CORVEL CORP
Form 10-Q
November 05, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2015

or

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

For the transition period from __________ to __________

Commission file number 0-19291

CORVEL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**33-0282651**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**
2010 Main Street, Suite 600	
Irvine, CA	**92614**
(Address of principal executive office)	**(zip code)**

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (check one)

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller Reporting Company	¨

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

The number of shares outstanding of the registrant s Common Stock, $0.0001 par value per share, as of October 30, 2015 was 19,689,764.

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CORVEL CORPORATION

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PART I - FINANCIAL INFORMATION

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Part I - Financial Information

Item 1 - Financial Statements

CORVEL CORPORATION

CONSOLIDATED BALANCE SHEETS

	March 31, 2015	September 30, 2015 (Unaudited)
Assets		
Current Assets		
Cash and cash equivalents (Note A)	$ 25,516,000	$ 24,887,000
Customer deposits	17,319,000	24,722,000
Accounts receivable, net	57,537,000	59,225,000
Prepaid taxes and expenses	11,675,000	6,470,000
Deferred income taxes	7,181,000	7,580,000
Total current assets	119,228,000	122,884,000
Property and equipment, net	56,299,000	54,647,000
Goodwill	36,814,000	36,814,000
Other intangibles, net (Note F)	4,736,000	4,508,000
Other assets	1,677,000	2,841,000
TOTAL ASSETS	$ 218,754,000	$ 221,694,000
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts and taxes payable	$ 15,770,000	$ 15,499,000
Accrued liabilities	58,318,000	61,853,000
Total current liabilities	74,088,000	77,352,000
Deferred income taxes	16,743,000	16,743,000
Commitments and contingencies (Notes G and H)		
Stockholders' Equity		
Common stock, $.0001 par value: 120,000,000 shares authorized at March 31, 2015 and September 30, 2015; 53,243,157 shares issued (20,250,669 shares outstanding, net of Treasury shares) and 53,339,469 shares issued (19,787,279 shares outstanding, net of Treasury shares) at March 31, 2015 and September 30, 2015, respectively	3,000	3,000
Paid-in capital	123,440,000	126,724,000
Treasury Stock (32,992,488 shares at March 31, 2015 and 33,552,190	(360,278,000)	(379,053,000)

shares at September 30, 2015)		
Retained earnings	364,758,000	379,925,000
Total stockholders' equity	127,923,000	127,599,000
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 218,754,000	$ 221,694,000

See accompanying notes to consolidated financial statements.

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CORVEL CORPORATION

CONSOLIDATED INCOME STATEMENTS UNAUDITED

	Three Months Ended September 30,	
	2014	2015
REVENUES	$ 123,714,000	$ 124,460,000
Cost of revenues	98,247,000	97,776,000
Gross profit	25,467,000	26,684,000
General and administrative expenses	12,749,000	13,209,000
Income before income tax provision	12,718,000	13,475,000
Income tax provision	4,835,000	5,208,000
NET INCOME	$ 7,883,000	$ 8,267,000
Net income per common and common equivalent share		
Basic	$ 0.38	$ 0.42
Diluted	$ 0.37	$ 0.41
Weighted average common and common equivalent shares		
Basic	20,819,000	19,902,000
Diluted	21,050,000	20,063,000

See accompanying notes to consolidated financial statements.

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CORVEL CORPORATION

CONSOLIDATED INCOME STATEMENTS UNAUDITED

	Six Months Ended September 30, 2014	2015
REVENUES	$ 248,078,000	$ 251,399,000
Cost of revenues	194,911,000	198,532,000
Gross profit	53,167,000	52,867,000
General and administrative expenses	26,954,000	28,171,000
Income before income tax provision	26,213,000	24,696,000
Income tax provision	10,031,000	9,529,000
NET INCOME	$ 16,182,000	$ 15,167,000
Net income per common and common equivalent share		
Basic	$ 0.78	$ 0.76
Diluted	$ 0.77	$ 0.75
Weighted average common and common equivalent shares		
Basic	20,877,000	20,026,000
Diluted	21,130,000	20,199,000

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CORVEL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS UNAUDITED

