HEALTHSOUTH CORP
Form 10-Q
August 08, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2007

OR

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

Commission File Number 000-14940

HealthSouth Corporation

(Exact name of Registrant as specified in its Charter)

Delaware	**63-0860407**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
One HealthSouth Parkway Birmingham, Alabama	**35243**
(Address of Principal Executive Offices)	**(Zip Code)**

(205) 967-7116

(Registrant s telephone number)

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 x No o

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. Large accelerated filer x Accelerated filer o Non-Accelerated filer o

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

The registrant had 78,780,353 shares of common stock outstanding, net of treasury shares, as of July 31, 2007.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

HealthSouth Corporation and Subsidiaries

Condensed Consolidated Balance Sheets

(Unaudited)

	June 30, 2007	December 31, 2006
	(In Millions, Except Share Data)	
Assets		
Current assets:		
Cash and cash equivalents	$ 21.0	$ 27.2
Current portion of restricted cash	50.9	60.3
Current portion of restricted marketable securities	16.8	37.5
Accounts receivable, net of allowance for doubtful accounts of $38.8 in 2007; $36.6 in 2006	215.4	217.3
Insurance recoveries receivable	230.0	230.0
Other current assets	69.1	78.1
Current assets held for sale	79.7	229.9
Total current assets	682.9	880.3
Property and equipment, net	766.0	811.2
Goodwill	406.0	406.1
Intangible assets, net	28.4	30.4
Investment in and advances to nonconsolidated affiliates	40.1	37.7
Assets held for sale	172.9	833.7
Income tax refund receivable	208.9	218.8
Other long-term assets	97.2	142.6
Total assets	$ 2,402.4	$ 3,360.8
Liabilities and Shareholders Deficit		
Current liabilities:		
Current portion of long-term debt	$ 40.7	$ 33.6
Accounts payable	58.7	67.5
Accrued expenses and other current liabilities	307.5	360.1
Refunds due patients and other third-party payors	12.9	12.7
Government, class action, and related settlements	454.0	570.6
Current liabilities held for sale	271.8	217.0
Total current liabilities	1,145.6	1,261.5
Long-term debt, net of current portion	2,360.0	3,343.1
Liabilities held for sale	13.4	40.6
Other long-term liabilities	175.0	241.7
	3,694.0	4,886.9
Commitments and contingencies		
Minority interest in equity of consolidated affiliates	109.8	271.1
Convertible perpetual preferred stock, $.10 par value; 1,500,000 shares authorized; 400,000 issued in 2007 and 2006; liquidation preference of $1,000 per share	387.4	387.4
Shareholders deficit:		
Common stock, $.01 par value; 200,000,000 shares authorized; issued: 88,094,777 in 2007; 87,999,513 in 2006	0.9	0.9
Capital in excess of par value	2,842.4	2,849.5
Accumulated deficit	(4,306.4)	(4,713.9)
Accumulated other comprehensive (loss) income	(1.5)	1.6
Treasury stock, at cost (9,463,426 shares in 2007 and 9,320,001 shares in 2006)	(324.2)	(322.6)
Notes receivable from shareholders, officers, and management employees		(0.1)
Total shareholders deficit	(1,788.8)	(2,184.6)
Total liabilities and shareholders deficit	$ 2,402.4	$ 3,360.8

The accompanying notes to condensed consolidated financial

statements are an integral part of these condensed balance sheets.

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HealthSouth Corporation and Subsidiaries

Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)

(Unaudited)

	Three Months Ended		**Six Months Ended**	
	June 30,		**June 30,**	
	2007	**2006**	**2007**	**2006**
	(In Millions, Except Per Share Data)			
Net operating revenues	$ 442.8	$ 443.5	$ 890.9	$ 883.9
Operating expenses:				
Salaries and benefits	217.2	205.9	434.7	412.2
Other operating expenses	60.7	61.5	131.2	129.7
General and administrative expenses	35.0	36.1	79.7	71.1
Supplies	25.8	25.4	52.1	51.0
Depreciation and amortization	20.0	22.5	38.1	42.7
Impairment of long-lived assets	14.7		14.7	
Occupancy costs	13.3	12.1	26.6	24.3
Provision for doubtful accounts	10.8	7.9	21.3	15.2
Loss on disposal of assets	1.7	3.3	1.7	4.2
Government, class action, and related settlements expense	(23.4)	17.2	(35.6)	21.5
Professional fees accounting, tax, and legal	13.3	27.7	35.1	76.3
Total operating expenses	389.1	419.6	799.6	848.2
Loss on early extinguishment of debt	17.7	4.6	17.7	365.6
Interest expense and amortization of debt discounts and fees	59.2	60.5	117.7	119.0
Other income	(0.4)	(1.2)	(5.2)	(3.9)
Gain on interest rate swap	(19.0)	(18.6)	(14.7)	(14.8)
Equity in net income of nonconsolidated affiliates	(2.4)	(2.5)	(5.1)	(4.4)
Minority interests in earnings of consolidated affiliates	7.8	7.6	16.1	16.3
Loss from continuing operations before income tax expense	(9.2)	(26.5)	(35.2)	(442.1)
Provision for income tax (benefit) expense	(10.3)	5.2	(7.1)	18.9
Income (loss) from continuing operations	1.1	(31.7)	(28.1)	(461.0)
Income (loss) from discontinued operations, net of income tax expense	467.2	(10.7)	439.7	(16.6)
Net income (loss)	468.3	(42.4)	411.6	(477.6)
Convertible perpetual preferred dividends	(6.5)	(9.2)	(13.0)	(9.2)
Net income (loss) available to common shareholders	$ 461.8	$ (51.6)	$ 398.6	$ (486.8)
Comprehensive income (loss):				
Net income (loss)	$ 468.3	$ (42.4)	$ 411.6	$ (477.6)
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment		0.3	0.1	(0.1)
Unrealized gain (loss) on available-for-sale securities	0.3	(0.3)	(3.2)	(0.2)
Other comprehensive income (loss), net of tax	0.3		(3.1)	(0.3)
Comprehensive income (loss)	$ 468.6	$ (42.4)	$ 408.5	$ (477.9)
Weighted average common shares outstanding:				
Basic	78.7	79.6	78.8	79.5
Diluted	92.1	92.9	92.1	87.9
Basic and diluted earnings (loss) per common share:				
Loss from continuing operations available to common shareholders	$ (0.07)	$ (0.51)	$ (0.52)	$ (5.91)
Income (loss) from discontinued operations, net of income tax expense	5.94	(0.14)	5.58	(0.21)
Net income (loss) per share available to common shareholders	$ 5.87	$ (0.65)	$ 5.06	$ (6.12)

The accompanying notes to condensed consolidated financial

statements are an integral part of these condensed statements.

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HealthSouth Corporation and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended June 30, 2007	**2006**
	(In Millions)	
Net cash used in operating activities	$ (111.0)	$ (58.2)
Cash flows from investing activities:		
Capital expenditures	(15.2)	(21.4)
Proceeds from sale and maturities of marketable securities		32.1
Proceeds from sale and maturities of restricted marketable securities	65.3	0.2
Purchase of investments		(8.2)
Purchase of restricted investments	(10.5)	(59.2)
Net change in restricted cash	9.4	70.1
Other	1.1	(1.9)
Net cash provided by investing activities of discontinued operations		
Proceeds from divestiture of divisions	1,089.4	
Other investing activities of discontinued operations	3.7	21.8
Net cash provided by investing activities	1,143.2	33.5
Cash flows from financing activities:		
Checks in excess of bank balance	(2.7)	(16.7)
Principal borrowings on notes		3,050.0
Proceeds from bond issuance		1,000.0
Principal payments on debt	(865.0)	(4,426.5)
Borrowings on revolving credit facility	175.0	50.0
Payments on revolving credit facility	(280.0)	
Principal payments under capital lease obligations	(6.3)	(6.9)
Issuance of convertible perpetual preferred stock		400.0
Dividends paid on convertible perpetual preferred stock	(6.5)	
Preferred stock issuance costs		(12.6)
Debt amendment and issuance costs	(11.2)	(77.7)
Distributions to minority interests of consolidated affiliates	(12.0)	(9.2)
Other	0.1	0.1
Net cash used in financing activities of discontinued operations	(39.3)	(44.9)
Net cash used in financing activities	(1,047.9)	(94.4)
Effect of exchange rate on cash and cash equivalents	0.1	0.1
Decrease in cash and cash equivalents	(15.6)	(119.0)
Cash and cash equivalents at beginning of period	27.2	166.4
Cash and cash equivalents of divisions and facilities held for sale at beginning of period	14.1	11.2
Less: Cash and cash equivalents of divisions and facilities held for sale at end of period	(4.7)	(0.4)
Cash and cash equivalents at end of period	$ 21.0	$ 58.2

The accompanying notes to condensed consolidated financial

statements are an integral part of these condensed statements.

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HealthSouth Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

1. Basis of Presentation:

HealthSouth Corporation, incorporated in Delaware in 1984, including its subsidiaries, is the largest provider of inpatient rehabilitation services in the United States. References herein to HealthSouth, the Company, we, our, or us refer to HealthSouth Corporation and its subsidiaries un otherwise stated or indicated by context.

The accompanying unaudited condensed consolidated financial statements of HealthSouth Corporation and Subsidiaries should be read in conjunction with the consolidated financial statements and accompanying notes filed with the United States Securities and Exchange Commission (the SEC) in HealthSouth s Current Report on Form 8-K filed on March 30, 2007 (the March 2007 Form 8-K). The unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the SEC applicable to interim financial information. Certain information and note disclosures included in financial statements prepared in accordance with generally accepted accounting principles in the United States of America (GAAP) have been omitted in these interim statements, as allowed by such SEC rules and regulations. The condensed consolidated balance sheet as of December 31, 2006 has been derived from audited financial statements, but it does not include all disclosures required by GAAP. However, we believe the disclosures are adequate to make the information presented not misleading.

The unaudited results of operations for the interim periods shown in these financial statements are not necessarily indicative of operating results for the entire year. In our opinion, the accompanying condensed consolidated financial statements recognize all adjustments of a normal recurring nature considered necessary to fairly state the financial position, results of operations, and cash flows for each interim period presented.

On August 14, 2006, we announced that we would begin exploring a range of strategic alternatives to enhance stockholder value and to reposition our primary focus on the post-acute care sector. As a result of the exploration of such alternatives, the following events have occurred:

1. As previously reported, on January 27, 2007, we entered into an agreement with Select Medical Corporation (Select Medical), a privately owned operator of specialty hospitals and outpatient rehabilitation facilities, to sell our outpatient rehabilitation division for approximately $245 million in cash, subject to certain adjustments. This transaction closed on May 1, 2007, other than with respect to certain facilities for which approvals for the transfer to Select Medical had not yet been received as of such date. See also Note 6, *Assets Held for Sale and Results of Discontinued Operations*.
2. As previously reported, on March 25, 2007, we entered into an agreement to sell our surgery centers division to ASC Acquisition LLC (ASC), a Delaware limited liability company and newly formed affiliate of TPG Partners V, L.P. (TPG), a private investment partnership. The purchase price consisted of cash consideration of $920 million, subject to certain adjustments, and a contingent option to acquire up to a 5% equity interest in the new company. This transaction closed on June 29, 2007, other than with respect to certain facilities for which approvals for the transfer to ASC had not yet been received as of such date. See also Note 6, *Assets Held for Sale and Results of Discontinued Operations*. ASC now owns and operates this business as Surgical Care Affiliates, LLC, a stand-alone surgical services company.
3. As previously reported, on April 19, 2007, we entered into an agreement with an affiliate of The Gores Group, a private equity firm, to sell our diagnostic division for approximately $47.5 million, subject to certain adjustments. This transaction closed on July 31, 2007, other than with respect to one facility for which approval for the transfer had not yet been received as of such date. See also Note 6, *Assets Held for Sale and Results of Discontinued Operations*.

As a result of the foregoing, our surgery centers, outpatient, and diagnostic divisions are reported as held for sale in our condensed consolidated balance sheets and in discontinued operations in our condensed consolidated statements of operations and comprehensive income (loss) and our condensed consolidated statements of cash flows

HealthSouth Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

in accordance with Financial Accounting Standards Board (FASB) Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. Amounts classified as assets held for sale declined from December 31, 2006 to June 30, 2007 due primarily to the closing of the transactions to sell our surgery centers and outpatient divisions in the second quarter of 2007.

