller of A-1 Nursing Registry, Inc. (A-1) in conjunction with the purchase of the assets of A-1. The principal amount of the note is \$250,000 and it bears interest at 6.25%.

Certain of the Company's loan agreements contain certain restrictive covenants, including limitations on indebtedness and the maintenance of certain financial ratios. At March 31, 2007 and at December 31, 2006, the Company was in compliance with all covenants.

Other Credit Arrangements

The Company maintains a revolving-debt arrangement. Under the terms of this arrangement, the Company may be advanced funds up to a defined limit of eligible accounts receivable not to exceed the borrowing limit. At March 31, 2007 and December 31, 2006, the borrowing limit was \$22,500,000, and no amounts were outstanding. Interest accrues on any outstanding amounts at a varying rate and is based on the Wells Fargo Bank, N.A. prime rate plus 1.5% (9.75% at March 31, 2007). The annual facility fee is 0.5% of the total availability. The agreement expires on April 15, 2010.

5. Income Taxes

The Company adopted the provisions of FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes (FIN 48) effective January 1, 2007. The adoption did not have a material effect on the consolidated financial position or results of operations of the Company. At the date of adoption, the Company had no unrecognized tax benefits. The Company recognizes interest and penalties related to uncertain tax positions in interest expense and general and administrative expenses, respectively. As of March 31, 2007, there were no accrued interest or penalties relating to unrecognized income tax benefits recognized in the statement of operations. There was no accrued liability for interest or penalties related to unrecognized income tax benefits recognized in the statement of financial position at March 31, 2007.

The Company is subject to both federal and state income tax for jurisdictions within which it operates. Within these jurisdictions, the Company is open to examination for tax years ended after December 31, 2002.

Table of Contents**6. Stockholders Equity**

The following table summarizes the activity in stockholders equity for the three month period ended March 31, 2007 (amounts in thousands, except per share data):

	Common Stock		Treasury		Additional Paid-In Capital	Retained Earnings	Total
	Amount	Issued Shares	Amount	Shares			
Balances at December 31, 2006	\$ 177	20,682,317	\$(2,856)	2,950,059	\$ 80,273	\$ 44,295	\$ 121,889
Net income						5,785	5,785
Issuance of 1,167 shares of vested restricted stock		1,167			33		33
Nonvested stock compensation					194		194
Issuance of vested restricted stock		13,477					
Excess tax benefits from issuance of nonvested stock					51		51
Issuance of common stock under Employee Stock Purchase Plan		3,240			88		88
Recording minority interest in joint venture at redemption value						35	35
Balances at March 31, 2007	\$ 177	20,700,201	\$(2,856)	2,950,059	\$ 80,639	\$ 50,115	\$ 128,075

Share Based Compensation

On January 20, 2005, the board of directors and stockholders of the Company approved the 2005 Long Term Incentive Plan (the Incentive Plan). The Incentive Plan provides for 1,000,000 shares of common stock that may be issued or transferred pursuant to awards made under the plan. A variety of discretionary awards for employees, officers, directors and consultants are authorized under the Incentive Plan, including incentive or non-qualified statutory stock options and restricted stock. All awards must be evidenced by a written award certificate which will include the provisions specified by the compensation committee of the board of directors. The compensation committee will determine the exercise price for non-statutory stock options. The exercise price for any option cannot be less than the fair market value of our common stock as of the date of grant.

Also on January 20, 2005, the 2005 Director Compensation Plan was adopted. The shares issued under our 2005 Director Compensation Plan are issued from the 1,000,000 shares reserved for issuance under our Incentive Plan.

Stock Options

At March 31, 2007, 21,000 options were issued and exercisable. No options were exercised or forfeited during the three months ended March 31, 2007. There were no options granted during the three months ended March 31, 2007. There were no options exercised, forfeited or granted during the three month period ended March 31, 2006.

Nonvested Stock

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During the three months ended March 31, 2007, 12,600 nonvested shares of stock were granted to our independent directors under the 2005 Director Compensation Plan. Of these 12,600 shares, 9,100 shares vest in one year, while the remaining 3,500 shares vest one third immediately, and the remaining two-thirds vest over the two year period following the grant date. During the three months ended March 31, 2007, 109,425 nonvested shares were granted to employees pursuant to the 2005 Long-Term Incentive Plan. Of these 109,425 shares, 2,000 shares vest over a three year period while the remaining 107,425 shares vest over a five year period. The fair value of nonvested shares is determined based on the closing trading price of the Company's shares on the grant date. The weighted average grant date fair values of nonvested shares granted during the three month period ended March 31, 2007 were \$30.30.