	Six Months Ended September 30, 2014	2015
Cash flows from Operating Activities		
NET INCOME	$ 16,182,000	$ 15,167,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8,718,000	9,916,000
Loss (gain) on disposal of assets	12,000	(5,000)
Stock compensation expense	1,162,000	1,104,000
Write-off of uncollectible accounts	785,000	897,000
Deferred income tax	(450,000)	(399,000)
Changes in operating assets and liabilities		
Accounts receivable	(3,856,000)	(2,585,000)
Customer deposits	(311,000)	(7,403,000)
Prepaid taxes and expenses	(1,021,000)	5,205,000
Other assets	160,000	(571,000)
Accounts and taxes payable	(4,277,000)	(271,000)
Accrued liabilities	(1,466,000)	3,535,000
Net cash provided by operating activities	15,638,000	24,590,000
Cash Flows from Investing Activities		
Investment in private equity	(800,000)	(600,000)
Purchase of property and equipment	(9,873,000)	(8,025,000)
Net cash (used in) investing activities	(10,673,000)	(8,625,000)
Cash Flows from Financing Activities		
Purchase of treasury stock	(13,158,000)	(18,775,000)
Tax effect of stock option exercises	544,000	475,000
Exercise of common stock options	745,000	1,525,000
Exercise of employee stock purchase options	200,000	181,000
Net cash (used in) financing activities	(11,669,000)	(16,594,000)
Decrease in cash and cash equivalents	(6,704,000)	(629,000)
Cash and cash equivalents at beginning of period	34,866,000	25,516,000
Cash and cash equivalents at end of period	$ 28,162,000	$ 24,887,000

Supplemental Cash Flow Information:

Income taxes paid	$ 10,632,000	$ 6,946,000

See accompanying notes to consolidated financial statements.

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

Note A Basis of Presentation and Summary of Significant Accounting Policies

The unaudited financial statements herein have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). The accompanying interim financial statements have been prepared under the presumption that users of the interim financial information have either read or have access to the audited financial statements for the latest fiscal year ended March 31, 2015. Accordingly, note disclosures which would substantially duplicate the disclosures contained in the March 31, 2015 audited financial statements have been omitted from these interim financial statements.

The Company evaluated all subsequent events or transactions through the date of filing this report. Subsequent to the end of the quarter, through October 30, 2015, the Company repurchased 99,403 shares for $3,287,000 at an average of $33.07 per share. These shares were repurchased under the Company s ongoing share repurchase program described in Note C.

Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the three and six months ended September 30, 2015 are not necessarily indicative of the results that may be expected for the fiscal year ending March 31, 2016. For further information, refer to the consolidated financial statements and notes for the fiscal year ended March 31, 2015 included in the Company s Annual Report on Form 10-K filed with the SEC on June 11, 2015.

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

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

Cash and Cash Equivalents: Cash and cash equivalents consist of short-term, highly-liquid, investment-grade, interest-bearing securities with maturities of 90 days or less when purchased. Customer deposits represent cash that is expected to be returned or applied towards payment within one year through our provider reimbursement services.

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

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

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

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

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

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

The carrying amount of the Company s financial instruments (i.e. cash, accounts receivable, accounts payable, etc.) are all Level 1 and approximate their fair values at March 31, 2015 and September 30, 2015. The Company has no Level 2 or Level 3 assets.

Investment in Private Equity: During the quarter ended June 30, 2014, the Company s board of directors approved an investment of $2,000,000 into a private equity limited partnership that invests in start-up companies. During fiscal year 2015, the Company invested $1,400,000 into the partnership. The remaining $600,000 was invested during the quarter ended June 30, 2015. The Company accounts for the investment on the cost method and will periodically review the investment for possible impairment. There was no impairment on investment for the year ended March 31, 2015 and for the six months ended September 30, 2015. The investment is recorded in other assets on the accompanying consolidated balance sheets. There have been no identified events or changes in circumstances that may have a significant adverse effect on the fair value of the investment, and in accordance with ASC 825-10-50-16 through 50-19, it is not practicable to estimate the fair value of the investment.

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

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

Management evaluates agreements with customers in accordance with the provision of the revenue recognition topic ASC 605-25 that addresses multiple-deliverable revenue arrangements. The multiple-deliverable arrangements entered into consist of bundled managed care which includes various units of accounting such as network solutions, and patient management which includes claims administration. Such elements are considered separate units of accounting due to each element having value to the customer on a stand-alone basis. The selling price for each unit of accounting is determined using contract price and management estimates. When the Company s customers purchase several products, the pricing of the products sold is generally the same as if the products were sold on an individual basis. Revenue is recognized as the work is performed in accordance with the Company s customer contracts. Based upon the nature of the Company s products, bundled managed care elements are generally delivered in the same accounting period. The Company recognizes revenue for patient management claims administration services over the life of the customer contract. The Company estimates, based upon prior experience in managing claims, the deferral amount from when the claim is received to when the customer contract expires.