The proceeds of these divestitures were used to reduce debt, which allows us to set the platform to pursue growth opportunities in inpatient rehabilitative care and complementary post-acute businesses in the future. In March 2007, we amended our Credit Agreement (as defined in Note 9, *Long-term Debt*, to the consolidated financial statements included in our March 2007 Form 8-K) and received the appropriate lender approvals for our divestiture activities. See also Note 5, *Long-term Debt*.

Historically, we have reported five segments: inpatient, surgery centers, outpatient, diagnostic, and corporate and other. Based on our strategic focus in the inpatient rehabilitation industry and the reclassification of our surgery centers, outpatient, and diagnostic divisions to discontinued operations, we modified our segment reporting from five reportable segments to one reportable segment in the first quarter of 2007. Amounts historically reported as part of our corporate and other segment, which primarily represented the corporate overhead costs associated with our operating divisions, are no longer considered a reportable segment by our chief operating decision maker due to our strategic repositioning as a pure-play post-acute care provider and the change in the manner in which we now manage the Company. Rather, these corporate overhead costs are now presented on the line entitled *General and administrative expenses* in our condensed consolidated statements of operations and comprehensive income (loss) (see Reclassifications below). Therefore, the condensed consolidated results of operations of the Company presented herein represent the continuing operations of our inpatient division, including corporate overhead. Our condensed consolidated results of operations include overhead costs associated with managing and providing shared services to our surgery centers, outpatient, and diagnostic divisions, even though these divisions qualify as discontinued operations.

See also Note 5, *Long-term Debt*, for information regarding the allocation of interest expense to discontinued operations.

Reclassifications

Certain financial results have been reclassified to conform to the current period presentation. For the three months ended June 30, 2007, such reclassifications primarily relate to our electro-shock wave lithotripter units sold in June 2007 that qualified under FASB Statement No. 144 to be reported as assets held for sale and discontinued operations. Since the filing of our March 2007 Form 8-K, such reclassifications include the qualification of our surgery centers, outpatient, and diagnostic divisions as assets held for sale and discontinued operations under FASB Statement No. 144, as well as certain inpatient facilities we closed or sold in the first quarter of 2007 that also qualified under FASB Statement No. 144. We reclassified our condensed consolidated balance sheet as of December 31, 2006 to show the assets and liabilities of these qualifying facilities as held for sale. We also reclassified our condensed consolidated statements of operations and comprehensive income (loss) for the three and six months ended June 30, 2006 and our condensed consolidated statement of cash flows for the six months ended June 30, 2006 to show the results of those qualifying facilities as discontinued operations. In conjunction with our segment change described above, we also reclassified certain expenses considered to be corporate overhead historically reported primarily within the lines entitled *Salaries and benefits* and *Other operating expenses* into *General and administrative expenses* in our condensed consolidated statements of operations and comprehensive income (loss). These expenses primarily include administrative expenses such as corporate accounting, internal controls, legal, and information technology services.

Marketable Securities

As disclosed in Note 1, *Summary of Significant Accounting Policies*, Marketable Securities, to the consolidated financial statements included in our March 2007 Form 8-K, we record all investments in debt and equity securities with readily determinable fair values and for which we do not exercise significant influence as

HealthSouth Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

available-for-sale securities in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*.

As of December 31, 2006, we had approximately $71.1 million of restricted marketable securities included in our condensed consolidated balance sheet, of which approximately $33.6 million is included in *Other long-term assets*. These marketable securities represent assets held at our wholly owned insurance captive, HCS, Ltd. (HCS), in the Cayman Islands. HCS handles professional liability, workers compensation, and other insurance claims on behalf of HealthSouth. These funds are committed to pay third-party administrators for claims incurred and are restricted by insurance regulations and requirements in the Cayman Islands. During the first quarter of 2007, it was determined that there was excess cash and investments associated with HCS. We received the permission of the Cayman Islands Monetary Authority to advance approximately $65.0 million of these excess funds from HCS to HealthSouth. The funds advanced to HealthSouth included cash that resulted from the liquidation of certain of these marketable securities. HealthSouth used the advance to fund current operations.

Accounts Receivable

As disclosed in Note 1, *Summary of Significant Accounting Policies*, Accounts Receivable, to the consolidated financial statements included in our March 2007 Form 8-K, our accounts receivable are geographically dispersed, but a significant portion of our revenues are concentrated by type of payors. While revenues and receivables from government agencies have always been significant to our operations, our repositioning efforts to focus on the post-acute care sector and inpatient rehabilitation services have further increased their significance to us. The concentration of net patient service accounts receivable by payor class, as a percentage of total net patient service accounts receivable as of the end of each reporting period, is as follows:

	June 30, 2007	**December 31, 2006**
Medicare	56.7%	56.2%
Medicaid	3.0%	3.6%
Workers compensation	4.4%	4.5%
Managed care and other discount plans	23.0%	24.6%
Other third-party payors	10.6%	8.9%
Patients	2.3%	2.2%
Total	100.0%	100.0%

During the three months ended June 30, 2007 and 2006, approximately 68.2% and 68.3%, respectively, of our *Net operating revenues* related to patients participating in the Medicare program. During the six months ended June 30, 2007 and 2006, approximately 68.8% and 69.2%, respectively, of our *Net operating revenues* related to patients participating in the Medicare program. While revenues and accounts receivable from government agencies are significant to our operations, we do not believe there are significant credit risks associated with these government agencies. Because Medicare traditionally pays claims faster than our other third-party payors, the percentage of our Medicare charges in accounts receivable is less than the percentage of our Medicare revenues. We do not believe there are any other significant concentrations of revenues from any particular payor that would subject us to any significant credit risks in the collection of our accounts receivable.

Impairment of Long-lived Assets

For the three and six months ended June 30, 2007, we recognized long-lived asset impairment charges of approximately $14.7 million. Approximately $14.1 million of this charge relates to our corporate campus. On June 1, 2007, we entered into an agreement with an investment fund sponsored by Trammell Crow Company (Trammell Crow) pursuant to which Trammell Crow agreed to acquire our corporate campus for a purchase price of approximately $60 million, subject to certain adjustments. During the second quarter of 2007, we wrote the long-lived assets associated with our corporate campus down to their estimated fair value based on the estimated net proceeds we expected to receive from this sale.

HealthSouth Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

The agreement to sell our corporate campus to Trammell Crow was terminated on August 7, 2007, pursuant to an opt-out provision in the agreement. The Company is considering various alternatives for its corporate campus, recognizing the current downturn in credit markets and its potential impact on any sale transaction.

Recent Accounting Pronouncements

Since the filing of our 2006 Annual Report on Form 10-K (the 2006 Form 10-K), we do not believe any recently issued, but not yet effective, accounting standards will have a material effect on our consolidated financial position, results of operations, or cash flows.

2. Liquidity:

During the second quarter of 2007, we used the net proceeds from the divestiture of our surgery centers and outpatient divisions to pay down debt. As a result of these transactions, our total debt outstanding has decreased from $3.4 billion as of December 31, 2006 to $2.4 billion as of June 30, 2007. We also used the net proceeds received from the divestiture of our diagnostic division in July 2007 to further reduce our total debt outstanding. However, we remain highly leveraged.

Approximately $65.0 million of our $2.4 billion of long-term debt outstanding as of June 30, 2007 represents amounts drawn under our $400 million revolving credit facility (excluding approximately $121.6 million utilized under the revolving letter of credit subfacility). Amounts were drawn from the revolving credit facility primarily due to the timing of interest payments and government settlement payments (as discussed in Note 9, *Settlements*). Based on our current borrowing capacity and leverage ratio required under our Credit Agreement, we do not believe there is significant risk in our ability to make additional draws under our revolving credit facility, if needed.

The biggest risk relating to our high leverage is the possibility that a substantial down-turn in operating earnings could jeopardize our ability to service our debt payment obligations. In addition to debt service, we must also make the final settlement payments related to our Medicare Program Settlement and SEC Settlement (See Note 22, *Medicare Program Settlement*, and Note 23, *SEC Settlement*, to the consolidated financial statements included in our March 2007 Form 8-K.) See Note 1, *Summary of Significant Accounting Policies*, to the consolidated financial statements included in our March 2007 Form 8-K for a discussion of risks and uncertainties facing us. Changes in our business or other factors may occur that might have a material adverse impact on our financial position, results of operations, and cash flows.

3. Guarantees:

In conjunction with the sale of certain facilities, including the sale of our surgery centers and outpatient divisions in the second quarter of 2007, HealthSouth assigned the leases of certain properties to certain purchasers and, as a condition of the lease, agreed to act as a guarantor of the purchaser s performance on the lease. Should the purchaser fail to pay the rent due on these leases, the lessor would have contractual recourse against us.

As of June 30, 2007, we were secondarily liable for 192 such lease obligations. The remaining terms of these leases range from 1 month to 144 months. If we were required to perform under all such guarantees, the maximum amount we would be required to pay approximates $84.3 million.

Also, in connection with the closing of the transaction to sell our diagnostic division on July 31, 2007, HealthSouth remained as a guarantor of certain leases for properties and equipment and a guarantor to certain purchase and servicing contracts that were assigned to the buyer in connection with the sale. If we were required to perform under all such guarantees, we currently estimate the maximum amount we would be required to pay approximates $57.8 million. The remaining terms of these arrangements range from 3 to 224 months.

We have not recorded a liability for these guarantees, as we do not believe it is probable we will have to perform under these agreements. If we are required to perform under these guarantees, we could potentially have

HealthSouth Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

recourse against the purchaser for recovery of any amounts paid. In addition, the purchasers of our surgery centers, outpatient, and diagnostic divisions have agreed to seek releases from the lessors and vendors in favor of HealthSouth with respect to the guarantee obligations associated with these divestitures. To the extent the purchasers of these divisions are unable to obtain releases for HealthSouth, the purchasers have agreed to indemnify HealthSouth for damages incurred under the guarantee obligations, if any.

These guarantees are not secured by any assets under the agreements. As of June 30, 2007, we have not been required to perform under any such guarantees.

4. Investment in and Advances to Nonconsolidated Affiliates:

Investment in and advances to nonconsolidated affiliates represents our investment in 19 partially owned subsidiaries, of which 13 are general or limited partnerships, limited liability companies, or joint ventures in which HealthSouth or one of our subsidiaries is a general or limited partner, managing member, member, or venturer, as applicable. We do not control these affiliates, but have the ability to exercise significant influence over the operating and financial policies of certain of these affiliates. Our ownership percentages in these affiliates range from 4% to 51%. We account for these investments using the cost and equity methods of accounting.

The following summarizes the combined results of operations of our equity method affiliates (on a 100% basis, in millions):

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Net operating revenues	$ 15.9	$ 15.8	$ 32.6	$ 30.7
Operating expenses	(10.8)	(10.1)	(21.2)	(20.1)
Income from continuing operations	5.1	5.7	11.4	10.6
Net income	$ 4.9	$ 5.2	$ 11.1	$ 9.8

5. Long-term Debt:

Our long-term financing obligations outstanding consist of the following (in millions):

	June 30, 2007	**December 31, 2006**
Advances under $400 million revolving credit facility	$ 65.0	$ 170.0
Term Loan Facility	1,174.9	2,039.8
Bonds Payable		
7.000% Senior Notes due 2008	5.0	5.0
10.750% Senior Subordinated Notes due 2008	30.3	30.2
8.500% Senior Notes due 2008	9.4	9.4
8.375% Senior Notes due 2011	0.3	0.3
7.625% Senior Notes due 2012	1.5	1.5
Floating Rate Senior Notes due 2014	375.0	375.0
10.75% Senior Notes due 2016	616.2	615.9
Notes payable to banks and others at interest rates from 9.8% to 12.9%	4.9	5.0
Capital lease obligations	118.2	124.6
	2,400.7	3,376.7
Less: Current portion	(40.7)	(33.6)
Long-term debt, net of current portion	$ 2,360.0	$ 3,343.1

For a description of our indebtedness, see Note 9, *Long-term Debt*, to the consolidated financial statements included in our March 2007 Form 8-K.