- 14 -

Table of Contents

The following table represents the nonvested stock activity for the three months ended March 31, 2007:

	Number of Shares	Weighted average grant date fair value
Nonvested shares outstanding at December 31, 2006	86,716	\$ 18.29
Granted	122,025	30.30
Vested	(14,644)	18.96
Forfeited		
Nonvested shares outstanding at March 31, 2007	194,097	\$ 25.58

As of March 31, 2007, there was \$4.8 million of total unrecognized compensation cost related to nonvested shares granted. That cost is expected to be recognized over the weighted average period of 4.1 years. The total fair value of shares vested in the three month periods ended March 31, 2007 was \$397,000. No shares vested in the three months ended March 31, 2006. The Company records compensation expense related to nonvested share awards at the grant date for shares that are awarded fully vested, and over the vesting term on a straight line basis for shares that vest over time. The Company has recorded \$227,000 and \$96,000 in compensation expense related to nonvested stock grants in the periods ended March 31, 2007 and 2006 respectively.

Employee Stock Purchase Plan

The Company has a plan whereby eligible employees may purchase the Company's common stock at 95% of the market price on the last day of the calendar quarter. There are 250,000 shares reserved for the plan. The Company issued 3,240 shares of common stock under the plan at a per share price of \$27.08 during the three months ended March 31, 2007. At March 31, 2007 there were 239,664 shares available for future issuance.

7. Commitments and Contingencies**Contingencies**

The terms of several joint venture operating agreements grant a buy/sell option that would require the Company to either purchase or sell the existing membership interest in the joint venture within 30 days of the receipt of the notice to exercise the provision. Either the Company or its joint venture partner has the right to exercise the buy/sell option. The party receiving the exercise notice has the right to either purchase the interests held by the other party or sell its interests to the other party. The purchase price formula for the interests is set forth in the joint venture agreement and is typically based on a multiple of the earnings before income taxes, depreciation and amortization of the joint venture. Total revenue earned by the Company from joint ventures subject to these arrangements was \$3.8 million and \$3.5 million for the three months ended March 31, 2007 and 2006, respectively. The Company has not received notice from any joint venture partners of their intent to exercise the buy/sell option nor has the Company notified any joint venture partners of any intent to exercise the buy/sell option.

The Company is involved in various legal proceedings arising in the ordinary course of business. Although the results of litigation cannot be predicted with certainty, management believes the outcome of pending litigation will not have a material adverse effect, after considering the effect of the Company's insurance coverage, on the Company's consolidated financial statements.

Compliance

The laws and regulations governing the Company's operations, along with the terms of participation in various government programs, regulate how the Company does business, the services offered, and interactions with patients and the public. These laws and regulations, and their interpretations, are subject to frequent change. Changes in existing laws or regulations, or their interpretations, or the enactment of new laws or regulations could materially and adversely affect the Company's operations and financial condition.

The Company is subject to various routine and non-routine governmental reviews, audits, and investigations. In recent years, federal and state civil and criminal enforcement agencies have heightened and coordinated their oversight efforts related to the healthcare industry, including with respect to referral practices, cost reporting, billing practices, joint ventures, and other financial relationships among healthcare providers. Violation of the laws governing the Company's operations, or changes in the interpretation of those laws, could result in the imposition of

Table of Contents

finances, civil or criminal penalties, termination of the Company's rights to participate in federal and state-sponsored programs, and suspension or revocation of the Company's licenses.

If the Company's long-term acute care hospitals fail to meet or maintain the standards for Medicare certification as long-term acute care hospitals, such as average minimum length of patient stay, they will receive payments under the prospective payment system applicable to general acute care hospitals rather than payment under the system applicable to long-term acute care hospitals. Payments at rates applicable to general acute care hospitals would likely result in the Company receiving less Medicare reimbursement than currently received for patient services. Moreover, all of the Company's long-term acute care hospitals are subject to additional Medicare criteria because they operate as separate hospitals located in space leased from, and located in, a general acute care hospital, known as a host hospital. This is known as a "hospital within a hospital" model. These additional criteria include requirements concerning financial and operational separateness from the host hospital.