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

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

Recent Accounting Pronouncements: On May 28, 2014, the FASB issued ASU 2014-09 regarding ASC Topic 606, Revenue from Contracts with Customers. The standard provides principles for recognizing revenue for the transfer of promised goods or services to customers with the consideration to which the entity expects to be entitled in exchange for those goods or services. In July 2015, the FASB approved a one-year delay of the effective date of this new revenue recognition standard. The guidance will now be effective for our fiscal year beginning April 1, 2018. We are currently evaluating the accounting, transition, and disclosure requirements of the standard and cannot currently estimate the financial statement impact of adoption.

Accounts Receivable: The majority of the Company s accounts receivable are due from companies in the property and casualty insurance industries, self-insured employers, and government entities. Accounts receivable are generally due within 30 days and are stated as amounts due from customers net of an allowance for doubtful accounts. Those accounts outstanding longer than the contractual payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company s previous loss history, the customer s current ability to pay its obligation to the Company and the condition of the general economy and the industry as a whole. No one customer accounted for 10% or more of accounts receivable at either March 31, 2015 or September 30, 2015. No one customer accounted for 10% or more of revenue during the six months ended September 30, 2014 or 2015.

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

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

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

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

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

Earnings Per Share: Earnings per common share-basic is based on the weighted average number of common shares outstanding during the period. Earnings per common share-diluted is based on the weighted average number of common shares and common share equivalents outstanding during the period. In calculating earnings per share, earnings are the same for the basic and diluted calculations. Weighted average shares outstanding decreased in the September 2015 quarter compared to the same quarter of the prior year primarily due to repurchases of shares under the Company s share repurchase program. See also Note D.

Note B Stock-Based Compensation and Stock Options

Under the Company s Restated Omnibus Incentive Plan (formerly the Restated 1988 Executive Stock Option Plan) (the Plan) as in effect at September 30, 2015, options for up to 19,365,000 shares of the Company s common stock may be granted over the life of the Plan to key employees, non-employee directors and consultants at exercise prices not less than the fair market value of the stock at the date of grant. Options granted under the Plan are non-statutory stock options and generally vest 25% one year from date of grant and the remaining 75% vesting ratably each month for the next 36 months. The options granted to employees and the board of directors expire at the end of five years and ten years from date of grant, respectively.

The Company records compensation expense for employee stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes option-pricing model with the assumptions included in the table below. The Company uses historical data among other factors to estimate the expected volatility, the expected option life, and the expected forfeiture rate. The risk-free rate is based on the interest rate paid on a U.S. Treasury issue with a term similar to the estimated life of the option. Based upon the historical experience of options cancellations, the Company has estimated an annualized forfeiture rate of 12.46% and 12.28% for the three months ended September 30, 2014 and 2015, respectively. Forfeiture rates will be adjusted over the requisite service period when actual forfeitures differ, or are expected to differ, from the estimate. The following assumptions were used to estimate the fair value of options granted during the three months ended September 30, 2014 and 2015 using the Black-Scholes option-pricing model:

	Three Months Ended September 30,	
	2014	2015
Risk-free interest rate	1.66%	1.61%
Expected volatility	46%	44%
Expected dividend yield	0.00%	0.00%
Expected forfeiture rate	12.46%	12.28%

Expected weighted average life of option in years	4.4 years	4.4 years

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

Note B Stock-Based Compensation and Stock Options (continued)

All options granted in the six months ended September 30, 2014 and 2015 were granted with an exercise price equal to the fair value of the Company s common stock on the grant date and are non-statutory stock options.

For the three months ended September 30, 2014 and 2015, the Company recorded share-based compensation expense of $445,000 and $488,000, respectively. For the six months ended September 30, 2014 and 2015, the Company recorded share-based compensation expense of $1,162,000 and $1,104,000, respectively. The table below shows the amounts recognized in the consolidated financial statements for stock compensation expense for time-based options and performance-based options during the three and six months ended September 30, 2014 and 2015, respectively.