HealthSouth Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

The following chart shows scheduled principal payments due on long-term debt for the next five years and thereafter (in millions):

	Face Amount	Net Amount
July 1 through December 31, 2007	$ 13.0	$ 12.7
2008	71.7	71.0
2009	28.6	27.9
2010	29.0	28.2
2011	24.8	23.9
2012	88.0	87.0
Thereafter	2,154.5	2,150.0
Total	$ 2,409.6	$ 2,400.7

As discussed in Note 1, *Basis of Presentation*, we closed the transaction to sell our outpatient division to Select Medical on May 1, 2007. As of June 30, 2007, we had used approximately $212 million of the net proceeds from this transaction to reduce debt outstanding under our Credit Agreement.

As also discussed in Note 1, *Basis of Presentation*, we closed the transaction to sell our surgery centers division to an affiliate of TPG on June 29, 2007. As of June 30, 2007, we had used approximately $873 million of the net proceeds from this transaction to reduce debt outstanding under our Credit Agreement.

As a result of the above pre-payments under our Credit Agreement, the quarterly installments due on our Term Loan Facility (as defined in Note 9, *Long-term Debt*, to the consolidated financial statements included in our March 2007 Form 8-K) were reduced from approximately $5.1 million to approximately $3.0 million, with the balance payable upon the final maturity of the Term Loan Facility in 2013. Also as a result of these pre-payments, we allocated a portion of the loan fees associated with our Credit Agreement to the debt that was extinguished and wrote off loan fees totaling approximately $17. 7 million to *Loss on early extinguishment of debt* during the three and six months ended June 30, 2007.

As also discussed in Note 1, *Basis of Presentation*, we closed the transaction to sell our diagnostic division to The Gores Group on July 31, 2007. We used the net proceeds received from this transaction to further reduce our total debt outstanding.

HealthSouth Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements

Due to the requirements under our Credit Agreement to use the net proceeds from each divestiture (as discussed in Note 1, *Basis of Presentation*) to repay obligations outstanding under our Credit Agreement, and in accordance with the guidance in Emerging Issues Task Force Issue No. 87-24, Allocation of Interest to Discontinued Operations, we allocated the interest expense on the debt that is required to be repaid as a result of the disposal transactions to discontinued operations in all periods presented. The following table provides information regarding our total *Interest expense and amortization of debt discounts and fees* presented in our condensed consolidated statements of operations and comprehensive income (loss) for both continuing and discontinued operations (in millions):

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Continuing operations:				
Interest expense	$ 56.9	$ 55.0	$ 113.3	$ 104.7
Amortization of debt discounts	0.1		0.3	1.1
Amortization of consent fees/bond issue costs	0.5	0.2	1.0	5.2
Amortization of loan fees	1.7	5.3	3.1	8.0
Total interest expense and amortization of debt discounts and fees for continuing operations	59.2	60.5	117.7	119.0
Discontinued operations:				
Interest expense	20.1	23.0	44.5	50.6
Total interest expense for discontinued operations	20.1	23.0	44.5	50.6
Total interest expense and amortization of debt discounts and fees	$ 79.3	$ 83.5	$ 162.2	$ 169.6

On March 12, 2007, we announced that we had amended our existing Credit Agreement to lower the applicable interest rates and modify certain other covenants. The amendment and related supplement reduced the interest rate on our Term Loan Facility to LIBOR plus 2.5% (formerly LIBOR plus 3.25%), as well as reduced the applicable participation rate on the $100 million synthetic letter of credit facility to 2.5% (formerly 3.25%). The amendment also gave us the appropriate approvals required for our divestiture activities.

6. Assets Held for Sale and Results of Discontinued Operations:

For the facilities identified during the three months ended June 30, 2007 that met the requirements of FASB Statement No. 144, we reclassified our condensed consolidated balance sheet as of December 31, 2006 to show the assets and liabilities of those facilities as held for sale. We also reclassified our condensed consolidated statements of operations and comprehensive income (loss) for the three and six months ended June 30, 2006 and our condensed consolidated statement of cash flows for the six months ended June 30, 2006 to show the results of those facilities as discontinued operations. The operating results of discontinued operations, including the allocation of $18.9 million and $19.3 million of interest expense in the three months ended June 30, 2007 and 2006, respectively, and $43.0 million and $42.2 million of interest expense in the six months ended June 30, 2007 and 2006, respectively, (as discussed in Note 5, *Long-term Debt*), are as follows (in millions):

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Net operating revenues	$ 243.2	$ 347.1	$ 553.0	$ 709.9
Costs and expenses	230.1	349.1	527.5	716.5
Impairments		6.1	35.9	6.7
Income (loss) from discontinued operations	13.1	(8.1)	(10.4)	(13.3)
Gain on disposal of assets of discontinued operations	1.5	1.2	1.5	4.7
Gain on divestiture of divisions	403.2		403.2	
Income tax benefit (expense)	49.4	(3.8)	45.4	(8.0)
Income (loss) from discontinued operations, net of tax	$ 467.2	$ (10.7)	$ 439.7	$ (16.6)

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As discussed in Note 10, *Contingencies*, we have recorded charges related to ongoing negotiations with certain of our subsidiary partnerships related to the restatement of their historical financial statements. The portion of these charges that is attributable to partnerships of our surgery centers division has been included in our results of discontinued operations. No charges were made to partnerships in our outpatient or diagnostic divisions during the periods presented. We have and may continue to incur additional charges related to these ongoing negotiations with our partners.

As discussed in Note 1, *Summary of Significant Accounting Policies*, to the consolidated financial statements included in our March 2007 Form 8-K, we insure a substantial portion of our professional liability, general liability, and workers compensation risks through a self-insured retention program underwritten by HCS, which we fund annually. Expenses for retained professional and general liability risks and workers compensation risks associated with our surgery centers, outpatient, and diagnostic divisions have been included in our results of discontinued operations.

The income tax benefit of our results of discontinued operations for the three and six months ended June 30, 2007 is comprised primarily of (1) $61.7 million related to the reversal upon sale of deferred tax liabilities arising from indefinite-lived intangible assets of our surgery centers division, (2) $12.3 million of expense attributable to the utilization of the current period loss from continuing operations, and (3) $2.4 million of expense from projected Alternative Minimum Tax liability for 2007.

Assets and liabilities held for sale consist of the following (in millions):

	June 30, 2007	December 31, 2006
Assets:		
Cash and cash equivalents	$ 4.7	$ 14.1
Current portion of restricted cash	4.4	43.2
Accounts receivable, net	38.3	157.5
Other current assets	32.3	15.1
Total current assets	79.7	229.9
Property and equipment, net	62.1	287.4
Goodwill	98.6	490.9
Intangible assets, net	4.1	25.8
Other long-term assets	8.1	29.6
Total long-term assets	172.9	833.7
Total assets	$ 252.6	$ 1,063.6
Liabilities:		
Current portion of long-term debt	$ 1.0	$ 3.4
Accounts payable	9.3	38.8
Accrued expenses and other current liabilities	73.4	85.9
Deferred amounts related to sale of surgery centers division	129.3	
Refunds due patients and other third-party payors	58.8	88.9
Total current liabilities	271.8	217.0
Long-term debt, net of current portion	5.6	22.2
Other long-term liabilities	7.8	18.4
Total long-term liabilities	13.4	40.6
Total liabilities	$ 285.2	$ 257.6

Refunds due patients and other third-party payors consist primarily of overpayments received from our patients and other third-party payors. In instances where we are unable to determine the party due the refund, these amounts can become subject to escheat property laws and payable to various tax jurisdictions. These liabilities will remain with HealthSouth after each transaction closes. We are negotiating the settlement of these amounts with third-party payors and various tax jurisdictions. The result of these ongoing settlement negotiations may impact the carrying value of these liabilities.

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Our condensed consolidated financial statements include all assets, liabilities, revenues, and expenses of less-than-100%-owned affiliates that we control. Accordingly, we have recorded minority interests in the earnings and equity of such entities. As of June 30, 2007 and December 31, 2006, approximately $27.7 million and $183.7 million, respectively, of our consolidated *Minority interest in equity of consolidated affiliates* represent minority interests associated with our surgery centers, outpatient, and diagnostic divisions.

Surgery Centers Division

As discussed in Note 1, *Basis of Presentation*, the transaction to sell our surgery centers division to ASC closed on June 29, 2007, other than with respect to certain facilities for which approvals for the transfer to ASC had not yet been received as of such date. The purchase price consisted of cash consideration of $920 million, subject to certain adjustments, and a contingent option to acquire up to a 5% equity interest in the new company. The net cash proceeds received at closing, after deducting deal and separation costs, purchase price adjustments, and approximately $15.5 million of debt assumed by ASC, approximated $860.7 million.

As noted above, the closing of the sale of the surgery centers division occurred on June 29, 2007, other than with respect to certain facilities for which approvals for the transfer to ASC had not yet been received as of such date. In connection with the closing, HealthSouth and ASC agreed, among other things, that HealthSouth would retain its ownership interest in certain surgery centers until regulatory approvals for the transfer of such surgery centers to ASC have been received. In that regard, ASC will manage the operations of such surgery centers until such approvals have been received, and HealthSouth and ASC entered into arrangements designed to place them in approximately the same economic position, whether positive or negative, they would have occupied had all regulatory approvals been received prior to closing. Upon receipt of such approvals, HealthSouth s ownership interest in such facilities will be transferred to ASC. No portion of the purchase price was withheld at closing pending the transfer of these facilities. In the event regulatory approval for the transfer of any such facility is not received within one year, HealthSouth would be required to return to ASC a portion of the purchase price allocated to such facility.

The assets and liabilities presented below for the surgery centers division include the assets and liabilities associated with those facilities not transferred to ASC at closing as part of the surgery centers transaction, as these assets will not be transferred until approval for such transfer is obtained. We have deferred approximately $129.3 million of cash proceeds received at closing associated with these facilities awaiting regulatory approval for the transfer of such facilities to ASC. We will continue to report the results of operations of these facilities in discontinued operations until the transfer of these facilities occurs.

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The assets and liabilities of the surgery centers division reported as held for sale consist of the following (in millions):

	June 30, 2007	December 31, 2006
Assets:		
Cash and cash equivalents	$ 2.1	$ 12.0
Current portion of restricted cash	0.5	31.8
Accounts receivable, net	6.0	84.5
Other current assets	29.3	9.0
Total current assets	37.9	137.3
Property and equipment, net	19.8	181.3
Goodwill	88.9	462.5
Intangible assets, net	3.1	17.8
Other long-term assets	3.0	24.1
Total long-term assets	114.8	685.7
Total assets	$ 152.7	$ 823.0
Liabilities:		
Current portion of long-term debt	$ 0.4	$ 2.2
Accounts payable	2.1	22.4
Accrued expenses and other current liabilities	51.8	46.8
Deferred amounts related to sale of surgery centers division	129.3	
Refunds due patients and other third-party payors	13.0	26.8
Total current liabilities	196.6	98.2
Long-term debt, net of current portion	2.6	17.9
Other long-term liabilities	0.5	7.3
Total long-term liabilities	3.1	25.2
Total liabilities	$ 199.7	$ 123.4

The operating results of the surgery centers division included in discontinued operations consist of the following (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Net operating revenues	$ 175.4	$ 191.8	$ 363.2	$ 386.4
Costs and expenses	159.3	187.2	334.8	376.7
Impairments		1.6	3.0	1.6
Income from discontinued operations	16.1	3.0	25.4	8.1
Gain on disposal of assets of discontinued operations	0.3	3.3	1.9	14.2
Gain on divestiture of division	268.6		268.6	
Income tax benefit (expense)	52.4	(3.6)	48.5	(7.8)
Income from discontinued operations, net of tax	$ 337.4	$ 2.7	$ 344.4	$ 14.5

As a result of the disposition of our surgery centers division, we recorded an approximate $329.9 million post-tax gain on disposal in the second quarter of 2007. We expect to record an additional gain of approximately $55 million to $75 million once approval is obtained for the facilities that were not transferred at closing.