The Company anticipates there may be changes to the standard episode-of-care payment from Medicare in the future. Due to the uncertainty of the revised payment amount, the Company cannot estimate the impact that changes in the payment rate, if any, will have on its future financial statements. In August 2004, the Centers for Medicare and Medicaid Services, or CMS, adopted new regulations that implement significant changes affecting long-term acute care hospitals. Among other things, these new regulations, which became effective in October 2004, implemented new rules that provide long-term acute care hospitals operating in the hospital within a hospital model with lower rates of reimbursement for Medicare admissions from their host hospitals that are in excess of specified percentages.

These new rules also reclassified certain long-term acute care hospital diagnosis related groups, which could result in a decrease in reimbursement rates. Further, the new rules kept in place the financial penalties associated with the failure to limit to 5% the total number of Medicare patients discharged to the host hospital and subsequently readmitted to a long-term acute care hospital located within the host hospital.

The Company believes that it is in material compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such 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 program.

Table of Contents**8. Segment Information**

The Company's segments consist of (a) home-based services and (b) facility-based services. Home-based services include home nursing services and hospice services. Facility-based services include long-term acute care services and outpatient rehabilitation services. The accounting policies of the segments are the same as those described in the summary of significant accounting policies.

	Three Months Ended March 31, 2007 (as restated)		
	Home-Based Services	Facility-Based Services (in thousands)	Total
Net service revenue	\$ 55,066	\$ 14,185	\$ 69,251
Cost of service revenue	26,028	9,166	35,194
General and administrative expenses	17,835	5,203	23,038
Operating income (loss)	11,203	(184)	11,019
Interest expense	54	29	83
Non-operating income, including gain on sale of assets	(204)	(89)	(293)
Income from continuing operations before income taxes and minority interest and cooperative endeavor allocations	11,353	(124)	11,229
Minority interest and cooperative endeavor allocations	1,421	386	1,807
Income (loss) from continuing operations before income taxes	9,932	(510)	9,422
Total assets	\$ 128,165	\$ 35,856	\$ 164,021

	Three Months Ended March 31, 2006		
	Home-Based Services	Facility-Based Services (in thousands)	Total
Net service revenue	\$ 32,421	\$ 14,047	46,468
Cost of service revenue	16,233	8,627	24,860
General and administrative expenses	11,321	3,926	15,247
Operating income	4,867	1,494	6,361
Interest expense	54	32	86
Non-operating income, including gain on sale of assets	(111)	(55)	(166)
Income from continuing operations before income taxes and minority interest and cooperative endeavor allocations	4,924	1,517	6,441
Minority interest and cooperative endeavor allocations	557	438	995
Income from continuing operations before income taxes	4,367	1,079	5,446
Total assets	\$ 76,185	\$ 33,952	\$ 110,137

Table of Contents

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

On March 31, 2007, LHC Group, Inc. (the Company) management, including the Company s principal executive and principal financial officers, evaluated the Company s disclosure controls and procedures and concluded that its disclosure controls and procedures were effective. Subsequent to that date and in connection with the filing of this Amendment No. 1 to the Company s Form 10-Q to restate the Company s financial statements and corresponding financial information for the three months ended March 31, 2007, the Company s management re-evaluated the effectiveness of the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of March 31, 2007. As a result of a material weakness in internal control over financial reporting related to the Company s procedure for recording contractual adjustments related to commercial contracts in the Long-Term Acute Care Hospitals (LTACH), the Company s management, including the Company s principal executive and principal financial officers, has concluded that the Company s disclosure controls and procedures were not effective as of March 31, 2007. To address the material weakness described above, the Company has implemented additional manual controls and procedures over the recording of contractual adjustments related to commercial contracts in the LTACHs. The Company will work with outside consultants to continue identifying additional methods of ensuring these controls and procedures may not be circumvented in the future.

Changes in Internal Controls

Other than the matter described in this Item 4, there have been no significant changes in the Company s internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting. At the time of the filing of this Amendment No. 1 to Form 10-Q, management is in the process of remediating the material weakness surrounding the recording of contractual adjustments related to commercial contracts in the LTACHs noted above through the implementation of manual controls.

Table of Contents

SIGNATURES

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.

LHC GROUP, INC.

Date August 8, 2007

/s/ Barry E. Stewart

Barry E. Stewart
Executive Vice President and Chief
Financial Officer

- 19 -