	Three Months Ended	
	September 30, 2014	September 30, 2015
Cost of revenues	$ 255,000	$ 321,000
General and administrative	190,000	167,000
Total cost of stock-based compensation included in income before income tax provision	$ 445,000	$ 488,000
Amount of income tax benefit recognized	(169,000)	(188,000)
Amount charged against net income	$ 276,000	$ 300,000
Effect on diluted net income per share	$ (0.01)	$ (0.01)

	Six Months Ended	
	September 30, 2014	September 30, 2015
Cost of revenues	$ 494,000	$ 633,000
General and administrative	668,000	471,000
Total cost of stock-based compensation included in income before income tax provision	$ 1,162,000	1,104,000
Amount of income tax benefit recognized	(442,000)	(425,000)
Amount charged against net income	$ 720,000	$ 679,000

Effect on diluted net income per share	$	(0.03)	$	(0.03)

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

Note B Stock-Based Compensation and Stock Options (continued)

Summarized information for all stock options for the three and six months ended September 30, 2014 and 2015 follows:

	Three Months Ended September 30, 2014		Three Months Ended September 30, 2015	
	Shares	Average Price	Shares	Average Price
Options outstanding, beginning	1,118,530	$ 25.60	1,167,042	$ 28.15
Options granted	48,650	40.57	47,300	33.15
Options exercised	(30,957)	18.75	(59,804)	16.91
Options cancelled	(150)	24.24	(18,952)	36.25
Options outstanding, ending	1,136,073	$ 26.42	1,135,586	$ 28.81

	Six Months Ended September 30, 2014		Six Months Ended September 30, 2015	
	Shares	Average Price	Shares	Average Price
Options outstanding, beginning	1,115,984	$ 24.80	1,163,179	$ 27.65
Options granted	86,050	42.43	87,000	33.85
Options exercised	(56,950)	18.41	(95,641)	17.75
Options cancelled	(9,011)	29.32	(18,952)	36.25
Options outstanding, ending	1,136,073	$ 26.42	1,135,586	$ 28.81

The following table summarizes the status of stock options outstanding and exercisable at September 30, 2015:

Range of Exercise Price	Number of Outstanding Options	Weighted Average Remaining Contractual Life	Outstanding Options Weighted Average Exercise Price	Exercisable Options Number of Exercisable Options	Exercisable Options Weighted Average Exercise

						Price
\$9.05 to \$23.00	285,254	3.30	\$	17.66	255,802	\$ 17.15
\$23.01 to \$24.64	289,600	2.26		23.56	181,902	23.60
\$24.65 to \$34.78	290,581	3.89		33.19	63,311	29.23
\$34.79 to \$45.55	270,151	3.71		41.51	62,775	43.15
Total	1,135,586	3.28	\$	28.81	563,790	\$ 23.48

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

Note B Stock-Based Compensation and Stock Options (continued)

A summary of the status for all outstanding options at September 30, 2015, and changes during the three months then ended, is presented in the table below:

	Number of Options	Weighted Average Exercise Per Share	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value as of September 30, 2015
Options outstanding at July 1, 2015	1,167,042	$ 28.15		
Granted	47,300	33.15		
Exercised	(59,804)	16.91		
Cancelled forfeited	(18,952)	36.25		
Cancelled expired				
Ending outstanding	1,135,586	$ 28.81	3.28	$ 6,975,029
Ending vested and expected to vest	1,028,863	$ 28.08	3.20	$ 6,911,556
Ending exercisable at September 30, 2015	563,790	$ 23.48	2.78	$ 5,708,498

The weighted-average grant-date fair value of options granted during the three months ended September 30, 2014 and 2015, was $15.84 and $12.53, respectively.

Included in the above-noted stock option grants and stock compensation expense are performance-based stock options under which vesting occurs only upon the Company achieving certain revenue or earnings per shares targets on a calendar year basis as determined by the Company s Board of Directors. These options were valued in the same manner as the time-vesting options. However, the Company only recognizes stock compensation to the extent that the targets are determined to be achieved which allow the performance options to vest. The Company recognized ($64,000) and ($63,000) of stock compensation expense for the three months ended September 30, 2014 and 2015, respectively, for performance-based stock options.

Note C Treasury Stock and Subsequent Event

The Company s Board of Directors initially approved the commencement of a share repurchase program in the fall of 1996. In August 2013, the Board approved a 2,000,000 share expansion of the repurchase program to 34,000,000 shares over the life of the share repurchase program. Since the commencement of the share repurchase program, the Company has spent $379 million to repurchase 33,552,190 shares of its common stock, equal to 63% of the outstanding common stock had there been no repurchases. The average price of these repurchases was $11.30 per share. These repurchases were funded primarily from the net earnings of the Company, along with the proceeds from the exercise of common stock options. During the three and six months ended September 30, 2015, the Company repurchased 299,620 shares for $9.7 million at an average of $32.37 per share and 559,702 shares for $18.8 million at an average of $33.55 per share, respectively. The Company had 19,787,279 shares of common stock outstanding as of September 30, 2015, net of the 33,552,190 shares in treasury. Subsequent to the end of the quarter, through October 30, 2015, the Company repurchased 99,403 shares for $3,287,000 at an average of $33.07 per share.