In connection with this divestiture, we entered into a transition services agreement (TSA) with ASC whereby we will continue to provide back office services related to the operations of our surgery centers division. These back office services include certain information technology, accounting and finance, and human resource support services, among others. Services are expected to be provided for periods of up to 12 months, although certain services are subject to short extension periods. ASC will compensate us for these services, as outlined in the TSA. Such compensation is not expected to be material to either HealthSouth or the operations of the surgery centers division.

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Outpatient Division

As discussed in Note 1, *Basis of Presentation*, the transaction to sell our outpatient rehabilitation division to Select Medical closed on May 1, 2007, other than with respect to certain facilities for which approvals for the transfer to Select Medical had not yet been received as of such date. In connection with the closing of the sale of this division, we entered into a letter agreement with Select Medical whereby we agreed, among other things, that we would retain certain outpatient facilities until certain state regulatory approvals for the transfer of such facilities to Select Medical have been received. In that regard, we entered into agreements with Select Medical whereby Select Medical will manage certain operations of the applicable facilities until such approvals have been received. Approximately $24 million of the $245 million purchase price was withheld pending the transfer of these facilities. We expect to receive these additional sale proceeds once regulatory approval is obtained. The net cash proceeds received at closing, after deducting deal and separation costs, purchase price adjustments, and approximately $3.2 million of debt assumed by Select Medical, approximated $200.4 million.

The assets and liabilities presented below for the outpatient division include the assets and liabilities associated with these facilities as part of the outpatient divestiture, as these assets will not be transferred, nor will we receive the sale proceeds, until regulatory approval is obtained. We will continue to report the results of operations of these facilities in discontinued operations until the transfer of these facilities occurs.

The assets and liabilities of the outpatient division reported as held for sale consist of the following (in millions):

	June 30, 2007	**December 31, 2006**
Assets:		
Cash and cash equivalents	$	$ 0.6
Accounts receivable, net	0.6	36.9
Other current assets	0.6	1.5
Total current assets	1.2	39.0
Property and equipment, net	1.8	32.7
Goodwill	9.7	28.4
Intangible assets, net	1.0	3.7
Other long-term assets		0.3
Total long-term assets	12.5	65.1
Total assets	$ 13.7	$ 104.1
Liabilities:		
Current portion of long-term debt	$	$ 0.7
Accounts payable	0.1	2.8
Accrued expenses and other current liabilities	6.3	22.8
Refunds due patients and other third-party payors	34.2	46.7
Total current liabilities	40.6	73.0
Long-term debt, net of current portion	1.2	2.2
Other long-term liabilities	0.2	3.1
Total long-term liabilities	1.4	5.3
Total liabilities	$ 42.0	$ 78.3

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The operating results of the outpatient division included in discontinued operations consist of the following (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Net operating revenues	$ 27.9	$ 85.8	$ 107.8	$ 175.4
Costs and expenses	27.8	79.9	100.5	165.5
Impairments		0.3	0.2	0.3
Income from discontinued operations	0.1	5.6	7.1	9.6
Loss on disposal of assets of discontinued operations			(1.3)	(0.2)
Gain on divestiture of division	134.6		134.6	
Income tax expense	(4.2)		(4.3)	
Income from discontinued operations, net of tax	$ 130.5	$ 5.6	$ 136.1	$ 9.4

As a result of the disposition of our outpatient division, we recorded an approximate $135.0 million post-tax gain on disposal in the second quarter of 2007. We expect to receive additional proceeds and record an additional gain of approximately $10 million to $15 million once regulatory approval is obtained for the facilities that were not transferred at closing.

Diagnostic Division

As discussed in Note 1, *Basis of Presentation*, during the second quarter of 2007, we entered into an agreement with The Gores Group to sell our diagnostic division. This transaction closed on July 31, 2007, other than with respect to one facility for which approval for the transfer had not yet been received as of such date. The net cash proceeds received at closing, after deducting deal and separation costs and purchase price adjustments, approximated $39.7 million.

The assets and liabilities of the diagnostic division reported as held for sale consist of the following (in millions):

	June 30, 2007	**December 31, 2006**
Assets:		
Cash and cash equivalents	$ 1.6	$ 1.0
Accounts receivable, net	27.5	29.4
Other current assets	0.9	2.3
Total current assets	30.0	32.7
Property and equipment, net	40.3	72.3
Intangible assets, net		4.2
Other long-term assets	2.3	3.2
Total long-term assets	42.6	79.7
Total assets	$ 72.6	$ 112.4
Liabilities:		
Current portion of long-term debt	$ 0.6	$ 0.5
Accounts payable	5.6	11.5
Accrued expenses and other current liabilities	10.2	9.1
Refunds due patients and other third-party payors	10.6	14.3
Total current liabilities	27.0	35.4
Long-term debt, net of current portion	1.8	2.1
Other long-term liabilities	4.6	4.5
Total long-term liabilities	6.4	6.6
Total liabilities	$ 33.4	$ 42.0

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The operating results of the diagnostic division included in discontinued operations consist of the following (in millions):

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Net operating revenues	$ 37.8	$ 51.6	$ 76.7	$ 104.9
Costs and expenses	37.6	60.8	82.2	121.0
Impairments		2.4	32.7	2.9
Income (loss) from discontinued operations	0.2	(11.6)	(38.2)	(19.0)
Gain (loss) on disposal of assets of discontinued operations	1.2	(2.1)	1.3	(2.0)
Income tax benefit (expense)	1.0	(0.1)	1.0	(0.1)
Income (loss) from discontinued operations, net of tax	$ 2.4	$ (13.8)	$ (35.9)	$ (21.1)

During the first quarter of 2007, we wrote the intangible assets and certain long-lived assets of our diagnostic division down to their estimated fair value based on the estimated net proceeds to be received from the divestiture of the division. This charge is included in impairments in the above results of operations of our diagnostic division. As a result of the disposition of our diagnostic division and the impairment charge recorded in the first quarter of 2007, we do not expect to record a material gain or loss on disposal in the third quarter of 2007.

In connection with the divestiture of our diagnostic division, we entered into a TSA with an affiliate of The Gores Group whereby we will continue to provide back office services related to the operations of our diagnostic division. These back office services include certain information technology, accounting and finance, communications, and payor relationship support services, among others. We also entered into an agreement whereby an affiliate of The Gores Group will provide certain services related to the accounts receivable and other assets and operations that we retained. Services are expected to be provided for periods up to 12 months, although certain services are subject to short extension periods. The compensation that we will pay and receive related to these services is not expected to be material to either HealthSouth or the operations of the diagnostic division.

7. Income Taxes:

Our *Provision for income tax (benefit) expense* for the three months ended June 30, 2007 includes the following: (1) current income tax expense of $1.6 million attributable to state income taxes of subsidiaries which have separate state tax filing requirements, income taxes for other subsidiaries that are not included in our federal consolidated income tax return, and interest income accrued with respect to expected income tax refunds resulting from updated prior tax filings which are still in progress, (2) a current income tax benefit of $12.3 million attributable to the utilization of the period s pre-tax loss from continuing operations to offset the gains attributable to the sales of the surgery centers and outpatient divisions (see Note 6, *Assets Held for Sale and Results of Discontinued Operations)*, and (3) deferred income tax expense of $0.4 million attributable to future tax liabilities to be incurred by subsidiaries that are not included in our federal consolidated income tax return and increases in the basis difference of certain indefinite-lived assets.

Our *Provision for income tax (benefit) expense* for the six months ended June 30, 2007 includes the following: (1) current income tax expense of $3.6 million attributable to state income taxes of subsidiaries which have separate state tax filing requirements, income taxes for other subsidiaries that are not included in our federal consolidated income tax return, and interest income accrued with respect to expected income tax refunds resulting from updated prior tax filings which are still in progress, (2) a current income tax benefit of $12.3 million attributable to the utilization of the period s pre-tax loss from continuing operations to offset the gains attributable to the sales of the surgery centers and outpatient divisions (see Note 6, *Assets Held for Sale and Results of Discontinued Operations*), and (3) deferred income tax expense of $1.6 million attributable to future tax liabilities to be incurred by subsidiaries that are not included in our federal consolidated income tax return and increases in the basis difference of certain indefinite-lived assets.

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We have significant federal and state net operating losses. During the second quarter of 2007, we utilized a portion of these federal net operating loss carryforwards to offset the gains arising from the sales of the surgery centers and outpatient divisions. We assess the realization of our deferred tax assets quarterly to determine whether an adjustment to our valuation allowance is required. After consideration of all evidence, both positive and negative, management concluded that it is more likely than not that we will not realize a portion of our deferred tax assets. Therefore, a valuation allowance has been established on substantially all of our net deferred tax assets. No valuation allowance has been provided on deferred assets and liabilities attributable to subsidiaries not included within the federal consolidated group. Certain of the Company s deferred tax liabilities are related to indefinite-lived intangible assets. For purposes of scheduling the expected utilization of deferred tax assets as required by FASB Statement No. 109, *Accounting for Income Taxes*, these deferred tax liabilities cannot be looked upon as a source of future taxable income, and therefore cannot be considered in an assessment of the amount of any valuation allowance.

Our *Provision for income tax (benefit) expense* for the same periods in 2006 consisted of substantially the same items of current and deferred taxes, excluding an accrual for interest income with respect to expected income tax refunds and excluding the benefit attributable to the gains on sales discussed above. Income tax (benefit) expense for the six months ended June 30, 2007 changed from an expense of $18.9 million for the six months ended June 30, 2006 to a benefit of $7.1 million for the six months ended June 30, 2007 due to the $12.3 million benefit attributable to the gains on sales discussed above and the fact that we filed a request for a tax accounting method change in the first quarter of 2006 which accelerated the amortization of certain indefinite-lived assets. This tax accounting method change gave rise to an additional difference between the book and tax bases of the assets effected and, accordingly, resulted in our recording an additional deferred tax liability and deferred tax expense related to these indefinite-lived assets. The entire impact of this change of approximately $8.3 million was reflected in the three months ended March 31, 2006.

We adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, on January 1, 2007. As a result of our adoption of FASB Interpretation No. 48, we recognized a $4.2 million increase to reserves for uncertain tax positions. This increase was accounted for as an addition to *Accumulated deficit* as of January 1, 2007. Including the cumulative effect increase to the reserves for uncertain tax positions, at the beginning of the year, we had approximately $277.2 million of total gross unrecognized tax benefits, of which approximately $253.3 million would affect our effective tax rate if recognized. However, we have a full valuation allowance recorded against our net deferred tax assets. Therefore, the combined effect on our federal effective tax rate would be zero. The amount of the unrecognized tax benefits did not change significantly during the three or six months ended June 30, 2007. Our continuing practice is to recognize interest and/or penalties related to income tax matters in income tax expense. For the three and six months ended June 30, 2007, we accrued $0.8 million and $1.7 million of interest income, respectively. Total accrued interest income was $38.5 million and $36.8 million as of June 30, 2007 and December 31, 2006, respectively. We are currently undergoing a process with the applicable taxing authorities that we expect will result in the resolution of these matters in late 2007 or early 2008. We are actively pursuing the maximization of our income tax refund claims. Although management believes its estimates and judgments related to these claims are reasonable, depending on the ultimate resolution of these tax matters, actual amounts recovered could differ from management s estimates, and such differences could be material.

HealthSouth and its subsidiaries federal and state income tax returns are periodically examined by various regulatory taxing authorities. In connection with such examinations, we have settled our federal income tax liabilities with the Internal Revenue Service (the IRS) for all tax years through 1995. In May 2006, we received the IRS s report and assessment of additional income taxes for the years 1996 through 1998. We filed a formal reply in July 2006 and are currently working to resolve the matters from this report and assessment. In May 2007, we received the IRS s report for the tax year 1999 that entitled HealthSouth to an income tax refund and net operating loss carrybacks to recover additional income tax refunds in prior tax years, subject to review by the Joint Committee of Congress. We expect to have all remaining open years under audit by the IRS in the near future. Amounts related to these tax deficiencies and other contingencies have been considered by management in its estimate of our potential net recovery of prior income taxes. However, at this time, we cannot estimate a range of the reasonably possible change that may occur.

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8. Earnings (Loss) per Common Share:

The calculation of earnings (loss) per common share is based on the weighted-average number of our common shares outstanding during the applicable period. The calculation for diluted earnings (loss) per common share recognizes the effect of all dilutive potential common shares that were outstanding during the respective periods, unless their impact would be antidilutive. The following table sets forth the computation of basic and diluted earnings (loss) per common share (in millions, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Numerator:				
Income (loss) from continuing operations	$ 1.1	$ (31.7)	$ (28.1)	$ (461.0)
Less: Convertible perpetual preferred stock dividends	(6.5)	(9.2)	(13.0)	(9.2)
Loss from continuing operations available to common shareholders	(5.4)	(40.9)	(41.1)	(470.2)
Income (loss) from discontinued operations, net of tax	467.2	(10.7)	439.7	(16.6)
Net income (loss) available to common shareholders	$ 461.8	$ (51.6)	$ 398.6	$ (486.8)
Denominator:				
Basic weighted average common shares outstanding	78.7	79.6	78.8	79.5
Diluted weighted average common shares outstanding	92.1	92.9	92.1	87.9
Basic and diluted earnings (loss) per common share:				
Loss from continuing operations available to common shareholders	$ (0.07)	$ (0.51)	$ (0.52)	$ (5.91)
Income (loss) from discontinued operations, net of tax	5.94	(0.14)	5.58	(0.21)
Net income (loss) per share available to common shareholders	$ 5.87	$ (0.65)	$ 5.06	$ (6.12)

Diluted earnings per share report the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. These potential shares include dilutive stock options, restricted stock awards, restricted stock units, and convertible perpetual preferred stock. For the three months ended June 30, 2007 and 2006, the number of potential shares approximated 13.4 million and 13.3 million, respectively. For the six months ended June 30, 2007 and 2006, the number of potential shares approximated 13.3 million and 8.4 million, respectively. Including these potential common shares in the denominator resulted in an antidilutive per share amount due to our *Loss from continuing operations available to common shareholders*. Although including these potential common shares in our per common share computations for *Income from discontinued operations, net of tax* and *Net income per share available to common shareholders* may be dilutive to their comparable basic per share amounts, under the guidance in FASB Statement No. 128, *Earnings per Share*, no potential common shares are included in the computation of any diluted per share amount when a *Loss from continuing operations available to common shareholders* exists. Therefore, no separate computation of diluted earnings (loss) per share is presented.

Options to purchase approximately 3.2 million and 3.7 million shares of common stock were outstanding as of June 30, 2007 and 2006, respectively, but were not included in the computation of diluted weighted-average shares because to do so would have been antidilutive.

In January 2004, we repaid our then-outstanding 3.25% Convertible Debentures using the net proceeds of a loan arranged by Credit Suisse First Boston. In connection with this transaction, we issued warrants to the lender to purchase two million shares of our common stock. Each warrant has a term of ten years from the date of issuance and an exercise price of $32.50 per share. The warrants were not assumed exercised for dilutive shares outstanding because they were antidilutive in the period.

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In March 2006, we issued 400,000 shares of convertible perpetual preferred stock as part of a recapitalization of HealthSouth. We use the if-converted method to include the convertible perpetual preferred stock in our computation of diluted earnings (loss) per share.

In September 2006, we agreed to issue approximately 5.0 million shares of common stock and warrants to purchase approximately 8.2 million shares of common stock to settle our class action securities litigation. This agreement received final court approval on January 11, 2007. As of June 30, 2007, these shares of common stock and warrants have not been issued and are not included in our basic or diluted common shares outstanding. For additional information, see Note 9, *Settlements*.

9. Settlements:

Medicare Program Settlement

Under the terms of our settlement with the United States, which is described in Note 22, *Medicare Program Settlement*, to the consolidated financial statements accompanying our March 2007 Form 8-K, we agreed to make cash payments to the United States in the aggregate amount of $325 million, plus accrued interest from November 4, 2004 at an annual rate of 4.125%. Through June 30, 2007, we have made payments of approximately $281.3 million (excluding interest), with the remaining balance of $43.7 million (excluding interest) due in two installments, one to be paid in each of the remaining two quarters of 2007. As of June 30, 2007 and December 31, 2006, approximately $43.7 million and $86.7 million, respectively, of the cash settlement amount are included in *Government, class action, and related settlements* in our condensed consolidated balance sheets.

SEC Settlement

Under the terms of our settlement with the SEC, which is described in Note 23, *SEC Settlement*, to the consolidated financial statements accompanying our March 2007 Form 8-K, we agreed to pay a $100 million civil penalty and disgorgement of $100 to the SEC in the following installments: $12,500,100 by October 15, 2005; $12.5 million by April 15, 2006; $25.0 million by October 15, 2006; $25.0 million by April 15, 2007; and $25.0 million by October 15, 2007. As of the date of this filing, we are current with all payments required under the above payment schedule. Payments due under the SEC Settlement are included in *Government, class action, and related settlements* in our condensed consolidated balance sheets.

Securities Litigation Settlement

In February 2006, we announced that we had reached a preliminary agreement in principle with the lead plaintiffs in the Stockholder Securities Action, the Bondholder Securities Action, and the derivative litigation (as defined in Note 24, *Securities Litigation Settlement*, to the consolidated financial statements accompanying our March 2007 Form 8-K), as well as with our insurance carriers to settle claims filed in those actions against us and many of our former directors and officers. In September 2006, the plaintiffs in the Stockholder Securities Action and the Bondholder Securities Action, HealthSouth, and certain individual former HealthSouth employees and board members entered into and filed a stipulation of partial settlement of this litigation. We also entered into definitive agreements with the lead plaintiffs in these actions and the derivative actions, as well as certain of our insurance carriers, to settle the litigation. In September 2006, the U.S. District Court entered an order preliminarily approving the stipulation and settlement. Following a period to allow class members to opt out of the settlement and for objections to the settlement to be lodged, the U.S. District Court held a hearing in January 2007 and determined that the proposed settlement is fair, reasonable, and adequate to the class members and that it should receive final approval. Individual class members representing approximately 205,000 shares of common stock and one bondholder whose bonds have a face value of $1.5 million elected to be excluded from the settlement. The order approving the settlement bars claims by the non-settling defendants arising out of or relating to the Stockholder Securities Action, the Bondholders Securities Action, and the derivative litigation but does not prevent other security holders excluded from the settlement from asserting claims directly against HealthSouth.

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Under the terms of our securities litigation settlement, which is described in more detail in Note 24, *Securities Litigation Settlement*, to the consolidated financial statements accompanying our March 2007 Form 8-K, federal securities and fraud claims brought in the Consolidated Securities Action (as defined in our March 2007 Form 8-K) against us and certain of our former directors and officers were settled in exchange for aggregate consideration of $445 million, consisting of HealthSouth common stock and warrants valued at $215 million and cash payments by HealthSouth s insurance carriers of $230 million. In addition, the settlement agreements provided that the plaintiffs in the Stockholder Securities Action and the Bondholder Securities Action will receive 25% of any net recoveries from future judgments obtained by us or on our behalf with respect to certain claims against Richard M. Scrushy, our former chairman and chief executive officer (excluding the $48 million judgment against Mr. Scrushy on January 3, 2006, as discussed in Note 25, *Contingencies and Other Commitments*, to the consolidated financial statements accompanying our March 2007 Form 8-K), Ernst & Young LLP, our former auditor, and UBS, our former primary investment bank, each of which remains a defendant in the derivative actions as well as the Consolidated Securities Action. Mr. Scrushy has appealed one provision of the bar order, which is a component of the settlement, and that appeal remains pending before the Eleventh Circuit Court of Appeals. The settlement is subject to the satisfaction of a number of conditions, including a favorable resolution of any appeal. The settlement was also conditioned upon the approval of bar orders in the derivative litigation by the Alabama Circuit Court that would, among other things, preclude certain claims by the non-settling co-defendants against HealthSouth and the insurance carriers relating to matters covered by the settlement. As more fully described in Note 10, *Contingencies*, that approval was obtained on January 11, 2007. The settlement agreements also required HealthSouth to indemnify the settling insurance carriers, to the extent permitted by law, for any amounts that they are legally obligated to pay to any non-settling defendants. As of June 30, 2007, we have not recorded a liability regarding these indemnifications, as we do not believe it is probable we will have to perform under the indemnification portion of these settlement agreements and any amount we would be required to pay is not estimable at this time.

Despite approval of the securities class action settlement, there are class members who have elected to opt out of the securities class action settlement and pursue claims individually. In addition, AIG Global Investment Corporation (AIG), which failed to opt out of the class settlement on a timely basis, has requested that the court allow it to opt out despite missing the district court s deadline. In the court s Partial Final Judgment and Order of Dismissal with Prejudice dated January 11, 2007, the court found that allowing AIG to opt out after the deadline would result in serious prejudice to us and denied AIG s request for an expansion of time to opt out. On January 26, 2007, AIG moved for reconsideration of the court s decision on this issue. On March 22, 2007, the district court denied AIG s motion for reconsideration. On April 17, 2007, AIG filed a notice of appeal with the Eleventh Circuit Court of Appeals, and that appeal remains pending. If the appellate court were to reverse the district court s denial of AIG s motions and allow AIG to opt out despite missing the deadline, AIG would likely bring individual claims alleging substantial damages relating to the purchase by AIG and its affiliates of HealthSouth bonds. If AIG is not successful with an appeal of that denial, AIG s individual claims would be precluded by the securities class action settlement.

We recorded a charge of $215.0 million as *Government, class action, and related settlements expense* in our 2005 consolidated statement of operations. During the fourth quarter of 2006, we reduced our liability for this settlement by approximately $31.2 million based on the value of our common stock and the associated common stock warrants on the date the order granting court approval was entered. During the three and six months ended June 30, 2007, we reduced our liability for this settlement by an additional $31.5 million and $49.0 million, respectively, based on the value of our common stock and the associated common stock warrants at quarter end. The corresponding liability of $134.8 million and $183.8 million as of June 30, 2007 and December 31, 2006, respectively, is included in *Government, class action, and related settlements* in our condensed consolidated balance sheets. The charge for this settlement will be revised in future periods to reflect additional changes in the fair value of the common stock and warrants until they are issued.

In addition, *Government, class action, and related settlements* in our condensed consolidated balance sheets also includes a liability in the amount of $230.0 million in order to state the total liability related to the securities litigation settlement at the aggregate value of the consideration to be exchanged the securities to be

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issued by us and the cash to be paid by the insurers. The related receivable from our insurers in the amount of $230.0 million is included in our condensed consolidated balance sheets as *Insurance recoveries receivable*.

Insurance Coverage Litigation

In 2003, approximately 14 insurance companies filed complaints in state and federal courts in Alabama, Delaware, and Georgia alleging that the insurance policies issued by those companies to us and/or some of our directors and officers should be rescinded on grounds of fraudulent inducement. The complaints also sought a declaration that we and/or some of our current and former directors and officers are not covered under various insurance policies. These lawsuits challenged the majority of our director and officer liability policies, including our primary director and officer liability policy in effect for the claims at issue. Actions filed by insurance companies in the United States District Court for the Northern District of Alabama were consolidated for pretrial and discovery purposes under the caption *In re HealthSouth Corp. Insurance Litigation*, Consolidated Case No. CV-03-BE-1139-S. Four lawsuits filed by insurance companies in the Circuit Court of Jefferson County, Alabama were consolidated with the *Tucker* case for discovery and other pretrial purposes. Cases related to insurance coverage that were filed in Georgia and Delaware have been dismissed. We filed counterclaims against a number of the plaintiffs in these cases alleging, among other things, bad faith for wrongful failure to provide coverage.

On September 26, 2006, in connection with the settlement of the Consolidated Securities Action and derivative litigation, we executed a settlement agreement with the insurers that is substantively consistent with the preliminary agreement in principle reached in February 2006. The settlement agreement also requires HealthSouth to indemnify the settling insurance carriers, to the extent permitted by law, for any amounts they are legally obligated to pay to any non-settling defendants.

Non-Prosecution Agreement

On May 17, 2006, we announced that we reached a non-prosecution agreement (the Non-Prosecution Agreement) with the United States Department of Justice (the DOJ) with respect to the accounting fraud committed by members of our former management. We have pledged to continue our cooperation with the DOJ and have paid $3.0 million to the U.S. Postal Inspection Services Consumer Fraud Fund during the three months ended June 30, 2006 in connection with the execution of the Non-Prosecution Agreement. This payment was recorded in *Government, class action, and related settlements expense* in our condensed consolidated statements of operations and comprehensive income (loss).