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

Note D Weighted Average Shares and Net Income Per Share

Weighted average basic common shares decreased from 20,819,000 for the quarter ended September 30, 2014 to 19,902,000 for the quarter ended September 30, 2015. Weighted average diluted common and common equivalent shares decreased from 21,050,000 for the quarter ended September 30, 2014 to 20,063,000 for the quarter ended September 30, 2015. The net decrease in both of these weighted share calculations is due to the repurchase of common stock as noted above, offset by an increase in shares outstanding due to the exercise of stock options under the Company s employee stock option plan.

Net income per common and common equivalent shares was computed by dividing net income by the weighted average number of common and common stock equivalents outstanding during the quarter. The calculations of the basic and diluted weighted shares for the three and six months ended September 30, 2014 and 2015, are as follows:

	Three Months Ended September 30,	
	2014	2015
Net Income	$ 7,883,000	$ 8,267,000
Basic:		
Weighted average common shares outstanding	20,819,000	19,902,000
Net Income per share	$ 0.38	$ 0.42
Diluted:		
Weighted average common shares outstanding	20,819,000	19,902,000
Treasury stock impact of stock options	231,000	161,000
Total common and common equivalent shares	21,050,000	20,063,000
Net Income per share	$ 0.37	$ 0.41

	Six Months Ended September 30,	
	2014	2015
Net Income	$ 16,182,000	$ 15,167,000
Basic:		
Weighted average common shares outstanding	20,877,000	20,026,000

Net Income per share	$	0.78	$	0.76
Diluted:				
Weighted average common shares outstanding		20,877,000		20,026,000
Treasury stock impact of stock options		253,000		173,000
Total common and common equivalent shares		21,130,000		20,199,000
Net Income per share	$	0.77	$	0.75

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

Note E Shareholder Rights Plan

During fiscal 1997, the Company s Board of Directors approved the adoption of a Shareholder Rights Plan. The Shareholder Rights Plan provides for a dividend distribution to CorVel stockholders of one preferred stock purchase right for each outstanding share of CorVel s common stock under certain circumstances. In November 2008, the Company s Board of Directors approved an amendment to the Shareholder Rights Plan to extend the expiration date of the rights to February 10, 2022.

The rights are designed to assure that all shareholders receive fair and equal treatment in the event of any proposed takeover of the Company and to encourage a potential acquirer to negotiate with the Board of Directors prior to attempting a takeover. The rights have an exercise price of $118 per right, subject to subsequent adjustment. The rights trade with the Company s common stock and will not be exercisable until the occurrence of certain takeover-related events.

Generally, the Shareholder Rights Plan provides that if a person or group acquires 15% or more of the Company s common stock without the approval of the Board, subject to certain exceptions, the holders of the rights, other than the acquiring person or group, would, under certain circumstances, have the right to purchase additional shares of the Company s common stock having a market value equal to two times the then-current exercise price of the right.

In addition, if the Company is thereafter merged into another entity, or if 50% or more of the Company s consolidated assets or earning power are sold, then the right will entitle its holder to buy common shares of the acquiring entity having a market value equal to two times the then-current exercise price of the right. The Company s Board of Directors may exchange or redeem the rights under certain conditions.

Note F Other Intangible Assets

Other intangible assets consist of the following at September 30, 2015:

Item	Life	Cost	Six Months Ended September 30, 2015 Amortization Expense	Accumulated Amortization at September 30, 2015	Cost, Net of Accumulated Amortization at September 30, 2015
Covenants Not to Compete	5 Years	775,000	10,000	772,000	$ 3,000
Customer Relationships	18-20 Years	7,922,000	211,000	3,510,000	$ 4,412,000
TPA Licenses	15 Years	204,000	7,000	111,000	$ 93,000
Total		8,901,000	228,000	4,393,000	$ 4,508,000

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CORVEL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2015

Note G Line of Credit

In September 2015, the Company renewed a line of credit agreement. The line is with a financial institution to provide a revolving credit facility with borrowing capacity of up to $10 million. Borrowings under this agreement, as amended, bear interest, at the Company s option, at a fixed LIBOR-based rate plus 1.50% or at a fluctuating rate determined by the financial institution to be 1.50% above the daily one-month LIBOR rate. The loan covenants require the Company to maintain the current assets to liabilities ratio of at least 1.25:1, debt to tangible net worth not greater than 1.25:1 and have positive net income. There were no outstanding revolving loans as of September 30, 2015, but letters of credit in the aggregate amount of $4.5 million have been issued separate from the line of credit and therefore do not reduce the amount of borrowings available under the revolving credit facility. The renewed credit agreement expires in September 2016.