Notwithstanding the foregoing, the DOJ has reserved the right to prosecute us for any crimes committed by our employees if we violate the terms of the Non-Prosecution Agreement. The Non-Prosecution Agreement expires on May 17, 2009.

10. Contingencies:

Significant Legal Proceedings

We operate in a highly regulated and litigious industry. As a result, various lawsuits, claims, and legal and regulatory proceedings have been and can be expected to be instituted or asserted against us. The resolution of any such lawsuits, claims, or legal and regulatory proceedings could materially and adversely affect our results of operations and financial position in a given period.

Securities Litigation

See Note 9, *Settlements*, of these condensed consolidated financial statements and Note 24, *Securities Litigation Settlement*, to the consolidated financial statements accompanying our March 2007 Form 8-K for a discussion of the settlement entered into with the lead plaintiffs in certain securities actions.

On November 24, 2004, an individual securities fraud action captioned *Burke v. HealthSouth Corp., et al.*, 04-B-2451 (OES), was filed in the United States District Court of Colorado against us, some of our former directors

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and officers, and our former auditor. The complaint makes allegations similar to those in the Consolidated Securities Action, as defined in Note 24, *Securities Litigation Settlement*, to the consolidated financial statements accompanying our March 2007 Form 8-K, and asserts claims under the federal securities laws and Colorado state law based on plaintiff s alleged receipt of unexercised options and his open-market purchases of our stock. By order dated May 3, 2005, the action was transferred to the United States District Court for the Northern District of Alabama, where it remains pending. The plaintiff in this case has not opted out of the Consolidated Securities Action settlement discussed in Note 9, *Settlements*. Although the deadline for opting out in the Consolidated Securities Action has passed, if the *Burke* action resumes, we will continue to vigorously defend ourselves in this case. However, based on the stage of litigation, and review of the current facts and circumstances, we are unable to determine an amount of loss or range of possible loss that might result from an adverse judgment or a settlement of this case should litigation continue or whether any resultant liability would have a material adverse effect on our financial position, results of operations, or cash flows.

Derivative Litigation

Between 1998 and 2004, a number of lawsuits purporting to be derivative actions (*i.e.*, lawsuits filed by shareholder plaintiffs on our behalf) were filed in several jurisdictions, including the Circuit Court for Jefferson County, Alabama, the Delaware Court of Chancery, and the United States District Court for the Northern District of Alabama. All derivative complaints filed in the Circuit Court of Jefferson County, Alabama since 2002 have been consolidated and stayed in favor of the first-filed action captioned *Tucker v. Scrushy*, CV-02-5212, filed August 28, 2002. The *Tucker* complaint names as defendants a number of former HealthSouth officers and directors. *Tucker* also asserts claims on our behalf against Ernst & Young LLP, UBS Group, UBS Investment Bank, and UBS Securities, LLC, as well as against MedCenterDirect.com, Source Medical Solutions, Inc., Capstone Capital Corp., Healthcare Realty Trust, and G.G. Enterprises. Two derivative lawsuits filed in the United States District Court for the Northern District of Alabama were consolidated under the caption *In re HealthSouth Corp. Derivative Litigation*, CV-02-BE-2565. The court stayed further action in this federal consolidated action in deference to litigation filed in state courts in Alabama and Delaware. Two derivative lawsuits filed in the Delaware Court of Chancery were consolidated under the caption *In re HealthSouth Corp. Shareholders Litigation*, Consolidated Case No. 19896. Plaintiffs counsel in this litigation and in *Tucker* agreed to litigate all claims asserted in those lawsuits in the *Tucker* litigation, except for claims relating to an agreement to retire a HealthSouth loan to Richard M. Scrushy with shares of our stock (the Buyback Claim). On November 24, 2003, the court granted the plaintiffs motion for summary judgment on the Buyback Claim and rescinded the retirement of Scrushy s loan. The court s judgment was affirmed on appeal. We have collected a judgment of $12.5 million, net of attorneys fees awarded by the court. See also Note 13, *Shareholders Deficit*, to the consolidated financial statements accompanying our March 2007 Form 8-K.

When originally filed, the primary allegations in the *Tucker* case involved self-dealing by Mr. Scrushy and other insiders through transactions with various entities allegedly controlled by Mr. Scrushy. The complaint was amended four times to add additional defendants and include claims of accounting fraud, improper Medicare billing practices, and additional self-dealing transactions. On January 3, 2006, the Alabama Circuit Court in the *Tucker* case granted the plaintiff s motion for summary judgment against Mr. Scrushy on a claim for the restitution of incentive bonuses Scrushy received for years 1996 through 2002. Including pre-judgment interest, the court s total award was approximately $48 million, which amount was affirmed by the Alabama Supreme Court on August 25, 2006. The judgment does not resolve other claims brought by the plaintiffs against Mr. Scrushy. With interest, the final judgment amount was approximately $52.8 million.

As of December 31, 2006, we had collected approximately $47.9 million of this judgment and had entered into an agreement with Mr. Scrushy which required him to pledge certain parcels of real estate as security for payment of the remainder of the amount. Of the $47.9 million collected as of December 31, 2006, approximately $14.8 million was collected via Mr. Scrushy s return of 723,921 shares of HealthSouth common stock and approximately $21.5 million represents the right of offset discussed below under Litigation by and Against Richard M. Scrushy. During 2006, we recorded $47.8 million as *Recovery of amounts due from Richard M. Scrushy* in our consolidated statement of operations, with the remaining $5.0 million of the total award recorded as *Interest income* (see the consolidated financial statements accompanying our March 2007 Form 8-K). As of December 31, 2006, the

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remainder of the amount owed to us by Mr. Scrushy, or $4.9 million plus interest, was included in *Other current assets* in our condensed consolidated balance sheet. This amount was received in February 2007.

Additionally, we have entered into an agreement with the plaintiffs attorneys in the *Tucker* litigation under which we have agreed to pay them a fee of $17.5 million for obtaining this judgment. This fee was recorded in *Professional fees accounting, tax, and legal* during the fourth quarter of 2006. As of December 31, 2006, we had a remaining balance of approximately $5.9 million of this fee owed to the plaintiffs attorneys. This liability was included in *Accrued expenses and other current liabilities* in our condensed consolidated balance sheet as of December 31, 2006. The remaining balance was paid in February 2007.

On September 26, 2006, certain parties to the *Tucker* litigation entered into and filed a stipulation of settlement. The settlement resolves all claims against former directors and officers of the Company, with the exception of Mr. Scrushy and individuals who have pled guilty to violations of federal criminal law. The substantive terms of the settlement are consistent with the preliminary agreement reached in February 2006. Of the $445 million to be paid in accordance with the settlement of the Consolidated Securities Action, $100 million is being credited to the plaintiffs in the *Tucker* litigation. On September 27, 2006, the Alabama Circuit Court entered an order preliminarily approving the stipulation and settlement. The Court held a hearing on January 9, 2007 to determine the fairness, reasonableness and adequacy of the settlement, whether the settlement should be finally approved by the Court, and to hear and determine any objections to the settlement. The settlement was approved, and an order granting such approval was entered on January 11, 2007. All objections to the settlement were withdrawn, and no individual class members opted out of the settlement. Additionally, we reached an agreement with the plaintiffs attorneys in the *Tucker* litigation under which we have agreed to pay them a fee of $15 million in connection with the settlement of the Consolidated Securities Action (which is in addition to the $17.5 million fee discussed above). This fee was recorded in *Professional fees accounting, tax, and legal* during the fourth quarter of 2006. The related liability was included in *Accrued expenses and other current liabilities* in our condensed consolidated balance sheet as of December 31, 2006. The fee was paid on June 29, 2007.

The *Tucker* derivative claims against Mr. Scrushy, UBS Group, UBS Investment Bank and UBS Securities, LLC remain pending and are moving through discovery.

Litigation by and Against Former Independent Auditor

On March 18, 2005, Ernst & Young LLP filed a lawsuit captioned *Ernst & Young LLP v. HealthSouth Corp.*, CV-05-1618, in the Circuit Court of Jefferson County, Alabama. The complaint asserts that the filing of the claims against us was for the purpose of suspending any statute of limitations applicable to those claims. The complaint alleges that HealthSouth s former management provided Ernst & Young LLP with fraudulent management representation letters, financial statements, invoices, bank reconciliations, and journal entries in an effort to conceal accounting fraud. Ernst & Young LLP claims that as a result of our actions, Ernst & Young LLP s reputation has been injured and it has and will incur damages, expense, and legal fees. Ernst & Young LLP seeks recoupment and setoff of any recovery against Ernst & Young LLP in the *Tucker* case, as well as litigation fees and expenses, damages for loss of business and injury to reputation, and such other relief to which it may be entitled. On April 1, 2005, we answered Ernst & Young LLP s claims and asserted counterclaims alleging, among other things, that from 1996 through 2002, when Ernst & Young LLP served as our independent auditor, Ernst & Young LLP acted recklessly and with gross negligence in performing its duties, and specifically that Ernst & Young LLP failed to perform reviews and audits of our financial statements with due professional care as required by law and by its contractual agreements with us. Our counterclaims further allege that Ernst & Young LLP either knew of or, in the exercise of due care, should have discovered and investigated the fraudulent and improper accounting practices being directed by Richard M. Scrushy and certain other officers and employees, and should have reported them to our board of directors and the Audit Committee. The counterclaims seek compensatory and punitive damages, disgorgement of fees received from us by Ernst & Young LLP, and attorneys fees and costs. Upon Ernst & Young LLP s motion, the Alabama state court referred Ernst & Young LLP s claims and HealthSouth s counterclaims to arbitration. On July 12, 2006, the derivative plaintiff filed an arbitration demand on behalf of HealthSouth against Ernst & Young LLP. On August 7, 2006, Ernst & Young LLP filed an answering statement and counterclaim in the arbitration reasserting the claims made in state court.

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We are vigorously defending the claims against us in this case, and also vigorously pursuing our claims against Ernst & Young LLP. Based on the stage of litigation, and review of the current facts and circumstances, it is not possible to estimate the amount of loss or range of possible loss that might result from an adverse judgment or a settlement of this case. Discovery relating to the claims is now moving forward on a schedule coordinated with parallel federal securities laws claims by former stockholders and bondholders of the Company against Ernst & Young LLP.

ERISA Litigation

In 2003, six lawsuits were filed in the United States District Court for the Northern District of Alabama against us and some of our current and former officers and directors alleging breaches of fiduciary duties in connection with the administration of our Employee Stock Benefit Plan (the ESOP). These lawsuits were consolidated under the caption *In re HealthSouth Corp. ERISA Litigation*, Consolidated Case No. CV-03-BE-1700-S (the ERISA Action). The plaintiffs filed a consolidated complaint on December 19, 2003 that alleged, generally, that fiduciaries to the ESOP breached their duties to loyally and prudently manage and administer the ESOP and its assets in violation of sections 404 and 405 of the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1001 *et seq.* (ERISA), by failing to monitor the administration of the ESOP, failing to diversify the portfolio held by the ESOP, and failing to provide other fiduciaries with material information about the ESOP. The plaintiffs sought actual damages including losses suffered by the plan, imposition of a constructive trust, equitable and injunctive relief against further alleged violations of ERISA, costs pursuant to 29 U.S.C. § 1132(g), and attorneys fees. The plaintiffs also sought damages related to losses under the plan as a result of alleged imprudent investment of plan assets, restoration of any profits made by the defendants through use of plan assets, and restoration of profits that the plan would have made if the defendants had fulfilled their fiduciary obligations. Pursuant to an Amended Class Action Settlement Agreement entered into on March 6, 2006, all parties agreed to a global settlement of the claims in the ERISA Action. Under the terms of this settlement, Michael Martin, a former chief financial officer of the Company, contributed $350,000 to resolve claims against him, Richard M. Scrushy and our insurance carriers contributed $3.5 million to resolve claims against him, and HealthSouth and its insurance carriers contributed $25 million to settle claims against all remaining defendants, including HealthSouth. In addition, we were required to contribute the first $1.0 million recovered from Mr. Scrushy for the restitution of incentive bonuses paid to him during 1996 through 2002. On June 28, 2006, the Court granted final approval to the Amended Class Action Settlement Agreement and the ERISA Action was dismissed with prejudice.

Litigation by and Against Richard M. Scrushy

After the dismissal of several lawsuits filed against us by Richard M. Scrushy, on December 9, 2005, Mr. Scrushy filed a complaint in the Circuit Court of Jefferson County, Alabama, captioned *Scrushy v. HealthSouth*, CV-05-7364. The complaint alleges that, as a result of Mr. Scrushy s removal from the position of chief executive officer in March 2003, we owe him in excess of $70 million pursuant to an employment agreement dated as of September 17, 2002. On December 28, 2005, HealthSouth counterclaimed against Mr. Scrushy, asserting claims for breaches of fiduciary duty and fraud arising out of Mr. Scrushy s tenure at HealthSouth, and seeking compensatory damages, punitive damages, and disgorgement of wrongfully obtained benefits. Both the claims by Mr. Scrushy and HealthSouth s counterclaims remain pending in Circuit Court.

In addition, on or about December 19, 2005, Mr. Scrushy filed a demand for arbitration with the American Arbitration Association pursuant to an indemnity agreement with us. The arbitration demand sought to require us to pay expenses which he estimated exceeded $31 million incurred by Mr. Scrushy, including attorneys fees, in connection with the defense of criminal fraud claims against him and in connection with a preliminary hearing in the SEC litigation.

On October 17, 2006, the arbitrator issued a final award of approximately $17.0 million to Mr. Scrushy and further ruled that Mr. Scrushy was entitled to payment by HealthSouth of approximately $4.0 million in pre-judgment interest and attorneys fees and expenses incurred by Mr. Scrushy in connection with the arbitration proceeding. On August 31, 2006, HealthSouth and the *Tucker* plaintiffs filed a joint motion in the *Tucker* case to offset the entire award to Mr. Scrushy in the arbitration, including fees and interest, against the approximately $48

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million judgment against Mr. Scrushy in *Tucker* for repayment of his bonuses, which judgment is accruing interest. Mr. Scrushy opposed that effort, and on October 17, 2006 filed a lawsuit captioned *Scrushy v. HealthSouth Corporation*, CA No. 2483-N, in the Delaware Court of Chancery for New Castle County seeking confirmation of the arbitration award in that court. A settlement was reached with Mr. Scrushy by which he agreed to an offset of the arbitrator s award in the amount of $21.5 million, which amount is included in the amount collected from Mr. Scrushy on the *Tucker* judgment. We accrued an estimate of these fees as part of *Professional fees accounting, tax, and legal* in our December 31, 2005 and 2004 consolidated statements of operations. While the arbitrator s ruling provided that we may have an obligation to indemnify Mr. Scrushy for certain costs associated with ongoing litigation, the court s order approving the securities litigation settlement prohibits Mr. Scrushy from seeking indemnity or contribution in the securities class action. This order has been appealed by Mr. Scrushy. As of June 30, 2007 and December 31, 2006, an estimate of these legal fees is included in *Accrued expenses and other current liabilities* in our condensed consolidated balance sheets.

Litigation Against Former Officers

On June 10, 2004, we filed a collection action in the Circuit Court of Jefferson County, Alabama, captioned *HealthSouth Corp. v. James Goodreau*, CV-04-3619, to collect unpaid loans in the original principal amount of $55,500 that we made to James A. Goodreau, our former Director of Corporate Security, while he was a HealthSouth employee. Mr. Goodreau asserted counterclaims against us seeking compensatory damages in the approximate amount of $6 million dollars, plus punitive damages, based upon his contention that he was promised lifetime employment with us by Mr. Scrushy and that he was wrongfully terminated by us in May of 2003. On September 26, 2006, the Circuit Court entered an order on our motion for summary judgment requiring Mr. Goodreau to repay the loans plus accrued interest and to reimburse us for the reasonable attorneys fees that we have incurred to collect those loans. Mr. Goodreau s counterclaims were tried by a jury and on October 27, 2006, the jury returned an award in Mr. Goodreau s favor in the approximate amount of $1.9 million, which we recorded in *Government, class action, and related settlements expense* in the third quarter of 2006. We filed a notice of appeal for this award to the Alabama Supreme Court and attended a court-ordered mediation. The liability associated with this jury award was included in *Government, class action, and related settlements* in our condensed consolidated balance sheets as of June 30, 2007 and December 31, 2006. On July 17, 2007, we entered into a confidential settlement agreement with Mr. Goodreau to resolve this matter.

Certain Regulatory Actions

The False Claims Act, 31 U.S.C. § 3729, allows private citizens, called relators, to institute civil proceedings alleging violations of the False Claims Act. These so-called *qui tam*, or whistleblower, cases are sealed by the court at the time of filing. The only parties privy to the information contained in the complaint are the relator, the federal government, and the presiding court. It is possible that *qui tam* lawsuits other than those discussed in these financial statements have been filed against us and that we are unaware of such filings or have been ordered by the presiding court not to discuss or disclose the filing of such lawsuits. We may be subject to liability under one or more undisclosed qui tam cases brought pursuant to the False Claims Act.

On April 1, 1999, a plaintiff relator filed a lawsuit under the False Claims Act captioned *United States ex rel. Mathews v. Alexandria Rehabilitation Hospital*, CV-99-0604, in the United States District Court for the Western District of Louisiana. On February 29, 2000, the United States elected not to intervene in the lawsuit. The complaint, as amended, alleged, among other things, that we filed fraudulent reimbursement claims under the Medicare program on a nationwide basis. On November 14, 2006, the plaintiff relator filed a motion for partial summary judgment, and we filed a cross-motion for summary judgment on January 16, 2007. On July 18, 2007, the court granted our motion for summary judgment, dismissing the case with prejudice.

On October 27, 2006, we settled two sealed lawsuits brought under the federal False Claims Act, related to services provided at our inpatient rehabilitation hospitals. These lawsuits, captioned *United States ex rel. Knight v. HealthSouth, et al.,* Civil No. 5:03cv367, and *United States ex rel. Bateman Gibson v. HealthSouth, et al.*, Civil No. 04-2668, were filed in the United States District Court for the Northern District of Florida and the United States District Court for the Western District of Tennessee, respectively. Each lawsuit was filed under seal by a *qui tam*

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relator and related to purchasing policies for orthotic and prosthetic devices. The complaints alleged that we began a practice of engaging in improper billing practices relating to certain prosthetic and orthotic devices in 1994 that resulted in false claims under the federal Medicare program. Pursuant to the settlement, we paid $4.0 million to the United States and entered into an addendum to our Corporate Integrity Agreement. The addendum requires additional compliance training and annual audits of billing practices relating to prosthetic and orthotic devices. The addendum has a term of three years and will run concurrently with our existing five-year Corporate Integrity Agreement. Approximately $3.0 million of this settlement was included in *Government, class action, and related settlements expense* in the second quarter of 2006, with the remaining $1.0 million recorded to the same line item in the third quarter of 2006. We paid this settlement in the fourth quarter of 2006.

General Medicine, Meadowbrook, and Greystone Ventures Actions

On August 16, 2004, General Medicine, P.C. (General Medicine) filed a lawsuit against us captioned *General Medicine, P.C. v. HealthSouth Corp.*, CV-04-958, in the Circuit Court of Shelby County, Alabama, seeking the recovery of allegedly fraudulent transfers involving assets of Horizon/CMS Healthcare Corporation (Horizon/CMS), a former subsidiary of HealthSouth. The claim against Horizon/CMS originates from a contract entered into in 1995 between General Medicine and Horizon/CMS whereby General Medicine agreed to provide management services to skilled nursing facilities owned by Horizon/CMS. Horizon/CMS terminated the agreement six months after it was executed, and General Medicine then initiated a lawsuit in the United States District Court for the Eastern District of Michigan in 1996. HealthSouth acquired Horizon/CMS in 1997 and sold it to Meadowbrook Healthcare, Inc. (Meadowbrook) in 2001 pursuant to a stock purchase agreement. In 2004, Meadowbrook consented to the entry of a final judgment in the amount of $376 million (the Consent Judgment) in favor of General Medicine against Horizon/CMS for the alleged wrongful termination of the contract with General Medicine. The settlement agreement which was the basis for the Consent Judgment provided that Meadowbrook would pay only $0.3 million and would receive a release. The settlement agreement further provided that General Medicine would seek to recover the balance from HealthSouth. The complaint by General Medicine against HealthSouth alleged that while Horizon/CMS was a wholly owned subsidiary of HealthSouth and General Medicine was an existing creditor of Horizon/CMS, we caused Horizon/CMS to transfer its assets to us for less than a reasonably equivalent value and/or with the actual intent to defraud creditors of Horizon/CMS, including General Medicine, in violation of the Alabama Uniform Fraudulent Transfer Act. General Medicine s complaint requests relief including recovery of the unpaid amount of the Consent Judgment, the avoidance of the subject transfers of assets, attachment of the assets transferred to us, appointment of a receiver over the transferred properties, and a monetary judgment for the value of properties transferred.

We filed an answer denying liability to General Medicine, and on February 28, 2005, the General Medicine case was transferred to the Circuit Court of Jefferson County, Alabama, and assigned case number CV-05-1483. We asserted counterclaims against Meadowbrook, General Medicine, and Horizon/CMS for fraud, injurious falsehood, tortious interference with business relations, bad faith, conspiracy, unjust enrichment, and other causes of action. In our counterclaims, we allege that the Consent Judgment is the product of fraud, collusion and bad faith by Meadowbrook, General Medicine, and Horizon/CMS and, further, that these parties are guilty of a conspiracy to manufacture a lawsuit against HealthSouth in favor of General Medicine and to divert the assets of Horizon/CMS to Meadowbrook and away from creditors, including HealthSouth. On January 3, 2006, we filed a motion for summary judgment challenging General Medicine s standing under the Alabama Uniform Fraudulent Transfer Act to bring this action against us to collect monies allegedly owed by Horizon/CMS. After the court s denial of our motion, we filed a petition for writ of mandamus with the Supreme Court of Alabama requesting a reversal of that decision, which was denied. We filed an Application for Rehearing on March 2, 2007 requesting the Alabama Supreme Court to reconsider its ruling, which was denied on June 15, 2007.

On June 15, 2007, we entered into a confidential settlement agreement with Meadowbrook and Horizon/CMS to resolve our counterclaims against them in the General Medicine action (as well as other claims and disputes between the parties). The settlement of our counterclaims against Meadowbrook and Horizon/CMS does not affect the claims asserted by General Medicine against us or our counterclaims against General Medicine, which claims and counterclaims are currently in the discovery phase. We intend to vigorously defend ourselves against General Medicine s claim and to vigorously prosecute our counterclaims against General Medicine. Based on the

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stage of litigation, and review of the current facts and circumstances, it is not possible to estimate the amount of loss or range of possible loss that might result from an adverse judgment or settlement of this case.

After our sale of all of our stock in Horizon/CMS to Meadowbrook, Meadowbrook changed its name to Greystone Ventures, Inc. (Greystone). On June 8, 2006, Greystone and Horizon/CMS filed a lawsuit against us in the Circuit Court of Jefferson County, Alabama captioned *Greystone Ventures, Inc., et al. v. HealthSouth Corporation*, CV-2006-03403. The complaint alleges that we received a settlement from Gulf Insurance Company in June of 2004 in the approximate amount of $4.0 million dollars, and that some or all of the proceeds of that settlement belong to Horizon/CMS and Greystone. The complaint further alleges that we are liable to Horizon/CMS and Greystone for conversion, fraudulent failure to disclose, money had and received, unjust enrichment, negligence and wantonness in connection with our alleged failure to pay the proceeds of the Gulf Insurance Company settlement to Greystone and Horizon/CMS. We filed an answer on July 17, 2006 denying that we have any liability to Greystone or Horizon/CMS with regard to allegations made in their complaint. On June 15, 2007, we entered into a confidential settlement agreement with Greystone and Horizon/CMS to resolve the Greystone Action (as well as other claims and disputes between the parties). The settlement did not have a material impact on our financial position, results of operations, or cash flows.