Note H Contingencies and Legal Proceedings

The Company is involved in litigation arising in the normal course of business. Management believes that resolution of these matters will not result in any payment that, individually or in the aggregate, would be material to the financial position or results of the operations of the Company.

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Item 2 - MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This report may include certain forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including (without limitation) statements with respect to anticipated future operating and financial performance, growth and acquisition opportunities and other similar forecasts and statements of expectation. Words such as expects, anticipates, intends, plans, predicts, believes, seeks, estimates, potential, continue, strive, ongoing, may, will, wou variations of these words and similar expressions, are intended to identify these forward-looking statements. Forward-looking statements made by the Company and its management are based on estimates, projections, beliefs, and assumptions of management at the time of such statements and are not guarantees of future performance.

The Company disclaims any obligations to update or revise any forward-looking statement based on the occurrence of future events, the receipt of new information or otherwise, except as required by law. Actual future performance, outcomes and results may differ materially from those expressed in forward-looking statements made by the Company and its management as a result of a number of risks, uncertainties, and assumptions. Representative examples of these factors include (without limitation) general industry and economic conditions, including a decreasing number of national claims due to decreasing number of injured workers; cost of capital and capital requirements; existing and possible litigation and legal liability in the course of operations and the Company s ability to resolve such litigation; competition from other managed care companies; the ability to expand certain areas of the Company s business; shifts in customer demands; the ability of the Company to produce market-competitive software; changes in operating expenses including employee wages, benefits and medical inflation; governmental and public policy changes, including but not limited to legislative and administrative law and rule implementation or change; and dependence on key personnel.

Overview

CorVel Corporation is an independent nationwide provider of medical cost containment and managed care services designed to address the escalating medical costs of workers compensation and auto claims. The Company s services are provided to insurance companies, third party administrators (TPA s), governmental entities, and self-administered employers to assist them in managing the medical costs and monitoring the quality of care associated with healthcare claims.

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Network Solutions Services

The Company s network solutions services are designed to reduce the price paid by its customers for medical services rendered in workers compensation cases, auto policies and, to a lesser extent, group health policies. The network solutions offered by the Company include automated medical fee auditing, preferred provider services, retrospective utilization review, independent medical examinations, and inpatient bill review. Network solutions services also includes revenue from the Company s directed care network (CareIQ), including imaging and physical therapy.

Patient Management Services

In addition to its network solutions services, the Company also operates as a TPA offering a range of patient management services, which involve working on a one-on-one basis with injured employees and their various healthcare professionals, employers, and insurance company adjusters. The services are designed to monitor the medical necessity and appropriateness of healthcare services provided to workers compensation and other healthcare claimants and to expedite return to work. The Company offers these services on a stand-alone basis, or as an integrated component of its medical cost containment services. Patient management services include the processing of claims for self-insured payors to property and casualty insurance.

Seasonality

While we are not directly impacted by seasonal shifts, we are affected by the change in working days in a given quarter. There are generally fewer working days for our employees to generate revenue in the third fiscal quarter as we experience vacations, inclement weather, and holidays.

Organizational Structure

The Company s management is structured geographically with regional vice-presidents who report to the Chief Executive Officer of the Company. Each of these regional vice-presidents is responsible for all services provided by the Company in his or her particular region and for the operating results of the Company in multiple states. These regional vice-presidents have area and district managers who are also responsible for all services provided by the Company in their given area and district.

Business Enterprise Segments

The Company operates in one reportable operating segment, managed care. The Company s services are delivered to its customers through its local offices in each region and financial information for the Company s operations follows this service delivery model. All regions provide the Company s patient management and network solutions services. FASB ASC 280-10 establishes standards for the way that public business enterprises report information about operating segments in annual and interim consolidated financial statements. The Company s internal financial reporting is segmented geographically, as discussed above, and managed on a geographic rather than service line basis, with virtually all of the Company s operating revenue generated within the United States.

Under FASB ASC 280-10, two or more operating segments may be aggregated into a single operating segment for financial reporting purposes if aggregation is consistent with the objective and basic principles, if the segments have similar economic characteristics, and if the segments are similar in each of the following areas: 1) the nature of products and services; 2) the nature of the production processes; 3) the type or class of customer for their products and services; and 4) the methods used to distribute their products or provide their services. The Company believes each of its regions meet these criteria as each provides similar services and products to similar customers using similar methods of productions and similar methods to distribute the services and products.

Summary of Quarterly Results

The Company generated revenues of $124.5 million for the quarter ended September 30, 2015, an increase of $0.7 million, or 0.6%, compared to revenues of $123.7 million for the quarter ended September 30, 2014.

Cost of revenues decreased by $0.5 million, from $98.2 million in the September 30, 2014 quarter to $97.8 million in the September 30, 2015 quarter, a decrease of 0.5%. The decrease in cost of revenues was primarily due to a decrease in variable costs related to CareIQ and group health medical costs offset by an increase in salaries.

General and administrative expense increased by $0.5 million, from $12.7 million in the September 30, 2014 quarter to $13.2 million in the September 30, 2015 quarter, an increase of 3.6%. This increase was primarily due to one-time refunds that were recognized from the prior year and otherwise all other costs were flat.

Income tax expense increased by $0.4 million, or 7.7%, from $4.8 million, in the September 30, 2014 quarter to $5.2 million in the September 30, 2015 quarter. The increase in income tax expense was primarily due to the increase in income before income taxes from $12.7 million to $13.5 million.

Weighted diluted shares decreased from 21.1 million shares in the September 30, 2014 quarter to 20.1 million shares in the September 30, 2015 quarter, a decrease of 987,000 shares, or 4.7%. This decrease was due primarily to the repurchase of 1,094,764 shares of common stock in the twelve months ended September 30, 2015.

Diluted earnings per share increased from $0.37 in the September 30, 2014 quarter to $0.41 in the September 30, 2015 quarter, an increase of $0.04 per share, or 10.8%. The increase in diluted earnings per share was due to the increase in net income and by a reduction in the number of shares outstanding due to shares repurchased under our stock repurchase program.

Results of Operations for the three months ended September 30, 2014 and 2015

The Company derives its revenues from providing patient management and network solutions services to payers of workers compensation benefits, auto insurance claims, and health insurance benefits. Patient management services include claims management and all services sold to claims management customers, case management, 24/7 nurse triage, utilization management, vocational rehabilitation, and life care planning. Network solutions services include medical bill review, PPO management, facility claim review, provider reimbursement, professional review, pharmacy services, directed care services, Medicare solutions, and clearinghouse services. The percentages of total revenues attributable to patient management and network solutions services for the quarters ended September 30, 2014 and September 30, 2015 are as follows:

	September 30, 2014	September 30, 2015
Patient management services	54.2%	54.7%
Network solutions services	45.8%	45.3%

The following table sets forth, for the periods indicated, the dollar amounts, dollar and percent changes, share changes, and the percentage of revenues represented by certain items reflected in the Company s consolidated income statements for the three months ended September 30, 2014 and September 30, 2015. The Company s past operating results are not necessarily indicative of future operating results.

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	Three Months Ended September 30, 2014	Three Months Ended September 30, 2015	Change	Percentage Change
Revenue	$ 123,714,000	$ 124,460,000	$ 746,000	0.6%
Cost of revenues	98,247,000	97,776,000	(471,000)	(0.5%)
Gross profit	25,467,000	26,684,000	1,217,000	4.8%
Gross profit as percentage of revenue	20.6%	21.4%		
General and administrative	12,749,000	13,209,000	460,000	3.6%
General and administrative as percentage of revenue	10.3%	10.6%		
Income before income tax provision	12,718,000	13,475,000	757,000	6.0%
Income before income tax provision as percentage of revenue	10.3%	10.8%		
Income tax provision	4,835,000	5,208,000	373,000	7.7%
Net income	$ 7,883,000	$ 8,267,000	$ 384,000	4.9%
Weighted Shares				
Basic	20,819,000	19,902,000	(917,000)	(4.4%)
Diluted	21,050,000	20,063,000	(987,000)	(4.7%)
Earnings Per Share				
Basic	$ 0.38	$ 0.42	$ 0.04	10.5%
Diluted	$ 0.37	$ 0.41	$ 0.04	10.8%

Revenues

Change in revenue from the quarter ended September 30, 2014 to the quarter ended September 30, 2015

Revenues increased from $123.7 million for the three months ended September 30, 2014 to $124.5 million for the three months ended September 30, 2015, an increase of $0.7 million, or 0.6%. The increase in revenues was due to an increase in patient management services that includes all services sold to TPA customers, which increased by 1.5% from $67.1 million to $68.1 million. The increase in patient management services was offset by a decrease in network solutions services, which decreased from $56.6 million to $56.3 million.