Other Litigation

On September 17, 1998, John Darling, who was one of the federal False Claims Act relators in the now-settled *Devage* case, filed a lawsuit captioned *Darling v. HealthSouth Sports Medicine & Rehabilitation, et al*., 98-6110-CI-20, in the Circuit Court for Pinellas County, Florida. The complaint alleged that Mr. Darling was injured while receiving physical therapy during a 1996 visit to a HealthSouth outpatient rehabilitation facility in Clearwater, Florida. The complaint was amended in December 2004 to add a punitive damages claim. This amended complaint alleged that fraudulent misrepresentations and omissions by us resulted in the injury to Mr. Darling. The court ordered the parties to participate in non-binding arbitration which resulted in a finding in our favor on December 27, 2005. We entered into a settlement agreement with Mr. Darling on February 3, 2007 pursuant to which we paid certain damages pursuant to a confidential settlement agreement during the first quarter of 2007. The cost of the settlement is included in *Government, class action, and related settlements expense* in our results of operations for the fourth quarter of 2006 and in *Government, class action, and related settlements* in our condensed consolidated balance sheet as of December 31, 2006.

We have been named as a defendant in two lawsuits brought by individuals in the Circuit Court of Jefferson County, Alabama, *Nichols v. HealthSouth Corp.*, CV-03-2023, filed March 28, 2003, and *Hilsman v. Ernst & Young, HealthSouth Corp., et al.*, CV-03-7790, filed December 12, 2003. The plaintiffs allege that we, some of our former officers, and our former auditor engaged in a scheme to overstate and misrepresent our earnings and financial position. The plaintiffs seek compensatory and punitive damages. On March 24, 2003, a lawsuit captioned *Warren v. HealthSouth Corp., et al.*, CV-03-5967, was filed in the Circuit Court of Montgomery County, Alabama. The lawsuit, which claims damages for the defendants alleged negligence, wantonness, fraud and breach of fiduciary duty, was transferred to the Circuit Court of Jefferson County, Alabama. Each of these three lawsuits described in this paragraph was consolidated with the *Tucker* case for discovery and other pretrial purposes. The plaintiffs in these cases are subject to the Consolidated Securities Action settlement discussed in Note 9, *Settlements*, and thereby foreclosed from pursuing these state court actions based on purchases made during the class period unless they opted out of that settlement. The plaintiffs in *Warren v. HealthSouth Corp., et al.* did not opt out of the settlement. The plaintiffs in *Hilsman v. Ernst & Young, et al.* attempted to opt out of the settlement, but their election was deemed invalid by the agent. At present, it is unclear whether the plaintiffs in the *Hilsman* action will challenge this determination. The *Nichols* lawsuit asserts claims on behalf of a number of plaintiffs, all but three of whom opted out of the settlement. John Kapoor, who claimed to have purchased over 180,000 shares of stock, attempted to opt-out, but his attempt was deemed invalid by the court. It is unclear whether Mr. Kapoor will challenge this determination. The remaining *Nichols* plaintiffs that opted out of the settlement claim losses of approximately $5.4 million. The *Nichols* case remains stayed in Circuit Court. We intend to vigorously defend ourselves in these cases. Based on the stage of litigation, and review of the current facts and circumstances, it is not possible to estimate the amount of loss or range of possible loss that might result from an adverse judgment or a settlement of these cases.

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On December 28, 2004, we commenced a collection action in the Circuit Court of Jefferson County, Alabama, captioned *HealthSouth Medical Center, Inc. v. Neurological Surgery Associates, P.C.,* CV-04-7700, to collect unpaid loans in the original principal amount of approximately $0.3 million made to Neurological Surgery Associates, P.C. (NSA), pursuant to a written Practice Guaranty Agreement. The purpose of the loans was to enable NSA to employ a physician who would bring necessary specialty skills to patients served by both NSA and the acute-care hospital in Birmingham, Alabama we sold in March 2006. NSA has asserted counterclaims alleging that we breached verbal promises to lease space and employees from NSA, to pay NSA for billing and coding services performed by NSA on behalf of the subject physician-employee, and to pay NSA to manage the subject physician-employee. On December 21, 2006, NSA filed an Amendment to Counterclaim asserting new counterclaims against us and adding NSA s principal, Dr. Swaid Swaid, M.D., as a counterclaim plaintiff. NSA and Dr. Swaid allege that we are liable to them in connection with the subject Practice Guaranty Agreement under a variety of legal theories, including fraud, breach of fiduciary duty, conspiracy, abuse of process, breach of contract and unjust enrichment. Dr. Swaid also alleges that we breached a Medical Director Agreement with him. The Amendment to Counterclaim seeks unspecified damages and other relief. This case is currently in the discovery phase. We intend to vigorously defend ourselves against these counterclaims. Based on the stage of litigation, and review of the current facts and circumstances, it is not possible to estimate the amount of loss or range of possible loss that might result from an adverse judgment or settlement of this case.

On June 2, 2006, we were named as a defendant in a lawsuit captioned *Brockovich v. HealthSouth Corporation, et al.*, Case No. SACV06-546-DOC(MLGx), filed under the Medicare Secondary Payor statute, 42 U.S.C. § 1395y(b), in the United States District Court for the Central District of California, Southern Division, against HealthSouth, HealthSouth Hospital Corporation, HCS, and certain insurance companies. The complaint alleged that HealthSouth charged Medicare to treat illnesses that it caused, at least in part, by medical error or neglect and seeks recovery of unspecified damages. On October 24, 2006, the court dismissed the plaintiff s complaint with prejudice due to lack of constitutional standing. This case has been appealed to the Ninth Circuit Court of Appeals where it remains pending.

Other Matters

The reconstruction of our historical financial records has resulted in the restatement of not only our 2001 and 2000 consolidated financial statements, but also the financial statements of certain of our subsidiary partnerships. The process of communicating the effect of these restatements to the outside partners will continue in 2007. These restatements have had a negative impact on our relationships with our partners and may result in litigation against us. We have and may continue to incur additional charges to reduce the economic impact to our partners.

In addition, as it is our obligation as a participant in Medicare and other federal health care programs, we routinely conduct audits and reviews of the accuracy of our billing systems and other regulatory compliance matters. As a result of these reviews, we have made, and will continue to make, disclosures to the United States Department of Health & Human Services Office of Inspector General relating to amounts that we suspect represent over-reimbursements from these programs, whether due to inaccurate billing or otherwise. Some of these disclosures have resulted in, or may result in, the Company refunding amounts to Medicare or other federal health care programs.

11. Condensed Consolidating Financial Information:

The accompanying condensed consolidating financial information has been prepared and presented pursuant to SEC Regulation S-X, Rule 3-10, Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered. Each of the subsidiary guarantors are 100% owned by HealthSouth, and all guarantees are full and unconditional and joint and several. HealthSouth s investments in its consolidated subsidiaries, as well as guarantor subsidiaries investments in non-guarantor subsidiaries and non-guarantor subsidiaries investments in guarantor subsidiaries, are presented under the equity method of accounting.

As described in Note 9, *Long-term Debt*, to the consolidated financial statements accompanying our March 2007 Form 8-K, the terms of our Credit Agreement restrict us from declaring or paying cash dividends on our

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common stock unless: (1) we are not in default under our Credit Agreement and (2) the amount of the dividend, when added to the aggregate amount of certain other defined payments made during the same fiscal year, does not exceed certain maximum thresholds. However, as described in Note 12, *Convertible Perpetual Preferred Stock*, to the consolidated financial statements accompanying our March 2007 Form 8-K, our Series A Preferred Stock generally provides for the payment of cash dividends, subject to certain limitations.

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Notes to Condensed Consolidated Financial Statements

Condensed Consolidating Balance Sheet

	As of June 30, 2007 HealthSouth Corporation (In Millions)	Guarantor Subsidiaries	Non Guarantor Subsidiaries	Eliminating Entries	HealthSouth Consolidated
Assets					
Current assets:					
Cash and cash equivalents	$	$ 11.9	$ 9.1	$	$ 21.0
Current portion of restricted cash	5.4		45.5		50.9
Current portion of restricted marketable securities			16.8		16.8
Accounts receivable, net	16.3	137.9	61.2		215.4
Insurance recoveries receivable	230.0				230.0
Other current assets	73.7	37.2	56.0	(97.8)	69.1
Current assets held for sale	58.8	1.8	19.1		79.7
Total current assets	384.2	188.8	207.7	(97.8)	682.9
Property and equipment, net	84.2	491.1	190.7		766.0
Goodwill	51.3	201.7	153.0		406.0
Intangible assets, net	3.4	15.9	9.1		28.4
Investment in and advances to nonconsolidated affiliates	3.6	27.7	9.8	(1.0)	40.1
Assets held for sale	14.9	32.9	126.0	(0.9)	172.9
Income tax refund receivable	208.9				208.9
Other long-term assets	84.3	48.1	113.6	(148.8)	97.2
Intercompany (payable) receivable	(103.2)	(1.2)	(72.0)	176.4	
Total assets	$ 731.6	$ 1,005.0	$ 737.9	$ (72.1)	$ 2,402.4
Liabilities and Shareholders (Deficit) Equity					
Current liabilities:					
Current portion of long-term debt	$ 28.2	$ 10.7	$ 1.8	$	$ 40.7
Accounts payable	31.7	18.4	8.6		58.7
Accrued expenses and other current liabilities	272.2	44.9	29.7	(39.3)	307.5
Refunds due patients and other third-party payors	12.9				12.9
Government, class action, and related settlements	454.0				454.0
Current liabilities held for sale	253.8	6.0	12.0		271.8
Total current liabilities	1,052.8	80.0	52.1	(39.3)	1,145.6
Long-term debt, net of current portion	2,355.2	73.3	31.5	(100.0)	2,360.0
Liabilities held for sale	2.8	5.9	4.7		13.4
Other long-term liabilities	61.0	7.6	127.2	(20.8)	175.0
Intercompany (receivable) payable	(1,338.8)	480.0	1,209.4	(350.6)	
	2,133.0	646.8	1,424.9	(510.7)	3,694.0
Commitments and contingencies					
Minority interest in equity of consolidated affiliates			109.8		109.8
Convertible perpetual preferred stock	387.4				387.4
Shareholders (deficit) equity	(1,788.8)	358.2	(796.8)	438.6	(1,788.8)
Total liabilities and shareholders (deficit) equity	$ 731.6	$ 1,005.0	$ 737.9	$ (72.1)	$ 2,402.4

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Notes to Condensed Consolidated Financial Statements

Condensed Consolidating Balance Sheet

	As of December 31, 2006 HealthSouth Corporation (In Millions)	Guarantor Subsidiaries	Non Guarantor Subsidiaries	Eliminating Entries	HealthSouth Consolidated
Assets					
Current assets:					
Cash and cash equivalents	$ 17.5	$ 2.8	$ 6.9	$	$ 27.2
Current portion of restricted cash	3.0		57.3		60.3
Current portion of restricted marketable securities			37.5		37.5
Accounts receivable, net	11.7	141.2	64.4		217.3
Insurance recoveries receivable	230.0				230.0
Other current assets	64.5	37.3	32.0	(55.7)	78.1
Current assets held for sale	18.0	46.4	165.5		229.9
Total current assets	344.7	227.7	363.6	(55.7)	880.3
Property and equipment, net	106.2	515.5	189.5		811.2
Goodwill	50.5	201.7	153.9		406.1
Intangible assets, net	1.8	16.8	11.8		30.4
Investment in and advances to nonconsolidated affiliates	1.7	26.0	10.0		37.7
Assets held for sale	171.3	135.7	528.4	(1.7)	833.7
Income tax refund receivable	218.8				218.8
Other long-term assets	96.4	63.3	89.2	(106.3)	142.6
Intercompany (payable) receivable	(6.0)	262.3	(69.8)	(186.5)	
Total assets	$ 985.4	$ 1,449.0	$ 1,276.6	$ (350.2)	$ 3,360.8
Liabilities and Shareholders (Deficit) Equity					
Current liabilities:					
Current portion of long-term debt	$ 21.7	$ 10.2	$ 1.7	$	$ 33.6
Accounts payable	35.4	21.8	10.3		67.5