Cost of Revenues

The Company s cost of revenues consist of direct expenses, costs directly attributable to the generation of revenue, and field indirect costs which are incurred in the field to support the operations in the field offices which generate the revenue. Direct costs are primarily case manager salaries, bill review analysts, related payroll taxes and fringe benefits, costs for independent medical examination (IME), and prescription drugs and MRI providers. Most of the Company s revenues are generated in offices which provide both patient management services and network solutions services. The largest of the field indirect costs are manager salaries and bonuses, account executive base pay and commissions, administrative and clerical support, field systems personnel, PPO network developers, related payroll taxes and fringe benefits, office rent, and telephone expenses. Approximately 35% of the costs incurred in the field are field indirect costs which support both the patient management services and network solutions operations of the Company s field operations.

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Change in cost of revenues from the quarter ended September 30, 2014 to the quarter ended September 30, 2015

Cost of revenues decreased from $98.2 million in the three months ended September 30, 2014 to $97.8 million in the three months ended September 30, 2015, a decrease of $0.5 million or 0.5%. The decrease in cost of revenues was primarily due to a decrease in units provided related to CareIQ due to lower CareIQ revenue. Additionally, group health medical costs decreased which was offset by an increase in salaries and headcount.

General and Administrative Expense

For the quarter ended September 30, 2015, general and administrative expense consisted of approximately 62% of corporate systems costs, which include corporate systems support, implementation and training, rules engine development, national information technology (IT) strategy and planning, amortization of software development costs, depreciation of the hardware costs in the Company s national systems, the Company s national wide area network, and other systems related costs. The remaining 38% of the general and administrative expense consisted of national marketing, national sales support, corporate legal, corporate insurance, human resources, accounting, product management, new business development and other general corporate matters.

Change in general and administrative expense from the quarter ended September 30, 2014 to the quarter ended September 30, 2015

General and administrative expense increased from $12.7 million in the quarter ended September 30, 2014 to $13.2 million in the quarter ended September 30, 2015, an increase of $0.5 million, or 3.6%. This increase was primarily due to one-time refunds that were recognized from the prior year and otherwise all other costs were flat.

Income Tax Provision

Change in income tax expense from the quarter ended September 30, 2014 to the quarter ended September 30, 2015

Income tax expense increased by $0.4 million, or 7.7%, from $4.8 million for the quarter ended September 30, 2014 to $5.2 million for the quarter ended September 30, 2015 due to the increase in income before income taxes from $12.7 million to $13.5 million during the same periods. The income tax expense as a percentage of income before income taxes, also known as the effective tax rate, was 38.0% for the quarter ended September 30, 2014 and 38.6% for the quarter ended September 30, 2015.

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Results of Operations for the six months ended September 30, 2014 and the six months ended September 30, 2015

The following table sets forth, for the periods indicated, the dollar amounts, dollar and percent changes, share changes, and the percentage of revenues represented by certain items reflected in the Company s consolidated income statements for the six months ended September 30, 2014 and September 30, 2015. The Company s past operating results are not necessarily indicative of future operating results.

	Six Months Ended September 30, 2014	Six Months Ended September 30, 2015	Change	Percentage Change
Revenue	$ 248,078,000	$ 251,399,000	$ 3,321,000	1.3%
Cost of revenues	194,911,000	198,532,000	3,621,000	1.9%
Gross profit	53,167,000	52,867,000	(300,000)	(0.6%)
Gross profit as percentage of revenue	21.4%	21.0%		
General and administrative	26,954,000	28,171,000	1,217,000	4.5%
General and administrative as percentage of revenue	10.9%	11.2%		
Income before income tax provision	26,213,000	24,696,000	(1,517,000)	(5.8%)
Income before income tax provision as percentage of revenue	10.6%	9.8%		
Income tax provision	10,031,000	9,529,000	(502,000)	(5.0%)
Net income				